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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-Q**

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(Mark one)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2011**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_**

**Commission File Number: 333-20277**

**PHL VARIABLE INSURANCE COMPANY**

(Exact name of registrant as specified in its charter)

**Connecticut**

(State or other jurisdiction of  
incorporation or organization)

**06-1045829**

(I.R.S. Employer Identification No.)

**One American Row, Hartford, Connecticut**

(Address of principal executive offices)

**06102-5056**

(Zip Code)

**(860) 403-5000**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

*(Do not check if smaller reporting company)*

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES  NO

PHL Variable Insurance Company is a wholly-owned indirect subsidiary of The Phoenix Companies, Inc., and there is no market for the registrant's common stock. As of May 12, 2011, there were 500 shares of the registrant's common stock outstanding.

**The registrant meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this Form with the reduced disclosure format permitted by that General Instruction.**

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## PART I. FINANCIAL INFORMATION

### Item 1. FINANCIAL STATEMENTS

**PHL VARIABLE INSURANCE COMPANY**  
**Unaudited Interim Balance Sheets**  
(\$ in thousands, except share data)  
**March 31, 2011 (unaudited) and December 31, 2010**

	<u>Mar 31,</u> <u>2011</u>	<u>Dec 31,</u> <u>2010</u>
<b>ASSETS:</b>		
Available-for-sale debt securities, at fair value (amortized cost of \$1,790,466 and \$1,541,506)	\$ 1,782,929	\$ 1,520,398
Venture capital partnerships, at equity in net assets	3,569	3,226
Policy loans, at unpaid principal balances	58,346	57,326
Other investments	83,149	90,757
Fair value option investments	12,019	11,731
<b>Total investments</b>	<b>1,940,012</b>	<b>1,683,438</b>
Cash and cash equivalents	37,419	51,059
Accrued investment income	14,964	12,019
Receivables	384,899	367,142
Deferred policy acquisition costs	590,124	594,126
Receivable from related parties	30,175	13,649
Other assets	53,114	54,727
Separate account assets	2,947,541	2,922,946
<b>Total assets</b>	<b><u>\$ 5,998,248</u></b>	<b><u>\$ 5,699,106</u></b>
<b>LIABILITIES:</b>		
Policy liabilities and accruals	\$ 1,293,761	\$ 1,283,034
Policyholder deposit funds	977,257	793,142
Deferred income taxes	18,231	13,371
Payable to related parties	40,864	9,924
Other liabilities	96,734	66,534
Separate account liabilities	2,947,541	2,922,946
<b>Total liabilities</b>	<b><u>5,374,388</u></b>	<b><u>5,088,951</u></b>
<b>CONTINGENT LIABILITIES (Note 15)</b>		
<b>STOCKHOLDER'S EQUITY:</b>		
Common stock, \$5,000 par value: 1,000 shares authorized; 500 shares issued	2,500	2,500
Additional paid-in capital	802,152	802,152
Accumulated deficit	(171,401)	(182,041)
Accumulated other comprehensive loss, net of tax	(9,391)	(12,456)
<b>Total stockholder's equity</b>	<b><u>623,860</u></b>	<b><u>610,155</u></b>
<b>Total liabilities and stockholder's equity</b>	<b><u>\$ 5,998,248</u></b>	<b><u>\$ 5,699,106</u></b>

The accompanying notes are an integral part of these financial statements.

**PHL VARIABLE INSURANCE COMPANY**  
**Unaudited Interim Statements of Income and Comprehensive Income**  
(\$ in thousands)  
**Three Months Ended March 31, 2011 and 2010**

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>REVENUES:</b>		
Premiums	\$ 163	\$ 1,179
Insurance and investment product fees	101,830	107,236
Net investment income	21,398	17,712
Net realized investment gains (losses):		
Total other-than-temporary impairment (“OTTI”) losses	(880)	(5,684)
Portion of OTTI losses recognized in other comprehensive income	386	2,116
Net OTTI losses recognized in earnings	(494)	(3,568)
Net realized investment gains (losses), excluding OTTI losses	(3,968)	4,562
Total realized investment gains (losses)	(4,462)	994
<b>Total revenues</b>	<b>118,929</b>	<b>127,121</b>
<b>BENEFITS AND EXPENSES:</b>		
Policy benefits	50,569	55,521
Policy acquisition cost amortization	39,052	38,457
Other operating expenses	18,381	23,333
<b>Total benefits and expenses</b>	<b>108,002</b>	<b>117,311</b>
Income before income taxes	10,927	9,810
Income tax expense	287	3,958
<b>Net income</b>	<b>\$ 10,640</b>	<b>\$ 5,852</b>
<b>COMPREHENSIVE INCOME (LOSS):</b>		
<b>Net income</b>	<b>\$ 10,640</b>	<b>\$ 5,852</b>
Net unrealized investment gains (losses)	3,316	(8,564)
Non-credit portion of OTTI losses recognized in other comprehensive income	(251)	(1,375)
<b>Other comprehensive income (loss)</b>	<b>3,065</b>	<b>(9,939)</b>
<b>Comprehensive income (loss)</b>	<b>\$ 13,705</b>	<b>\$ (4,087)</b>

The accompanying notes are an integral part of these financial statements.

**PHL VARIABLE INSURANCE COMPANY**  
**Unaudited Interim Statement of Cash Flows**  
(\$ in thousands)  
**Three Months Ended March 31, 2011 and 2010**

	<b>Three Months Ended</b>	
	<b>March 31</b>	
	<b>2011</b>	<b>2010</b>
<b>OPERATING ACTIVITIES:</b>		
Net income	\$ 10,640	\$ 5,852
Net realized investment (gains) losses	4,462	(994)
Deferred income tax expense (benefit)	(483)	13,161
Increase in receivables	(24,927)	(6,642)
Increase in accrued investment income	(3,223)	(3,122)
Decrease in deferred policy acquisition costs	2,591	35,339
Increase (decrease) in policy liabilities and accruals	10,391	(27,277)
Other assets and other liabilities net change	33,378	(15,803)
<b>Cash from operating activities</b>	<b>32,829</b>	<b>514</b>
<b>INVESTING ACTIVITIES:</b>		
Investment purchases	(703,069)	(564,609)
Investment sales, repayments and maturities	464,663	518,965
Policy loan advances, net	(1,020)	(3,356)
<b>Cash for investing activities</b>	<b>(239,426)</b>	<b>(49,000)</b>
<b>FINANCING ACTIVITIES:</b>		
Policyholder deposit fund deposits	215,745	28,376
Policyholder deposit fund withdrawals	(22,788)	(39,765)
Capital contributions from parent	--	14,000
<b>Cash from financing activities</b>	<b>192,957</b>	<b>2,611</b>
<b>Change in cash and cash equivalents</b>	<b>(13,640)</b>	<b>(45,875)</b>
Cash and cash equivalents, beginning of period	51,059	83,518
<b>Cash and cash equivalents, end of period</b>	<b>\$ 37,419</b>	<b>\$ 37,643</b>

Included in cash and cash equivalents above is cash held as collateral by a third party of \$7,510 thousand as of March 31, 2011. There was no cash held as collateral by a third party as of March 31, 2010.

During the three months ended March 31, 2011, the Company received no capital contributions. During the three months ended March 31, 2010, the Company received \$14,000 thousand in capital contributions, all of which was in cash.

The accompanying notes are an integral part of these financial statements.

**PHL VARIABLE INSURANCE COMPANY**  
**Unaudited Interim Statement of Changes in Stockholder's Equity**  
(\$ in thousands)  
**Three Months Ended March 31, 2011 and 2010**

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>COMMON STOCK:</b>		
Balance, beginning of period	\$ 2,500	\$ 2,500
<b>Balance, end of period</b>	<b>\$ 2,500</b>	<b>\$ 2,500</b>
<b>ADDITIONAL PAID-IN CAPITAL:</b>		
Balance, beginning of period	\$ 802,152	\$ 788,152
Capital contributions from parent	--	14,000
<b>Balance, end of period</b>	<b>\$ 802,152</b>	<b>\$ 802,152</b>
<b>RETAINED EARNINGS (ACCUMULATED DEFICIT):</b>		
Balance, beginning of period	\$ (182,041)	\$ (156,603)
Net income (loss)	10,640	5,852
<b>Balance, end of period</b>	<b>\$ (171,401)</b>	<b>\$ (150,751)</b>
<b>ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS):</b>		
Balance, beginning of period	\$ (12,456)	\$ (20,085)
Other comprehensive income (loss)	3,065	(9,939)
<b>Balance, end of period</b>	<b>\$ (9,391)</b>	<b>\$ (30,024)</b>
<b>TOTAL STOCKHOLDER'S EQUITY:</b>		
Balance, beginning of period	\$ 610,155	\$ 613,964
Change in stockholder's equity	13,705	9,913
<b>Balance, end of period</b>	<b>\$ 623,860</b>	<b>\$ 623,877</b>

The accompanying notes are an integral part of these financial statements.

**PHL VARIABLE INSURANCE COMPANY**  
**Notes to Unaudited Interim Financial Statements**  
**Three Months Ended March 31, 2011 and 2010**

**1. Organization and Operations**

PHL Variable Insurance Company (“PHL Variable” or the “Company”) is a life insurance company offering variable and fixed annuity and life insurance products. It is a wholly-owned subsidiary of PM Holdings, Inc. and PM Holdings, Inc. is a wholly-owned subsidiary of Phoenix Life Insurance Company (“Phoenix Life”), which is a wholly-owned subsidiary of The Phoenix Companies, Inc. (“PNX”), a New York Stock Exchange listed company. Phoenix Home Life Mutual Insurance Company demutualized on June 25, 2001 by converting from a mutual life insurance company to a stock life insurance company, became a wholly-owned subsidiary of PNX and changed its name to Phoenix Life Insurance Company.

Subsequent to the first quarter of 2009, when we lost several key distribution partners and experienced downgrades to our ratings, the Company has had minimal sales of its life and annuity products. In 2010, the Company repositioned its annuity product line through distributors that focus primarily on the middle market, including independent marketing organizations, and had improved annuity sales.

**2. Basis of Presentation and Significant Accounting Policies**

We have prepared these unaudited financial statements in accordance with accounting principles generally accepted in the United States of America (“GAAP”), which differ materially from the accounting practices prescribed by various insurance regulatory authorities. Certain prior year amounts have been reclassified to conform to the current year presentation.

These financials include all adjustments (consisting primarily of accruals) considered necessary for the fair statement of the balance sheet, statements of income, and statements of cash flows for the interim periods. Certain financial information that is not required for interim reporting has been omitted. The interim financial statements should be read in conjunction with our 2010 Annual Report on Form 10-K. Financial results for the three months ended March 31, 2011 are not necessarily indicative of full year results.

**Use of estimates**

In preparing these financial statements in conformity with GAAP, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates and assumptions are made in the determination of estimated gross profits (“EGPs”) used in the valuation and amortization of assets and liabilities associated with universal life and annuity contracts; policyholder liabilities and accruals; valuation of investments in debt securities and venture capital partnerships; valuation of deferred tax assets; and accruals for contingent liabilities. We are also subject to estimates made by our ultimate parent company related to discount rates and other assumptions for our pension and other post-employment benefits expense.

**Adoption of new accounting standards**

The Company did not adopt any new accounting standards during the quarter ended March 31, 2011. Our adoption of new accounting standards during 2010 are presented in the notes to our consolidated financial statements in our 2010 Annual Report on Form 10-K.

## 2. Basis of Presentation and Significant Accounting Policies (continued)

### Accounting standards not yet adopted

#### *Amendment to Troubled Debt Restructuring Guidance*

In April 2011, the Financial Accounting Standards Board (the “FASB”) issued amended guidance to ASC 310, *Receivables*, to clarify guidance on troubled debt restructurings related to a creditor’s determination of whether or not a restructuring constitutes a concession and if the debtor is experiencing financial difficulties. This guidance is effective for interim periods beginning after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. Retrospective application to all prior periods presented on the date of application is also permitted, but not required. We expect to adopt this guidance with no material effect on our financial statements.

#### *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts*

In October 2010, the FASB issued amended guidance to ASC 944, *Financial Services – Insurance*, to address the diversity in practice for accounting for costs associated with acquiring or renewing insurance contracts. The amendment clarifies the definition of acquisition costs (i.e., costs which qualify for deferral) to incremental direct costs that result directly from, and are essential to, a contract and would not have been incurred by the insurance entity had the contract transaction not occurred. Therefore, only costs related to successful efforts of acquiring a new, or renewal, contract should be deferred. This guidance is effective for periods beginning after December 15, 2011, on a prospective basis. Retrospective application to all prior periods presented on the date of application is also permitted, but not required. We are in the process of determining the effect on our financial statements.

### Significant accounting policies

Our significant accounting policies are presented in the notes to our financial statements in our 2010 Annual Report on Form 10-K.

## 3. Deferred Policy Acquisition Costs

### Deferred Policy Acquisition Costs:

*(\$ in thousands)*

	Three Months Ended	
	March 31,	
	2011	2010
Policy acquisition costs deferred	\$ 36,461	\$ 3,118
Costs amortized to expenses:		
Recurring costs	(38,894)	(39,674)
Realized investment gains (losses)	(158)	1,217
Offsets to net unrealized investment gains or losses included in accumulated other comprehensive loss <sup>(1)</sup>	(5,270)	(58,087)
Other	3,859	5,113
Change in deferred policy acquisition costs	(4,002)	(88,313)
Deferred policy acquisition costs, beginning of period	594,126	837,567
<b>Deferred policy acquisition costs, end of period</b>	<b>\$ 590,124</b>	<b>\$ 749,254</b>

<sup>(1)</sup> An offset to deferred policy acquisition costs and accumulated other comprehensive income is recorded each period to the extent that, had unrealized holding gains or losses from securities classified as available-for-sale actually been realized, an adjustment to deferred policy acquisition costs amortized using gross profits or gross margins would result.

We amortize deferred policy acquisition costs based on the related policy’s classification. For universal life, variable universal life and accumulation annuities, deferred policy acquisition costs are amortized in proportion to EGPs.

The projection of EGPs requires the use of various assumptions, estimates and judgments about the future. Assumptions considered to be significant in the development of EGPs include separate account fund performance, surrender and lapse rates, interest margin, mortality, premium persistency, funding patterns, expenses and reinsurance costs and recoveries. These assumptions are reviewed on a regular basis and are based on our past experience, industry studies, regulatory requirements and estimates about the future.

### 3. Deferred Policy Acquisition Costs (continued)

We conduct a comprehensive assumption review on an annual basis, or as circumstances warrant. Upon completion of these assumption reviews, we revise our assumptions to reflect our current best estimate, thereby changing our estimate of EGPs in the deferred policy acquisition cost amortization models. The deferred policy acquisition cost asset is then adjusted with an offsetting benefit or charge to income to reflect such changes in the period of the revision, a process known as “unlocking.”

During the three months ended March 31, 2011 and 2010, it was determined that an unlocking was not warranted.

### 4. Investing Activities

#### Debt securities

##### Fair Value and Cost of General Account Securities:

(\$ in thousands)

	March 31, 2011		December 31, 2010	
	Fair Value	Cost	Fair Value	Cost
U.S. government and agency	\$ 107,902	\$ 105,879	\$ 98,283	\$ 96,137
State and political subdivision	32,677	33,089	32,509	33,092
Foreign government	16,746	15,351	16,086	14,683
Corporate	777,566	770,850	693,777	692,780
CMBS	214,942	211,486	173,955	172,850
RMBS	434,860	449,449	333,605	350,729
CDO/CLO	64,112	70,570	63,184	72,603
Other asset-backed	134,124	133,792	108,999	108,632
<b>Available-for-sale debt securities</b>	<b>\$ 1,782,929</b>	<b>\$ 1,790,466</b>	<b>\$ 1,520,398</b>	<b>\$ 1,541,506</b>

##### Unrealized Gains (Losses) from General Account Securities:

(\$ in thousands)

	March 31, 2011		December 31, 2010	
	Gains	Losses	Gains	Losses
U.S. government and agency	\$ 2,328	\$ (305)	\$ 2,483	\$ (337)
State and political subdivision	318	(730)	216	(799)
Foreign government	1,405	(10)	1,463	(60)
Corporate	40,562	(33,846)	39,804	(38,807)
CMBS	6,412	(2,956)	5,673	(4,568)
RMBS	4,720	(19,309)	4,429	(21,553)
CDO/CLO	1,591	(8,049)	1,940	(11,359)
Other asset-backed	1,381	(1,049)	1,320	(953)
<b>Debt securities gains and losses</b>	<b>\$ 58,717</b>	<b>\$ (66,254)</b>	<b>\$ 57,328</b>	<b>\$ (78,436)</b>
<b>Debt securities net losses</b>		<b>\$ (7,537)</b>		<b>\$ (21,108)</b>

Net unrealized investment gains and losses on securities classified as available for sale and certain other assets are included in the balance sheet as a component of accumulated other comprehensive income (loss) (“AOCI”). The table below presents the special category of AOCI for debt securities that are other-than-temporarily impaired when the impairment loss has been split between the credit loss component (in earnings) and the non-credit component (separate category of AOCI).

#### 4. Investing Activities (continued)

##### Fixed Maturity Non-Credit OTTI Losses in AOCI, by Security Type: (*\$ in thousands*)

	Mar 31, 2011 <sup>(1)</sup>	Dec 31, 2010 <sup>(1)</sup>
U.S. government and agency	\$ --	\$ --
State and political subdivision	--	--
Foreign government	--	--
Corporate	(1,504)	(1,512)
CMBS	(4,519)	(4,519)
RMBS	(15,675)	(15,263)
CDO/CLO	(5,432)	(6,279)
Other asset-backed	--	--
<b>Total fixed maturity non-credit OTTI losses in AOCI</b>	<b>\$ (27,130)</b>	<b>\$ (27,573)</b>

<sup>(1)</sup> Represents the amount of non-credit OTTI losses recognized in AOCI excluding net unrealized gains or losses subsequent to the date of impairment.

##### Aging of Temporarily Impaired General Account Debt Securities: (*\$ in thousands*)

	March 31, 2011					
	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Debt securities</b>						
U.S. government and agency	\$ 2,586	\$ (13)	\$ 3,650	\$ (292)	\$ 6,236	\$ (305)
State and political subdivision	17,249	(317)	915	(413)	18,164	(730)
Foreign government	1,017	(10)	--	--	1,017	(10)
Corporate	80,311	(1,869)	90,843	(31,977)	171,154	(33,846)
CMBS	23,416	(200)	8,626	(2,756)	32,042	(2,956)
RMBS	128,992	(3,022)	87,037	(16,287)	216,029	(19,309)
CDO/CLO	--	--	43,767	(8,049)	43,767	(8,049)
Other asset-backed	50,505	(504)	7,245	(545)	57,750	(1,049)
<b>Total temporarily impaired securities</b>	<b>\$ 304,076</b>	<b>\$ (5,935)</b>	<b>\$ 242,083</b>	<b>\$ (60,319)</b>	<b>\$ 546,159</b>	<b>\$ (66,254)</b>
<b>Below investment grade</b>	<b>\$ 3,562</b>	<b>\$ (123)</b>	<b>\$ 93,511</b>	<b>\$ (37,157)</b>	<b>\$ 97,073</b>	<b>\$ (37,280)</b>
<b>Below investment grade after offsets for deferred policy acquisition cost adjustment and taxes</b>		<b>\$ (21)</b>		<b>\$ (3,122)</b>		<b>\$ (3,143)</b>
<b>Number of securities</b>		<b>192</b>		<b>156</b>		<b>348</b>

Unrealized losses on below investment grade debt securities with a fair value of less than 80% of amortized cost totaled \$29,484 thousand at March 31, 2011, of which \$29,148 thousand was below 80% of amortized cost for more than 12 months.

These securities were considered to be temporarily impaired at March 31, 2011 because each of these securities had performed, and was expected to perform, in accordance with its original contractual terms and because it was more likely than not that we would not be required to sell these securities before recovery.

#### 4. Investing Activities (continued)

Aging of Temporarily Impaired General Account Debt Securities: ( <i>\$ in thousands</i> )	As of December 31, 2010					
	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Debt Securities</b>						
U.S. government and agency	\$ 592	\$ (8)	\$ 3,613	\$ (329)	\$ 4,205	\$ (337)
State and political subdivision	20,184	(381)	910	(418)	21,094	(799)
Foreign government	968	(60)	--	--	968	(60)
Corporate	38,680	(1,833)	89,756	(36,974)	128,436	(38,807)
CMBS	22,577	(401)	12,851	(4,167)	35,428	(4,568)
RMBS	61,907	(2,296)	96,254	(19,257)	158,161	(21,553)
CDO/CLO	88	--	43,920	(11,359)	44,008	(11,359)
Other asset-backed	35,346	(355)	7,456	(598)	42,802	(953)
<b>Total temporarily impaired securities</b>	<b>\$ 180,342</b>	<b>\$ (5,334)</b>	<b>\$ 254,760</b>	<b>\$ (73,102)</b>	<b>\$ 435,102</b>	<b>\$ (78,436)</b>
<b>Below investment grade</b>	<b>\$ 3,946</b>	<b>\$ (276)</b>	<b>\$ 88,564</b>	<b>\$ (43,094)</b>	<b>\$ 92,510</b>	<b>\$ (43,370)</b>
<b>Below investment grade after offsets for deferred policy acquisition cost adjustment and taxes</b>		<b>\$ (35)</b>		<b>\$ (3,310)</b>		<b>\$ (3,345)</b>
<b>Number of securities</b>		<b>142</b>		<b>174</b>		<b>316</b>

Unrealized losses on below investment grade debt securities with a fair value of less than 80% of amortized cost totaled \$37,304 thousand at December 31, 2010, of which \$36,499 thousand was below 80% of amortized cost for more than 12 months.

These securities were considered to be temporarily impaired at December 31, 2010 because each of these securities had performed, and was expected to perform, in accordance with its original contractual terms and because it was more likely than not that we would not be required to sell these securities before recovery.

#### Maturities of General Account Debt Securities: (*\$ in thousands*)

	As of March 31, 2011	
	Fair Value	Amortized Cost
Due in one year or less	\$ 82,732	\$ 82,349
Due after one year through five years	233,571	220,468
Due after five years through ten years	317,302	298,610
Due after ten years	301,286	323,742
CMBS/RMBS/ABS/CDO/CLO	848,038	865,297
<b>Total</b>	<b>\$ 1,782,929</b>	<b>\$ 1,790,466</b>

The maturities of general account debt securities, as of March 31, 2011, are summarized in the table above by contractual maturity. Actual maturities may differ from contractual maturities as certain borrowers have the right to call or prepay obligations with or without call or prepayment penalties, and we have the right to put or sell certain obligations back to the issuers.

#### Other-than-temporary impairments

A credit-related loss impairment for structured securities is determined by calculating the present value of the expected credit losses on a given security's coupon and principal cash flows until maturity. All other fixed income securities are written down to fair value. The impairment amount is separated into the amount related to credit losses, which is recorded as a charge to net realized investment losses included in our earnings, and the amount related to all other factors, which is recognized in other comprehensive income. The non-credit related loss component is equal to the difference between the fair value of a security and its impaired carrying value.

#### 4. Investing Activities (continued)

Management exercised significant judgment with respect to certain securities in determining whether impairments are temporary or other than temporary. At March 31, 2011, this included securities with \$17,518 thousand of gross unrealized losses of 50% or more for which no OTTI was ultimately indicated. In reaching its conclusions, management used a number of issuer-specific quantitative indicators and qualitative judgments to assess the probability of receiving a given security's contractual cash flows. This included the issue's implied yield to maturity, cumulative default rate based on rating, comparisons of issue-specific spreads to industry or sector spreads, specific trading activity in the issue, and other market data such as recent debt tenders and upcoming refinancing requirements. Management also reviewed fundamentals such as issuer credit and liquidity metrics, business outlook and industry conditions. Management does not have the intention to sell nor does it expect to be required to sell these securities prior to their recovery. Management maintains a watch list of securities that is reviewed for impairments. Each security on the watch list was evaluated, analyzed and discussed, with the positive and negative factors weighed in the ultimate determination of whether or not the security was other-than-temporarily impaired.

##### *Debt Securities*

Fixed maturity OTTIs recorded in the first quarter of 2011 were primarily concentrated in corporate bonds and structured securities. These impairments were driven primarily by significant rating downgrades and increased collateral default rates. In our judgment, these credit events or other adverse conditions of the issuers have caused, or will most likely lead to, a deficiency in the contractual cash flows related to the investment. Therefore, based upon these credit events, we have determined that OTTIs exist. Total impairments recognized through earnings related to such credit-related circumstances were \$494 thousand in the first quarter of 2011 and \$3,568 thousand in the first quarter of 2010.

In addition to these credit-related impairments recognized through earnings, we impaired securities to fair value through other comprehensive loss for any impairments related to non-credit related factors. These types of impairments were driven primarily by market or sector credit spread widening or by a lack of liquidity in the securities. The amount of impairments recognized as an adjustment to other comprehensive loss due to these factors was \$386 thousand in the first quarter of 2011 and \$2,116 thousand in the first quarter of 2010.

Prospectively, we will account for the OTTI security as if the debt security had been purchased on the impairment date, using an amortized cost basis equal to the previous cost basis less the amount of the credit loss impairment. We will continue to estimate the present value of future cash flows expected and, if significantly greater than the new cost basis, accrete the difference as interest income.

The following table rolls forward the amount of credit losses recognized in earnings on debt securities held at the beginning of the period, for which a portion of the OTTI was recognized in other comprehensive income.

##### **Credit Losses Recognized in Earnings on Debt Securities for which a Portion of the OTTI Loss was Recognized in Other Comprehensive Income:**

*(\$ in thousands)*

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2011</b>	<b>2010</b>
Balance, beginning of period	\$ (17,335)	\$ (12,442)
Add: Credit losses on securities not previously impaired <sup>(1)</sup>	(250)	(246)
Add: Credit losses on securities previously impaired <sup>(1)</sup>	(244)	(3,322)
Less: Credit losses on securities impaired due to intent to sell	--	--
Less: Credit losses on securities sold	958	--
Less: Increases in cash flows expected on previously impaired securities	--	--
<b>Balance, end of period</b>	<b>\$ (16,871)</b>	<b>\$ (16,010)</b>

<sup>(1)</sup> Additional credit losses on securities for which a portion of the OTTI loss was recognized in AOCI are included within net OTTI losses recognized in earnings on the statements of income and comprehensive income.

#### 4. Investing Activities (continued)

##### Venture capital partnerships

The following table presents investments in limited partnerships interests. We make contributions to partnerships under existing or new funding commitments.

##### Investment Activity in Venture Capital Partnerships:

*(\$ in thousands)*

	Three Months Ended March 31,	
	2011	2010
Contributions	\$ 247	\$ 137
Equity in earnings of partnerships	96	--
Distributions	--	(92)
Change in venture capital partnerships	343	45
Venture capital partnership investments, beginning of period	3,226	1,437
<b>Venture capital partnership investments, end of period</b>	<b>\$ 3,569</b>	<b>\$ 1,482</b>

##### Net investment income

##### Sources of Net Investment Income:

*(\$ in thousands)*

	Three Months Ended March 31,	
	2011	2010
Debt securities	\$ 20,442	\$ 17,093
Policy loans	720	723
Other investments	104	147
Fair value option investments	274	85
Venture capital	96	--
Cash and cash equivalents	4	12
Total investment income	21,640	18,060
Less: Investment expenses	242	348
<b>Net investment income</b>	<b>\$ 21,398</b>	<b>\$ 17,712</b>

#### 4. Investing Activities (continued)

##### Net realized investment gains (losses)

###### Sources and Types of

###### Net Realized Investment Gains (Losses):

(\$ in thousands)

	Three Months Ended	
	March 31,	
	2011	2010
Total other-than-temporary debt impairment losses	\$ (880)	\$ (5,684)
Portion of loss recognized in other comprehensive income	386	2,116
<b>Net debt impairment losses recognized in earnings</b>	<b>\$ (494)</b>	<b>\$ (3,568)</b>
Debt security impairments:		
U.S. government and agency	\$ --	\$ --
State and political subdivision	--	--
Foreign government	--	--
Corporate	(250)	--
CMBS	--	(570)
RMBS	(244)	(1,484)
CDO/CLO	--	(1,514)
Other asset-backed	--	--
Net debt security impairments	(494)	(3,568)
Other investments impairments	--	--
<b>Impairment losses</b>	<b>(494)</b>	<b>(3,568)</b>
Debt security transaction gains	631	237
Debt security transaction losses	(325)	(1,624)
Other investments transaction gains (losses)	--	265
<b>Net transaction losses</b>	<b>306</b>	<b>(1,122)</b>
Realized gains (losses) on derivative assets and liabilities	(4,274)	5,684
<b>Net realized investment gains (losses), excluding impairment losses</b>	<b>(3,968)</b>	<b>4,562</b>
<b>Net realized investment gains (losses), including impairment losses</b>	<b>\$ (4,462)</b>	<b>\$ 994</b>

##### Unrealized investment gains (losses)

###### Sources of Changes in

###### Net Unrealized Investment Gains (Losses):

(\$ in thousands)

	Three Months Ended	
	March 31,	
	2011	2010
Debt securities	\$ 13,571	\$ 36,172
Equity securities	133	(47)
Other investments	(26)	322
<b>Net unrealized investment gains</b>	<b>\$ 13,678</b>	<b>\$ 36,447</b>
Net unrealized investment gains	\$ 13,678	\$ 36,447
Applicable deferred policy acquisition cost	5,270	58,087
Applicable deferred income tax expense (benefit)	5,343	(11,873)
Offsets to net unrealized investment losses	10,613	46,214
<b>Net unrealized investment gains included in other comprehensive income</b>	<b>\$ 3,065</b>	<b>\$ 9,767</b>

##### Non-consolidated variable interest entities

Entities which do not have sufficient equity at risk to allow the entity to finance its activities without additional financial support or in which the equity investors, as a group, do not have the characteristic of a controlling financial interest are referred to as VIEs. We perform ongoing assessments of our investments in VIEs to determine whether we have a controlling financial interest in the VIE and therefore would be considered to be the primary beneficiary. An entity would be considered a primary beneficiary and be required to consolidate a VIE when the entity has both the power to direct the activities of a VIE that most significantly impact the entity's economic performance and the obligation to absorb losses, or right to receive benefits, that could potentially be significant to the VIE. We reassess our VIE determination with respect to an entity on an ongoing basis.

#### 4. Investing Activities (continued)

We are involved with various entities that are deemed to be VIEs primarily as a passive investor in private equity limited partnerships and through direct investments, in which we are not related to the general partner. These investments are accounted for under the equity method of accounting and are included in the venture capital category of the balance sheet. The carrying value of assets and liabilities, as well as the maximum exposure to loss, relating to significant VIEs for which we are not the primary beneficiary was \$3,569 thousand and \$3,226 thousand as of March 31, 2011 and December 31, 2010, respectively. The asset value of our investments in VIEs for which we are not the primary beneficiary is based upon sponsor values and financial statements of the individual entities. Our maximum exposure to loss related to these non-consolidated VIEs is limited to the amount of our investment.

#### Issuer and counterparty credit exposure

Credit exposure related to issuers and derivatives counterparties is inherent in investments and derivative contracts with positive fair value or asset balances. We manage credit risk through the analysis of the underlying obligors, issuers and transaction structures. We review our debt security portfolio regularly to monitor the performance of obligors and assess the stability of their credit ratings. We also manage credit risk through industry and issuer diversification and asset allocation. Maximum exposure to an issuer or derivative counterparty is defined by quality ratings, with higher quality issuers having larger exposure limits. As of March 31, 2011, we were not exposed to any credit concentration risk of a single issuer greater than 10% of stockholder's equity other than U.S. government and government agencies backed by the faith and credit of the U.S. government. We have an overall limit on below investment grade rated issuer exposure. To further mitigate the risk of loss on derivatives, we only enter into contracts in which the counterparty is a financial institution with a rating of A or higher.

As of March 31, 2011, we held derivative assets, net of liabilities, with a fair value of \$69,711 thousand. Derivative credit exposure was diversified with seven different counterparties. We also had debt securities of these issuers with a carrying value of \$19,117 thousand. Our maximum amount of loss due to credit risk with these issuers was \$88,828 thousand. See Note 6 to these financial statements for more information regarding derivatives.

#### 5. Separate Accounts, Death Benefits and Other Insurance Benefit Features

Separate account products are those for which a separate investment and liability account is maintained on behalf of the policyholder. Investment objectives for these separate accounts vary by fund account type, as outlined in the applicable fund prospectus or separate account plan of operations. Our separate account products include variable annuities and variable life insurance contracts. The assets supporting these contracts are carried at fair value and reported as separate account assets with an equivalent amount reported as separate account liabilities. Amounts assessed against the policyholder for mortality, administration, and other services are included within revenue in insurance and investment product fees. During the three month periods ended March 31, 2011 and 2010, there were no gains or losses on transfers of assets from the general account to a separate account.

#### Variable and fixed annuities

Many of our variable annuity contracts offer various guaranteed minimum death, accumulation, withdrawal and income benefits. These benefits are offered in various forms as described below.

#### Separate Account Investments of Account Balances of Contracts with Guarantees: (*\$ in thousands*)

	<u>Mar 31, 2011</u>	<u>Dec 31, 2010</u>
Debt securities	\$ 748,076	\$ 599,803
Equity funds	1,869,384	1,850,010
Other	66,025	68,677
<b>Total</b>	<b><u>\$ 2,683,485</u></b>	<b><u>\$ 2,518,490</u></b>

## 5. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

We establish policy benefit liabilities for minimum death and income benefit guarantees relating to certain annuity policies as follows:

- Liabilities associated with the guaranteed minimum death benefit (“GMDB”) are determined by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. The assumptions used for calculating the liabilities are generally consistent with those used for amortizing deferred policy acquisition costs.
- Liabilities associated with the guaranteed minimum income benefit (“GMIB”) are determined by estimating the expected value of the income benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. The assumptions used for calculating such guaranteed income benefit liabilities are generally consistent with those used for amortizing deferred policy acquisition costs.

For annuities with GMDB and GMIB, reserves are calculated based on 200 stochastically generated scenarios. The GMDB and GMIB guarantees are recorded in policy liabilities and accruals on our balance sheet. Changes in the liability are recorded in policy benefits, excluding policyholder dividends, on our statements of income. We regularly evaluate estimates used and adjust the additional liability balances, with a related charge or credit to benefit expense if actual experience or other evidence suggests that earlier assumptions should be revised.

### Changes in Guaranteed Liability Balances:

*(\$ in thousands)*

	<b>As of</b>	
	<b>March 31, 2011</b>	
	<b>Annuity GMDB</b>	<b>Annuity GMIB</b>
Liability balance as of January 1, 2011	\$ 4,570	\$ 17,456
Incurred	27	(799)
Paid	342	--
<b>Liability balance as of March 31, 2011</b>	<b>\$ 4,939</b>	<b>\$ 16,657</b>

### Changes in Guaranteed Liability Balances:

*(\$ in thousands)*

	<b>Year Ended</b>	
	<b>December 31, 2010</b>	
	<b>Annuity GMDB</b>	<b>Annuity GMIB</b>
Liability balance as of January 1, 2010	\$ 5,063	\$ 15,811
Incurred	3,330	1,646
Paid	(3,823)	--
<b>Liability balance as of December 31, 2010</b>	<b>\$ 4,570</b>	<b>\$ 17,457</b>

## 5. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

For those guarantees of benefits that are payable in the event of death, the net amount at risk is generally defined as the benefit payable in excess of the current account balance at the balance sheet date. We have entered into reinsurance agreements to reduce the net amount of risk on certain death benefits. Following are the major types of death benefits currently in-force:

### GMDB Benefits by Type:

(\$ in thousands)

	<u>Account Value</u>	<u>Net Amount at Risk after Reinsurance</u>	<u>Average Attained Age of Annuitant</u>
GMDB return of premium	\$ 976,638	\$ 10,566	61
GMDB step up	1,512,631	55,121	62
GMDB earnings enhancement benefit (EEB)	47,285	174	62
GMDB greater of annual step up and roll up	31,631	7,013	65
<b>Total GMDB at March 31, 2011</b>	<b><u>\$ 2,568,185</u></b>	<b><u>\$ 72,874</u></b>	
GMDB return of premium	\$ 981,787	\$ 17,685	61
GMDB step up	1,507,216	82,613	62
GMDB earnings enhancement benefit ("EEB")	47,123	291	61
GMDB greater of annual step up and roll up	32,083	7,680	65
<b>Total GMDB at December 31, 2010</b>	<b><u>\$ 2,568,209</u></b>	<b><u>\$ 108,269</u></b>	

*Return of Premium:* The death benefit is the greater of current account value or premiums paid (less any adjusted partial withdrawals).

*Step Up:* The death benefit is the greater of current account value, premiums paid (less any adjusted partial withdrawals) or the annual step up amount prior to the oldest original owner attaining a certain age. On and after the oldest original owner attains that age, the death benefit is the greater of current account value or the death benefit at the end of the contract year prior to the oldest original owner's attaining that age plus premium payments (less any adjusted partial withdrawals) made since that date.

*Earnings Enhancement Benefit:* The death benefit is the greater of the premiums paid (less any adjusted partial withdrawals) or the current account value plus the EEB. The EEB is an additional amount designed to reduce the impact of taxes associated with distributing contract gains upon death.

*Greater of Annual Step Up and Annual Roll up:* The death benefit is the greatest of premium payments (less any adjusted partial withdrawals), the annual step up amount, the annual roll up amount or the current account value prior to the eldest original owner attaining age 81. On and after the eldest original owner attained age 81, the death benefit is the greater of current account value or the death benefit at the end of the contract year prior to the eldest original owner's attained age of 81 plus premium payments (less any adjusted partial withdrawals) made since that date.

### Additional Insurance Benefits:

(\$ in thousands)

	<u>Account Value</u>	<u>Average Attained Age of Annuitant</u>
COMBO	\$ 10,950	59
GMAB	431,788	56
GMIB	513,578	62
GMWB	601,377	62
GPAF	14,317	76
<b>Total at March 31, 2011</b>	<b><u>\$ 1,572,010</u></b>	
COMBO	\$ 10,837	59
GMAB	427,315	56
GMIB	511,971	62
GMWB	587,053	61
GPAF	13,251	76
<b>Total at December 31, 2010</b>	<b><u>\$ 1,550,427</u></b>	

## 5. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

We also offer certain separate account variable products with a guaranteed minimum withdrawal benefit (“GMWB”), a guaranteed minimum accumulation benefit (“GMAB”), a guaranteed pay-out annuity floor (“GPAF”) and a combination rider (“COMBO”).

The GMWB rider guarantees the policyholder a minimum amount of withdrawals and benefit payments over time, regardless of the investment performance of the contract, subject to an annual limit. Optional resets are available. In addition, these contracts have a feature that allows the policyholder to receive the guaranteed annual withdrawal amount for as long as they are alive.

The GMAB rider provides the contract owner with a minimum accumulation of the contract owner’s purchase payments deposited within a specific time period, adjusted for withdrawals, after a specified amount of time determined at the time of issuance of the variable annuity contract.

The GPAF rider provides the policyholder with a minimum payment amount if the variable annuity payment falls below this amount on the payment calculation date.

The COMBO rider includes the GMAB and GMWB riders as well as the GMDB rider at the policyholder’s option.

Fixed indexed annuities also offer a variety of index options: policy credits that are calculated based on the performance of an outside equity market or other index over a specified term.

We have entered into a contract with Phoenix Life whereby we reinsure 100% of any claims related to GMWB liabilities on policies issued after April 30, 2008 and to GMAB liabilities on policies issued after December 31, 2008. Because this contract does not transfer sufficient risk to be accounted for as reinsurance, we use deposit accounting for the contract.

The GMWB, GMAB, GPAF, COMBO and index options represent embedded derivatives in the variable and fixed indexed annuity contracts that are required to be reported separately from the host variable annuity contract. They are carried at fair value and reported in policyholder deposit funds. The fair value of the GMWB, GMAB, GPAF, COMBO and index option obligation is calculated based on actuarial and capital market assumptions related to the projected cash flows, including benefits and related contract charges, over the lives of the contracts, incorporating expectations concerning policyholder behavior. As markets change, contracts mature and actual policyholder behavior emerges, we continually evaluate and may from time to time adjust these assumptions.

In order to manage the risk associated with these embedded derivative liabilities, we have established a risk management strategy under which we hedge our GMAB, GMWB and COMBO exposure using equity index options, equity index futures, equity index variance swaps, interest rate swaps and swaptions. We hedge our fixed index annuity options using equity index options. These investments are included in other investments on our balance sheet. Embedded derivative liabilities for GMWB, GMAB, GPAF, COMBO and index options are shown in the table below. There were no benefit payments made for the GMWB and GMAB during 2010 or during the three months ended March 31, 2011. There were benefit payments made for GPAF of \$351 thousand during 2010 and \$44 thousand during the three months ended March 31, 2011.

### Embedded Derivative Liabilities:

*(\$ in thousands)*

	<u>Mar 31,</u> <u>2011</u>	<u>Dec 31,</u> <u>2010</u>
GMWB	\$ (8,710)	\$ (1,664)
GMAB	8,057	13,098
GPAF	1,744	2,286
COMBO	(769)	(695)
Index options	937	(2,597)
<b>Total embedded derivatives</b>	<b><u>\$ 1,259</u></b>	<b><u>\$ 10,428</u></b>

## 5. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

### Universal life

Liabilities for universal life are generally determined by estimating the expected value of losses when death benefits exceed revenues and recognizing those benefits ratably over the accumulation period based on total expected assessments. The assumptions used in estimating these liabilities are consistent with those used for amortizing deferred policy acquisition costs. A single set of best estimate assumptions is used since these insurance benefits do not vary significantly with capital market conditions. At March 1, 2011 and December 31, 2010, we held additional universal life benefit reserves in accordance with death benefit and other insurance benefit reserves of \$104,530 thousand and \$95,742 thousand, respectively.

## 6. Derivative Instruments

### Derivative instruments

We use derivatives to manage certain risks in our general account portfolio as well as our insurance liabilities. Our derivatives generally do not qualify for hedge accounting treatment and are stated at fair value (market value) with changes in valuation reported in net realized capital gains/losses. Derivatives that are designated as hedges for accounting purposes are also stated at fair value. However, changes in the fair value of such derivatives are recorded in other comprehensive income, or net income, depending on the nature and effectiveness of the hedge. The Company seeks to enter into over-the-counter (“OTC”) derivative transactions pursuant to master agreements that provide for a netting of payments and receipts with a single counterparty. As of March 31, 2011, \$7,510 thousand of cash and cash equivalents was held as collateral by a third party related to our derivative transactions.

#### Derivative Instruments Held in General Account: (*\$ in thousands*)

	Notional Amount	Maturity	As of March 31, 2011		As of December 31 2010	
			Asset	Liability	Asset	Liability
<b>Non-Hedging Derivative Instruments</b>						
Interest rate swaps	\$ 101,000	2017-2026	\$ 7	\$ 894	\$ 3,593	\$ 1,469
Variance swaps	935	2015-2017	--	1,952	--	577
Swaptions	25,000	2024	818	--	2,097	--
Put options	224,000	2014-2021	37,282	--	45,019	--
Call options	204,156	2011-2016	21,776	10,143	11,231	5,980
Equity futures	112,887	2011	22,817	--	28,501	--
<b>Total non-hedging derivative instruments</b>	<b>\$ 667,978</b>		<b>\$ 82,700</b>	<b>\$ 12,989</b>	<b>\$ 90,441</b>	<b>\$ 8,026</b>

See Note 5 to these financial statements for more information on our embedded derivatives related to our variable annuity guarantees.

#### Interest Rate Swaps

We maintain an overall interest rate risk-management strategy that primarily incorporates the use of interest rate swaps as hedges of our exposure to changes in interest rates. Our exposure to changes in interest rates primarily results from our commitments to fund interest-sensitive insurance liabilities, as well as from our significant holdings of fixed rate financial instruments. We use interest rate swaps that effectively convert variable rate cash flows to fixed cash flows in order to hedge the interest rate risks associated with guaranteed minimum living benefit (GMAB/GMWB) rider liabilities.

#### Interest Rate Options

We use interest rate options, such as swaptions, to hedge against market risks to assets or liabilities from substantial changes in interest rates. An interest rate swaption gives us the right but not the obligation to enter into an underlying swap. Swaptions are options on interest rate swaps. All of our swaption contracts are receiver swaptions, which give us the right to enter into a swap where we will receive the agreed-upon fixed rate and pay the floating rate. If the market conditions are favorable and the swap is needed to continue hedging our inforce liability business, we will exercise the swaption and enter into a fixed rate swap. If a swaption contract is not exercised by its option maturity date, it expires with no value.

## 6. Derivative Instruments (continued)

### *Exchange Traded Future Contracts*

We use equity index futures to hedge the market risks from changes in the value of equity indices, such as S&P 500, associated with guaranteed minimum living benefit (GMAB/GMWB) rider liabilities. Positions are short-dated, exchange-traded futures with maturities of three months.

### *Equity Index Options*

The Company uses equity index options to hedge against market risks from changes in equity markets, volatility and interest rates.

An equity index option affords the Company the right to make or receive payments based on a specified future level of an equity market index. The Company may use exchange-trade or OTC options.

Generally, the Company has used long-dated options to hedge its GMAB and GMWB liabilities and a combination of put and call options to hedge its fixed indexed annuity option liabilities.

### **Contingent features**

Derivative counterparty agreements contain certain provisions that require our insurance companies' financial strength rating to be above a certain threshold. If our financial strength ratings were to fall below a specified rating threshold, certain derivative counterparties could request immediate payment or demand immediate and ongoing full collateralization on derivative instruments in net liability positions, or even trigger a termination of existing derivatives and/or future derivative transactions.

In certain derivative counterparty agreements, our financial strength ratings remain below the specified threshold levels as a result of a rating downgrade in early 2009. However, the Company held no derivative instruments as of March 31, 2011 in a net liability position payable to any counterparty (i.e., such derivative instruments have fair values in a net asset position payable to the Company if such holdings were liquidated).

## 7. Fair Value of Financial Instruments

ASC 820-10 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value and enhances disclosure requirements for fair value measurements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

ASC 820-10 establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels, from highest to lowest, are defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets. Level 1 securities include highly liquid government bonds and exchange-traded equities.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Examples of such instruments include government-backed mortgage products, certain collateralized mortgage and debt obligations and certain high-yield debt securities.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement. Securities classified within Level 3 include broker quoted investments, certain residual interests in securitizations and other less liquid securities. Most valuations that are based on brokers' prices are classified as Level 3 due to a lack of transparency in the process they use to develop prices.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

## 7. Fair Value of Financial Instruments (continued)

The following tables present the financial instruments carried at fair value by ASC 820-10 valuation hierarchy (as described above).

### Assets and Liabilities at Fair Value:

(\$ in thousands)

#### Assets

Available-for-sale debt securities

U.S. government and agency

State and political subdivision

Foreign government

Corporate

CMBS

RMBS

CDO/CLO

Other asset-backed

Derivative assets

Separate account assets<sup>(1)</sup>

Fair value option investments

**Total assets**

#### Liabilities

Embedded derivative liabilities

**Total liabilities**

	As of March 31, 2011			Total
	Level 1	Level 2	Level 3	
Available-for-sale debt securities				
U.S. government and agency	\$ 77,444	\$ 30,458	\$ --	\$ 107,902
State and political subdivision	--	32,677	--	32,677
Foreign government	--	16,746	--	16,746
Corporate	--	744,787	32,779	777,566
CMBS	--	192,861	22,081	214,942
RMBS	--	423,093	11,767	434,860
CDO/CLO	--	--	64,112	64,112
Other asset-backed	--	119,235	14,889	134,124
Derivative assets	--	82,700	--	82,700
Separate account assets <sup>(1)</sup>	2,828,966	73,487	--	2,902,453
Fair value option investments	--	4,537	7,482	12,019
<b>Total assets</b>	<b>\$ 2,906,410</b>	<b>\$ 1,720,581</b>	<b>\$ 153,110</b>	<b>\$ 4,780,101</b>
<b>Liabilities</b>				
Embedded derivative liabilities	\$ --	\$ 12,989	\$ 1,259	\$ 14,248
<b>Total liabilities</b>	<b>\$ --</b>	<b>\$ 12,989</b>	<b>\$ 1,259</b>	<b>\$ 14,248</b>

<sup>(1)</sup> Excludes \$38,973 thousand in limited partnerships and real estate investments accounted for on the equity method as well as \$6,115 thousand in cash and cash equivalents and money market funds.

There were no transfers of assets between Level 1 and Level 2 during the quarter ended March 31, 2011.

### Assets and Liabilities at Fair Value:

(\$ in thousands)

#### Assets

Available-for-sale debt securities

U.S. government and agency

State and political subdivision

Foreign government

Corporate

CMBS

RMBS

CDO/CLO

Other asset-backed

Derivative assets

Separate account assets<sup>(1)</sup>

Fair value option investments

**Total assets**

#### Liabilities

Embedded derivative liabilities

**Total liabilities**

	As of December 31, 2010			Total
	Level 1	Level 2	Level 3	
Available-for-sale debt securities				
U.S. government and agency	\$ 68,724	\$ 29,559	\$ --	\$ 98,283
State and political subdivision	--	32,509	--	32,509
Foreign government	--	16,086	--	16,086
Corporate	--	663,717	30,060	693,777
CMBS	--	163,647	10,308	173,955
RMBS	--	326,168	7,437	333,605
CDO/CLO	--	--	63,184	63,184
Other asset-backed	--	89,328	19,671	108,999
Derivative assets	--	90,441	--	90,441
Separate account assets <sup>(1)</sup>	2,800,500	77,195	--	2,877,695
Fair value option investments	--	4,442	7,289	11,731
<b>Total assets</b>	<b>\$ 2,869,224</b>	<b>\$ 1,493,092</b>	<b>\$ 137,949</b>	<b>\$ 4,500,265</b>
<b>Liabilities</b>				
Embedded derivative liabilities	\$ --	\$ 8,026	\$ 10,428	\$ 18,454
<b>Total liabilities</b>	<b>\$ --</b>	<b>\$ 8,026</b>	<b>\$ 10,428</b>	<b>\$ 18,454</b>

<sup>(1)</sup> Excludes \$37,949 thousand in limited partnerships and real estate investments accounted for on the equity method as well as \$7,302 thousand in cash and cash equivalents and money market funds.

There were no transfers of assets between Level 1 and Level 2 for the year ended December 31, 2010.

## 7. Fair Value of Financial Instruments (continued)

### Level 3 financial assets and liabilities

The following table sets forth a summary of changes in the fair value of our Level 3 financial assets and liabilities. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. For example, a hypothetical derivative contract with Level 1, Level 2 and significant Level 3 inputs would be classified as a Level 3 financial instrument in its entirety. Subsequently, even if only Level 1 and Level 2 inputs are adjusted, the resulting gain or loss is classified as Level 3. Further, Level 3 instruments are frequently hedged with instruments that are classified as Level 1 or Level 2 and, accordingly, gains or losses reported as Level 3 in the table below may be offset by gains or losses attributable to instruments classified in Level 1 or 2 of the fair value hierarchy.

Level 3 Financial Assets: (\$ in thousands)	Three Months Ended March 31, 2011						
	Asset-Backed	CDO/CLO	Corporate	CMBS	RMBS	Fair Value Options	Total Assets
Balance, beginning of period	\$ 19,671	\$ 63,184	\$ 30,060	\$ 10,308	\$ 7,437	\$ 7,289	\$ 137,949
Purchases	2,600	--	29	11,295	4,500	--	18,424
Sales	(994)	(2,027)	(9)	(122)	(197)	--	(3,349)
Transfers into Level 3 <sup>(1)</sup>	--	--	--	--	--	--	--
Transfers out of Level 3 <sup>(2)</sup>	(6,411)	--	--	--	--	--	(6,411)
Realized gains (losses) included in earnings	48	(71)	--	--	--	119	96
Unrealized gains (losses) included in other comprehensive income (loss)	(32)	2,960	2,683	600	(21)	61	6,251
Amortization/accretion	7	66	16	--	48	13	150
<b>Balance, end of period</b>	<b>\$ 14,889</b>	<b>\$ 64,112</b>	<b>\$ 32,779</b>	<b>\$ 22,081</b>	<b>\$ 11,767</b>	<b>\$ 7,482</b>	<b>\$ 153,110</b>

(1) Transfers into Level 3 for the three months ended March 31, 2011 primarily represent private securities for which Level 2 input assumptions for valuation pricing were no longer applicable.

(2) Transfers out of Level 3 for the three months ended March 31, 2011 primarily represent private securities for which reliable Level 2 input assumptions for valuation pricing became obtainable.

Level 3 Financial Assets: (\$ in thousands)	Three Months Ended March 31, 2010						
	Asset-Backed	CDO/CLO	Corporate	CMBS	RMBS	Total Assets	
Balance, beginning of period	\$ 18,854	\$ 64,999	\$ 41,257	\$ 11,784	\$ 15,637	\$ 152,531	
Purchases	5,999	50	41,465	1,327	1,035	49,876	
Sales	(297)	(270)	(51,932)	(1,503)	(1,416)	(55,418)	
Transfers into Level 3 <sup>(1)</sup>	--	--	3,405	--	--	3,405	
Transfers out of Level 3 <sup>(2)</sup>	(5,914)	--	(8,710)	--	(3,270)	(17,894)	
Realized gains (losses) included in earnings	5	(1,514)	25	--	--	(1,484)	
Unrealized gains (losses) included in other comprehensive income (loss)	256	3,576	4,069	684	(1,820)	6,765	
Amortization/accretion	3	5	(9)	2	114	115	
<b>Balance, end of period</b>	<b>\$ 18,906</b>	<b>\$ 66,846</b>	<b>\$ 29,570</b>	<b>\$ 12,294</b>	<b>\$ 10,280</b>	<b>\$ 137,896</b>	

(1) Net transfers into Level 3 for the three months ended March 31, 2010 primarily represent private securities for which Level 2 input assumptions for valuation pricing were no longer applicable.

(2) Net transfers out of Level 3 for the three months ended March 31, 2010 primarily represent private securities for which reliable Level 2 input assumptions for valuation pricing became obtainable.

## 7. Fair Value of Financial Instruments (continued)

### Level 3 Financial Liabilities:

(\$ in thousands)

	Three Months Ended	
	March 31,	
	2011	2010
	<b>Embedded Derivatives</b>	
Balance, beginning of period	\$ (10,428)	\$ (26,113)
Net purchases/(sales)	--	--
Transfers into Level 3	--	--
Transfers out of Level 3	--	--
Realized gains (losses)	9,169	10,838
Unrealized gains (losses) included in other comprehensive loss	--	--
Amortization/accretion	--	--
<b>Balance, end of period</b>	<b>\$ (1,259)</b>	<b>\$ (15,275)</b>
<b>Portion of gain (loss) included in net income (loss) relating to those liabilities still held</b>	<b>\$ 9,169</b>	<b>\$ 10,838</b>

### Carrying Amounts and Fair Values of Financial Instruments:

(\$ in thousands)

	As of March 31, 2011		As of December 31, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	\$ 37,419	\$ 37,419	\$ 51,059	\$ 51,059
Available-for-sale debt securities	1,782,929	1,782,929	1,520,398	1,520,398
Separate account assets	2,947,541	2,947,541	2,922,946	2,922,946
Policy loans	58,346	58,346	57,326	57,326
Derivative financial instruments	82,700	82,700	90,441	90,441
Fair value option investments	12,019	12,019	11,731	11,731
<b>Financial assets</b>	<b>\$ 4,920,954</b>	<b>\$ 4,920,954</b>	<b>\$ 4,653,901</b>	<b>\$ 4,653,901</b>
Investment contracts	\$ 977,257	\$ 985,250	\$ 793,142	\$ 804,107
Separate account liabilities	2,947,541	2,947,541	2,922,946	2,922,946
Derivative financial instruments	14,248	14,248	18,454	18,454
<b>Financial liabilities</b>	<b>\$ 3,939,046</b>	<b>\$ 3,947,039</b>	<b>\$ 3,734,542</b>	<b>\$ 3,745,507</b>

Fair value option investments include a structured loan asset valued at \$4,537 thousand and \$4,442 thousand as of March 31, 2011 and December 31, 2010, respectively. Election of the fair value option allows current earnings recognition and is more consistent with management's view of the securities' underlying economics. Changes in the fair value of this asset are included in net investment income.

In addition, pursuant to ASC 815, *Derivatives and Hedging*, adopted on July 1, 2010, this amount also includes beneficial interests in four securitized financial assets for which an irrevocable election was made to use the fair value option. These securities contain an embedded derivative feature. These securities were valued at \$7,482 thousand and \$7,289 thousand as of March 31, 2011 and December 31, 2010, respectively.

We have an established process for determining fair values. Fair value is based upon quoted market prices, where available. If listed prices or quotes are not available, or are based on disorderly transactions or inactive markets, fair value is based upon internally developed models that use primarily market-based or independently-sourced market parameters, including interest rate yield curves, option volatilities and currency rates. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments include amounts to reflect counterparty credit quality, our own creditworthiness, liquidity and unobservable parameters that are applied consistently over time. The majority of the valuations of Level 3 assets were internally calculated or obtained from independent third-party broker quotes.

## 7. Fair Value of Financial Instruments (continued)

We determine fair value as the price received in an orderly transaction. Thus, we evaluate broker pricing indications, if available, to determine whether the weight of evidence indicates that markets are inactive, or transactions are disorderly. In order to determine whether the volume and level of activity for an asset or liability has significantly decreased, we compare current activity with normal market activity for the asset or liability. We may observe a notable decrease in the number of recent transactions, and the significant decline or absence of a market for new issuances for the security or a similar security. If we do receive a broker pricing indication, we look for substantiation, such as a significant increase in implied liquidity risk premiums, yields, or performance indications when compared to the expected cash flow analysis. We look to see if the pricing indications have varied substantially in a short amount of time where no fundamental event or occurrence has prompted the large variation, or if there is a significant increase in the bid-ask spread. We review published indexes that may have been historically highly correlated with the fair values that no longer are representative of an active market. For corporate positions, we utilize TRACE, for which published trade activity is made available, to assess trading activity levels. For other positions, we rely on many factors such as the observable flows through Bloomberg, trading levels and activity as reported by market participants, and industry publications that speak to trading volume and current market conditions. Using professional judgment and experience, we evaluate and weigh the relevance and significance of all applicable factors to determine if there has been a significant decrease in the volume and level of activity for an asset, or group of similar assets.

Similarly, in order to identify transactions that are not orderly, we take into consideration the activity in the market as stated above, because that can influence the determination and occurrence of an orderly transaction. In addition, we assess the period of the exposure to the market before measurement date to determine adequacy for customary marketing activities. Also, we look to see if it was marketed to a single or limited number of participants. We assess the financial condition of the seller, if available, to determine whether observed transactions may have been forced. If the trading price is an outlier when compared to similar recent transactions, we consider whether this is an indicator of a disorderly trade. Using professional judgment and experience, we evaluate and weigh the relevance and significance of all applicable factors to determine if the evidence suggests that a transaction or group of similar transactions is not orderly.

Following is a description of our valuation methodologies for assets and liabilities measured at fair value. Such valuation methodologies were applied to all of the assets and liabilities carried at fair value.

### Structured securities

For structured securities, we consider the best estimate of cash flows until maturity to determine our ability to collect principal and interest and compare this to the anticipated cash flows when the security was purchased. In addition, management judgment is used to assess the probability of collecting all amounts contractually due to us. After consideration is given to the available information relevant to assessing the collectibility, including historical events, current conditions and reasonable forecasts, an estimate of future cash flows is determined. This includes evaluating the remaining payment terms, prepayment speeds, the underlying collateral, expected defaults using current default data and the financial condition of the issuer. Other factors considered are composite credit ratings, industry forecast, analyst reports and other relevant market data are also considered, similar to those the Company believes market participants would use. For securities for which observable market data is available and substantiated, valuations reflect the quoted fair value.

To determine fair values for certain structured, CLO and CDO assets for which current pricing indications either do not exist, or are based on inactive markets or sparse transactions, we utilize model pricing using a third-party forecasting application that leverages historical trustee information for each modeled security. Principal and interest cash flows are modeled under various default scenarios for a given tranche of a security in accordance with its contractual cash flow priority of claim and subordination with respect to credit losses. The key assumptions include the level of annual default rates, loss-given-default (LGD) or recovery rate, collateral prepayment rate and reinvestment spread.

Fair value is then determined based on discounted projected cash flows. We use a discount rate based upon a combination of the current U.S. Treasury rate plus the most recent gross CDO/CLO spreads (including the corresponding swap spread) by original tranche rating, which is representative of the inherent credit risk exposure in a deal's capital structure. A credit loss margin is then deducted from this blended rate equal to the baseline annual default rate times a loss severity rate. The rationale behind the deduction of such credit loss margins is necessary as the projected cash flows have already been default risk-adjusted, taking into account the impact of the projected credit losses in the underlying collateral.

## **7. Fair Value of Financial Instruments (continued)**

### **Derivatives**

Exchange-traded derivatives valued using quoted prices are classified within Level 1 of the valuation hierarchy. However, few classes of derivative contracts are listed on an exchange. Therefore, the majority of our derivative positions are valued using internally developed models that use as their basis readily observable market parameters. These positions are classified within Level 2 of the valuation hierarchy. Such derivatives include basic interest rate swaps, options and credit default swaps.

Fair values for OTC derivative financial instruments, principally forwards, options and swaps, represent the present value of amounts estimated to be received from or paid to a marketplace participant in settlement of these instruments (i.e., the amount we would expect to receive in a derivative asset assignment or would expect to pay to have a derivative liability assumed). These derivatives are valued using pricing models based on the net present value of estimated future cash flows and directly observed prices from exchange-traded derivatives or other OTC trades, while taking into account the counterparty's credit ratings, or our own credit ratings, as appropriate. Determining the fair value for OTC derivative contracts can require a significant level of estimation and management judgment.

New and/or complex instruments may have immature or limited markets. As a result, the pricing models used for valuation often incorporate significant estimates and assumptions that market participants would use in pricing the instrument, which may impact the results of operations reported in the financial statements. For long-dated and illiquid contracts, extrapolation methods are applied to observed market data in order to estimate inputs and assumptions that are not directly observable. This enables us to mark to market all positions consistently when only a subset of prices is directly observable. Values for OTC derivatives are verified using observed information about the costs of hedging the risk and other trades in the market. As the markets for these products develop, we continually refine our pricing models to correlate more closely to the market risk of these instruments.

### **Retained interest in securitization**

Retained interests in securitizations do not trade in an active, open market with readily observable prices. Accordingly, we estimate the fair value of certain retained interests in securitizations using discounted cash flow ("DCF") models.

For certain other retained interests in securitizations (such as interest-only strips), a single interest rate path DCF model is used and generally includes assumptions based upon projected finance charges related to the securitized assets, estimated net credit losses, prepayment assumptions and contractual interest paid to third-party investors. Changes in the assumptions used may have a significant impact on our valuation of retained interests and such interests are, therefore, typically classified within Level 3 of the valuation hierarchy.

We compare the fair value estimates and assumptions to observable market data where available and to recent market activity and actual portfolio experience.

### **Separate accounts**

Separate account assets are primarily invested in mutual funds but also have investments in fixed maturity and equity securities. The separate account investments are valued in the same manner, and using the same pricing sources and inputs, as the fixed maturity, equity security and short-term investments of the Company. Mutual funds are included in Level 1. Most debt securities and short-term investments are included in Level 2.

### **Fair value of investment contracts**

For purposes of fair value disclosures, we determine the fair value of guaranteed interest contracts by assuming a discount rate equal to the appropriate U.S. Treasury rate plus 100 basis points to determine the present value of projected contractual liability payments through final maturity. We determine the fair value of deferred annuities and supplementary contracts without life contingencies with an interest guarantee of one year or less at the amount of the policy reserve. In determining the fair value of deferred annuities and supplementary contracts without life contingencies with interest guarantees greater than one year, we use a discount rate equal to the appropriate U.S. Treasury rate plus 100 basis points to determine the present value of the projected account value of the policy at the end of the current guarantee period.

## 7. Fair Value of Financial Instruments (continued)

Deposit type funds, including pension deposit administration contracts, dividend accumulations, and other funds left on deposit not involving life contingencies, have interest guarantees of less than one year for which interest credited is closely tied to rates earned on owned assets. For these liabilities, we assume fair value to be equal to the stated liability balances.

### Valuation of embedded derivatives

We make guarantees on certain variable and fixed indexed annuity contracts, including GMAB and GMWB as well as provide credits based on the performance of certain indices (“index credits”) on our fixed annuity contracts that meet the definition of an embedded derivative. The GMAB and GMWB embedded derivatives are accounted for at fair value using a risk neutral stochastic valuation methodology with changes in fair value recorded in realized investment gains. The inputs to our fair value methodology include information derived from the asset derivatives market, including the volatility surface and the swap curve. Several additional inputs are not obtained from independent sources, but instead reflect our internally developed assumptions related to mortality rates, lapse rates and policyholder behavior. The fair value of the embedded derivatives associated with our fixed indexed annuity is calculated using the budget method where the initial value is established based on the fair value of the options used to hedge the liabilities. The budget amount for future years is based on the impact of projected interest rates on the discounted liabilities. Several additional inputs reflect our internally developed assumptions related to lapse rates and policyholder behavior. As there are significant unobservable inputs included in our fair value methodology for these embedded derivative liabilities, we consider the above-described methodology as a whole to be Level 3 within the fair value hierarchy.

Our fair value calculation includes a credit standing adjustment (the “CSA”). The CSA represents the adjustment that market participants would make to reflect the risk that guaranteed benefit obligations may not be fulfilled (“non-performance risk”). In analyzing various alternatives to the CSA calculation, we determined that we could not use credit default swap spreads as there are no such observable instruments on PNX’s life insurance subsidiaries, including us, nor could we consistently obtain an observable price on the surplus notes issued by Phoenix Life, as the surplus notes are not actively traded. Therefore, when discounting the rider cash flows for calculation of the fair value of the liability, we calculated the CSA that reflects the credit spread (based on a Standard & Poor’s BB- credit rating) for financial services companies similar to the Company’s life insurance subsidiaries. This average credit spread is recalculated every quarter therefore the fair value will change with the passage of time even in the absence of any other changes that would affect the valuation. The impact of the CSA, net of the reinsurance impact from a contract with Phoenix Life, at March 31, 2011 and December 31, 2010 was a reduction of \$11,508 thousand and \$19,231 thousand in the reserves associated with these riders, respectively.

## 8. Income Taxes

It is our policy to estimate taxes for interim periods based on estimated annual effective tax rates which are derived, in part, from expected annual pre-tax income. However, the federal income tax expense for the three months ended March 31, 2011 has been computed based on the first three months of 2011 as a discrete period due to the uncertainty regarding our ability to reliably estimate pre-tax income for the remainder of the year. Due to this uncertainty, we are unable to develop a reasonable estimate of the annual effective tax rate for the full year 2011.

As of March 31, 2011, we performed our assessment of net deferred tax assets. Significant management judgment is required in determining the provision for income taxes and, in particular, any valuation allowance recorded against our deferred tax assets. For the quarter ended March 31, 2011, we recognized a decrease in the valuation allowance of \$1,000 thousand. Accounting guidance requires that this change be allocated to the various financial statement components of income or loss. The decrease to the valuation allowance corresponds to a decrease of \$500 thousand in income statement related deferred tax balances and a decrease of \$500 thousand in other comprehensive income related deferred tax balances.

An income tax benefit of \$2,900 thousand recognized in the income statement reflected the exception to intraperiod allocation rules in accordance with ASC 740-20, *Accounting for Income Taxes – Intra-period Tax Allocation*. Additionally, an income tax benefit of \$500 thousand recognized through the income statement related to the reduction in the valuation allowance. Offsetting the benefit recognized through the income statement is an income tax expense of \$3,687 thousand primarily driven by current year pre-tax income.

## **8. Income Taxes (continued)**

We concluded that a valuation allowance on \$149,800 thousand of gross deferred tax assets at March 31, 2011 was not required. Our methodology for determining the realizability of deferred tax assets considers estimates of future taxable income from our operations and consideration of available tax planning strategies and actions that could be implemented, if necessary. We also considered future reversals of existing taxable temporary differences. In concluding that a valuation allowance was not required on the remaining deferred tax assets, we considered the more likely than not criteria pursuant to ASC 740, *Accounting for Income Taxes*.

We are included in the consolidated federal income tax return filed by PNX and are party to a tax sharing agreement by and among PNX and its subsidiaries. In accordance with this agreement, federal income taxes are allocated as if they had been calculated on a separate company basis, except that benefits for any net operating losses or other tax credits used to offset a tax liability of the consolidated group will be provided to the extent such loss or credit is utilized in the consolidated federal tax return.

Within the consolidated tax return, we are required by regulations of the Internal Revenue Service (“IRS”) to segregate the entities into two groups: life insurance companies and non-life insurance companies. We are limited as to the amount of any operating losses from the non-life group that can be offset against taxable income of the life group. These limitations may affect the amount of any operating loss carryovers that we have now or in the future.

The Company is no longer subject to U.S. federal income tax examinations by tax authorities for years before 2008.

In accordance with the tax sharing agreement, we had an intercompany current tax payable of \$6,570 thousand and \$5,800 thousand as of March 31, 2011 and December 31, 2010, respectively.

To the extent required under the relevant tax law, we recognize interest and penalties related to amounts accrued on uncertain tax positions and amounts paid or refunded from federal and state income tax authorities in tax expense. The interest and penalties recorded during the three month period ending March 31, 2011 were not material.

## **9. Contingent Liabilities**

### *Litigation and Arbitration*

We are regularly involved in litigation and arbitration, both as a defendant and as a plaintiff. The litigation and arbitration naming us as a defendant ordinarily involves our activities as an insurer, investor or investment advisor.

It is not feasible to predict or determine the ultimate outcome of all legal or arbitration proceedings or to provide reasonable ranges of potential losses. Based on current information, we believe that the outcomes of our litigation and arbitration matters are not likely, either individually or in the aggregate, to have a material adverse effect on our financial condition. However, given the large or indeterminate amounts sought in certain of these matters and the inherent unpredictability of litigation and arbitration, it is possible that an adverse outcome in certain matters could, from time to time, have a material adverse effect on our results of operations or cash flows in particular quarterly or annual periods.

### *Regulatory Matters*

State regulatory bodies, the SEC, the Financial Industry Regulatory Authority, the IRS and other regulatory bodies regularly make inquiries of us and, from time to time, conduct examinations or investigations concerning our compliance with laws and regulations related to, among other things, our insurance and broker-dealer subsidiaries, securities offerings and registered products. We endeavor to respond to such inquiries in an appropriate way and to take corrective action if warranted.

## **9. Contingent Liabilities (continued)**

Regulatory actions may be difficult to assess or quantify. The nature and magnitude of their outcomes may remain unknown for substantial periods of time. It is not feasible to predict or determine the ultimate outcome of all pending inquiries, investigations, legal proceedings and other regulatory actions, or to provide reasonable ranges of potential losses. Based on current information, we believe that the outcomes of our regulatory matters are not likely, either individually or in the aggregate, to have a material adverse effect on our financial condition. However, given the inherent unpredictability of regulatory matters, it is possible that an adverse outcome in certain matters could, from time to time, have a material adverse effect on our results of operation or cash flows in particular quarterly or annual periods.

## **Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **FORWARD-LOOKING STATEMENTS**

*The discussion in this Annual Report on Form 10-Q may contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. We intend for these forward-looking statements to be covered by the safe harbor provisions of the federal securities laws relating to forward-looking statements. These forward-looking statements include statements relating to trends in, or representing management's beliefs about our future transactions, strategies, operations and financial results, and often contain words such as "will," "anticipate," "believe," "plan," "estimate," "expect," "intend," "may," "should" and other similar words or expressions. Forward-looking statements are made based upon management's current expectations and beliefs concerning trends and future developments and their potential effects on us. They are not guarantees of future performance. Our actual business, financial condition or results of operations may differ materially from those suggested by forward-looking statements as a result of risks and uncertainties which include, among others: (i) unfavorable general economic developments including, but not limited to, specific related factors such as the performance of the debt and equity markets and changes in interest rates; (ii) the potential adverse affect of interest rate fluctuations on our business and results of operations; (iii) the effect of adverse capital and credit market conditions on our ability to meet our liquidity needs, our access to capital and our cost of capital; (iv) the effect of guaranteed benefits within our products; (v) potential exposure to unidentified or unanticipated risk that could adversely affect our businesses or result in losses; (vi) the consequences related to variations in the amount of our statutory capital due to factors beyond our control; (vii) the possibility that we not be successful in our efforts to implement a new business plan; (viii) the impact on our results of operations and financial condition of any required increase in our reserves for future policyholder benefits and claims if such reserves prove to be inadequate; (ix) changes in our investment valuations based on changes in our valuation methodologies, estimations and assumptions; (x) further downgrades in our debt or financial strength ratings; (xi) the possibility that mortality rates, persistency rates, funding levels or other factors may differ significantly from our assumptions used in pricing products; (xii) the availability, pricing and terms of reinsurance coverage generally and the inability or unwillingness of our reinsurers to meet their obligations to us specifically; (xiii) our ability to attract and retain key personnel in a competitive environment; (xiv) our dependence on third parties to maintain critical business and administrative functions; (xv) the strong competition we face in our business from banks, insurance companies and other financial services firms; (xvi) tax developments that may affect us directly, or indirectly through the cost of, the demand for or profitability of our products or services; (xvii) the possibility that the actions and initiatives of the U.S. government, including those that we elect to participate in, may not improve adverse economic and market conditions generally or our business, financial condition and results of operations specifically; (xviii) legislative or regulatory developments; (xix) regulatory or legal actions; (xx) changes in accounting standards; (xxi) the potential impact of a material weakness in our internal control over financial reporting on the accuracy of our reported financial results, investor confidence; and (xxii) other risks and uncertainties described herein or in any of our filings with the SEC. Certain other factors which may impact our business, financial condition or results of operations or which may cause actual results to differ from such forward-looking statements are discussed or included in our periodic reports filed with the SEC and are available on our website at [www.phoenixwm.com](http://www.phoenixwm.com) under "Investor Relations." You are urged to carefully consider all such factors. We do not undertake or plan to update or revise forward-looking statements to reflect actual results, changes in plans, assumptions, estimates or projections, or other circumstances occurring after the date in this Form 10-Q, even if such results, changes or circumstances make it clear that any forward-looking information will not be realized. If we make any future public statements or disclosures which modify or impact any of the forward-looking statements contained in or accompanying this Form 10-Q, such statements or disclosures will be deemed to modify or supersede such statements in this Form 10-Q.*

### **MANAGEMENT'S NARRATIVE ANALYSIS OF THE RESULTS OF OPERATIONS**

This section reviews our financial condition as of March 31, 2011 as compared to December 31, 2010; our results of operations for the three months ended March 31, 2011 and 2010; and, where appropriate, factors that may affect our future financial performance. This discussion should be read in conjunction with the unaudited interim financial statements and notes contained in this filing as well as in conjunction with our financial statements for the year ended December 31, 2010 in our 2010 Annual Report on Form 10-K.

## Executive Overview

### *Business*

We provide life insurance and annuity products through third-party distributors, supported by wholesalers and financial planning specialists employed by us. Our policyholder base includes both affluent and middle market consumers, with our more recent business concentrated in the middle market. Most of our life insurance in force is permanent life insurance (universal and variable universal life) insuring one or more lives. Our annuity products include deferred, fixed and variable annuities with a variety of death benefit and guaranteed living benefit options.

In 2010, our ultimate parent company, The Phoenix Companies, Inc. (“PNX”), pursued a business plan that focused on products and services that are less capital intensive and less ratings sensitive, continuing a direction set in 2009. This plan leverages existing strengths and includes a distribution subsidiary of PNX, Saybrus Partners, Inc., as well as developing core life and annuity products for the middle market and expanding distribution within that market, and building sales through distribution partners for our alternative retirement solutions products.

Underlying this plan is a business strategy based on four pillars:

- Balance sheet strength;
- Policyholder service;
- Operational efficiency; and
- Profitable growth.

### *Earnings Drivers*

Our profitability is driven by interaction of the following elements:

- *Mortality margins in our universal and variable universal life product lines.* We earn cost of insurance fees based on the difference between face amounts and the account values (referred to as the net amount at risk or NAR). We pay policyholder benefits and set up reserves for future benefit payments on these products. We define mortality margins as the difference between these fees and benefit costs. Mortality margins are affected by:
  - Number and face amount of policies sold;
  - Actual death claims net of reinsurance relative to our assumptions, a reflection of our underwriting and actuarial pricing discipline, the cost of reinsurance and the natural volatility inherent in this kind of risk; and
  - The policy funding levels or actual account values relative to our assumptions, a reflection of policyholder behavior and investment returns.
- *Fees on life and annuity products.* Fees consist primarily of asset-based (including mortality and expense charges) and premium-based fees which we charge on our variable life and variable annuity products and depend on the premiums collected and account values of those products. Asset-based fees are calculated as a percentage of assets under management within our separate accounts. Fees also include surrender charges. Non-asset-based fees include charges to cover premium taxes and renewal commissions.
- *Interest margins.* Net investment income earned on universal life and other policyholder funds managed as part of our general account, less the interest credited to policyholders on those funds. Interest margins also include investment income on assets supporting the Company’s surplus.
- *Non-deferred operating expenses,* including expenses related to servicing the products and policyholders offered by the Company, consisting of various maintenance and overhead-type expenses, including pension and other benefit costs.
- *Deferred policy acquisition cost amortization,* which is based on the amount of expenses deferred, actual results in each quarter and management’s assumptions about the future performance of the business. The amount of future profit or margin is dependent principally on investment returns in our separate accounts, investment income in excess of the amounts credited to policyholders, surrender and lapse rates, death claims and other benefit payments, premium persistency, funding patterns and expenses. These factors enter into management’s estimates of gross profits or margins, which generally are used to amortize deferred policy acquisition costs. Actual equity market movements, net investment income in excess of amounts credited to policyholders, claims payments and other key factors can vary significantly from our assumptions, resulting in a misestimate of gross profits or margins, and a change in amortization, with a resulting impact to income. In addition, we regularly review and reset our assumptions in light of actual experience, which can result in material changes in amortization.
- *Net realized investment gains or losses* on our general account investments and hedging programs.

- *Income tax expense* which is a function of pre-tax income and significant judgments we make with respect to the reversal of certain temporary book-to-tax differences, and specifically our estimates of taxable income over the periods in which the deferred tax assets are expected to reverse, including consideration of the expiration dates and amounts of carryforwards related to net operating losses, capital losses, foreign tax credits and general business tax credits.

Certain of our Life and Annuity products include guaranteed benefits. These include guaranteed minimum death benefits (“GMDBs”), guaranteed minimum accumulation benefits (“GMABs”), guaranteed minimum withdrawal benefits (“GMWBs”) and guaranteed minimum income benefits (“GMIBs”). Periods of significant and sustained downturns in equity markets, increased equity volatility or reduced interest rates would result in an increase in the valuation of the future policy benefit or policyholder account balance liabilities associated with such products, resulting in a reduction to earnings.

Under accounting principles generally accepted in the United States of America (“GAAP”), premiums and deposits for variable life, universal life and annuity products are not recorded as revenues. For certain investment options of variable products, deposits are reflected on our balance sheet as an increase in separate account liabilities. Premiums and deposits for universal life, fixed annuities and certain investment options of variable annuities are reflected on our balance sheet as an increase in policyholder deposit funds. Premiums and deposits for other products are reflected on our balance sheet as an increase in policy liabilities and accruals.

#### *Recent Trends on Earnings Drivers*

- *Mortality margins.* Fluctuations in mortality are inherent in our lines of business. Universal life mortality margins decreased by \$7,475 thousand to \$40,071 thousand in the quarter ended March 31, 2011, compared to \$47,546 thousand in the quarter ended March 31, 2010. This was a result of lower fee income related to cost of insurance charges as well as higher death benefits. Mortality margins for variable universal life were steady at \$1,921 thousand in the quarter ended March 31, 2011, compared to \$1,923 thousand in the quarter ended March 31, 2010, with a slight decrease in both death benefits and cost of insurance charges.
- *Interest margins.* Interest margins on universal life and annuities were \$5,991 thousand in the quarter ended March 31, 2011, compared to \$1,142 thousand in the quarter ended March 31, 2010. The increase in interest margins of \$4,849 thousand was primarily a result of lower interest credited on universal life consistent with declining funds under management, as well as an increase in net investment income on assets supporting our annuity products.
- *Operating expenses.* Non-deferred operating expenses decreased by \$4,952 thousand to \$18,381 thousand in the quarter ended March 31, 2011, compared to \$23,333 thousand in the quarter ended March 31, 2010. Lower operating expenses were a result of lower premium taxes and lower compensation and employee-related expenses.
- *Deferred policy acquisition cost.* Excluding the impact of realized investment gains, policy acquisition cost amortization decreased \$780 thousand to \$38,894 thousand from \$39,674 thousand in the quarters ended March 31, 2011 and 2010, respectively. Amortization decreased related to universal life as a result of lower mortality margins. Partially offsetting these declines was higher amortization related to annuities as deferred expenses related to new sales have begun to amortize.
- *Net realized investment gains or losses on our general account investments.* Net realized investment losses of \$4,462 thousand were recognized during the quarter ended March 31, 2011 compared to net realized investment gains of \$994 thousand during the quarter ended March 31, 2010. This decrease in realized income was a result of realized losses on derivative assets and liabilities which increased \$9,958 thousand to a loss of \$4,274 thousand in the quarter ended March 31, 2011 compared to a gain of \$5,684 thousand during the quarter ended March 31, 2010. This was primarily attributable to our net embedded derivatives associated with variable and fixed indexed annuity guarantees which had increased losses of \$7,311 thousand for the quarter ended March 31, 2011 compared to March 31, 2010. Of this increase, \$3,059 thousand was associated with the non-performance risk factor. There were also losses of \$2,647 thousand were recognized on our surplus hedge that was entered into during 2010. Partially offsetting these additional losses was an improvement of \$3,074 thousand in impairment losses as well as an improvement of \$1,428 thousand from net transaction losses during the quarter ended March 31, 2010 compared to transaction gains during the quarter ended March 31, 2011.
- *Income taxes.* The Company recorded an income tax expense of \$287 thousand in the first quarter of 2011 compared to \$3,958 thousand in the first quarter of 2010. The decrease in tax expense in 2011 as compared to 2010 was primarily driven by a reduction in the valuation allowance combined with a benefit related to the exception to intraperiod allocation rules in accordance with ASC 740-20, *Accounting for Income Taxes – Intraperiod Tax Allocation*.

## *Economic Market Conditions and Industry Trends*

Although the U.S. economy is recovering, the potential for another economic downturn remains.

The availability of credit, consumer spending, business investment, capital market conditions and inflation affect our business. In an economic downturn, higher unemployment, lower family income, lower corporate earnings, lower business investment and lower consumer spending may depress the demand for life insurance, annuities and investment products. In addition, this type of economic environment may result in higher lapses or surrenders of life and annuity policies we provide. Accordingly, the risks we face related to general economic and business conditions are pronounced.

More specifically, our business is exposed to the performance of the debt and equity markets. These adverse conditions include, but are not limited to, a lack of buyers for certain assets, volatility, credit spread changes and benchmark interest rate changes. Each of these factors may impact the liquidity and value of our investments. The lower interest rate environment may also impact our net investment income.

Further, recent trends in the life insurance industry may affect our mortality, persistency and funding levels. The evolution of the financial needs of policyholders, the emergence of a secondary market for life insurance, and increased availability and subsequent contraction of premium financing suggest that the reasons for purchasing our products changed. At the same time, prior to 2009, we experienced an increase in life insurance sales to older individuals. While we instituted certain controls and procedures to screen applicants, we believe that our sales of universal life products include sales of policies to third party investors who, at the time of policy origination, had no insurable interest in the insured. The effect that these changes may have on our actual experience and profitability will emerge over time.

Most of our current products permit us to increase charges and adjust crediting rates during the life of the policy or contract (subject to guarantees in the policies and contracts). For example, effective April 1, 2010 we implemented an increase in the cost of insurance rates for certain universal life policies. However, this adjustment, any other permitted adjustments or any additional steps taken to manage our in force business may not be sufficient to maintain profitability. In addition, increasing charges on in force policies or contracts may adversely affect our relationships with distributors, future sales and surrenders and may result in claims against us by policyholders. Furthermore, some of our in force business consists of products that do not permit us to adjust the charges and credited rates of in force policies or contracts.

## *Outlook*

Since 2009, we have taken significant actions to reduce expenses, effectively manage our in-force business, reduce balance sheet risk, increase liquidity and pursue new growth opportunities. These actions are beginning to have their intended effect and, we believe, position us for continued improvement in results in 2011 and beyond. However, significant capital market dislocations or another economic downturn could have a material adverse effect on our business, financial condition and results of operations. In such an environment, we could face lower fees and net investment income as well as higher deferred policy acquisition cost amortization from life and annuity products, adverse mortality as a result of anti-selective policy lapses and surrenders, and additional net realized investment losses on our general account investments, including further other-than-temporary impairments (“OTTIs”). Additionally, we could experience higher costs for guaranteed benefits and the potential for further deferred policy acquisition cost unlocking. Furthermore, a lack of availability of premium financing, an illiquid secondary market for life insurance policies and a cost of insurance rate increase for certain of our universal life policies has had and could have further adverse effects on lapses in our PAUL series of universal life policies.

We expect to continue to focus on the following key strategic pillars in 2011:

- Balance sheet strength;
- Policyholder service;
- Operational efficiency; and
- Profitable growth.

## **Impact of New Accounting Standards**

For a discussion of accounting standards, see Note 2 to our financial statements in this Form 10-Q.

## Critical Accounting Estimates

The discussion and analysis of our financial condition and results of operations is based upon our financial statements, which have been prepared in accordance with GAAP. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Critical accounting estimates are reflective of significant judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

A complete description of our critical accounting estimates is set forth in our 2010 Annual Report on Form 10-K. Management believes that those critical accounting estimates as set forth in the 2010 Annual Report on Form 10-K are important to understanding our results of operations and financial condition. Certain of our critical accounting estimates are as follows:

### *Deferred Income Taxes*

We account for income taxes in accordance with ASC 740, *Accounting for Income Taxes*. Deferred tax assets and/or liabilities are determined by multiplying the differences between the financial reporting and tax reporting basis for assets and liabilities by the enacted tax rates expected to be in effect when such differences are recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances on deferred tax assets are estimated based on our assessment of the realizability of such amounts.

As of March 31, 2011, we performed our assessment of net deferred tax assets. Significant management judgment is required in determining the provision for income taxes and, in particular, any valuation allowance recorded against our deferred tax assets. For the quarter ended March 31, 2011, we recognized a decrease in the valuation allowance of \$1,000 thousand. Accounting guidance requires that this change be allocated to the various financial statement components of income or loss. The decrease to the valuation allowance corresponds to a decrease of \$500 thousand in income statement related deferred tax balances and a decrease of \$500 thousand in other comprehensive income related deferred tax balances.

An income tax benefit of \$2,900 thousand recognized in the income statement reflected the exception to intraperiod allocation rules in accordance with ASC 740-20, *Accounting for Income Taxes – Intra-period Tax Allocation*. Additionally, an income tax benefit of \$500 thousand recognized through the income statement related to the reduction in the valuation allowance. Offsetting the benefit recognized through the income statement is an income tax expense of \$3,687 thousand primarily driven by current year pre-tax income.

We concluded that a valuation allowance on the remaining \$149,800 thousand of deferred tax assets at March 31, 2011, was not required. Our methodology for determining the realizability of deferred tax assets involves estimates of future taxable income and consideration of available tax planning strategies and actions that could be implemented, if necessary. These estimates are projected through the life of the related deferred tax assets based on assumptions that we believe to be reasonable and consistent with current operating results. Changes in future operating results not currently forecasted may have a significant impact on the realization of deferred tax assets.

### *Other-Than-Temporary Impairments*

We recognize realized investment losses when declines in fair value of debt securities are considered to be other-than-temporary. For debt securities, the other-than-temporarily impaired amount is separated into the amount related to a credit loss and is reported as net realized investment losses included in earnings, and any amounts related to other factors are recognized in other comprehensive income. The credit loss component is calculated using our best estimate of the present value of cash flows expected to be collected from the debt security, by discounting the expected cash flows at the effective interest rate implicit in the security at the time of acquisition. Subsequent to recognition of an impairment loss, the difference between the new cost basis and the cash flows expected to be collected is accreted as interest income.

In evaluating whether a decline in value is other than temporary, we consider several factors including, but not limited to the following:

- the extent and the duration of the decline;
- the reasons for the decline in value (credit event, interest related or market fluctuations);
- our intent to sell the security, or whether it is more likely than not that we will be required to sell it before recovery, and
- the financial condition and near term prospects of the issuer.

A debt security impairment is deemed other than temporary if:

- we either intend to sell the security, or it is more likely than not that we will be required to sell the security before recovery; or
- it is probable we will be unable to collect cash flows sufficient to recover the amortized cost basis of the security.

Impairments due to deterioration in credit that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security are considered other than temporary. Other declines in fair value (for example, due to interest rate changes, sector credit rating changes or company-specific rating changes) that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security may also result in a conclusion that an OTTI has occurred. In situations where the Company has asserted its ability and intent to hold a security to a forecasted recovery, but where now it is more likely than not that we will be required to sell the security before recovery, an impairment is considered other than temporary, even if the present value of cash flows expected to be collected will be sufficient to recover the amortized cost basis of the security.

We employ a comprehensive process to determine whether or not a security is in an unrealized loss position and is other-than-temporarily impaired. This assessment is done on a security-by-security basis and involves significant management judgment, especially given recent severe market dislocations.

On a quarterly basis, we review all securities for potential recognition of an OTTI. We maintain a watch list of securities in default, near default or otherwise considered by our investment professionals as being distressed, potentially distressed or requiring a heightened level of scrutiny. We also identify all securities whose carrying value has been below amortized cost on a continuous basis for zero to six months, six months to 12 months and greater than 12 months. Using this analysis, coupled with our watch list, we review all securities whose fair value is less than 80% of amortized cost (significant unrealized loss) with emphasis on below investment grade securities with a continuous significant unrealized loss in excess of six months. In addition, we review securities that experienced lesser declines in value on a more selective basis to determine whether any are other-than-temporarily impaired.

Specifically for structured securities, to determine whether a collateralized security is impaired, we obtain underlying data from the security's trustee and analyze it for performance trends. A security-specific stress analysis is performed using the most recent trustee information. This analysis forms the basis for our determination of whether the security will pay in accordance with the contractual cash flows.

#### *Deferred Policy Acquisition Costs*

We amortize deferred policy acquisition costs based on the related policy's classification. For universal life, variable universal life and accumulation annuities, deferred policy acquisition costs are amortized in proportion to estimated gross profits ("EGPs"). Policies may be surrendered for value or exchanged for a different one of our products (internal replacement). The deferred policy acquisition costs balance associated with the replaced or surrendered policies is amortized to reflect these surrenders. In addition, an offset to deferred policy acquisition costs and accumulated other comprehensive income is recorded each period to the extent that, had unrealized holding gains or losses from securities classified as available-for-sale actually been realized, an adjustment to deferred policy acquisition costs amortized using gross profits or gross margins would result.

The projection of EGPs requires the use of various assumptions, estimates and judgments about the future. Future EGPs are projected for the estimated lives of the contracts. The assumptions developed as part of our annual process are based on our current best estimates of future events. Assumptions considered to be significant in the development of EGPs include separate account fund performance, surrender and lapse rates, interest margin, mortality, premium persistency, funding patterns, expenses and reinsurance costs and recoveries. These assumptions are reviewed on a regular basis and are based on our past experience, industry studies, regulatory requirements and estimates about the future.

The separate account fund performance assumption is critical to the development of the EGPs related to our variable annuity and variable life insurance businesses. As equity markets do not move in a systematic manner, we use a mean reversion method (reversion to the mean assumption), a common industry practice, to determine the future equity market growth rate assumption used for the amortization of deferred policy acquisition costs. This practice assumes that the expectation for long-term appreciation is not changed by short-term market fluctuations. The average long-term rate of assumed separate account fund performance used in estimating gross profits was 6.0% (after fund fees and mortality and expense charges) for the variable annuity business and 6.9% (after fund fees and mortality and expense charges) for the variable life business at both March 31, 2011 and December 31, 2010.

To determine the reasonableness of the prior assumptions used and their impact on previously projected account values and the related EGPs, we evaluate, on a quarterly basis, our previously projected EGPs. Our process to assess the reasonableness of our EGPs involves the use of internally developed models, together with actual experience. Actual gross profits that vary from management's initial estimates in a given reporting period, result in increases or decreases in the rate of amortization recorded in the period.

In addition to our quarterly reviews, we conduct a comprehensive assumption review on an annual basis, or as circumstances warrant. Upon completion of these assumption reviews, we revise our assumptions to reflect our current best estimate, thereby changing our estimate of EGPs in the deferred policy acquisition cost and unearned revenue amortization models, as well as projections within the death benefit and other insurance benefit reserving models. The deferred policy acquisition cost asset, the unearned revenue reserves and death benefit and other insurance benefit reserves are then adjusted with an offsetting benefit or charge to income to reflect such changes in the period of the revision, a process known as "unlocking." Finally, an analysis is performed periodically to assess whether there are sufficient gross margins or gross profits to amortize the remaining deferred policy acquisition costs balances. If the estimates of gross profits or margins cannot support the continued amortization or recovery of deferred policy acquisition costs, as was the case in 2010, the amortization of such costs is accelerated in the period in which the assumptions are changed, resulting in a charge to income.

Underlying assumptions for future periods of EGPs are not altered unless experience deviates significantly from original assumptions. For example, when lapses of our insurance products meaningfully exceed levels assumed in the existing policy projection, we adjust amortization to reflect the change in future premiums or EGPs resulting from the unexpected lapses. If revised EGPs based on new assumptions are lower, we would increase deferred policy acquisition cost amortization resulting in a reduction in the deferred policy acquisition cost asset. Favorable experience on key assumptions could result in a decrease to deferred policy acquisition cost amortization and an increase in the deferred policy acquisition costs asset.

## Results of Operations

### Summary Financial Data:

(\$ in thousands)

	Three Months Ended March 31,		Increase (decrease) and percentage change	
	2011	2010	2011 vs. 2010	
<b>REVENUES:</b>				
Premiums	\$ 163	\$ 1,179	\$ (1,016)	(86%)
Insurance and investment product fees	101,830	107,236	(5,406)	(5%)
Net investment income	21,398	17,712	3,686	21%
Net realized investment gains (losses):				
Total other-than-temporary impairment (“OTTI”) losses	(880)	(5,684)	4,804	85%
Portion of OTTI losses recognized in other comprehensive income	386	2,116	(1,730)	(82%)
Net OTTI losses recognized in earnings	(494)	(3,568)	3,074	86%
Net realized investment gains (losses), excluding OTTI losses	(3,968)	4,562	(8,530)	(187%)
Total realized investment gains	(4,462)	994	(5,456)	NM
<b>Total revenues</b>	<b>118,929</b>	<b>127,121</b>	<b>(8,192)</b>	<b>(6%)</b>
<b>BENEFITS AND EXPENSES:</b>				
Policy benefits	50,569	55,521	(4,952)	(9%)
Policy acquisition cost amortization	39,052	38,457	595	2%
Other operating expenses	18,381	23,333	(4,952)	(21%)
<b>Total benefits and expenses</b>	<b>108,002</b>	<b>117,311</b>	<b>(9,309)</b>	<b>(8%)</b>
Income before income taxes	10,927	9,810	1,117	11%
Income tax expense	287	3,958	(3,671)	(93%)
<b>Net income</b>	<b>\$ 10,640</b>	<b>\$ 5,852</b>	<b>\$ 4,788</b>	<b>82%</b>

Not meaningful (NM)

### Three months ended March 31, 2011 compared to three months ended March 31, 2010

Net income for the three months ended March 31, 2011 was \$10,640 thousand compared to \$5,852 thousand for the three months ended March 31, 2010. The increase in results from operations reflects lower operating expenses, policy benefits and income taxes as well as higher net investment income. These were partially offset by an increase in net realized investment losses as well as lower insurance and investment product fees.

Operating expenses improved \$4,952 thousand to \$18,381 thousand in the first quarter of 2011 from \$23,333 thousand in the first quarter of 2010. Lower operating expenses were a result of lower premium taxes and lower compensation and employee-related expenses.

Policy benefits primarily decreased as a result of lower interest credited associated with the decline in universal life policies in force.

The Company recorded an income tax expense of \$287 thousand in the first quarter of 2011 compared to \$3,958 thousand in the first quarter of 2010. The decrease in tax expense in 2011 as compared to 2010 was primarily driven by a reduction in the valuation allowance combined with a benefit related to the exception to intraperiod allocation rules in accordance with ASC 740-20, *Accounting for Income Taxes – Intraperiod Tax Allocation*.

Income on debt securities was the primary driver of the increase in net investment income of \$3,686 thousand for the quarter ended March 31, 2011 compared to the quarter ended March 31, 2010. This increase was a result of a larger debt security portfolio attributable to higher sales of our fixed indexed annuity products as well as an overall transition towards longer duration assets given the Company’s changing liquidity needs.

Net realized investment losses of \$4,462 thousand were recognized during the quarter ended March 31, 2011 compared to net realized investment gains of \$994 thousand during the quarter ended March 31, 2010. This decrease in realized income was a result of realized losses on derivative assets and liabilities which increased \$9,958 thousand to a loss of \$4,274 thousand in the quarter ended March 31, 2011 compared to a gain of \$5,684 thousand during the quarter ended March 31, 2010. This was primarily attributable to our net embedded derivatives associated with variable and fixed indexed annuity guarantees which had increased losses of \$7,311 thousand for the quarter ended March 31, 2011 compared to March 31, 2010. Of this increase, \$3,059 thousand was associated with the non-performance risk factor. There were also losses of \$2,647 thousand were recognized on our surplus hedge that was entered into during 2010. Partially offsetting these additional losses was an improvement of \$3,074 thousand in impairment losses as well as an improvement of \$1,428 thousand from net transaction losses during the quarter ended March 31, 2010 compared to transaction gains during the quarter ended March 31, 2011.

Insurance and investment product fees declined primarily as a result of the decline in universal life.

### Debt and Equity Securities Held in Our General Account

Our general account debt securities portfolios consist primarily of investment grade publicly-traded and privately-placed corporate bonds, residential mortgage-backed securities (“RMBS”), commercial mortgage-backed securities (“CMBS”) and asset-backed securities. As of March 31, 2011, our general account held debt securities with a carrying value of \$1,782,929 thousand, representing 91.9% of total general account investments. Public debt securities represented 81.1% of total debt securities, with the remaining 18.9% represented by private debt securities.

#### Debt Securities by Type and Credit Quality:

*(\$ in thousands)*

	As of March 31, 2011			
	Investment Grade		Below Investment Grade	
	Fair Value	Cost	Fair Value	Cost
U.S. government and agency	\$ 107,902	\$ 105,879	\$ --	\$ --
State and political subdivision	31,762	31,761	915	1,328
Foreign government	15,338	14,232	1,408	1,119
Corporate	725,965	699,596	51,601	71,254
CMBS	205,362	200,999	9,580	10,487
RMBS	413,769	421,485	21,091	27,964
CDO/CLO	10,897	10,585	53,215	59,985
Other asset-backed	130,214	129,661	3,910	4,131
<b>Total debt securities</b>	<b>\$ 1,641,209</b>	<b>\$ 1,614,198</b>	<b>\$ 141,720</b>	<b>\$ 176,268</b>
<b>Percentage of total debt securities</b>	<b>92.0%</b>	<b>90.2%</b>	<b>8.0%</b>	<b>9.8%</b>

We manage credit risk through industry and issuer diversification. Maximum exposure to an issuer is defined by quality ratings, with higher quality issuers having larger exposure limits. Our investment approach emphasizes a high level of industry diversification. The top five industry holdings as of March 31, 2011 in our debt securities portfolio were banking (4.8%), electric utilities (4.1%), diversified financial services (3.4%), insurance (3.3%) and oil (2.5%).

#### Residential Mortgage-Backed Securities

The weakness in the U.S. residential real estate markets, tighter credit standards and high unemployment, continue to impact the RMBS market. Delinquency rates for all sectors of the RMBS market, including sub-prime, Alt-A and prime, are above historical averages.

We invest directly in RMBS through our general account. To the extent these assets deteriorate in credit quality and decline in value for an extended period, we may realize impairment losses. When making investment decisions, we have been focused on identifying those securities that could withstand significant increases in delinquencies and foreclosures in the underlying mortgage pools before incurring a loss of principal.

Most of our RMBS portfolio is highly rated. At March 31, 2011, 79.8% of the total residential portfolio was rated AAA or AA. We have \$58,235 thousand of sub-prime exposure, \$101,487 thousand of Alt-A exposure and \$126,893 thousand of prime exposure, which combined amount to 14.7% of our general account. The majority of our sub-prime, Alt-A, and prime exposure is investment grade, with 61% being AAA rated, and another 15% in AA/A securities. We have employed a disciplined approach in the analysis and monitoring of our mortgage-backed securities. Our approach involves a monthly review of each security. Underlying mortgage data is obtained from the security's trustee and analyzed for performance trends. A security-specific stress analysis is performed using the most recent trustee information. This analysis forms the basis for our determination of whether the security will pay in accordance with the contractual cash flows. RMBS impairments as of March 31, 2011 totaled \$244 thousand. These impairments consist of \$0 from sub-prime, \$244 thousand from Alt-A and \$0 thousand from prime.

**General Account Residential Mortgage-Backed Securities:**

(\$ in thousands)

	As of March 31, 2011							
	Carrying Value <sup>(1)</sup>	Market Value <sup>(1)</sup>	% General Account <sup>(2)</sup>	AAA	AA	A	BBB	BB and Below
<b>Collateral</b>								
Agency	\$ 146,797	\$ 148,245	7.7%	100.0%	0.0%	0.0%	0.0%	0.0%
Prime	129,597	126,893	6.5%	64.5%	6.9%	6.2%	1.6%	20.8%
Alt-A	106,312	101,487	5.2%	60.3%	8.7%	11.1%	0.0%	19.9%
Sub-prime	66,743	58,235	3.0%	52.9%	12.2%	0.0%	11.0%	23.9%
<b>Total</b>	<b>\$ 449,449</b>	<b>\$ 434,860</b>	<b>22.4%</b>	<b>74.1%</b>	<b>5.7%</b>	<b>4.4%</b>	<b>1.9%</b>	<b>13.9%</b>

(1) Individual categories may not agree with the Debt Securities by Type table on previous page due to nature of underlying collateral.

(2) Percentages based on Market Value.

**General Account Prime Mortgage-Backed Securities:**

(\$ in thousands)

	As of March 31, 2011								
	Carrying Value	Market Value	% General Account <sup>(1)</sup>	Year of Issue					2003 & Prior
Post-2007				2007	2006	2005	2004		
<b>Rating</b>									
AAA	\$ 82,548	\$ 81,873	4.2%	0.0%	0.0%	0.0%	9.0%	47.4%	43.6%
AA	8,750	8,708	0.4%	0.0%	0.0%	11.6%	53.3%	35.1%	0.0%
A	7,853	7,891	0.4%	0.0%	0.0%	0.0%	77.7%	22.3%	0.0%
BBB	2,164	2,017	0.1%	0.0%	0.0%	0.0%	100.0%	0.0%	0.0%
BB and Below	28,282	26,404	1.4%	0.0%	4.0%	42.8%	50.7%	0.1%	2.4%
<b>Total</b>	<b>\$ 129,597</b>	<b>\$ 126,893</b>	<b>6.5%</b>	<b>0.0%</b>	<b>0.8%</b>	<b>9.7%</b>	<b>26.4%</b>	<b>34.5%</b>	<b>28.6%</b>

(1) Percentages based on Market Value.

**General Account Alt-A Mortgage-Backed Securities:**

(\$ in thousands)

	As of March 31, 2011								
	Carrying Value	Market Value	% General Account <sup>(1)</sup>	Year of Issue					2003 & Prior
Post-2007				2007	2006	2005	2004		
<b>Rating</b>									
AAA	\$ 61,615	\$ 61,148	3.1%	0.0%	0.0%	0.0%	8.1%	59.7%	32.2%
AA	9,170	8,856	0.5%	0.0%	0.0%	39.3%	0.0%	44.2%	16.5%
A	11,219	11,260	0.6%	0.0%	0.0%	0.0%	89.3%	2.5%	8.2%
BBB	--	--	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
BB and Below	24,308	20,223	1.0%	0.0%	15.4%	21.9%	55.2%	6.4%	1.1%
<b>Total</b>	<b>\$ 106,312</b>	<b>\$ 101,487</b>	<b>5.2%</b>	<b>0.0%</b>	<b>3.1%</b>	<b>7.8%</b>	<b>25.8%</b>	<b>41.4%</b>	<b>21.9%</b>

(1) Percentages based on Market Value.

**General Account Sub-Prime Mortgage-Backed Securities:**

(\$ in thousands)

As of March 31, 2011

Rating	Carrying Value	Market Value	% General Account <sup>(1)</sup>	Year of Issue					2003 & Prior
				Post-2007	2007	2006	2005	2004	
AAA	\$ 31,120	\$ 30,804	1.6%	21.5%	7.2%	11.8%	13.5%	28.5%	17.5%
AA	7,398	7,119	0.4%	0.0%	0.0%	0.0%	93.6%	0.0%	6.4%
A	--	--	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
BBB	9,013	6,379	0.3%	0.0%	51.7%	11.1%	8.0%	0.0%	29.2%
BB and Below	19,212	13,933	0.7%	0.0%	47.2%	11.8%	30.5%	0.0%	10.5%
<b>Total</b>	<b>\$ 66,743</b>	<b>\$ 58,235</b>	<b>3.0%</b>	<b>11.4%</b>	<b>20.7%</b>	<b>10.3%</b>	<b>26.8%</b>	<b>15.1%</b>	<b>15.7%</b>

(1) Percentages based on Market Value.

*Commercial Mortgage-Backed Securities*

**General Account Commercial Mortgage-Backed Securities:**

(\$ in thousands)

As of March 31, 2011

Rating	Carrying Value <sup>(1)</sup>	Market Value <sup>(1)</sup>	% General Account <sup>(2)</sup>	Year of Issue				2004 and Prior
				Post-2007	2007	2006	2005	
AAA	\$ 142,982	\$ 146,841	7.6%	19.2%	11.8%	21.7%	21.6%	25.7%
AA	28,876	28,967	1.5%	11.0%	10.9%	9.0%	14.9%	54.2%
A	20,832	21,401	1.1%	88.1%	2.5%	9.4%	0.0%	0.0%
BBB	10,697	9,045	0.5%	0.0%	71.2%	15.7%	0.0%	13.1%
BB and below	11,065	10,683	0.5%	76.9%	8.3%	0.0%	10.1%	4.7%
<b>Total</b>	<b>\$ 214,452</b>	<b>\$ 216,937</b>	<b>11.2%</b>	<b>27.0%</b>	<b>13.1%</b>	<b>17.4%</b>	<b>17.1%</b>	<b>25.4%</b>

(1) Includes commercial mortgage-backed CDOs with carrying and market values of \$2,966 thousand and \$1,995 thousand, respectively.

(2) Percentages based on Market Value.

## Realized Gains and Losses

The following table presents certain information with respect to realized investment gains and losses, including those on debt securities pledged as collateral, with losses from OTTI charges reported separately in the table. These impairment charges were determined based on our assessment of factors enumerated below, as they pertain to the individual securities determined to be other-than-temporarily impaired.

Sources and Types of Net Realized Investment Gains (Losses): <i>(\$ in thousands)</i>	Three Months Ended March 31,	
	2011	2010
Total other-than-temporary debt impairment losses	\$ (880)	\$ (5,684)
Portion of loss recognized in other comprehensive income	386	2,116
<b>Net debt impairment losses recognized in earnings</b>	<b>\$ (494)</b>	<b>\$ (3,568)</b>
Debt security impairments:		
U.S. government and agency	\$ --	\$ --
State and political subdivision	--	--
Foreign government	--	--
Corporate	(250)	--
CMBS	--	(570)
RMBS	(244)	(1,484)
CDO/CLO	--	(1,514)
Other asset-backed	--	--
Net debt security impairments	(494)	(3,568)
Other investments impairments	--	--
<b>Impairment losses</b>	<b>(494)</b>	<b>(3,568)</b>
Debt security transaction gains	631	237
Debt security transaction losses	(325)	(1,624)
Other investments transaction gains (losses)	--	265
<b>Net transaction losses</b>	<b>306</b>	<b>(1,122)</b>
Realized gains (losses) on derivative assets and liabilities	(4,274)	5,684
<b>Net realized investment gains (losses), excluding impairment losses</b>	<b>(3,968)</b>	<b>4,562</b>
<b>Net realized investment gains (losses), including impairment losses</b>	<b>\$ (4,462)</b>	<b>\$ 994</b>

## Other-than-Temporary Impairments

A credit-related loss impairment for structured securities is determined by calculating the present value of the expected credit losses on a given security's coupon and principal cash flows until maturity. All other fixed income securities are written down to fair value. The impairment amount is separated into the amount related to credit losses, which is recorded as a charge to net realized investment losses included in our earnings, and the amount related to all other factors, which is recognized in other comprehensive income. The non-credit related loss component is equal to the difference between the fair value of a security and its impaired carrying value.

Management exercised significant judgment with respect to certain securities in determining whether impairments are temporary or other than temporary. At March 31, 2011, this included securities with \$17,158 thousand of gross unrealized losses of 50% or more for which no OTTI was ultimately indicated. In reaching its conclusions, management used a number of issuer-specific quantitative indicators and qualitative judgments to assess the probability of receiving a given security's contractual cash flows. This included the issue's implied yield to maturity, cumulative default rate based on rating, comparisons of issue-specific spreads to industry or sector spreads, specific trading activity in the issue, and other market data such as recent debt tenders and upcoming refinancing requirements. Management also reviewed fundamentals such as issuer credit and liquidity metrics, business outlook and industry conditions. Management does not have the intention to sell nor does it expect to be required to sell these securities prior to their recovery. Management maintains a watch list of securities that is reviewed for impairments. Each security on the watch list was evaluated, analyzed and discussed, with the positive and negative factors weighed in the ultimate determination of whether or not the security was other-than-temporarily impaired.

## Debt Securities

Fixed maturity OTTI recorded in the first quarter of 2011 were primarily concentrated in corporate bonds and structured securities. These impairments were driven primarily by significant rating downgrades and increased collateral default rates. In our judgment, these credit events or other adverse conditions of the issuers have caused, or will most likely lead to, a deficiency in the contractual cash flows related to the investment. Therefore, based upon these credit events, we have determined that OTTI exist. Total impairments recognized through earnings related to such credit-related circumstances were \$494 thousand in the first quarter of 2011 and \$3,568 thousand in the first quarter of 2010.

In addition to these credit-related impairments recognized through earnings, we impaired securities to fair value through other comprehensive loss for any impairments related to non-credit related factors. These types of impairments were driven primarily by market or sector credit spread widening or by a lack of liquidity in the securities. The amount of impairments recognized as an adjustment to other comprehensive loss due to these factors was \$386 thousand in the first quarter of 2011 and \$2,116 thousand in the first quarter of 2010.

Prospectively, we will account for the OTTI security as if the debt security had been purchased on the impairment date, using an amortized cost basis equal to the previous cost basis less the amount of the credit loss impairment. We will continue to estimate the present value of future cash flows expected and, if significantly greater than the new cost basis, accrete the difference as interest income.

The following table rolls forward the amount of credit losses recognized in earnings on debt securities held at the beginning of the period, for which a portion of the OTTI was recognized in other comprehensive income.

### Credit Losses Recognized in Earnings on Debt Securities for which a Portion of the OTTI Loss was Recognized in Other Comprehensive Income:

*(\$ in thousands)*

	Three Months Ended	
	March 31,	
	2011	2010
Balance, beginning of period	\$ (17,335)	\$ (12,442)
Add: Credit losses on securities not previously impaired <sup>(1)</sup>	(250)	(246)
Add: Credit losses on securities previously impaired <sup>(1)</sup>	(244)	(3,322)
Less: Credit losses on securities impaired due to intent to sell	--	--
Less: Credit losses on securities sold	958	--
Less: Increases in cash flows expected on previously impaired securities	--	--
<b>Balance, end of period</b>	<b>\$ (16,871)</b>	<b>\$ (16,010)</b>

<sup>(1)</sup> Additional credit losses on securities for which a portion of the OTTI loss was recognized in AOCI are included within net OTTI losses recognized in earnings on the statements of income and comprehensive income.

### Unrealized Gains and Losses

Net unrealized investment gains and losses on securities classified as available for sale and certain other assets are included in the balance sheet as a component of accumulated other comprehensive income (loss) ("AOCI"). The table below presents the special category of AOCI for debt securities that are other-than-temporarily impaired when the impairment loss has been split between the credit loss component (in earnings) and the non-credit component (separate category of AOCI).

**Fixed Maturity Non-Credit OTTI Losses in AOCI, by Security Type:***(\$ in thousands)*

	<u>Mar 31, 2011<sup>(1)</sup></u>	<u>Dec 31, 2010<sup>(1)</sup></u>
U.S. government and agency	\$ --	\$ --
State and political subdivision	--	--
Foreign government	--	--
Corporate	(1,504)	(1,512)
CMBS	(4,519)	(4,519)
RMBS	(15,675)	(15,263)
CDO/CLO	(5,432)	(6,279)
Other asset-backed	--	--
<b>Total fixed maturity non-credit OTTI losses in AOCI</b>	<b><u>\$ (27,130)</u></b>	<b><u>\$ (27,573)</u></b>

<sup>(1)</sup> Represents the amount of non-credit OTTI losses recognized in AOCI excluding net unrealized gains or losses subsequent to the date of impairment.

The following table presents certain information with respect to our gross unrealized losses related to our investments in general account debt securities as of March 31, 2011. Applicable deferred acquisition costs and deferred income taxes reduce the effect of these losses on our comprehensive income.

**Duration of Gross Unrealized Losses on General Account Securities:***(\$ in thousands)*

	<u>As of March 31, 2011</u>			
	<u>Total</u>	<u>0 – 6 Months</u>	<u>6 – 12 Months</u>	<u>Over 12 Months</u>
<b>Debt securities</b>				
Total fair value	\$ 546,159	\$ 294,036	\$ 10,040	\$ 242,083
Total amortized cost	612,413	298,783	11,228	302,402
Unrealized losses	<u>\$ (66,254)</u>	<u>\$ (4,747)</u>	<u>\$ (1,188)</u>	<u>\$ (60,319)</u>
Unrealized losses after offsets	<u>\$ (7,448)</u>	<u>\$ (2,192)</u>	<u>\$ (145)</u>	<u>\$ (5,111)</u>
Number of securities	<u>348</u>	<u>182</u>	<u>10</u>	<u>156</u>
<b>Investment grade:</b>				
Unrealized losses	<u>\$ (28,974)</u>	<u>\$ (4,726)</u>	<u>\$ (1,086)</u>	<u>\$ (23,162)</u>
Unrealized losses after offsets	<u>\$ (4,305)</u>	<u>\$ (2,179)</u>	<u>\$ (137)</u>	<u>\$ (1,989)</u>
<b>Below investment grade:</b>				
Unrealized losses	<u>\$ (37,280)</u>	<u>\$ (21)</u>	<u>\$ (102)</u>	<u>\$ (37,157)</u>
Unrealized losses after offsets	<u>\$ (3,143)</u>	<u>\$ (13)</u>	<u>\$ (8)</u>	<u>\$ (3,122)</u>

Total net unrealized losses on debt securities were \$7,537 thousand (unrealized losses of \$66,254 thousand less unrealized gains of \$58,717 thousand).

For debt securities with gross unrealized losses, 57.8% of the unrealized losses after offsets pertain to investment grade securities and 42.2% of the unrealized losses after offsets pertain to below investment grade securities at March 31, 2011.

The following table represents those securities whose fair value is less than 80% of amortized cost (significant unrealized loss) that have been at a significant unrealized loss position on a continuous basis.

<b>Duration of Gross Unrealized Losses on General Account Securities:</b> <i>(\$ in thousands)</i>	<b>As of March 31, 2011</b>			
	<b>Total</b>	<b>0 – 6 Months</b>	<b>6 – 12 Months</b>	<b>Over 12 Months</b>
<b>Debt securities</b>				
Unrealized losses over 20% of cost	\$ (44,982)	\$ (336)	\$ (1,135)	\$ (43,511)
Unrealized losses over 20% of cost after offsets	\$ (3,719)	\$ (25)	\$ (87)	\$ (3,607)
Number of securities	40	1	2	37
<b>Investment grade:</b>				
Unrealized losses over 20% of cost	\$ (15,498)	\$ --	\$ (1,135)	\$ (14,363)
Unrealized losses over 20% of cost after offsets	\$ (1,183)	\$ --	\$ (87)	\$ (1,096)
<b>Below investment grade:</b>				
Unrealized losses over 20% of cost	\$ (29,484)	\$ (336)	\$ --	\$ (29,148)
Unrealized losses over 20% of cost after offsets	\$ (2,536)	\$ (25)	\$ --	\$ (2,511)

### **Liquidity and Capital Resources**

In the normal course of business, we enter into transactions involving various types of financial instruments such as debt securities. These instruments have credit risk and also may be subject to risk of loss due to interest rate and market fluctuations.

Our liquidity requirements principally relate to the liabilities associated with various life insurance and annuity products and operating expenses. Liabilities arising from life insurance and annuity products include the payment of benefits, as well as cash payments in connection with policy surrenders, withdrawals and loans.

Historically, we have used cash flow from operations, investment activities and capital contributions from our shareholder to fund liquidity requirements. Our principal cash inflows from life insurance and annuities activities come from premiums, annuity deposits and charges on insurance policies and annuity contracts. Principal cash inflows from investment activities result from repayments of principal, proceeds from maturities, sales of invested assets and investment income.

The primary liquidity risks regarding cash inflows from our investment activities are the risks of default by debtors, interest rate and other market volatility and potential illiquidity of investments. We closely monitor and manage these risks.

We believe that our current and anticipated sources of liquidity are adequate to meet our present and anticipated needs.

### *Ratings*

Rating agencies assign financial strength ratings to Phoenix Life and its subsidiaries based on their opinions of the Companies' ability to meet their financial obligations. Rating downgrades may result in lower sales, higher surrenders and increased or decreased interest costs in connection with future borrowings.

On February 8, 2011, A.M. Best Company, Inc. affirmed our financial strength rating of B+ and changed their outlook from negative to stable. On January 13, 2010, A.M. Best Company, Inc. downgraded our financial strength rating to B+ from B++ and maintained their negative outlook.

On June 17, 2010, Moody's Investor Services downgraded our financial strength rating from Ba1 to Ba2. They changed their outlook from negative to stable.

On March 24, 2011, Standard & Poor's affirmed our financial strength rating of BB- and changed their outlook from negative to stable. On February 12, 2010, Standard & Poor's downgraded our financial strength rating from BB to BB- and maintained their negative outlook.

The financial strength ratings as of March 31, 2011 were as follows:

<u>Rating Agency</u>	<u>Financial Strength Ratings of Phoenix Life and PHL Variable Life</u>	<u>Outlook</u>
A.M. Best Company, Inc.	B+	Stable
Moody's	Ba2	Stable
Standard & Poor's	BB-	Stable

Reference in this report to any credit rating is intended for the limited purposes of discussing or referring to changes in our credit ratings or aspects of our liquidity or costs of funds. Such reference cannot be relied on for any other purposes, or used to make any inference concerning future performance, future liquidity or any future credit rating.

### **Contractual Obligations and Commercial Commitments**

As of March 21, 2011, there were no significant changes to our outstanding contractual obligations and commercial commitments as disclosed in our 2010 Annual Report on Form 10-K.

### **Off-Balance Sheet Arrangements**

As of March 31, 2011 and December 31, 2010, we did not have any significant off-balance sheet arrangements as defined by Item 303(a)(4)(ii) of SEC Regulation S-K.

### **Obligations Related to Pension and Postretirement Employee Benefit Plans**

Our ultimate parent company provides employees with post-employment benefits that include retirement benefits, through pension and savings plans, and other benefits, including health care and life insurance. This includes three defined benefit pension plans. We incur applicable employee benefit expenses through the process of cost allocation by PNX.

The employee pension plan, covering substantially all employees, provides benefits up to the amount allowed under the Internal Revenue Code. The two supplemental plans provide benefits in excess of the primary plan. Retirement benefits under the plans are a function of years of service and compensation. The employee pension plan is funded with assets held in a trust, while the supplemental plans are unfunded. Effective March 31, 2010, all benefit accruals under our funded and unfunded defined benefit plans were frozen.

Employee benefit expense allocated to us for these benefits totaled \$727 thousand and \$1,440 thousand at March 31, 2011 and 2010, respectively. Phoenix Life made contributions to the pension plans in the first quarter of 2011, of which \$1,042 thousand has been allocated to us. By December 31, 2011, Phoenix Life expects to make contributions to the pension plans, of which approximately \$4,951 thousand will be allocated to us.

### **Reinsurance**

We maintain life reinsurance programs designed to protect against large or unusual losses in our life insurance business. Based on our review of their financial statements, reputations in the reinsurance marketplace and other relevant information, we believe that these reinsurers are financially sound and, therefore, that we have no material exposure to uncollectible life reinsurance.

### **Statutory Capital and Surplus**

Our statutory basis capital and surplus (including asset valuation reserve ("AVR")) increased from \$278,822 thousand at December 31, 2010 to \$299,894 thousand at March 31, 2011. The principal factors resulting in this increase were net gains from operations after tax of \$44,629 thousand offset by \$9,627 thousand of unrealized capital losses and a \$14,578 thousand reduction in net deferred income taxes.

## **Enterprise Risk Management**

Our ultimate parent company, PNX, has a comprehensive, enterprise-wide risk management program under which PHL Variable operations are covered. The Chief Risk Officer reports to the Chief Financial Officer and monitors our risk management activities. During 2009, as part of our strategic repositioning and overall expense reduction effort, we refined our approach to risk management across the enterprise. We have an Enterprise Risk Management Committee, chaired by the our ultimate parent company's Chief Executive Officer, whose functions are to establish risk management principles, monitor key risks and oversee our risk-management practices. Several management committees oversee and address issues pertaining to all our major risks—operational, market and product—as well as capital management.

See our 2010 Annual Report on Form 10-K for more information regarding our enterprise risk management. There were no material changes in our exposure to operational and market risk exposure at March 31, 2011 in comparison to December 31, 2010.

### **Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

For information about our management of market risk, see “Item 2: Management’s Discussion and Analysis of Financial Condition and Results of Operations” under the heading “Enterprise Risk Management.

### **Item 4. CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

We have carried out an evaluation under the supervision and with the participation of our management, including our President and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon our evaluation, these officers have concluded that, as of March 31, 2011, our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) were effective to provide reasonable assurance that information required to be disclosed in the reports we file and submit under the Exchange Act is recorded, processed, summarized and reported within the time period specified in the SEC’s rules and forms and that such information is accumulated and communicated to our management, including our President and our Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

#### **Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting during the quarter ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. LEGAL PROCEEDINGS**

We are regularly involved in litigation and arbitration, both as a defendant and as a plaintiff. In addition, various regulatory bodies regularly make inquiries of us and, from time to time, conduct examinations or investigations concerning our compliance with, among other things, insurance laws, securities laws, laws governing the activities of broker-dealers and other laws and regulations affecting our registered products. It is not feasible to predict or determine the ultimate outcome of all legal or regulatory proceedings or to provide reasonable ranges of potential losses. We believe that the outcomes of our litigation and regulatory matters are not likely, either individually or in the aggregate, to have a material adverse effect on our financial condition. However, given the large or indeterminate amounts sought in certain of these matters and the inherent unpredictability of litigation and regulatory matters, it is possible that an adverse outcome in certain matters could, from time to time, have a material adverse effect on our results of operations or cash flows in particular quarterly or annual periods. See Item 1A, "Risk Factors" in Part I, Item A of our 2010 Annual Report on Form 10-K and Note 9 to our financial statements in this Form 10-Q for additional information.

### **Item 1A. RISK FACTORS**

The Company is subject to risks and uncertainties, any of which could have a significant or material adverse effect on our business, financial condition, operating results or liquidity. Before investing in our securities, you should carefully consider the risk factors disclosed in Part I, Item 1A of our 2010 Annual Report on Form 10-K. The risks described therein are not the only ones we face. This information should be considered carefully together with the other information contained in this report and the other reports and materials the Company files with the SEC.

### **Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

We have omitted this information from this report as we meet the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and are therefore filing this Form with the reduced disclosure format permitted by that General Instruction.

### **Item 3. DEFAULTS UPON SENIOR SECURITIES**

We have omitted this information from this report as we meet the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and are therefore filing this Form with the reduced disclosure format permitted by that General Instruction.

### **Item 4. (REMOVED AND RESERVED)**

### **Item 5. OTHER INFORMATION**

- (a) Not applicable.
- (b) No material changes.

### **Item 6. EXHIBITS**

#### Exhibit

- 3.1 Form of Amended and Restated Certificate of Incorporation (as amended and restated effective May 31, 1994) (incorporated herein by reference to Exhibit 3.1 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)

- 3.2 Bylaws of PHL Variable Life Insurance Company (as amended and restated effective May 16, 2002) (incorporated herein by reference to Exhibit 3.2 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- 10.1 Services Agreement effective as of January 1, 1995 by and among PHL Variable Insurance Company, Phoenix Life Insurance Company, American Life and Reassurance Company, Phoenix American Life Insurance Company and Phoenix Home Life Mutual Insurance Company (incorporated herein by reference to Exhibit 10.1 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- 10.2 Investment Management Agreement effective as of January 1, 1995 by and between PHL Variable Insurance Company and Phoenix Investment Counsel, Inc. (incorporated herein by reference to Exhibit 10.2 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- 10.3 Amendment #1 (effective as of January 1, 1998) to the Investment Management Agreement dated as of January 1, 1995 by and between PHL Variable Insurance Company and Phoenix Investment Counsel, Inc. (incorporated herein by reference to Exhibit 10.3 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- 10.4 Amended and Restated Tax Allocation Agreement dated as of January 1, 2001 by and among The Phoenix Companies, Inc. and most of its subsidiaries (incorporated herein by reference to Exhibit 10.4 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- 10.5 Amendment #1 (effective as of January 1, 2006) to the Amended and Restated Tax Allocation Agreement dated as of January 1, 2001 by and among The Phoenix Companies, Inc. and most of its subsidiaries (incorporated herein by reference to Exhibit 10.5 to the PHL Variable Insurance Company's Annual Report on Form 10-K filed March 31, 2006)
- [31.1](#) Certification of James D. Wehr, President, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002\*
- [31.2](#) Certification of Peter A. Hofmann, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002\*
- [32](#) Certification by James D. Wehr, President and Peter A. Hofmann, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002\*

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\* Filed herewith

**We will furnish any exhibit upon the payment of a reasonable fee, which fee shall be limited to our reasonable expenses in furnishing such exhibit.** Requests for copies should be directed to: Corporate Secretary, PHL Variable Insurance Company, One American Row, P.O. Box 5056, Hartford, Connecticut 06102-5056.

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**PHL VARIABLE INSURANCE COMPANY**

Date: May 16, 2011

By: /s/ Peter A. Hofmann

Peter A. Hofmann

Senior Executive Vice President and Chief Financial Officer