

COMMON *w* HEALTH ANNUITY

(a wholly-owned subsidiary of The Goldman Sachs Group, Inc.)

**CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2010**

Commonwealth Annuity and Life Insurance Company
(a wholly-owned subsidiary of The Goldman Sachs Group, Inc.)

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholder of
Commonwealth Annuity and Life Insurance Company:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, shareholder's equity, comprehensive income and cash flows present fairly, in all material respects, the financial position of Commonwealth Annuity and Life Insurance Company and its subsidiaries at December 31, 2010 and December 31, 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

April 21, 2011

Commonwealth Annuity and Life Insurance Company
(a wholly-owned subsidiary of The Goldman Sachs Group, Inc.)
Consolidated Balance Sheets

December 31,	2010	2009
(In millions, except per share data)		
ASSETS		
Investments:		
Available-for-sale fixed maturities at fair value (amortized cost of \$2,647.6 and \$2,797.8 in 2010 and 2009, respectively)	\$ 2,844.3	\$ 2,954.4
Trading fixed maturities at fair value (amortized cost of \$491.2 and \$397.2 in 2010 and 2009, respectively)	526.4	424.5
Equity securities at fair value (cost of \$0.1 in 2010 and 2009, respectively)	0.1	0.1
Policy loans	306.4	320.3
Total investments	<u>3,677.2</u>	<u>3,699.3</u>
Cash and cash equivalents	251.4	300.2
Accrued investment income	41.7	41.1
Premiums, accounts and notes receivable, net	2.0	2.7
Reinsurance receivable on paid and unpaid losses, benefits, unearned premiums and modified coinsurance	4,725.0	4,824.1
Value of business acquired	27.3	30.3
Deferred policy acquisition costs	207.1	243.3
Deferred federal income taxes	80.4	137.9
Derivative instruments receivable	115.0	149.3
Other assets	31.0	20.5
Separate account assets	4,023.6	4,186.5
Total assets	<u>\$ 13,181.7</u>	<u>\$ 13,635.2</u>
LIABILITIES		
Policy liabilities and accruals:		
Future policy benefits (includes liabilities with a fair value of \$585.3 and \$579.0 in 2010 and 2009, respectively)	\$ 5,476.9	\$ 5,870.2
Outstanding claims and losses (includes liabilities with a fair value of \$5.8 and \$6.5 in 2010 and 2009, respectively)	88.6	101.7
Contractholder deposit funds and other policy liabilities (includes liabilities with a fair value of \$97.2 and \$98.6 in 2010 and 2009, respectively)	234.7	282.5
Total policy liabilities and accruals	<u>5,800.2</u>	<u>6,254.4</u>
Derivative instruments payable	98.0	137.4
Collateral on derivative instruments	11.6	53.6
Securities sold under agreements to repurchase	89.6	-
Dividend payable to shareholder	250.0	-
Accrued expenses and other liabilities	69.5	83.5
Reinsurance payable	1,964.0	1,941.5
Separate account liabilities	4,023.6	4,186.5
Total liabilities	<u>\$ 12,306.5</u>	<u>\$ 12,657.0</u>
Commitments and contingencies (Notes 18 and 19)		
SHAREHOLDER'S EQUITY		
Common stock, \$1,000 par value, 10,000 shares authorized, 2,526 shares issued and outstanding	\$ 2.5	\$ 2.5
Additional paid-in capital	716.9	716.9
Accumulated other comprehensive income	94.2	66.6
Retained earnings	61.6	192.2
Total shareholder's equity	<u>875.2</u>	<u>978.2</u>
Total liabilities and shareholder's equity	<u>\$ 13,181.7</u>	<u>\$ 13,635.2</u>

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

Commonwealth Annuity and Life Insurance Company
(a wholly-owned subsidiary of The Goldman Sachs Group, Inc.)
Consolidated Statements of Operations

For the Years Ended December 31,	2010	2009	2008
(In millions)			
REVENUES			
Premiums	\$ 51.0	\$ 48.5	\$ -
Universal life and investment product policy fees	193.3	234.7	189.6
Net investment income	191.4	323.3	125.6
Net realized investment gains/(losses)			
Total other-than-temporary impairment (“OTTI”) losses	-	(10.0)	(42.0)
OTTI losses recognized in other comprehensive income	-	(2.6)	-
Net OTTI losses recognized in earnings	-	(7.4)	(42.0)
Net realized capital gains/(losses), excluding net OTTI losses recognized in earnings	91.0	30.0	(7.6)
Total net realized investment gains/(losses)	91.0	22.6	(49.6)
Other income	33.6	7.1	21.6
Total revenues	560.3	636.2	287.2
BENEFITS, LOSSES AND EXPENSES			
Policy benefits, claims, losses and loss adjustment expenses	259.1	346.5	297.1
Policy acquisition expenses	64.5	96.8	106.9
(Gains)/losses on derivative instruments	(4.9)	27.5	(175.6)
Other operating expenses	79.7	67.6	59.5
Total benefits, losses and expenses	398.4	538.4	287.9
Income/(loss) before federal income taxes	161.9	97.8	(0.7)
FEDERAL INCOME TAX EXPENSE			
Total federal income tax expense	42.7	6.3	10.8
Net income/(loss)	\$ 119.2	\$ 91.5	\$ (11.5)

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Commonwealth Annuity and Life Insurance Company
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Consolidated Statements of Shareholder's Equity

(In millions)	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income/(Loss)	Retained Earnings	Total Shareholder's Equity
Balance at January 1, 2008	\$ 2.5	\$ 416.9	\$ (3.2)	\$ 161.2	\$ 577.4
Net loss				(11.5)	(11.5)
Other comprehensive income - Net unrealized losses			(21.8)		(21.8)
Capital contribution		50.0			50.0
Balance at December 31, 2008	\$ 2.5	\$ 466.9	\$ (25.0)	\$ 149.7	\$ 594.1
Net income				91.5	91.5
Cumulative effect of change in accounting principle, net of income tax			(7.9)	11.0	3.1
Other comprehensive income - Net unrealized gains			99.5		99.5
Capital contribution		250.0			250.0
Dividend to shareholder				(60.0)	(60.0)
Balance at December 31, 2009	\$ 2.5	\$ 716.9	\$ 66.6	\$ 192.2	\$ 978.2
Net income				119.2	119.2
Other comprehensive income - Net unrealized gains			27.6	0.2	27.8
Dividend to shareholder				(250.0)	(250.0)
Balance at December 31, 2010	\$ 2.5	\$ 716.9	\$ 94.2	\$ 61.6	\$ 875.2

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

Commonwealth Annuity and Life Insurance Company
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Consolidated Statements of Comprehensive Income

For the Years Ended December 31,	2010	2009	2008
(In millions)			
Net income/(loss)	\$ 119.2	\$ 91.5	\$ (11.5)
Other comprehensive income/(loss):			
Available-for-sale securities, net of policyholder amounts:			
Net appreciation/(depreciation) during the period	42.5	153.1	(33.5)
(Expense)/benefit for deferred federal income taxes	(14.9)	(53.6)	11.7
Total available-for-sales securities	27.6	99.5	(21.8)
Comprehensive income/(loss)	\$ 146.8	\$ 191.0	\$ (33.3)

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

Commonwealth Annuity and Life Insurance Company
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Consolidated Statements of Cash Flows

For the Years Ended December 31,	2010	2009	2008
(In millions)			
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income/(loss)	\$ 119.2	\$ 91.5	\$ (11.5)
Adjustments to reconcile net income/(loss) to net cash (used in)/provided by operating activities:			
Changes in fair value of trading fixed maturities	(7.8)	(27.5)	-
Net realized investment (gains)/losses	(91.0)	(22.6)	49.6
Non cash derivative activity	29.8	27.4	(172.6)
Net accretion and amortization on investments	(68.5)	(56.6)	(1.1)
Net amortization and depreciation	64.8	100.7	107.5
Interest credited to contractholder deposit funds and trust instruments supported by funding obligations	0.9	0.8	-
Deferred federal income taxes	42.7	6.3	10.8
Change in deferred policy acquisition costs	-	(4.1)	13.8
Change in premiums and notes receivable, net of reinsurance premiums payable	23.2	7.7	4.1
Change in accrued investment income	(0.6)	(5.3)	(1.0)
Change in policy liabilities and accruals, net	(430.2)	(372.2)	622.5
Change in reinsurance receivable and modified coinsurance	99.1	109.6	(502.6)
Change in accrued expenses and other liabilities	(14.4)	(64.1)	(9.9)
Other, net	(52.8)	57.6	11.5
Net cash (used in)/provided by operating activities	<u>(285.6)</u>	<u>(150.8)</u>	<u>121.1</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from disposals of available-for-sale fixed maturities	1,776.9	1,509.7	1,511.5
Proceeds from maturities of available-for-sale fixed maturities	45.4	519.6	39.3
Proceeds from disposals of trading fixed maturities	108.8	68.0	-
Proceeds from maturities of trading fixed maturities	4.8	49.1	-
Proceeds from other investments	364.2	349.8	271.9
Business acquisitions, net of cash acquired	-	7.2	-
Purchase of available-for-sale fixed maturities	(1,515.5)	(2,239.5)	(1,580.2)
Purchase of trading fixed maturities	(200.7)	(60.5)	-
Purchase of other investments	(389.1)	(288.4)	(212.9)
Net cash provided by/(used in) investing activities	<u>194.8</u>	<u>(85.0)</u>	<u>29.6</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Settlement of repurchase agreements	(101.2)	-	-
Proceeds from issuance of repurchase agreements	190.6	-	-
(Withdrawals from)/deposits in contractholder deposit funds	(46.6)	69.5	19.3
Withdrawals from trust instruments supported by funding obligations	(0.8)	(0.9)	-
Capital contribution	-	250.0	50.0
Dividend to shareholder	-	(60.0)	-
Net cash provided by financing activities	<u>42.0</u>	<u>258.6</u>	<u>69.3</u>
Net change in cash and cash equivalents	<u>(48.8)</u>	<u>22.8</u>	<u>220.0</u>
Cash and cash equivalents, beginning of period	300.2	277.4	57.4
Cash and cash equivalents, end of period	<u>\$ 251.4</u>	<u>\$ 300.2</u>	<u>\$ 277.4</u>

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

Commonwealth Annuity and Life Insurance Company
(a wholly-owned subsidiary of The Goldman Sachs Group, Inc.)
Notes to the Consolidated Financial Statements

1. ORGANIZATION

Commonwealth Annuity and Life Insurance Company (“the Company”) is a stock life insurance company organized under the laws of Massachusetts, and is a wholly-owned subsidiary of The Goldman Sachs Group, Inc. (“Goldman Sachs”). The Company manages blocks of fixed and variable annuities, universal and variable universal life insurance, traditional life insurance and to a lesser extent group retirement products.

2. BASIS OF PRESENTATION

The accompanying audited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“U.S. GAAP”). The preparation of financial statements in conformity with U.S. GAAP requires the Company to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The most significant estimates are those used in determining the fair value of financial instruments, deferred policy acquisition costs (“DAC”), value of business acquired (“VOBA”), liabilities for future contract and policyholder benefits, other-than-temporary impairments of investments, and valuation allowance on deferred tax assets. Although these and other estimates and assumptions are based on the best available information, actual results could differ from those estimates.

On January 2, 2009, The Hanover Insurance Group, Inc. (“THG”) sold all the outstanding shares of capital stock of First Allmerica Financial Life Insurance Company (“FAFLIC”) to the Company pursuant to a Stock Purchase Agreement entered into on July 30, 2008. The Company paid a purchase price of \$105.8 million. Coincident with the sale transaction, FAFLIC and The Hanover Insurance Company (“HIC”) entered into a reinsurance contract whereby HIC assumed FAFLIC’s exited accident and health insurance business through a 100% coinsurance agreement totaling \$113.5 million in net liabilities. An equal amount of assets was also transferred as part of this agreement.

The FAFLIC transaction was accounted for using the purchase method of accounting under Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 805, “Business Combinations” and purchase accounting adjustments were “pushed down” to FAFLIC’s financial statements accordingly. Under the purchase method of accounting, assets acquired and liabilities assumed were recorded at fair value at the date of purchase. See Note 4 for further information about the purchase accounting balance sheet.

The consolidated financial statements include the accounts of the Company and its subsidiaries. As of December 31, 2010, the Company directly owned all of the outstanding shares of FAFLIC, which manages run-off blocks of traditional life insurance, universal and variable universal life insurance, group retirement products, a Guaranteed Investment Contract (“GIC”), variable annuities and an exited accident and health business.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Financial Instruments

In the normal course of business, the Company enters into transactions involving various types of financial instruments. The Company separates its financial instruments into two categories: cash instruments and derivative contracts. The Company accounts for its financial instruments at fair value in accordance with ASC 820. The fair value of a financial instrument is the amount 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. See Notes 7-9 for further information about investments, investment income and gains and losses and fair value measurements respectively.

Cash instruments include U.S. government and federal agency obligations; asset backed, commercial and residential mortgage backed securities (“structured securities”); investment-grade corporate bonds; money market securities; state, municipal and provincial obligations; mutual funds held in separate accounts and other non-derivative financial instruments.

Derivatives are instruments that derive their value from underlying asset prices, indices, reference rates and other inputs or a combination of these factors. Derivatives may be privately negotiated contracts, which are usually referred to as over-the-counter (“OTC”) derivatives, or they may be listed and traded on an exchange (“exchange-traded”).

The Company has entered into certain OTC derivatives, primarily equity put options and interest rate swaptions, to manage certain equity market, credit and interest rate risk. These instruments do not qualify for hedge accounting and are carried at fair value or amounts that approximate fair value.

Commonwealth Annuity and Life Insurance Company
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Notes to the Consolidated Financial Statements

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Financial Instruments (Continued)

The Company trades equity futures contracts pursuant to an investment management agreement with Goldman Sachs Asset Management, L.P. (“GSAM”). Exchange-traded futures are effected through a regulated exchange and positions are marked to market through the Consolidated Statements of Operations. From time to time, futures contracts are terminated. The clearinghouse guarantees the performance of both counterparties, which mitigates credit risk.

Depending on the nature of the derivative transaction, the Company maintains Credit Support Agreements (“CSA”) with each counterparty. In general, the CSA sets a minimum threshold of exposure that must be collateralized although thresholds may vary by CSA.

B. Valuation of Investments

The Company accounts for its investments at fair value. Fixed maturities and equity securities may be classified as either available-for-sale or trading. Available-for-sale securities are carried at fair value, with unrealized gains and losses, net of tax, reported in accumulated other comprehensive income, a separate component of shareholder’s equity. Trading securities are carried at fair value, with unrealized gains and losses reported in net investment income. The amortized cost of fixed maturities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and accretion is included in net investment income.

Policy loans are carried principally at unpaid principal balances. Interest income on such loans is recorded as earned using the contractually agreed upon interest rate. Generally, interest is capitalized on the policy’s anniversary date.

Realized investment gains and losses, other than those related to separate accounts for which the Company does not bear the investment risk and that meet the conditions for separate account reporting under ASC 944-80, “Accounting and Reporting by Insurance Enterprises for Certain Non Traditional Long Duration Contracts and for Separate Accounts,” are reported as a component of revenues based upon specific identification of the investment assets sold.

Realized investment gains and losses related to separate accounts that meet the conditions for separate account reporting under ASC 944-80 accrue to and are borne by the contract holder.

The Company recognizes OTTI for securities classified as available-for-sale in accordance with FASB ASC Topic 320. At least quarterly, management reviews impaired securities for OTTI. The Company considers several factors when determining if a security is other-than-temporarily impaired, including but not limited to: its intent and ability to hold the impaired security until an anticipated recovery in value, the issuer’s ability to meet current and future principal and interest obligations for fixed maturity securities, the length and severity of the impairment, the financial condition and near term and long term prospects for the issuer. In making these evaluations, the Company exercises considerable judgment.

If the Company intends to sell or if it is more likely than not that, it will be required to sell, an impaired security prior to recovery of its cost basis the Company recognizes a charge to earnings for the full amount of the impairment (the difference between the amortized cost and fair value of the security). For fixed maturity securities that are considered other-than-temporarily impaired and that the Company does not intend to sell and will not be required to sell the Company separates the impairment into two components: credit loss and non-credit loss. Credit losses are charged to net realized investment losses and non-credit losses are charged to other comprehensive loss.

The credit loss component is the difference between the security’s amortized cost and the present value of its expected future cash flows discounted at the current effective rate. The remaining difference between the security’s fair value and the present value of its expected future cash flows is the non-credit loss. For corporate bonds both historical default (by rating) data is used as a proxy for the probability of default, and loss given default (by issuer) projections are applied to the par amount of the bond. Potential losses incurred on structured securities are based on expected loss models, not incurred loss models. Expected cash flows include assumptions about key systematic risks (e.g. unemployment rates, housing prices) and loan-specific information (e.g. delinquency rates, loan-to-volume ratios). Estimating future cash flows is a quantitative and qualitative process that incorporates information received from third parties, along with assumptions and judgments about the future performance of the underlying collateral.

Commonwealth Annuity and Life Insurance Company
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Notes to the Consolidated Financial Statements

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Valuation of Investments (Continued)

As a result of the Company's adoption of FASB ASC Topic 320 on April 1, 2009, a cumulative effect adjustment, net of tax, of \$7.9 million was recorded to increase accumulated other comprehensive loss with a corresponding decrease to accumulated deficit for the non-credit loss component of previously impaired securities that the Company neither intends to sell, nor is it more likely than not that the Company will be required to sell before recovery of amortized cost.

C. Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, amounts due from banks, highly liquid overnight deposits, discount notes and commercial paper held in the ordinary course of business. The Company also invests cash in an overnight tri-party reverse repurchase agreement, in which the Company receives investment grade, highly liquid securities as collateral from counterparties. None of this is restricted or segregated for specific business reasons.

D. DAC and Deferred Sales Inducements ("DSI")

DAC consists of commissions, ceding commissions, and other costs, that are related directly to the successful acquisition of new or renewal insurance contracts. The Company defers sales inducements generated by variable annuities that offer enhanced crediting rates or bonus payments.

DAC and DSI amortization are reviewed periodically and adjusted retrospectively when the Company revises its estimate of current or future gross profits to be recognized from these products. Acquisition costs and sales inducements related to variable annuity products and universal and variable universal life insurance products are amortized in proportion to total estimated gross profits from investment yields, mortality, surrender charges and expense margins over the expected life of the contracts. Acquisition costs related to traditional life products are amortized in proportion to premium revenue recognized. See Note 15 for further information about deferred policy acquisition costs.

E. Reinsurance

Reinsurance accounting is followed for ceded and assumed transactions when the risk transfer provisions of ASC 944-40, "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts," have been met. To meet risk transfer requirements, a long duration reinsurance contract must transfer mortality or morbidity risks, and subject the reinsurer to a reasonable possibility of a significant loss.

With respect to ceded reinsurance, the valuation of claims recoverable depends on whether the underlying claim is a reported claim, recognized in accordance with contract terms. For reported claims, the Company values reinsurance recoverable at the time the underlying claim is recognized, in accordance with contract terms. For future policy benefits, the Company estimates the amount of reinsurance recoverable based on the terms of the reinsurance contracts and historical reinsurance recovery information and applies that information to the future policy benefit estimates. The reinsurance recoverables are based on what the Company believes are reasonable estimates and the balance is disclosed separately in the financial statements. However, the ultimate amount of the reinsurance recoverable is not known until all claims are settled. Reinsurance contracts do not relieve the Company from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Company; consequently, allowances can be established for amounts deemed uncollectible. There were no valuation allowances deemed necessary at December 31, 2010 and 2009, respectively. See Note 14 for further information about reinsurance.

F. Property, Equipment and Capitalized Software

Property, equipment, leasehold improvements and capitalized software are stated at cost, less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method over the estimated useful lives of the related assets. Certain costs of software developed or obtained for internal use are capitalized and amortized on a straight-line basis over the useful life of the software. Amortization of leasehold improvements is calculated using the straight-line method over the lesser of the term of the leases or the estimated useful life of the improvements.

Commonwealth Annuity and Life Insurance Company
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Notes to the Consolidated Financial Statements

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Property, Equipment and Capitalized Software (Continued)

The Company tests for the potential impairment of long-lived assets whenever events or changes in circumstances suggest that the carrying amounts may not be recoverable in accordance with ASC 360, "Accounting for the Impairment or Disposal of Long-Lived Assets." The Company recognizes impairment losses only when the carrying amounts of long-lived assets exceed the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the assets. In such cases, the Company reduces the carrying value of the asset to fair value. Fair values are estimated using discounted cash flow analysis.

G. VOBA

VOBA reflects the estimated fair value of in-force contracts. VOBA represents the portion of the purchase price that is allocated to the value of the right to receive future cash flows from the business in-force at the acquisition date. VOBA is amortized over the life of the policies in relation to the emergence of estimated gross profits ("EGPs") from surrender charges, investment income, and mortality net of reinsurance ceded and expense margins and actual realized gain (loss) on investments. Contract lives for variable universal life policies are estimated to be 30 years.

VOBA is reviewed periodically to ensure that the unamortized portion does not exceed the expected recoverable amount.

For the January 2, 2009 purchase of FAFLIC, negative VOBA was recognized to reduce the carrying value of the insurance liability to fair value. Negative VOBA pertains to the business outside of the closed block participating policies. In order to reflect the fair value of the policyholder liabilities required under purchase accounting, we determined the fair value of the policyholder liabilities using market participants' assumptions to determine the present value of benefit payments and maintenance expenses plus a risk margin based on the cost of holding capital to back the business. The resulting fair value of the policyholder liabilities was greater than the amount calculated using GAAP assumptions and is recorded as negative VOBA on the opening balance sheet. Since the Company's contracts do not have any future premiums, negative VOBA is amortized in proportion to the change in the underlying reserves for those policies outside of the closed block participating policies.

The carrying amount of VOBA is adjusted for the effects of realized and unrealized gains and losses on debt securities classified as available-for-sale and certain derivatives. See Note 13 for further information about VOBA.

H. Separate Accounts

Separate account assets and liabilities represent segregated funds administered and invested by the Company for the benefit of variable annuity and variable universal life insurance contractholders. Assets consist principally of mutual funds at fair value. The investment income and gains and losses of these accounts generally accrue to the contractholders and therefore, are not included in the Company's net income. However, the Company's net income reflects fees assessed and earned on fund values of these contracts. See Note 6 for further information about liabilities for minimum guarantees under ASC 944-80, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and Separate Accounts."

Separate account assets representing contract holder funds are measured at fair value and reported as a summary total in the Consolidated Balance Sheet, with an equivalent summary total reported for related liabilities.

I. Policy Liabilities and Accruals

Future policy benefits are liabilities for annuity, life, and health products. Such liabilities are established in amounts adequate to meet the estimated future obligations of policies in-force. Future policy benefits for individual life insurance and annuity policies are computed using interest rates ranging from 2.0 % to 11.25 % for annuities and 2.5 % to 6.0 % for life insurance. Mortality, morbidity and withdrawal assumptions for all policies are based on the Company's own experience and industry standards.

Liabilities for universal life, variable universal life and variable annuities include deposits received from customers and investment earnings on their fund balances, less administrative charges. Universal life fund balances are also assessed mortality and surrender charges. Liabilities for variable annuities include a reserve for guaranteed minimum death benefits ("GMDB") in excess of contract values. See Note 6 for further information about liabilities for minimum guarantees.

Commonwealth Annuity and Life Insurance Company
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Notes to the Consolidated Financial Statements

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

I. Policy Liabilities and Accruals (Continued)

Liabilities for outstanding claims and claims adjustment expenses are estimates of payments to be made on life and health insurance contracts for reported losses and claims adjustment expenses and estimates of losses and claims adjustment expenses incurred but not reported. These liabilities are determined using case basis evaluations and statistical analyses and represent estimates of the ultimate cost of all claims incurred but not paid. These estimates are continually reviewed and adjusted as necessary; such adjustments are reflected in current operations. See Note 16 for further information about outstanding claims, losses and loss adjustment expenses.

Contractholder deposit funds and other policy liabilities include deposit administration funds and immediate participation guarantee funds and consist of deposits received from customers and investment earnings on their fund balances.

Policy liabilities and accruals are based on the various estimates discussed above. Although the adequacy of these amounts cannot be assured, the Company believes that policy liabilities and accruals will be sufficient to meet future obligations of policies in-force. The amount of liabilities and accruals, however, could be revised in the near-term if the estimates discussed above are revised.

J. Premium, Fee Revenue and Related Expenses

Premiums for individual life insurance and individual and group annuity products, excluding universal life and investment-related products, are considered revenue when due. Benefits, losses and related expenses are matched with premiums, resulting in their recognition over the lives of the contracts. This matching is accomplished through the provision for future benefits, estimated and unpaid losses, amortization of value of business acquired and amortization of deferred policy acquisition costs. Revenues for investment-related products consist of net investment income and contract charges assessed against the fund values. Related benefit expenses include annuity benefit claims for guaranteed minimum death benefits in excess of contract values, and net investment income credited to the fund values after deduction for investment and risk charges.

Revenues for universal life and investment products consist of net investment income, with mortality, administration and surrender charges assessed against the fund values. Related benefit expenses include universal life benefit claims in excess of fund values and net investment income credited to universal life fund values. Certain policy charges such as enhanced crediting rates or bonus payments that represent compensation for services to be provided in future periods are classified as deferred sales inducements and amortized over the period benefited using the same assumptions used to amortize deferred acquisition costs. See Note 15 and Note 6 for further information regarding revaluation of DAC and deferred sales inducements.

K. Closed Block

The Company's wholly-owned subsidiary, FAFLIC, established and began operating a closed block ("Closed Block") for the benefit of participating policies, consisting of certain individual life insurance participating policies, individual deferred annuity contracts and supplementary contracts not involving life contingencies which were in-force as of FAFLIC's demutualization on October 16, 1995.

The purpose of the Closed Block is to benefit certain classes of policies and contracts for which the Company has a dividend scale payable. Unless the Commonwealth of Massachusetts Commissioner of Insurance consents to an earlier termination, the Closed Block will continue to be in effect until none of the Closed Block policies are in-force. FAFLIC allocated to the Closed Block assets in an amount that is expected to produce cash flows which, together with future revenues from the Closed Block, are reasonably sufficient to support the Closed Block, including provision for payment of policy benefits, certain future expenses and taxes, and for continuation of policyholder dividend scales payable in 1994 so long as the experience underlying such dividend scales continues.

FAFLIC expects that the factors underlying such experience will fluctuate in the future and policyholder dividend scales for the Closed Block will be set accordingly.

Although the assets and cash flow generated by the Closed Block inure solely to the benefit of the holders of policies included in the Closed Block, the excess of Closed Block liabilities over Closed Block assets as measured on a GAAP basis represent the expected future after-tax income from the Closed Block which may be recognized in income over the period the policies and contracts in the Closed Block remain in-force.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

K. Closed Block (Continued)

Profitability attributable to the Closed Block is ultimately paid to the policyholders via policy dividends. Dividend payable formulas are set before the outset of the calendar year, and adverse investment performance does not change the dividend liability to the policyholders. A trading fixed maturity portfolio was established to back the Closed Block policy liabilities to appropriately match fair value asset and liability movements. See Note 10 for further information about Closed Block.

L. New and Adopted Accounting Pronouncements

Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts (ASC 944). In October 2010, the FASB issued amended accounting principles regarding accounting for deferred acquisition costs effective for the fiscal year beginning after December 15, 2011. These principles were codified as Accounting Standards Update (“ASU”) No. 2010-26, “Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts.” These principles clarify the costs that should be deferred by insurance entities when issuing and renewing insurance contracts and also specify that only costs related directly to successful acquisition of new or renewal contracts can be capitalized. All other acquisition-related costs should be expensed as incurred. As the Company is already in compliance with the provisions of this guidance, adoption of ASU No. 2010-26 will not have an effect on the Company’s financial condition, results of operations or cash flows.

How Investments Held through Separate Accounts Affect an Insurer’s Consolidation Analysis of Those Investments (ASC 810 and 944). In April 2010, the FASB issued amended accounting principles codified as ASU No. 2010-15, “How Investments Held through Separate Accounts Affect an Insurer’s Consolidation Analysis of Those Investments,” which clarifies that an insurance entity should not generally consider any separate account interests held for the benefit of policy holders in an investment to be the insurer’s interests and should not combine those interests with its general account interest in the same investment when assessing the investment for consolidation. In addition, the guidance clarifies that an insurer can retain the separate account’s specialized industry accounting for consolidation, and would not have to consolidate an investment in which a separate account holds a controlling financial interest if the investment is not or would not be consolidated in the standalone financial statements of the separate account. ASU No. 2010-15 is effective for fiscal years beginning after December 15, 2010 and adoption will not have an effect on the Company’s financial condition, results of operations or cash flows.

Fair Value Measurements and Disclosures (ASC 820). In January 2010, the FASB issued ASU No. 2010-06, “Fair Value Measurements and Disclosures (Topic 820) - Improving Disclosures about Fair Value Measurements.” ASU No. 2010-06 provides amended disclosure requirements related to fair value measurements. Certain of these disclosures were effective for the Company in 2010, while others are effective for financial statements issued for reporting periods beginning after December 15, 2010. Since these amended principles require only additional disclosures concerning fair value measurements, adoption did not and will not have an impact on the Company’s consolidated financial condition, results of operations or cash flows.

Recognition and Presentation of Other-Than-Temporary Impairments (ASC 320). In April 2009, the FASB issued amended accounting principles related to the recognition and presentation of other-than-temporary impairments (ASC 320). These amended principles prescribe that only the portion of an other-than-temporary impairment on a debt security related to credit loss is recognized in current period earnings, with the remainder recognized in other comprehensive income, if the holder does not intend to sell the security and it is more likely than not that the holder will not be required to sell the security prior to recovery. Previously, the entire other-than-temporary impairment was recognized in current period earnings. The Company adopted these amended accounting principles in the second quarter of 2009. Adoption of FASB ASC Topic 320 resulted in a cumulative effect adjustment, net of tax, of \$7.9 million to increase accumulated other comprehensive loss with a corresponding decrease to accumulated deficit for the non-credit loss component of previously impaired securities that the Company neither intends to sell, nor is it more likely than not that the Company will be required to sell, before recovery of amortized cost.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

L. New and Adopted Accounting Pronouncements (Continued)

Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (ASC 820). In April 2009, the FASB issued amended accounting principles related to determining fair value when the volume and level of activity for the asset or liability have significantly decreased and for identifying transactions that are not orderly (ASC 820). Specifically, these amended principles list factors which should be evaluated to determine whether a transaction is orderly; clarify that adjustments to transactions or quoted prices may be necessary when the volume and level of activity for an asset or liability have decreased significantly; and provide guidance for determining the concurrent weighting of the transaction price relative to fair value indications from other valuation techniques when estimating fair value. The Company adopted these amended accounting principles in the second quarter of 2009. Since the Company's fair value methodologies were consistent with these amended accounting principles, adoption did not affect the Company's financial condition, results of operations or cash flows.

Transfers of Financial Assets and Interests in Variable Interest Entities ("VIE's") (ASC 860 and 810). In June 2009, the FASB issued amended accounting principles which change the accounting for securitizations and VIE's. These principles were codified as ASU No. 2009-16, "Transfers and Servicing (Topic 860) - Accounting for Transfers of Financial Assets" and ASU No. 2009-17, "Consolidations (Topic 810) - Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities" in December 2009. ASU No. 2009-16 eliminates the concept of Qualified Special Purpose Entity ("QSPE"), changes the requirements for derecognizing financial assets, and requires additional disclosures about transfers of financial assets, including securitization transactions and continuing involvement with transferred financial assets. ASU No. 2009-17 changes the determination of when a VIE should be consolidated. Under ASU No. 2009-17, the determination of whether to consolidate a VIE is based on the power to direct the activities of the VIE that most significantly impact the VIE's economic performance together with either the obligation to absorb losses or the right to receive benefits that could be significant to the VIE, as well as the VIE's purpose and design. ASU No. 2009-16 and 2009-17 are effective for fiscal years beginning after November 15, 2009. In February 2010, the FASB finalized a standard, which defers the requirements of ASU No. 2009-17 for certain interests in investment funds and certain similar entities. Adoption of ASU Nos. 2009-16 and 2009-17 on January 1, 2010 did not have a material effect on the Company's financial condition, results of operations or cash flows.

M. Reclassifications

Certain reclassifications have been made to previously reported amounts to conform to the current presentation.

4. PURCHASE ACCOUNTING

In 2009, the acquisition of FAFLIC's assets and liabilities was recorded at fair value. Negative VOBA of \$41.7 million was recorded to reduce the carrying value of the insurance liability to fair value and is included within other liabilities at fair value reported below. No goodwill was recorded on acquisition. \$2.7 million was recorded as intangible assets for state licenses acquired and are included within other assets at fair value reported below.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of January 2, 2009 from the Company's purchase of FAFLIC.

Fair Value (In millions)	January 2, 2009
Assets:	
Total investments at fair value	\$ 1,029.3
Cash and cash equivalents	113.0
Other assets at fair value	410.2
Separate account assets	263.4
Total assets acquired	1,815.9
Liabilities:	
Policyholder account balances	1,325.8
Other liabilities at fair value	120.9
Separate account liabilities	263.4
Total liabilities assumed	1,710.1
Total purchase price	\$ 105.8

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5. SIGNIFICANT TRANSACTIONS

On December 31, 2009, the Company ceded via coinsurance and modified coinsurance, 100% of its variable annuity business to an affiliate, Arrow Capital Reinsurance Company, Limited (“Arrow”), a Bermuda domiciled Reinsurance Company. As part of this reinsurance agreement, the returns associated with the derivatives hedging program supporting the variable annuity products are passed to Arrow. In addition, in connection with this transaction, on December 31, 2009, with the approval of the Commonwealth of Massachusetts Commissioner of Insurance, the Company paid a dividend of \$60.0 million to Goldman Sachs. See Note 14 for further information on reinsurance.

On December 18, 2009, the Company entered into an Assumption Reinsurance Agreement with Metropolitan Life Insurance Company (“MetLife”) where the Company will assumption reinsure certain individual disability income insurance policies to MetLife. These policies are currently 100% coinsured with MetLife. The Company paid \$5.0 million to MetLife in connection with the transaction.

On April 1, 2009, the Company assumed on a 100% coinsurance basis the life and fixed annuity blocks of the life insurance subsidiaries of Universal American Corporation (“UAC”). Subsequently, on October 29, 2010, December 8, 2010 and December 23, 2010, the Company assigned all of its rights, titles, interests and privileges and certain duties and obligations related to the block of fixed annuity contracts assumed from the subsidiaries of UAC to Athene Life Re, Ltd (“Athene”), a Bermuda domiciled reinsurance company. Upon closing of the transactions, the Company paid a total novation fee of \$1.2 million to UAC and its life insurance subsidiary American Progressive Life and Health Insurance Company of New York (“American Progressive”). See Note 14 for further information on reinsurance.

On March 31, 2009, the Company entered into a coinsurance and modified coinsurance agreement with The Lincoln National Life Insurance Company (“Lincoln National”). Effective April 1, 2010, the agreement was amended to recognize the cession of all mortality risk to an affiliate of Lincoln National, thereby reducing mortality exposure for the Company. See Note 14 for further information on reinsurance.

On January 2, 2009, the Company acquired FAFLIC, a subsidiary of THG, comprising primarily traditional life insurance products, group retirement products and a Guaranteed Investment Contract. As a result of the transaction, FAFLIC became a wholly-owned subsidiary of the Company. As part of this transaction, the Company paid a purchase price of \$105.8 million and assumed general account reserves of \$1.3 billion. See Note 4 for further information on purchase accounting.

6. LIABILITIES FOR MINIMUM GUARANTEES UNDER ASC 944 - 80, ACCOUNTING AND REPORTING BY INSURANCE ENTERPRISES FOR CERTAIN NONTRADITIONAL LONG-DURATION CONTRACTS AND FOR SEPARATE ACCOUNTS

Guaranteed Minimum Death Benefits

The Company has issued variable annuity contracts with a GMDB feature. The GMDB feature provides annuity contractholders with a guarantee that the benefit received at death will be no less than a prescribed minimum amount. This amount is based on either the net deposits paid into the contract, the net deposits accumulated at a specified rate, the highest historical account value on a contract anniversary, or more typically, the greatest of these values. If the GMDB is higher than the current account value at the time of death, the Company incurs a cost equal to the difference.

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6. LIABILITIES FOR MINIMUM GUARANTEES UNDER ASC 944 - 80, ACCOUNTING AND REPORTING BY INSURANCE ENTERPRISES FOR CERTAIN NONTRADITIONAL LONG-DURATION CONTRACTS AND FOR SEPARATE ACCOUNTS (Continued)

The following table summarizes the liability for GMDB contracts reflected in the general account. The GMDB exposure includes reinsurance assumed, however, modified coinsurance is excluded as it provides negligible GMDB reserves and significant account values:

For the Years Ended December 31,	2010	2009
(In millions)		
Beginning balance	\$ 239.4	\$ 315.0
Provision for GMDB:		
GMDB expense incurred	39.8	40.3
Volatility ⁽¹⁾	14.9	(19.0)
	54.7	21.3
Claims, net of reinsurance:		
Claims from policyholders	(70.4)	(102.3)
Claims ceded to reinsurers	64.0	99.3
	(6.4)	(3.0)
GMDB reinsurance premium	(71.0)	(93.9)
Ending balance	\$ 216.7	\$ 239.4

(1) Volatility reflects the difference between actual and expected investment performance, persistency, age distribution, mortality and other factors that are assumptions within the GMDB reserving model.

The reserve represents estimates, over a range of stochastic scenarios, of the present value of future GMDB net benefits expected to be paid less the present value of future GMDB net fees charged to the policyholders.

The following information relates to the reserving methodology and assumptions for GMDB at December 31, 2010 and 2009.

- The projection model uses 500 stochastically generated return scenarios with mean performance ranging from 5% to 10% depending on the underlying fund type.
- Implied volatilities by duration are based on a combination of over the counter quotes (when available) and historical volatilities. For 2010, volatility assumptions range from 23% to 42%, varying by equity fund type and duration; 6% for bond funds; and 1% for money market funds. For 2009, volatility assumptions range from 26% to 69%, varying by equity fund type and duration; 7% to 13% for bond funds; and 0% to 2% for money market funds .
- The mortality assumptions are factors of the 1994 GMDB table based on company experience varying by age and gender. Mortality improvement of 1% per year for 10 years is assumed.
- The full surrender rate assumption varies from 1% to 35% depending on distribution channel, contract type, policy duration, and attained age. The aggregate projected full surrender rates for 2011 and 2012 are approximately 11% and 10%, respectively (full surrender rates include annuitizations, but they do not reflect partial withdrawals or deaths).
- The partial withdrawal rate assumption varies by distribution channel, tax qualified status, and attained age. Total projected partial withdrawals are from 6% - 7% for all years.

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6. LIABILITIES FOR MINIMUM GUARANTEES UNDER ASC 944 - 80, ACCOUNTING AND REPORTING BY INSURANCE ENTERPRISES FOR CERTAIN NONTRADITIONAL LONG DURATION CONTRACTS AND FOR SEPARATE ACCOUNTS (Continued)

The following table presents the account value, net amount at risk and average attained age of underlying contractholders for guarantees in the event of death as of December 31, 2010 and 2009. The net amount at risk is the death benefit coverage in-force or the amount that the Company would have to pay if all contractholders had died as of the specified date, and represents the excess of the guaranteed benefit over the account value.

December 31, (in millions, except for contractholder information)	2010	2009
Net deposits paid		
Account value.....	\$ 2,732	\$ 2,762
Net amount at risk	\$ 22	\$ 44
Average attained age of contractholders	63	62
Ratchet (highest historical account value at specified anniversary dates)		
Account value.....	\$ 756	\$ 807
Net amount at risk	\$ 90	\$ 162
Average attained age of contractholders	68	68
Roll-up (net deposits accumulated at a specified rate)		
Account value.....	\$ 45	\$ 49
Net amount at risk	\$ 24	\$ 29
Average attained age of contractholders	79	79
Higher of ratchet or roll-up		
Account value.....	\$ 2,706	\$ 2,821
Net amount at risk	\$ 1,326	\$ 1,638
Average attained age of contractholders	75	74
Total of guaranteed benefits categorized above		
Account value.....	\$ 6,239	\$ 6,439
Net amount at risk	\$ 1,462	\$ 1,873
Average attained age of contractholders (weighted by account value).....	69	68
Number of contractholders	146,931	162,403

Guaranteed Minimum Income Benefit

Additionally, the Company previously issued variable annuity contracts with a guaranteed minimum income benefit (“GMIB”) feature. The GMIB liability as of December 31, 2010 was \$11.9 million with a benefit paid of approximately \$10.5 million for the year ended December 31, 2010. The GMIB liability at December 31, 2009 was \$21.3 million with a benefit paid of approximately \$1.0 million for the year ended December 31, 2009. Similar to the approach employed to value the GMDB reserve, the fair value reserve for the GMIB feature was computed using a risk neutral approach. The reserve was determined by estimating the present value of future GMIB benefits expected to be paid less the present value of future GMIB fees charged to the policyholders, over a range of stochastic scenarios.

Sales Inducements

The Company’s variable annuity product offerings included contracts that offered enhanced crediting rates or bonus payments. The following reflects the changes to the deferred sales inducement asset:

For the years ended December 31,	2010	2009
(In millions)		
Balance at beginning of year	\$ -	\$ 0.5
Acquisition expenses deferred	0.3	0.3
Reinsurance treaty impacts	(0.3)	(0.8)
Balance at end of year	\$ -	\$ -

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6. LIABILITIES FOR MINIMUM GUARANTEES UNDER ASC 944 - 80, ACCOUNTING AND REPORTING BY INSURANCE ENTERPRISES FOR CERTAIN NONTRADITIONAL LONG DURATION CONTRACTS AND FOR SEPARATE ACCOUNTS (Continued)

Separate Accounts with Credited Interest Guarantees

The Company issued variable annuity and life contracts through its separate accounts for which net investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contractholder. The Company also issued variable annuity and life contracts through separate accounts where the Company contractually guarantees to the contractholder the total deposits made to the contract less any partial withdrawals plus a minimum return.

The market value adjusted (“MVA”) product attributable to Protective Life Insurance Company (“Protective”) was assumed on a modified coinsurance basis. Therefore, the assets related to these liabilities are recorded as a modified coinsurance receivable which is included within recoverable from reinsurers. See Note 14 for further information on reinsurance.

The Company had the following variable annuities with guaranteed minimum returns:

December 31,	2010	2009
(In millions)		
Account value	\$ 23.8	\$ 31.0
Range of guaranteed minimum return rates	2.8 - 5.7 %	2.8 - 6.5 %

Account balances of these contracts with guaranteed minimum returns were invested as follows:

December 31,	2010	2009
(In millions)		
Asset Type:		
Fixed maturities.....	\$ 28.7	\$ 28.8
Cash and cash equivalents.....	5.6	10.4
Total	\$ 34.3	\$ 39.2

7. INVESTMENTS

A. Fixed Maturities and Equity Securities

The amortized cost and fair value for fixed maturities and equity securities were as follows:

Available-for-sale fixed maturities and equity securities

December 31, 2010	<i>Amortized Cost</i> ⁽¹⁾	<i>Gross Unrealized Gains</i>	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>
(In millions)				
U.S. Treasury securities and U.S. government and agency securities	\$ 469.5	\$ 12.4	\$ (15.7)	\$ 466.2
States and political subdivisions	293.5	5.9	(3.8)	295.6
Foreign governments	2.0	-	-	2.0
Corporate fixed maturities	976.2	110.4	(5.9)	1,080.7
Structured securities	906.4	99.7	(6.3)	999.8
Total available-for-sale fixed maturities	\$ 2,647.6	\$ 228.4	\$ (31.7)	\$ 2,844.3
Equity securities	\$ 0.1	\$ -	\$ -	\$ 0.1

(1) Amortized cost for available-for-sale fixed maturities and cost for equity securities.

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7. INVESTMENTS (Continued)

Available-for-sale fixed maturities and equity securities

December 31, 2009	<i>Amortized Cost⁽¹⁾</i>	<i>Gross Unrealized Gains</i>	<i>Gross Unrealized Losses</i>	<i>OTTI Losses⁽²⁾</i>	<i>Fair Value</i>
(In millions)					
U.S. Treasury securities and U.S. government and agency securities	\$ 729.7	\$ 5.6	\$ (34.3)	\$ -	\$ 701.0
States and political subdivisions	162.2	4.5	(1.6)	-	165.1
Foreign governments	32.5	0.7	(0.2)	-	33.0
Corporate fixed maturities	1,192.3	99.5	(2.8)	-	1,289.0
Structured securities	681.1	97.1	(8.7)	(3.2)	766.3
Total available-for-sale fixed maturities	\$ 2,797.8	\$ 207.4	\$ (47.6)	\$ (3.2)	\$ 2,954.4
Equity securities	\$ 0.1	\$ -	\$ -	\$ -	\$ 0.1

⁽¹⁾ Amortized cost for available-for-sale fixed maturities and cost for equity securities.

⁽²⁾ Represents the before tax non-credit OTTI loss recorded as a component of accumulated other comprehensive income for assets still held at the reporting date.

At December 31, 2010 and 2009, the amortized cost and fair value of the assets on deposit with various state and governmental authorities were \$70.2 million and \$76.1 million, and \$97.3 million and \$79.4 million, respectively.

The Company entered into various derivative and other arrangements that required assets, such as cash and fixed maturities, to be pledged or received as collateral. At December 31, 2010 and 2009, cash and fixed maturities held as collateral were \$15.4 million and \$55.7 million, respectively.

The amortized cost and fair value by maturity periods for fixed maturities are shown below. Actual maturities may differ from contractual maturities, because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties, or the Company may have the right to put or sell the obligations back to the issuers. Structured securities are included in the category representing their ultimate maturity.

The maturity distribution for available-for-sale fixed maturity securities is as follows:

	<i>December 31, 2010 Amortized Cost</i>	<i>December 31, 2010 Fair Value</i>
(In millions)		
Due in one year or less	\$ 32.7	\$ 33.4
Due after one year through five years	169.6	185.1
Due after five years through ten years	580.7	629.5
Due after ten years	1,864.6	1,996.3
Total	\$ 2,647.6	\$ 2,844.3

B. Derivative Instruments

The Company manages its risk through the purchase of equity derivative put options and equity futures used to protect against increases in GMD liability in the event that the market grows at a rate below LIBOR; trading in interest rate derivatives to manage certain guaranteed crediting rate risks; and trading in credit derivatives to manage counterparty risk on reinsurance transactions. In addition, the Company invests in exchange traded futures and options as part of its overall diversification and total return objectives.

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7. INVESTMENTS (Continued)

B. Derivative Instruments (Continued)

The Company has reinsurance contracts that are accounted for on a modified coinsurance arrangement. Under a traditional modified coinsurance arrangement, the ceding company owns the assets backing the liabilities and transfers their book investment returns to the reinsurer. The reinsurance contract represents a hybrid instrument that is bifurcated into its host contract and embedded derivative components. An embedded derivative exists because the arrangement exposes the reinsurer to third-party credit risk.

The Company does not employ hedge accounting.

Management monitors the Company's derivative activities by reviewing portfolio activities and risk levels. Management also oversees all derivative transactions to ensure that the types of transactions entered into and the results obtained from those transactions are consistent with both the Company's risk management strategy and Company policies and procedures.

The fair value of the derivative assets and liabilities were as follows:

As of December 2010

(In millions, except number of contracts)

	Derivative Assets	Derivative Liabilities	Number of Contracts
<u>Derivative contracts</u>			
Equity and non-hedging futures	\$ 30.5	\$ -	7,614
Foreign currency swap	1.6	-	1
GMDB product derivatives	23.9	-	331,192
Credit	-	1.1	3
Embedded derivatives under modified coinsurance contracts	59.0	96.9	2
Gross fair value of derivative contracts	<u>\$ 115.0</u>	<u>\$ 98.0</u>	<u>338,812</u>
Fair value included within total assets	<u>\$ 115.0</u>		
Fair value included within total liabilities		<u>\$ 98.0</u>	

As of December 2009

(In millions, except number of contracts)

	Derivative Assets	Derivative Liabilities	Number of Contracts
<u>Derivative contracts</u>			
Equity and non-hedging futures	\$ 24.5	\$ -	5,920
Foreign currency swap	2.1	-	1
GMDB product derivatives	63.4	-	240,642
Credit	-	2.2	4
Embedded derivatives under modified coinsurance contracts	59.3	135.2	2
Gross fair value of derivative contracts	<u>\$ 149.3</u>	<u>\$ 137.4</u>	<u>246,569</u>
Fair value included within total assets	<u>\$ 149.3</u>		
Fair value included within total liabilities		<u>\$ 137.4</u>	

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7. INVESTMENTS (Continued)

B. Derivative Instruments (Continued)

The derivative gains and losses for the year ended December 31, 2010 is reported as follows:

Derivative contracts	Location of gain/(loss) recognized in income on derivatives	Amount of gain/(loss) recognized in income on derivatives
General account derivatives	Net realized investment gains/(losses)	\$ (4.4)
Foreign currency swap	(Gains)/losses on derivative instruments	(0.6)
GMDB product derivatives	(Gains)/losses on derivative instruments	(65.5)
Credit default swaps	(Gains)/losses on derivative instruments	(1.6)
Embedded derivatives under modified coinsurance contacts	(Gains)/losses on derivative instruments	72.6
Total gain		\$ 0.5

The derivative gains and losses for the year ended December 31, 2009 is reported as follows:

Derivative contracts	Location of gain/(loss) recognized in income on derivatives	Amount of gain/(loss) recognized in income on derivatives
General account derivatives	Net realized investment gains/(losses)	\$ 2.4
Foreign currency swap	Losses/(gains) on derivative instruments	2.0
GMDB product derivatives	Losses/(gains) on derivative instruments	(138.2)
Credit default swaps	Losses/(gains) on derivative instruments	(6.9)
Embedded derivatives under modified coinsurance contacts	Losses/(gains) on derivative instruments	115.6
Total loss		\$ (25.1)

C. Unrealized Gains and Losses

Unrealized gains and losses on available-for-sale fixed maturities, equity securities and other securities included in accumulated other comprehensive income are summarized as follows:

December 31,	Fixed Maturities	Equity Securities and Other	Total
(In millions)			
2010			
Net appreciation, beginning of year	\$ 66.6	\$ -	\$ 66.6
Net appreciation on available-for-sale securities	39.9	-	39.9
Net effect on value of business acquired, and on policy liabilities	2.6	-	2.6
Provision for deferred federal income taxes	(14.9)	-	(14.9)
	27.6	-	27.6
Net appreciation, end of year	\$ 94.2	\$ -	\$ 94.2

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7. INVESTMENTS (Continued)

C. Unrealized Gains and Losses (Continued)

December 31,	Fixed Maturities	Equity Securities and Other	Total
(In millions)			
2009			
Net depreciation, beginning of year	\$ (8.3)	\$ (16.7)	\$ (25.0)
Cumulative effect of change in accounting principle, net of income tax	(7.9)	-	(7.9)
Net appreciation on available-for-sale securities	199.2	25.4	224.6
Net effect on value of business acquired, and on policy liabilities	(71.5)	-	(71.5)
Provision for deferred federal income taxes	(44.9)	(8.7)	(53.6)
	82.8	16.7	99.5
Net appreciation, end of year	\$ 66.6	\$ -	\$ 66.6

December 31,	Fixed Maturities	Equity Securities and Other	Total
(In millions)			
2008			
Net appreciation/(depreciation), beginning of year	\$ 0.4	\$ (3.6)	\$ (3.2)
Net depreciation on available-for-sale securities	(28.8)	(20.1)	(48.9)
Net effect on value of business acquired, and on policy liabilities	15.4	-	15.4
Benefit for deferred federal income taxes	4.7	7.0	11.7
	(8.7)	(13.1)	(21.8)
Net depreciation, end of year	\$ (8.3)	\$ (16.7)	\$ (25.0)

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7. INVESTMENTS (Continued)

D. Other-Than-Temporary Impairment

The table below presents a rollforward of the cumulative credit loss component of OTTI impairment losses recognized in earnings on fixed maturity securities still held by the Company at December 31, 2010 and 2009, respectively, for which a portion of the OTTI losses were recognized in other comprehensive income:

	<u>2010</u>	<u>2009</u>
Balance at beginning of year	\$ 5.0	\$ -
Credit loss component of OTTI loss not reclassified to other comprehensive income in the cumulative effect transition adjustment	-	10.3
Additions:		
Initial impairments - credit loss OTTI recognized on securities not previously impaired	-	0.5
Additional impairments - credit loss OTTI recognized on securities previously impaired	-	0.2
Reductions:		
Due to sales (or maturities, pay downs or prepayments) during the period of securities previously credit loss OTTI impaired	(1.3)	(6.0)
Balance at end of year	<u>\$ 3.7</u>	<u>\$ 5.0</u>

E. Securities in a Continuous Unrealized Loss Position

The following table provides information about the Company's available-for-sale fixed maturities that have been continuously in an unrealized loss position.

December 31, 2010 (In millions, except number of securities)	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Number of Securities With Gross Unrealized Losses</i>
Investment grade fixed maturities ⁽¹⁾ :			
0-12 months	\$ 16.5	\$ 413.0	69
Greater than 12 months	9.2	43.8	7
Total investment grade fixed maturities	<u>\$ 25.7</u>	<u>\$ 456.8</u>	<u>76</u>
Below investment grade fixed maturities:			
0-12 months	\$ 2.4	\$ 73.6	16
Greater than 12 months	3.6	17.5	10
Total below-investment-grade fixed maturities	<u>6.0</u>	<u>91.1</u>	<u>26</u>
Total fixed maturities	<u>\$ 31.7</u>	<u>\$ 547.9</u>	<u>102</u>

⁽¹⁾ Includes gross unrealized losses for investment grade fixed maturity obligations of the U.S. Treasury, U.S. government and agency securities, states, and political subdivisions of \$19.5 million at December 31, 2010.

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7. INVESTMENTS (Continued)

E. Securities in a Continuous Unrealized Loss Position (Continued)

December 31, 2009 (In millions, except number of securities)	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Number of Securities With Gross Unrealized Losses</i>
Investment grade fixed maturities ⁽¹⁾ :			
0-12 months	\$ 41.9	\$ 754.4	78
Greater than 12 months	1.5	35.2	15
Total investment grade fixed maturities	<u>\$ 43.4</u>	<u>\$ 789.6</u>	<u>93</u>
Below investment grade fixed maturities:			
0-12 months	\$ 4.7	\$ 59.7	17
Greater than 12 months	2.7	12.4	3
Total below-investment-grade fixed maturities	<u>7.4</u>	<u>72.1</u>	<u>20</u>
Total fixed maturities	<u>\$ 50.8</u>	<u>\$ 861.7</u>	<u>113</u>

⁽¹⁾ Includes gross unrealized losses for investment grade fixed maturity obligations of the U.S. Treasury, U.S. government and agency securities, states, and political subdivisions of \$35.9 million at December 31, 2009.

F. Variable Interest Entity

During 2010, the Company, through its subsidiary FAFLIC, held a GIC through Allmerica Global Funding (“AGF”), a Cayman Islands based entity. AGF was formed as a special purpose vehicle solely for the purposes of issuing debt instruments to third party investors and used the proceeds to purchase investment contracts from the Company. There was one medium term note outstanding as of December 31, 2010 and December 31, 2009 for \$16.0 million and \$16.6 million respectively with a 6.0% fixed rate, issued in June 1999, and maturing in April 2011. AGF is a VIE and is consolidated within the Company as the Company is the primary beneficiary.

G. Other

As of December 31, 2010 and 2009, the Company’s only investment at fair value that exceeded 10% of shareholder’s equity was in U.S. Treasuries for \$369.7 million and \$497.0 million, respectively.

8. INVESTMENT INCOME AND GAINS AND LOSSES

A. Net Investment Income

The components of net investment income were as follows:

For the Years Ended December 31,	2010	2009	2008
(In millions)			
Fixed maturities - interest and other income	\$ 227.6	\$ 206.5	\$ 53.4
Fixed maturities - change in fair value on trading securities	7.8	27.5	-
Equity securities	-	3.9	8.0
Policy loans	21.7	19.4	5.2
Modco interest income	70.3	68.7	62.7
Short-term investments and miscellaneous (loss) / income	(7.1)	2.7	(0.5)
Gross investment income	<u>320.3</u>	328.7	128.8
Less modco interest expense	(122.6)	-	-
Less investment expenses	(6.3)	(5.4)	(3.2)
Net investment income	<u>\$ 191.4</u>	<u>\$ 323.3</u>	<u>\$ 125.6</u>

The Company had no fixed maturities on non-accrual status at December 31, 2010, 2009 or 2008. The Company had no fixed maturities which were non-income producing at December 31, 2010, 2009 or 2008.

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8. INVESTMENT INCOME AND GAINS AND LOSSES (Continued)

B. Net Realized Investment Gains and Losses

Net realized gains and (losses) on investments were as follows:

For the Years Ended December 31,	2010	2009	2008
(In millions)			
Available-for-sale fixed maturities	\$ 94.2	\$ 22.5	\$ (38.0)
Trading fixed maturities	1.1	7.3	-
Equity securities	-	(9.7)	(14.5)
Other investments	(4.3)	2.5	2.9
Net realized investment gains/(losses)	\$ 91.0	\$ 22.6	\$ (49.6)

The proceeds from voluntary sales of available-for-sale fixed maturities and the gross realized gains and gross realized losses on those sales were as follows:

For the Years Ended December 31,	<i>Proceeds from</i> <i>Voluntary</i> <i>Sales</i>	<i>Gross</i> <i>Gains</i>	<i>Gross</i> <i>Losses</i>
(In millions)			
2010			
Fixed maturities	\$ 1,683.3	\$ 105.6	\$ 12.8
2009			
Fixed maturities	\$ 1,354.8	\$ 57.3	\$ 38.5
2008			
Fixed maturities	\$ 1,550.8	\$ 12.6	\$ 50.6

The Company recognized other-than-temporary impairments on fixed maturities of \$0.0 million and \$7.4 million in 2010 and 2009, respectively. There were no other-than-temporary impairments on equity securities in 2010 and 2009, respectively. In 2008, the Company recognized other-than-temporary impairments on fixed maturities of \$27.5 million and other-than-temporary impairments on equity securities of \$14.5 million.

C. Other Comprehensive Income Reconciliation

The following table provides a reconciliation of gross unrealized gains/(losses) to the net balance shown in the Consolidated Statements of Comprehensive Income/(Loss):

For the Years Ended December 31,	2010	2009	2008
(In millions)			
Unrealized appreciation/(depreciation) on available-for-sale securities:			
Unrealized holding gains/(losses) arising during period (net of income tax expense)/benefit of \$(47.9), \$(58.2) and \$30.2 million in 2010, 2009 and 2008, respectively)	\$ 88.8	\$ 108.0	\$ (56.1)
Less: reclassification adjustment for gains/(losses) included in net income (net of income tax expense/(benefit) of \$33.0, \$4.5 and \$(18.5) million in 2010, 2009 and 2008, respectively)	61.2	8.5	(34.3)
Total available-for-sale securities	27.6	99.5	(21.8)
Net unrealized appreciation/(depreciation) on available-for-sale securities	\$ 27.6	\$ 99.5	\$ (21.8)

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the amount 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 (the exit price).

The best evidence of fair value is a quoted price in an active market. If listed prices or quotations are not available, fair value is determined by reference to prices of similar instruments and quoted prices or recent prices in less active markets.

U.S. GAAP has a three-level fair value hierarchy for disclosure of fair value measurements. The fair value hierarchy prioritizes inputs to the valuation techniques used to measure fair value, giving the highest priority to level 1 inputs and the lowest priority to level 3 inputs. A financial instrument's level in the fair value hierarchy is based on the lowest level of any input that is significant to fair value measurement. The three levels of the fair value hierarchy are described below:

Basis of Fair Value Measurement

- Level 1 Inputs are unadjusted quoted prices in active markets to which the Company had access to at the measurement date for identical, unrestricted assets and liabilities.
- Level 2 Inputs to valuation techniques are observable either directly or indirectly.
- Level 3 One or more inputs to valuation techniques are significant and unobservable.

The following tables set forth by level within the fair value hierarchy financial assets and liabilities accounted for at fair value under ASC 820 as of December 31, 2010 and 2009. As required by ASC 820, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

December 31, 2010 (in millions)	Level 1	Level 2	Level 3	Total
Financial Assets				
Available-for-sale fixed maturities				
U.S. Treasury securities and U.S. Government and agency securities	\$ 367.4	\$ 98.8	\$ -	\$ 466.2
States and political subdivisions	-	295.6	-	295.6
Foreign governments	2.0	-	-	2.0
Corporate fixed maturities	-	1,080.4	0.3	1,080.7
Structured securities	-	999.8	-	999.8
Total available-for-sale fixed maturities	369.4	2,474.6	0.3	2,844.3
Trading fixed maturities				
U.S. Treasury securities and U.S. Government and agency securities	2.3	2.7	-	5.0
States and political subdivisions	-	29.2	-	29.2
Corporate fixed maturities	-	302.4	-	302.4
Structured securities	-	189.8	-	189.8
Total trading fixed maturities	2.3	524.1	-	526.4
Equity securities	0.1	-	-	0.1
Derivative instruments receivable				
Interest rate contracts	-	11.5	-	11.5
Foreign currency contracts	-	1.6	-	1.6
Equity market contracts	30.5	11.2	1.2	42.9
Embedded derivative within asset host contract	-	-	59.0	59.0
Total derivative instruments receivable	30.5	24.3	60.2	115.0
Separate account assets	4,023.6	-	-	4,023.6
Total assets at fair value	\$ 4,425.9	\$ 3,023.0	\$ 60.5	\$ 7,509.4

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

December 31, 2010 (in millions)	Level 1	Level 2	Level 3	Total
Financial Liabilities				
Derivative instruments payable				
Credit contracts	\$ -	\$ 0.6	\$ 0.5	\$ 1.1
Embedded derivative within liability host contract	-	-	96.9	96.9
Total derivative instruments payable	-	0.6	97.4	98.0
Closed Block policy liabilities	-	-	688.3	688.3
Total liabilities at fair value	\$ -	\$ 0.6	\$ 785.7	\$ 786.3
December 31, 2009 (in millions)				
	Level 1	Level 2	Level 3	Total
Financial Assets				
Available-for-sale fixed maturities				
U.S. Treasury securities and U.S. Government and agency securities	\$ 483.9	\$ 217.1	\$ -	\$ 701.0
States and political subdivisions	-	165.1	-	165.1
Foreign governments	13.7	19.3	-	33.0
Corporate fixed maturities	-	1,288.7	0.3	1,289.0
Structured securities	-	723.7	42.6	766.3
Total available-for-sale fixed maturities	497.6	2,413.9	42.9	2,954.4
Trading fixed maturities				
U.S. Treasury securities and U.S. Government and agency securities	13.0	2.7	-	15.7
States and political subdivisions	-	27.9	-	27.9
Corporate fixed maturities	-	222.7	-	222.7
Structured securities	-	158.2	-	158.2
Total trading fixed maturities	13.0	411.5	-	424.5
Equity securities	0.1	-	-	0.1
Derivative instruments receivable	24.5	63.4	61.4	149.3
Separate account assets	4,186.5	-	-	4,186.5
Total assets at fair value	\$ 4,697.2	\$ 2,913.3	\$ 104.3	\$ 7,714.8
Financial Liabilities				
Derivative instruments payable	\$ -	\$ 2.2	\$ 135.2	\$ 137.4
Closed Block policy liabilities	-	-	684.1	684.1
Total liabilities at fair value	\$ -	\$ 2.2	\$ 819.3	\$ 821.5

Cash Instruments

The Company's cash instruments are generally classified within level 1 or level 2.

Level 1 Cash Instruments:

Level 1 cash instruments include U.S. Treasury, agency and government guaranteed fixed maturity securities, foreign government securities and mutual funds held in separate accounts. Level 1 instruments are valued using quoted market prices for identical unrestricted instruments in active markets.

Level 2 Cash Instruments:

Level 2 cash instruments include fixed maturity securities and equity securities for which quoted market prices from active markets are not available. Level 2 cash instruments are priced using observable inputs, which can be verified to quoted prices, recent trading activity for identical or similar instruments, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations and the relationship of recent market activity to the prices provided from alternative pricing sources. The Company does not make valuation adjustments to level 2 instruments.

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

Level 3 Cash instruments:

Level 3 cash instruments have one or more significant valuation inputs that are not observable. Absent evidence to the contrary, level 3 investments are initially valued at transaction price, which is considered to be the best initial estimate of fair value. Subsequently, the Company uses other methodologies to determine fair value, which vary based on the type of instrument.

Valuation inputs and assumptions are changed when corroborated by substantive observable evidence, including values realized on sales of level 3 assets.

Structured securities. In 2009, certain structured securities were valued using the market approach. Valuation was based primarily on matrix pricing or other similar techniques that utilized inputs that were unobservable. At December 31, 2010, these securities were valued using observable inputs and, accordingly, are included in level 2.

Derivative Contracts

Level 1 Derivative Contracts:

Level 1 derivatives include exchange traded futures as they are actively traded and are valued at their quoted market price.

Level 2 Derivative Contracts:

Level 2 derivatives include most types of derivative instruments utilized by the Company and include derivatives for which all significant valuation inputs are corroborated by market evidence. These derivative contracts are principally valued using an income approach. The Company calculates the fair value of derivative assets by discounting future cash flows at a rate that incorporates counterparty credit spreads and the fair value of derivative liabilities by discounting future cash flows at a rate that incorporates the Company's own credit spreads.

When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence.

Interest rate derivatives. Valuations for non-option based derivatives are based on present value techniques, which utilize significant inputs that may include the swap yield curve, LIBOR basis curves, and repurchase rates. Valuations for option based derivatives are based on option pricing models, which utilize significant inputs that may include the swap yield curve, LIBOR basis curves, and interest rate volatility.

Foreign currency derivatives. Prices for currency derivatives based on the exchange rates of leading industrialized nations, including those with longer tenors, are generally transparent.

Equity market derivatives. Exchange traded and OTC equity derivatives generally have observable market prices, except for contracts with long tenors or reference prices that differ significantly from current market prices.

Credit derivatives. Credit derivatives are valued using inputs that may include credit correlation, repurchase rates and the extrapolation beyond observable limits of the swap yield curve and credit curves.

Level 3 Derivative Contracts:

Level 3 derivatives include credit derivatives and equity market derivatives, which are valued as described in level 2 but have significant unobservable inputs and also includes embedded derivatives which are principally valued using an income approach as explained in detail below. For level 3 equity derivatives, significant level 3 inputs generally include equity volatility inputs for options that are very long-dated. Valuations are based on present value techniques, which may utilize the swap yield curve and the spot equity and bond index level with significant unobservable inputs.

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

Fair Value of Other Assets and Liabilities

Embedded derivatives related to guaranteed minimum benefits

These embedded derivatives are principally valued using an income approach. Valuations are based on option pricing techniques, which utilize significant inputs that may include swap yield curve and implied volatilities. These embedded derivatives result in Level 3 classification because one or more of the significant inputs are not observable in the market or cannot be derived principally from, or corroborated by, observable market data. Significant unobservable inputs generally include the extrapolation beyond observable limits of the swap yield curve and implied volatilities, actuarial assumptions for policyholder behavior and mortality and the potential variability in policyholder behavior and mortality, nonperformance risk, counterparty credit spreads and cost of capital for purposes of calculating the risk margin.

Closed Block Policy Liabilities

The fair value of the Closed Block policy liabilities is calculated as the sum of the fair value of Closed Block assets, an adjustment to the fair value of Closed Block assets for non-performance risk, fair value of the Closed Block maintenance expenses, and a risk margin based on the cost of holding capital to back the Closed Block.

The estimated fair value for the provision for maintenance expense is determined by calculating the annual cost associated with administering the applicable policies, including servicing costs as well as provisions for overhead, both adjusted for inflation. The annual cost is discounted at a fair value rate, approximating risk free, with a provision for non-performance risk.

The estimated fair value for the provision for cost of capital is determined by calculating an annual cost inherent in having to hold risk capital to back the business. This amount is generally determined by using standard regulatory metrics to determine how much capital should be held. The amount of capital held is reduced by the net investment income that would be earned from the assets backing the capital. The annual cost is discounted at a rate determined to approximate a market participant's hurdle rate.

As the liability cash flows in total are based on the asset cash flows, the basic value of the liabilities are equal to the fair value of the Closed Block assets. By utilizing market participant assumptions, the Closed Block policy liabilities contain unobservable inputs resulting in a fair value measurement of level 3.

Transfers into or out of Level 3:

Overall, transfers into and/or out of Level 3 are attributable to a change in the observability of inputs. Assets and liabilities are transferred into Level 3 when a significant input cannot be corroborated with market observable data. This occurs when market activity decreases significantly and underlying inputs cannot be observed, current prices are not available, and/or when there are significant variances in quoted prices, thereby affecting transparency. Assets and liabilities are transferred out of Level 3 when circumstances change such that a significant input can be corroborated with market observable data. This may be due to a significant increase in market activity, a specific event, or one or more significant input(s) becoming observable. Transfers into and/or out of any level are assumed to occur at the beginning of the period. Accordingly, the tables do not include gains or losses that were reported in level 3 in prior periods for financial instruments that were transferred out of level 3 prior to the end of the period.

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

The tables below sets forth a summary of changes in the fair value of the Company's level 3 financial assets and liabilities for the years ended December 31, 2010 and 2009. The tables reflects gains and losses for the full year for all financial assets and liabilities categorized as level 3 as at December 31, 2010 and December 31, 2009.

Year ended December 2010	Balance, beginning of year	Net realized gains/ (losses)	Net unrealized gains/ (losses) relating to instruments still held at the reporting date	Net purchases, issuances and settlements	Net transfers in and/or out of level 3	Balance, end of year
(In millions)						
Financial Assets						
Available-for-sale fixed maturities						
Corporate fixed maturities	\$ 0.3	\$ -	\$ -	\$ -	\$ -	\$ 0.3
Structured securities	42.6	-	-	-	(42.6)	-
Derivative contracts						
Foreign currency	2.1	-	-	-	(2.1)	-
Equity market	-	(0.7)	-	1.9	-	1.2
Embedded derivative	59.3	-	(0.3)	-	-	59.0
Total derivative contracts	61.4	(0.7)	(0.3)	1.9	(2.1)	60.2
Total assets	\$ 104.3	\$ (0.7)	\$ (0.3)	\$ 1.9	\$ (44.7)	\$ 60.5
Financial Liabilities						
Closed Block policy liabilities	\$ 684.1	\$ -	\$ -	\$ 4.2 ⁽¹⁾	\$ -	\$ 688.3
Derivative contracts						
Credit	-	-	-	-	0.5	0.5
Embedded derivative	135.2	(28.0)	(44.9)	34.6	-	96.9
Total derivative contracts	135.2	(28.0)	(44.9)	34.6	0.5	97.4
Total liabilities	\$ 819.3	\$ (28.0)	\$ (44.9)	\$ 38.8	\$ 0.5	\$ 785.7

⁽¹⁾ Included in the change in the Closed Block policy liabilities of \$4.2 million is \$5.1 million of market appreciation on the closed Block investment portfolio offset by maintenance expenses of \$1.1 million and a decrease in cost of capital of \$0.2 million as of December 31, 2010.

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

Year ended December 2009	Balance, beginning of year	Purchase accounting adjustments	Net realized gains/ (losses)	Net unrealized gains/ (losses) relating to instruments still held at the reporting date	Net purchases, issuances and settlements	Net transfers in and/or out of level 3	Balance, end of year
(In millions)							
Financial Assets							
Available-for-sale fixed maturities							
Corporate fixed maturities	\$ 1.7	\$ 3.5	\$ -	\$ -	\$ (3.5)	\$ (1.4)	\$ 0.3
Mortgage-backed and asset-based securities	-	2.3	-	1.1	39.2	-	42.6
Derivative contracts	-	-	-	61.4	-	-	61.4
Total assets	\$ 1.7	\$ 5.8	\$ -	\$ 62.5	\$ 35.7	\$ (1.4)	\$ 104.3
Financial Liabilities							
Closed Block policy liabilities							
liabilities	\$ -	\$ 663.5	\$ -	\$ -	\$ 20.6 ⁽¹⁾	\$ -	\$ 684.1
Derivative contracts	56.3	-	(0.1)	(56.2)	135.2	-	135.2
Total liabilities	\$ 56.3	\$ 663.5	\$ (0.1)	\$ (56.2)	\$ 155.8	\$ -	\$ 819.3

(1) Included in the change in the Closed Block policy liabilities of \$20.6 million is \$24.7 million of market appreciation on the Closed Block investment portfolio offset by decreases in maintenance expenses of \$2.8 million and cost of capital of \$1.3 million as of December 31, 2009.

ASC 825, "Disclosures about Fair Value of Financial Instruments," as amended by ASC 820, requires disclosure of fair value information about certain financial instruments (insurance contracts, real estate, goodwill and taxes are excluded) for which it is practicable to estimate such values, whether or not these instruments are included in the balance sheet. The fair values presented for certain financial instruments are estimates which, in many cases, may differ significantly from the amounts which could be realized in an orderly transaction.

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:

Policy Loans

For policy loans with fixed interest rates, estimated fair values are determined by using discounted cash flow models applied to groups of similar policy loans determined by the nature of the underlying insurance liabilities. Cash flow estimates are developed by applying a weighted-average interest rate to the outstanding principal balance of the respective group of policy loans and an estimated average maturity determined through experience studies of the past performance of policyholder repayment behavior for similar loans. These cash flows are discounted using current risk-free interest rates with no adjustment for borrower credit risk as these loans are fully collateralized by the cash surrender value of the underlying insurance policy. The estimated fair value for policy loans with variable interest rates approximates carrying value due to the absence of borrower credit risk and the short time period between interest rate resets, which presents minimal risk of a material change in estimated fair value due to changes in market interest rates.

Securities sold under agreements to repurchase

During March of 2010, the Company entered into a series of third party repurchase agreements. The notional value as of December 31, 2010 was approximately \$89.6 million. The Company posted \$89.6 million in Treasury securities as collateral for these transactions. Fair value is estimated based on expected future cash flows and interest rates.

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9. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

Investment Contracts (Without Mortality Features)

Fair value of liabilities under supplementary contracts without life contingencies are estimated based on current fund balances and fair value of other individual contract funds represent the present value of future policy benefits.

Trust Instruments Supported by Funding Obligations

Fair values are estimated using discounted cash flow calculations using current interest rates for similar contracts with maturities consistent with those remaining for the contracts being valued.

The following presents carrying amounts and fair values of the Company's financial instruments not carried at fair value as of December 31, 2010 and 2009:

December 31,	2010		2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
(In millions)				
Financial Assets				
Policy loans	\$ 306.4	\$ 369.3	\$ 320.3	\$ 368.1
	\$ 306.4	\$ 369.3	\$ 320.3	\$ 368.1
Financial Liabilities				
Securities sold under agreements to repurchase	\$ 89.6	\$ 89.6	\$ -	\$ -
Supplementary contracts without life contingencies	7.4	7.4	36.4	36.4
Trust instruments supported by funding obligations	16.0	17.6	16.6	18.7
Other individual contract deposit funds	106.1	106.1	115.2	115.2
	\$ 219.1	\$ 220.7	\$ 168.2	\$ 170.3

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10. CLOSED BLOCK

Summarized financial information of the Closed Block is as follows:

Balance Sheets

December 31	2010	2009
(In millions)		
ASSETS		
Investments:		
Trading fixed maturities at fair value (amortized cost of \$491.2 and \$397.2, respectively)	\$ 526.4	\$ 424.5
Policy loans	96.8	102.5
Cash and cash equivalents	3.4	92.5
Accrued investment income	9.6	9.0
Deferred federal income taxes	20.6	17.8
Other assets	1.5	1.9
Total assets	<u>\$ 658.3</u>	<u>\$ 648.2</u>
LIABILITIES		
Policy liabilities and accruals at fair value	\$ 596.9	\$ 592.0
Policyholder dividends obligation at fair value ⁽¹⁾	77.9	78.6
Policyholder dividends payable at fair value ⁽¹⁾	13.5	13.5
Other liabilities	7.8	3.8
Total liabilities	<u>\$ 696.1</u>	<u>\$ 687.9</u>
Excess of Closed Block liabilities over assets designated to the Closed Block and maximum future earnings to be recognized from Closed Block assets and liabilities	<u>\$ 37.8</u>	<u>\$ 39.7</u>

⁽¹⁾ Included within contractholder deposit funds and other policy liabilities in the accompanying Consolidated Balance Sheets.

Statements of Income

For the Years Ended December 31	2010	2009
(In millions)		
REVENUES		
Premiums and other income	\$ 19.4	\$ 22.3
Net investment income	49.5	67.2
Net realized investment gains	1.1	7.3
Total revenues	<u>70.0</u>	<u>96.8</u>
BENEFITS AND EXPENSES		
Policy benefits	68.3	92.3
Policy acquisition and other expenses	0.4	0.4
Total benefits and expenses	<u>68.7</u>	<u>92.7</u>
Net contribution from the Closed Block	<u>\$ 1.3</u>	<u>\$ 4.1</u>

Many expenses related to Closed Block operations are charged to operations outside the Closed Block; accordingly, the contribution from the Closed Block does not represent the actual profitability of the Closed Block operations. Operating costs and expenses outside of the Closed Block are, therefore, disproportionate to the business outside the Closed Block.

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11. FEDERAL INCOME TAXES

Provision for Income Taxes

Income taxes are provided for using the asset and liability method under which deferred tax assets and liabilities are recognized for temporary differences between the financial reporting and tax bases of assets and liabilities. The Company reports interest expense related to income tax matters in Federal income tax expense/(benefit), and income tax penalties in other operating expenses in the Consolidated Statements of Income.

The Company is expected to file a consolidated tax return with FAFLIC for the period January 1, 2010 through December 31, 2010. The Company's tax return is eligible for consolidation into Goldman Sachs for calendar year end 2011. Any net operating loss carryforwards or foreign tax credits from prior to the acquisition date of December 30, 2005 can only be used against the income of the Company.

FAFLIC's tax return is ineligible for consolidation with Goldman Sachs until calendar year end 2015. Due to the purchase of FAFLIC, the capital loss carryforward acquired is subject to I.R.C Section 382, which provides an annual limit on utilization and can only be used against the income of FAFLIC.

The tables below present the components of the provision/(benefit) for taxes and a reconciliation of the U.S. federal statutory income tax rate to the Company's effective income tax rate.

For the Years Ended December 31,	2010	2009
(In millions)		
Federal income tax expense		
Current	\$ -	\$ -
Deferred	42.7	6.3
Total	\$ 42.7	\$ 6.3

For the Years Ended December 31,	2010	2009	2008
(In millions)			
Expected federal income tax expense	\$ 56.7	\$ 34.2	\$ (0.2)
Prior years' federal income tax adjustment	(2.9)	-	(0.6)
Dividend received deduction	(4.5)	(3.8)	(5.2)
Tax credits	(0.5)	-	(0.7)
Valuation allowance	(6.1)	(24.1)	17.2
Other, net	-	-	0.3
Federal income tax expense	\$ 42.7	\$ 6.3	\$ 10.8

Deferred Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the financial reporting and tax bases of assets and liabilities. These temporary differences result in taxable or deductible amounts in future years and are measured using the tax rates and laws that will be in effect when such differences are expected to reverse. Valuation allowances are established to reduce deferred tax assets to the amount that more likely than not will be realized.

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11. FEDERAL INCOME TAXES (Continued)

Following are the components of the Company's deferred tax assets and liabilities.

December 31,	2010	2009
(In millions)		
Deferred tax asset		
Insurance reserves	\$ 69.0	\$ 90.0
Sec. 848 capitalization	46.7	62.6
Tax credit carryforwards	11.0	9.5
Loss carryforwards	140.5	162.6
Ceding commission	13.4	17.9
Accrued policyholder dividends	4.7	4.7
Deferred compensation	0.1	0.2
Other, net	-	3.9
Subtotal deferred tax asset	<u>285.4</u>	<u>351.4</u>
Valuation allowance	(6.1)	(12.2)
Total deferred tax asset, net	<u>\$ 279.3</u>	<u>\$ 339.2</u>
Deferred tax liability		
VOBA/DAC	\$ (101.3)	\$ (129.9)
Investments, net	(76.4)	(61.8)
Fair value adjustment - Closed Block	(12.3)	(9.6)
Other, net	(8.9)	-
Total deferred tax liability	<u>(198.9)</u>	<u>(201.3)</u>
Total deferred tax asset, net	<u>\$ 80.4</u>	<u>\$ 137.9</u>

The Company has recorded a valuation allowance against tax benefits from tax credit carryforwards. The change in the valuation allowance was due to the removal of a partial valuation allowance of \$6.1 million against the capital loss carryforward as it is the Company's opinion that it is more likely than not that these deferred tax assets will be fully realized. In management's judgment, the remaining gross deferred tax asset will more likely than not be realized through reductions of future taxes, except as otherwise noted. This conclusion is based primarily on a review of expected taxable income and considers all available evidence, both positive and negative.

At December 31, 2010, the Company has foreign tax credit carryforwards of \$11.0 million which will expire beginning in 2013. At December 31, 2010, the Company has net operating loss carryforwards of \$136.3 million and capital loss carryforwards of \$4.2 million, which begin to expire in 2017 and 2013, respectively. All tax credits and net operating loss carryforwards generated prior to 2006 are subject to annual limitations on utilization. This includes \$6.1 million of foreign tax credits and \$35.8 million of net operating carryforwards.

Unrecognized Tax Benefits

The Company recognizes tax positions in the financials statements only when it is more likely than not that the position will be sustained on examination by the relevant taxing authority based on the technical merits of the position. A position that meets this standard is measured at the largest amount of benefit that will more likely than not be realized on settlement. A liability is established for differences between position taken in a tax return and amounts recognized in the financial statements. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will impact the Company's financial condition, results of operations, or cash flows. As of December 31, 2010 and December 31, 2009, the Company did not record a liability related to accounting for uncertainty in income taxes.

Regulatory Tax Examinations

The Company's federal income tax returns are routinely audited by the IRS, and when appropriate, provisions are made in the financial statements in anticipation of the results of these audits. THG has agreed to indemnify the Company and Goldman Sachs with respect to tax liabilities for periods before the acquisition as provided in the Transaction. However, the tax attributes carried over from THG are not guaranteed under the Transaction, and accordingly, such attributes may be adjusted in the future.

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12. DIVIDEND RESTRICTIONS

Massachusetts has enacted laws governing the payment of dividends to shareholders by insurers, which affect the dividend paying ability of the Company. The Company cannot pay any dividend without first obtaining written approval from the Massachusetts Commissioner of Insurance.

The Company must meet minimum capital and surplus requirements under a risk-based capital (“RBC”) formula. RBC is the standard measurement of an insurance company’s required capital on a statutory basis. It is based on a formula calculated by applying factors to various assets, premium and statutory reserve items. The formula takes into account the risk characteristics of the insurer, including asset risk, insurance risk, interest rate risk and business risk. Regulatory action is tied to the amount of a company’s surplus deficit under the RBC formula. Goldman Sachs has agreed with the Commissioner to continue the previous THG commitment to maintain total adjusted capital levels at a minimum of 100% of the Company’s Company Action Level as determined under the risk-based capital formula, which was \$75.0 million and \$68.5 million at December 31, 2010 and 2009, respectively. Total adjusted capital for life insurance companies is defined as statutory capital and surplus, plus asset valuation reserve, plus 50% of dividends apportioned for payment and was \$630.0 million and \$635.3 million at December 31, 2010 and 2009, respectively, for the Company.

The Company declared dividends payable to its stockholder of record, Goldman Sachs of \$250.0 million in 2010 which was paid in January 2011. The Company declared and paid dividends to Goldman Sachs of \$60.0 million in 2009.

13. VALUE OF BUSINESS ACQUIRED

The changes in VOBA for the years ended December 31 were as follows:

(In millions)	<u>2010</u>	<u>2009</u>
Balance at January 1	\$ 30.3	\$ 146.5
Amount recorded due to purchase accounting ⁽¹⁾	-	(45.6)
Cumulative effect of change in accounting principle, net of tax	-	(1.2)
Reinsurance treaty impacts	-	(76.5)
Amortized to expense during the year	(2.9)	23.8
Adjustment for unrealized investment losses during the year	(0.1)	(16.7)
Balance at December 31	<u>\$ 27.3</u>	<u>\$ 30.3</u>

⁽¹⁾ Refer to Footnote 4 - Purchase Accounting for further discussion on purchase accounting adjustments.

Estimated future amortization of VOBA as of December 31, 2010 is as follows:

(In millions)	
2011	\$ 3.7
2012	3.1
2013	2.7
2014	2.4
2015	2.2
2016 and thereafter	13.2
Total	<u>\$ 27.3</u>

14. REINSURANCE

The Company seeks to diversify risk and limit its overall financial exposure by reinsuring certain levels of risk in various areas of exposure through acquisition and cessions with other insurance companies or reinsurers. In addition, consistent with the overall business strategy, the Company assumes certain policy risks written by other insurance companies on a coinsurance and modified coinsurance basis. Under a coinsurance arrangement, depending upon the terms of the contract, the reinsurer may share in the risk of loss due to mortality or morbidity, lapses, and the investment risk, if any, inherent in the underlying policy. Modified coinsurance differs from coinsurance in that the assets supporting the reserves are retained by the ceding company while the risk is transferred to the reinsurer.

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14. REINSURANCE (Continued)

On December 31, 2009, the Company ceded via coinsurance and modified coinsurance, 100% of its variable annuity business to an affiliate, Arrow acting on behalf of and for the benefit of a segregated account established by Arrow. Upon execution of the treaty, the Company considered in its reinsurance costs \$76.5 million of VOBA and \$61.7 million of DAC associated with the variable annuity business; a net \$55.0 million was written off. The Company has evaluated the applicability of ASC 944-815-15 to its modified coinsurance agreement with Arrow. An embedded derivative requiring bifurcation exists and a liability of \$96.9 million and \$135.2 million is reflected on the Consolidated Balance Sheets as of December 31, 2010 and 2009, respectively. As of December 31, 2010 and December 31, 2009, the assumed reserves under this contract were \$2.1 billion respectively. In conjunction with this agreement, the Company and Arrow acting on behalf of and for the benefit of a segregated account established by Arrow entered into a trust agreement, whereby Arrow established a trust account for the sole use and benefit of the Company. The Company may withdraw funds from the trust account as reimbursements from Arrow for reinsured activity. As of December 31, 2010 and 2009, the trust account held \$99.6 million and \$70.0 million, respectively, of cash equivalents and fixed maturities.

On December 18, 2009, the Company entered into an Assumption Reinsurance Agreement with MetLife where the Company will assumption reinsure certain individual disability income insurance policies to MetLife. These policies are currently 100% coinsured with MetLife. The Company paid \$5.0 million to MetLife in connection with the transaction. Reinsurance recoverables related to this agreement were \$223.2 million and \$231.4 million at December 31, 2010 and 2009, respectively.

On April 1, 2009, the Company assumed on a 100% coinsurance basis the life and fixed annuity blocks of of the life insurance subsidiaries of UAC. Under the coinsurance agreement, the Company assumed \$527.2 million of reserves and paid the collective cedants \$77.6 million in ceding commission. Subsequently, on October 29, 2010 and December 8, 2010, the Company assigned all its rights, titles, interests and privileges and certain duties and obligations related to a block of fixed annuity contracts assumed from the subsidiaries of UAC to Athene, a Bermuda domiciled reinsurance company. Upon closing of the transaction, the Company paid a total novation fee of \$1.2 million to UAC and its subsidiary, American Progressive. As of December 31, 2010 and 2009, the assumed reserves under the existing contract were \$312.0 million and \$509.7 million, respectively.

On March 31, 2009, the Company entered into a coinsurance and modified coinsurance agreement with Lincoln National to reinsure an in-force block of universal life and variable universal life insurance policies. Effective April 1, 2010, the agreement was amended to recognize the cession of all mortality risk to an affiliate of Lincoln, thereby reducing mortality exposure for the Company. Under the coinsurance and modified coinsurance agreement, the Company assumed \$974.6 million in reserves and paid the cedant approximately \$204.5 million in ceding commission. As of December 31, 2010 and 2009, the assumed reserves under this contract were \$867.6 million and \$943.9 million, respectively.

On January 2, 2009, coincident with the purchase of the Company's subsidiary, FAFLIC, referenced in Note 5 – Significant Transactions, FAFLIC and The Hanover Insurance Company (“HIC”) entered into a reinsurance contract whereby HIC reinsured FAFLIC's discontinued accident and health insurance business through a 100% coinsurance agreement. This agreement totaled \$119.5 million in net statutory liabilities. An equal amount of assets were also transferred as part of this agreement. Reinsurance recoverable related to this agreement were \$132.2 million and \$139.6 million at December 31, 2010 and 2009, respectively.

On January 1, 2008, the Company reinsured a book of business from FML on an assumption reinsurance basis comprising primarily whole, term and universal life insurance policies. FML was in rehabilitation under the governance of the Commonwealth of Pennsylvania, and the Company has no responsibility for the dissolution or future state of FML and any of its remaining legal entity obligations or liabilities. As part of this transaction, the Company paid a ceding commission of \$4.3 million and assumed general account reserves of \$700.0 million.

During the first quarter of 2008, the Company effectively ceded the entire FML block of business to its affiliate, Columbia Capital Life Reinsurance Company (“Columbia”). In consideration of Columbia's assumption of the business, the Company received a ceding commission of \$4.1 million. As of December 31, 2010 and 2009, the Company ceded reserves of \$553.6 million and \$587.1 million, respectively.

The Company assumed on a modified coinsurance basis 100% of the variable annuity business of Protective. As of December 31, 2010 and 2009, the assumed reserves under this contract were \$1.2 billion, respectively.

The Company entered into a coinsurance agreement to cede 100% of its deferred fixed annuity insurance business to its affiliate, Columbia. As of December 31, 2010 and 2009 the Company ceded reserves of \$35.5 million and \$37.6 million.

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14. REINSURANCE (Continued)

On May 25, 2007 the Company entered into an agreement, retroactive to January 1, 2007, to assume 8% of the variable annuity products sold by Pacific Life in 2007. The base annuities were assumed on a modified coinsurance basis and the benefits provided via riders were assumed on a coinsurance basis. In February 2008, the Pacific Life contract was recaptured retroactive to January 1, 2008. Certain derivative options hedging the rider benefits of this treaty were disposed. The recapture of the Pacific Life block resulted in a reinsurance recapture fee of \$25.5 million with a subsequent reduction in policyholder liabilities and DAC. Due to the accounting treatment for acquiring this block of business, the recapture fee was bifurcated between the May 2007 and post May 2007 components, with the latter portion recognized through the Consolidated Statements of Income.

Historically, the Company maintained other reinsurance treaties including the cession of non core traditional life and health business, the largest being a universal life insurance treaty representing reinsurance recoverable of \$405.9 million and \$428.9 million at December 31, 2010 and 2009, respectively.

The Company determines the appropriate amount of reinsurance based on evaluation of the risks accepted and on market conditions (including the availability and pricing of reinsurance). The Company evaluates the financial condition of its reinsurers and monitors concentrations of credit risk. Based on its review of its reinsurers' financial statements and reputations in the reinsurance marketplace, the Company believes that its counterparties are financially sound.

As of December 31, 2010 and 2009, the Company's only concentrations of credit risk greater than 10% of the Company's stockholder's equity were approximately \$589.1 million and \$624.8 million, respectively, related to the block of business reinsured with an affiliate, Columbia.

The effects of reinsurance were as follows:

For the Years Ended December 31,	2010	2009	2008
<i>(In millions)</i>			
Life and accident and health insurance premiums:			
Direct	\$ 34.3	\$ 42.1	\$ 16.9
Assumed - non-affiliated	31.6	27.7	-
Ceded - non-affiliated	(14.9)	(21.3)	(16.9)
Net premiums	\$ 51.0	\$ 48.5	\$ -
Universal life and investment product policy fees:			
Direct	\$ 124.7	\$ 125.7	\$ 158.7
Assumed - affiliated	7.5	7.5	-
Assumed - non-affiliated	152.5	113.3	40.0
Ceded - affiliated	(91.4)	(12.5)	(9.1)
Ceded - non-affiliated	-	0.7	-
Net universal life and investment product policy fees	\$ 193.3	\$ 234.7	\$ 189.6
Life and accident and health insurance and other individual policy benefits, claims, losses and loss adjustment expenses:			
Direct	\$ 525.6	\$ 623.4	\$ 581.9
Assumed - affiliated	2.2	112.8	-
Assumed - non-affiliated	193.9	16.0	44.1
Ceded - affiliated	(163.3)	(101.7)	(36.7)
Ceded - non-affiliated	(299.3)	(304.0)	(292.2)
Net policy benefits, claims, losses and loss adjustment expenses	\$ 259.1	\$ 346.5	\$ 297.1

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15. DEFERRED POLICY ACQUISITION COSTS

The following reflects the changes to the deferred policy acquisition asset:

For the years ended December 31,	2010	2009
(In millions)		
Balance at beginning of year	\$ 243.3	\$ 118.3
Block acquisition	-	303.1
Reinsurance treaty impacts	-	(61.7)
Acquisition expenses deferred	-	4.1
Amortized to expense during the year	(61.6)	(65.6)
Adjustment for unrealized investment losses during the year	2.7	(54.9)
Capitalization, other	22.7	-
Balance at end of year	\$ 207.1	\$ 243.3

On December 31, 2009, the Company entered into a reinsurance treaty with Arrow ceding all the Company's variable annuity business. This reinsurance treaty resulted in a \$61.7 million reduction in the DAC asset.

On April 1, 2009, the Company entered into a coinsurance agreement with the life insurance subsidiaries of UAC, resulting in an initial DAC balance of \$75.8 million.

On March 31, 2009, the Company entered into a coinsurance and modified coinsurance agreement with Lincoln National, resulting in an initial DAC balance of \$250.0 million.

16. LIABILITIES FOR OUTSTANDING CLAIMS, LOSSES AND LOSS ADJUSTMENT EXPENSES

The Company regularly updates its reserve estimates as new information becomes available and further events occur which may impact the resolution of unsettled claims. Reserve adjustments are reflected in results of operations within policy benefits, claims, losses and loss adjustment expenses. Often these adjustments are recognized in periods subsequent to the period in which the underlying policy was written and loss event occurred. These types of subsequent adjustments are described as "prior year reserve development." Such development can be either favorable or unfavorable to the Company's financial results and may vary by line of business.

The liability for future policy benefits and outstanding claims and claims adjustment expenses, excluding the effect of reinsurance, related to the Company's accident and health business was \$305.0 million and \$315.5 million at December 31, 2010 and 2009, respectively. This business consists of the Company's exited health businesses. Reinsurance recoverables related to this business were \$370.1 million and \$386.6 million at December 31, 2010 and 2009 respectively.

17. COMPOSITION OF OTHER ASSETS, LIABILITIES, INCOME AND EXPENSES

Other assets consist of the following:

December 31,	2010	2009
(In millions)		
State licenses (intangible asset)	\$ 5.3	\$ 5.3
Accounts receivable	8.0	1.0
Deferred modco interest expense	12.2	5.7
Miscellaneous assets	5.5	8.5
Total other assets	\$ 31.0	\$ 20.5

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17. COMPOSITION OF OTHER ASSETS, LIABILITIES, INCOME AND EXPENSES (Continued)

Accrued expenses and other liabilities consist of the following:

December 31,	2010	2009
(In millions)		
Payables in process	\$ 31.0	\$ 42.1
Policyholder liabilities	20.7	20.4
Taxes payable	2.3	2.3
Accrued expenses	9.2	13.1
Miscellaneous liabilities	6.3	5.6
Total accrued expenses and other liabilities	\$ 69.5	\$ 83.5

Other income consists of the following:

December 31,	2010	2009	2008
(In millions)			
Asset management fees	\$ 1.6	\$ 8.3	\$ 12.6
Reinsurance administration fee	17.6	2.0	2.2
Miscellaneous income (loss)	14.4	(3.2)	6.8
Total other income	\$ 33.6	\$ 7.1	\$ 21.6

Other operating expenses consist of the following:

December 31,	2010	2009	2008
(In millions)			
Taxes, licenses and fees	\$ 6.2	\$ 6.0	\$ 0.3
Commission expense	13.4	4.4	12.5
Fees and operational services	34.2	36.7	28.9
Salaries and benefits	10.7	11.4	8.7
Legal and auditing	5.5	4.1	4.8
Miscellaneous operating expenses	9.7	5.0	4.3
Total other operating expenses	\$ 79.7	\$ 67.6	\$ 59.5

18. COMMITMENTS

The Company was allocated certain rental expenses by its parent, primarily for the building lease in Southborough, MA. Rental expenses for these operating leases amounted to \$0.5 million for 2010 and \$0.3 million for 2009, respectively. The Company does not have lease commitments for the Southborough, MA location. On April 19, 2007 the Company entered into a lease agreement for the Elgin, IL office. As of December 31, 2010, lease commitments relating to this lease were \$8.8 thousand for 2011 and 2012. The base rent is subject to adjustments for taxes, insurance premiums, water and utilities, heating and cooling and common area charges.

On March 31, 2009, the Company signed a Work Assignment with Dell Services (“Dell”) whereby Dell, as third party administrator, will provide contract/policy administration over certain of the Company’s fixed annuity and traditional life business for a period not less than ten years. Dell was formerly known as the Transaction Applications Group, Inc. (“TAG”).

On June 19, 2008, the Company signed a professional services agreement with LOGiQ³ Solutions Corp. (“LOGiQ³”). LOGiQ³ will manage certain aspects of the Company’s reinsurance portfolio for a period not less than five years.

On October 31, 2007, the Company signed a third party administrator agreement with Dell and an application service provider agreement with Exl Service Holdings, Inc. (“EXL”). Commencing January 1, 2008, Dell became the third party administrator for the Company’s whole life insurance, term life insurance and universal life insurance, utilizing an EXL platform. EXL was formerly known as the Professional Data Management Again, Inc.

The Company entered into an operational servicing agreement with se2, whereby se2, as third party administrator, will provide contract/policy administration over certain of the Company’s variable annuity and variable universal life business for a period of not less than ten years.

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18. COMMITMENTS (Continued)

As of December 31, 2010, the purchase commitments relating to agreements with Se2, Dell, EXL and LOGiQ³ were as follows:

(in millions)		
2011	\$	16.7
2012		16.2
2013		15.1
2014		13.6
2015		13.2
2016 and thereafter		10.4
Total	\$	<u>85.2</u>

19. CONTINGENCIES

Regulatory and Industry Developments

Unfavorable economic conditions may contribute to an increase in the number of insurance companies that are under regulatory supervision. This may result in an increase in mandatory assessments by state guaranty funds, or voluntary payments by solvent insurance companies to cover losses to policyholders of insolvent or rehabilitated companies. Mandatory assessments, which are subject to statutory limits, can be partially recovered through a reduction in future premium taxes in some states.

Litigation

The Company is involved from time to time in judicial, regulatory and arbitration proceedings concerning matters arising in connection with the conduct of its business. THG has agreed to indemnify the Company and Goldman Sachs with respect to certain of these matters as provided in the Stock Purchase Agreement. Management believes, based on currently available information, that the results of such proceedings, in the aggregate, will not have a material adverse effect on the Company's financial condition. Given the inherent difficulty of predicting the outcome of the Company's litigation and regulatory matters, particularly in cases or proceedings in which substantial or indeterminate damages or fines are sought, the Company cannot estimate losses or ranges of losses for cases or proceedings where there is only a reasonable possibility that a loss may be incurred. However, the Company believes that at the present time there are no pending or threatened lawsuits that are reasonably likely to have a material adverse effect on the its consolidated financial position or results of operations.

20. RELATED PARTY TRANSACTIONS

Effective February 26, 2010, the Company entered into a shared services and expense agreement with an affiliate, Longmore Credit Services, LLC ("LCS"). Under this agreement, the Company provides services including but not limited to seconding Company employees, management services, administrative support and use of Company facilities. The Company charged LCS approximately \$0.2 million for the year ended December 31, 2010. This amount is shown in other operating expenses within the Consolidated Statements of Operations.

On December 31, 2009, the Company ceded via coinsurance and modified coinsurance, 100% of its variable annuity business to an affiliate, Arrow acting on behalf of, and for the benefit of a segregated account established by Arrow. Under this agreement, Arrow agreed to pay the Company certain fees for continued administration of the variable annuity business. The Company received fee income of \$15.7 million from this reinsurance transaction for the year ended December 31, 2010. This amount is shown in other income within the Consolidated Statements of Operations.

Effective March 5, 2009, the Company entered into a shared services and expense agreement with affiliates, Columbia and Charleston Capital Reinsurance, LLC ("Charleston"). Under this agreement, the Company provides services including but not limited to seconding Company employees, management services, administrative support and use of Company facilities. The Company charged Columbia and Charleston approximately \$1.5 million for the years ended December 31, 2010 and 2009, respectively. These amounts are shown in other operating expenses within the Consolidated Statements of Operations.

The Company has an agreement with its affiliate, Columbia, to provide continued administration for the FML and deferred fixed annuity block of business ceded to Columbia. The Company received fee income of \$1.9 million, \$2.0 million and \$2.2 million for the year ended December 31, 2010, 2009 and 2008 respectively.

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20. RELATED PARTY TRANSACTIONS (Continued)

The Company signed a distribution and service agreement with its affiliate, Epoch Securities Inc. (“Epoch”), to serve as principal underwriter and distributor for variable annuity products issued by the Company and its separate accounts. This resulted in expense of \$0.3 million for the years ended December 31, 2010 and 2009, respectively, for these services. The Company performs certain administrative services on Epoch’s behalf. No income was generated for the years ended December 31, 2010, 2009, or 2008 from this agreement.

The Company has a management services agreement with its affiliate, GSCO. Under this service agreement, GSCO provides support to the Company in administrative, legal, compliance, technology, operations, financial reporting, human resources, risk management and other areas, and the Company is allocated costs for services received. GSCO charged the Company approximately \$6.1 million, \$3.3 million and \$3.0 million for the years ended December 31, 2010, 2009 and 2008 respectively, for these services. These amounts are shown within other operating expenses in the accompanying Consolidated Statements of Income.

The Company has entered into several derivative transactions with its affiliate, Goldman Sachs International (“GSI”). These derivative positions resulted in expense of \$7.8 million and \$68.8 million, and income of \$118.2 million, for 2010, 2009 and 2008, respectively, due to mark to market of the positions.

The Company has entered into several derivative transactions with its affiliate, GSCO, which resulted in expense of \$9.2 million and income of \$13.2 million for 2009 and 2008, respectively. There were no derivative transactions with GSCO in 2010.

The Company entered into several derivative transactions with its affiliate, Goldman Sachs Financial Markets L.L.C (“GSFM”), which resulted in income of \$2.6 million for 2008. There were no transactions with GSFM in 2010 or 2009.

The service agreement entered into with GSAM, an affiliate organization that provides investment management services, generated expense of \$3.7 million, \$3.2 million, and \$2.3 million for the years ended December 31, 2010, 2009 and 2008, respectively.

As part of the variable products in the separate account, the Company offers underlying Goldman Sachs Variable Investment Trust funds. Management fees are paid directly to GSAM and certain of these distribution and administration fees are passed to the Company resulting in revenue of \$4.3 million, \$2.6 million and \$6.9 million for the years ended December 31, 2010, 2009 and 2008, respectively.

The employees of the Company participate in The Goldman Sachs Amended and Restated Stock Incentive Plan (the “SIP”). Pursuant to the SIP, Goldman Sachs issued restricted stock units (RSUs) to certain employees of the Company as part of their overall compensation. Unvested RSUs require future service as a condition of delivery of the underlying shares of Goldman Sachs’ common stock generally over a three year period. Delivery of the underlying shares of common stock is also conditioned on the grantee’s satisfying certain other requirements as outlined in the award agreement. The Company incurred expenses of \$0.1 million, \$0.5 million and \$0.3 million relating to RSUs for the years ended December 31, 2010, 2009 and 2008, respectively.

21. STATUTORY FINANCIAL INFORMATION

The Company is required to file annual statements with state regulatory authorities prepared on an accounting basis prescribed or permitted by such authorities. Statutory surplus differs from shareholder’s equity reported in accordance with generally accepted accounting principles primarily because fixed maturities are required to be carried at amortized cost, policy acquisition costs are expensed when incurred, asset valuation and interest maintenance reserves are required, life insurance reserves are based on different assumptions and the recognition of deferred tax assets is based on different recoverability assumptions.

Statutory net income (loss) and surplus are as follows:

	(Unaudited)		
	2010	2009	2008
(In millions)			
Statutory net income (loss)	\$ 199.0	\$ (129.8)	\$ (247.1)
Statutory shareholders’ surplus	\$ 568.5	\$ 561.7	\$ 390.6