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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2009

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _______________ to _______________
Commission File Number: 001-31911

American Equity Investment Life Holding Company

(Exact name of registrant as specified in its charter)

Iowa (State of Incorporation)	**42-1447959** (I.R.S. Employer Identification No.)
6000 Westown Parkway **West Des Moines, Iowa** (Address of principal executive offices)	**50266** (Zip Code)

Registrant's telephone number, including area code: **(515) 221-0002**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common stock, par value $1	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value $1

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes o No ý

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this From 10-K. o

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

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant was $297,022,061 based on the closing price of $5.58 per share, the closing price of the common stock on the New York Stock Exchange on June 30, 2009.

Shares of common stock outstanding as of February 26, 2010: 58,294,559.

Documents incorporated by reference: Portions of the registrant's definitive proxy statement for the annual meeting of shareholders to be held June 10, 2010, which will be filed within 120 days after December 31, 2009 are incorporated by reference into Part III of this report.

AMERICAN EQUITY INVESTMENT LIFE HOLDING COMPANY
FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2009
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PART I

Item 1. Business

Introduction

We are a leader in the development and sale of fixed index and fixed rate annuity products. We were incorporated in the state of Iowa on December 15, 1995. We are a full service underwriter of fixed annuity and life insurance products through our wholly-owned life insurance subsidiaries, American Equity Investment Life Insurance Company ("American Equity Life"), American Equity Investment Life Insurance Company of New York, and Eagle Life Insurance Company ("Eagle Life"). Our business consists primarily of the sale of fixed index and fixed rate annuities and, accordingly, we have only one business segment. Our business strategy is to focus on our annuity business and earn predictable returns by managing investment spreads and investment risk. We are currently licensed to sell our products in 50 states and the District of Columbia. Throughout this report, unless otherwise specified or the context otherwise requires, all references to "American Equity", the "Company", "we", "our" and similar references are to American Equity Investment Life Holding Company and its consolidated subsidiaries.

Investor related information, including periodic reports filed on Forms 10-K, 10-Q and 8-K and all amendments to such reports may be found on our internet website at *www.american-equity.com* as soon as reasonably practicable after such reports are filed with the Securities and Exchange Commission ("SEC"). In addition, we have available on our website our: (i) code of business conduct and ethics; (ii) audit committee charter; (iii) compensation committee charter; (iv) nominating/corporate governance committee charter; and (v) corporate governance guidelines. The information incorporated herein by reference is also electronically accessible from the SEC's website at *www.sec.gov*.

Annuity Market Overview

Our target market includes the group of individuals ages 45-75 who are seeking to accumulate tax-deferred savings. We believe that significant growth opportunities exist for annuity products because of favorable demographic and economic trends. According to the U.S. Census Bureau, there were 35 million Americans age 65 and older in 2000, representing 12% of the U.S. population. By 2030, this sector of the population is expected to increase to 20% of the total population. Our fixed index and fixed rate annuity products are particularly attractive to this group as a result of the guarantee of principal with respect to those products, competitive rates of credited interest, tax-deferred growth and alternative payout options.

According to Advantage Group Associates, Inc., total industry sales of fixed index annuities increased 12% to $30.1 billion in 2009 from $26.8 billion in 2008. Our wide range of fixed index and fixed rate annuity products has enabled us to enjoy favorable growth during volatile equity and bond markets.

Strategy

Our business strategy is to grow our annuity business and earn predictable returns by managing investment spreads and investment risk. Key elements of this strategy include the following:

> ***Enhance our Current Independent Agency Network.*** We believe that our successful relationships with approximately 50 national marketing organizations represent a significant competitive advantage. Our objective is to improve the productivity and efficiency of our core distribution channel by focusing our marketing and recruiting efforts on those independent agents capable of selling $1 million or more of annuity premium annually. This level of production qualifies them for our Gold Eagle program which was introduced at the beginning of 2007. We believe the Gold Eagle program has been effective as evidenced by the increase in Gold Eagle agents to 890 in 2009 as compared to 566 in 2008. Gold Eagle qualifiers receive a combination of

cash and equity-based incentives as motivation for producing business for us. The equity-based incentive compensation component of our Gold Eagle program is unique in our industry and distinguishes us from our competitors. Our continuing focus on relationships and efficiency will ultimately reduce our independent agents to a core group of professional annuity producers. We will also be alert to opportunities to establish relationships with national marketing organizations and agents not presently associated with us and will continue to provide all of our marketers with the highest quality service possible.

Continue to Introduce Innovative and Competitive Products. We intend to be at the forefront of the fixed index and fixed rate annuity industry in developing and introducing innovative and new competitive products. We were one of the first companies to offer a fixed index annuity that allows a choice among interest crediting strategies which include both equity and bond indices as well as a traditional fixed rate strategy. Most recently, we were one of the first companies to include a living income benefit rider with our fixed index annuities. We believe that our continued focus on anticipating and being responsive to the product needs of our independent agents and policyholders will lead to increased customer loyalty, revenues and profitability.

Use our Expertise to Achieve Targeted Spreads on Annuity Products. We have had a successful track record in achieving the targeted spreads on our annuity products. We intend to continue to leverage our experience and expertise in managing the investment spread during a range of interest rate environments to achieve our targeted spreads.

Maintain our Profitability Focus and Improve Operating Efficiency. We are committed to improving our profitability by advancing the scope and sophistication of our investment management and spread capabilities and continuously seeking out efficiencies within our operations. We have implemented competitive incentive programs for our national marketing organizations, agents and employees to stimulate performance.

Take Advantage of the Growing Popularity of Index Products. We believe that the growing popularity of fixed index annuity products that allow equity and bond market participation without the risk of loss of the premium deposit presents an attractive opportunity to grow our business. We intend to capitalize on our reputation as a leading marketer of fixed index annuities in this expanding segment of the annuity market.

Focus on High Quality Service to Agents and Policyholders. We have maintained high quality personal service as one of our highest priorities since the inception of our business, and continue to strive for an unprecedented level of timely and accurate service to both our agents and policyholders. We believe this is one of our strongest competitive advantages.

Expand our Distribution Channels. We formed Eagle Life in 2008 with the vision of developing a network of affiliated and nonaffiliated broker-dealer firms to distribute a registered fixed index annuity product. We believe this to be the most effective means of building a core distribution channel of selling firms with registered representatives capable of selling $1 million or more of annuity premium annually.

Products

Annuities offer our policyholders a tax-deferred means of accumulating retirement savings, as well as a reliable source of income during the payout period. When our policyholders contribute cash to annuities, we account for these receipts as policy benefit reserves in the liability section of our consolidated balance sheet. The annuity deposits collected, by product type, during the three most recent fiscal years are as follows:

	Year Ended December 31,					
	2009		2008		2007	
	Deposits Collected	Deposits as a % of Total	Deposits Collected	Deposits as a % of Total	Deposits Collected	Deposits as a % of Total
	(Dollars in thousands)					
Fixed index annuities:						
Index strategies	$ 1,535,477	42%	$ 1,303,871	57%	$ 1,578,347	74%
Fixed strategy	1,849,833	50%	937,227	41%	515,229	24%
	3,385,310	92%	2,241,098	98%	2,093,576	98%
Fixed rate annuities	292,248	8%	47,908	2%	51,106	2%
	$ 3,677,558	100%	$ 2,289,006	100%	$ 2,144,682	100%

Fixed Index Annuities

Fixed index annuities allow policyholders to earn index credits based on the performance of a particular index without the risk of loss of their principal. Most of these products allow policyholders to transfer funds once a year among several different crediting strategies, including one or more index based strategies and a traditional fixed rate strategy. Approximately 94%, 93% and 86% of our fixed index annuity sales for the years ended December 31, 2009, 2008 and 2007, respectively, were "premium bonus" products. The initial annuity deposit on these policies is increased at issuance by a specified premium bonus ranging from 3% to 12%. Generally, there is a compensating adjustment in the commission paid to the agent or the surrender charges on the policy to offset the premium bonus.

The annuity contract value is equal to the sum of premiums paid, premium bonuses and interest credited ("index credits"), which is based upon an overall limit (or "cap") or a percentage (the "participation rate") of the annual appreciation (based in certain situations on monthly averages or monthly point-to-point calculations) in a recognized index or benchmark. Caps and participation rates limit the amount of annual interest the policyholder may earn in any one contract year and may be adjusted by us annually subject to stated minimums. Caps generally range from 4% to 12% and participation rates generally range from 25% to 100%. In addition, some products have an "asset fee" ranging from 1.5% to 5%, which is deducted from annual interest to be credited. For products with asset fees, if the annual appreciation in the index does not exceed the asset fee, the policyholder's index credit is zero. The minimum guaranteed contract values are equal to 87.5% of the premium collected plus interest credited at an annual rate ranging from 2% to 3.5%.

Fixed Rate Annuities

Fixed rate deferred annuities include annual reset and multi-year rate guaranteed products. Our annual reset fixed rate annuities have an annual interest rate (the "crediting rate") that is guaranteed for the first policy year. After the first policy year, we have the discretionary ability to change the crediting rate once annually to any rate at or above a guaranteed minimum rate. Our multi-year rate guaranteed annuities are similar to our annual reset products except that the initial crediting rate is guaranteed for up to a seven-year period before it may be changed at our discretion. The guaranteed rate on our fixed rate deferred annuities ranges from 2% to 4% and the initial guaranteed rate on our multi-year rate guaranteed policies ranges from 3.15% to 5.25%.

The initial crediting rate is largely a function of the interest rate we can earn on invested assets acquired with new annuity deposits and the rates offered on similar products by our competitors. For subsequent adjustments to crediting rates, we take into account the yield on our investment portfolio, annuity surrender assumptions, competitive industry pricing and crediting rate history for particular groups of annuity policies with similar characteristics. As of December 31, 2009, crediting rates on our outstanding fixed rate deferred annuities generally ranged from 2.9% to 5%. The average crediting rate on our outstanding fixed rate deferred annuities at December 31, 2009 was 3.43%.

We also sell single premium immediate annuities ("SPIAs"). Our SPIAs are designed to provide a series of periodic payments for a fixed period of time or for life, according to the policyholder's choice at the time of issue. The amounts, frequency and length of time of the payments are fixed at the outset of the annuity contract. SPIAs are often purchased by persons at or near retirement age who desire a steady stream of payments over a future period of years. The implicit interest rate on SPIAs is based on market conditions when the policy is issued. The implicit interest rate on our outstanding SPIAs averaged 3.34% at December 31, 2009.

Withdrawal Options Fixed Index and Fixed Rate Annuities

Policyholders are typically permitted penalty-free withdrawals up to 10% of the contract value in each year after the first year, subject to limitations. Withdrawals in excess of allowable penalty-free amounts are assessed a surrender charge during a penalty period which ranges from 5 to 17 years for fixed index annuities and 3 to 15 years for fixed rate annuities from the date the policy is issued. This surrender charge initially ranges from 4.7% to 20% for fixed index annuities and 8% to 25% for fixed rate annuities of the contract value and generally decreases by approximately one to two percentage points per year during the surrender charge period. Surrender charges are set at levels aimed at protecting us from loss on early terminations and reducing the likelihood of policyholders terminating their policies during periods of increasing interest rates. This practice lengthens the effective duration of the policy liabilities and enhances our ability to maintain profitability on such policies. The policyholder may elect to take the proceeds of the annuity either in a single payment or in a series of payments for life, for a fixed number of years or a combination of these payment options.

Beginning in July 2007, substantially all of our fixed index annuity policies were issued with a living income benefit rider. This rider provides an additional liquidity option to policyholders who elect to receive a guaranteed living income from their contract without requiring them to annuitize their contract value. The amount of the living income benefit available is determined by the growth in the policy's income account value as defined in the policy and the policyholder's age at the time the policyholder elects to begin receiving living income benefit payments. Living income benefit payments may be stopped and restarted at the election of the policyholder.

Life Insurance

These products include traditional ordinary and term, universal life and other interest-sensitive life insurance products. We have approximately $2.6 billion of life insurance in force as of December 31, 2009. We intend to continue offering a complete line of life insurance products for individual and group markets. Premiums related to this business accounted for 1% of revenues for the year ended December 31, 2009, 4% of revenues for the year ended December 31, 2008 and 2% of revenues for the years ended December 31, 2007.

Investments

Investment activities are an integral part of our business, and net investment income is a significant component of our total revenues. Profitability of many of our products is significantly affected by spreads between interest yields on investments, the cost of options to fund the annual index credits on our fixed index annuities and rates credited on our fixed rate annuities. We manage the index-based risk component of our fixed index annuities by purchasing call options on the applicable indices to fund the annual index credits on these annuities and by adjusting the caps, participation rates and asset fees on policy anniversary dates to reflect the change in the cost of such options which varies

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based on market conditions. All options are purchased to fund the index credits on our fixed index annuities on their respective anniversary dates, and new options are purchased at each of the anniversary dates to fund the next annual index credits. All credited rates on non-multi-year rate guaranteed fixed rate deferred annuities may be changed annually, subject to minimum guarantees. Changes in caps, participation rates and asset fees on fixed index annuities and crediting rates on fixed rate annuities may not be sufficient to maintain targeted investment spreads in all economic and market environments. In addition, competition and other factors, including the potential for increases in surrenders and withdrawals, may limit our ability to adjust or to maintain caps, participation rates, asset fees and crediting rates at levels necessary to avoid narrowing of spreads under certain market conditions. For the year ended December 31, 2009, the weighted average yield, computed on the average amortized cost basis of our investment portfolio, was 6.30% and the weighted average cost of our liabilities, excluding amortization of deferred sales inducements, was 3.26%.

For additional information regarding the composition of our investment portfolio and our interest rate risk management, see Management's Discussion and Analysis of Financial Condition and Results of Operations Financial Condition Investments, Quantitative and Qualitative Disclosures About Market Risk and note 3 to our audited consolidated financial statements.

Marketing

We market our products through a variable cost brokerage distribution network of approximately 50 national marketing organizations and, through them, 41,000 independent agents as of December 31, 2009. We emphasize high quality service to our agents and policyholders along with the prompt payment of commissions to our agents. We believe this has been significant in building excellent relationships with our existing agency force.

Our independent agents and agencies range in profile from national sales organizations to personal producing general agents. We actively recruit new agents and terminate those agents who have not produced business for us in recent periods and are unlikely to sell our products in the future. In our recruitment efforts, we emphasize that agents have direct access to our executive officers, giving us an edge in recruiting over larger and foreign-owned competitors. We also emphasize our products and our Gold Eagle program which provides unique cash and equity-based incentives to those agents selling $1 million or more of annuity premium annually. We also have favorable relationships with our national marketing organizations, which have enabled us to efficiently sell through an expanded number of independent agents.

The insurance distribution system is comprised of insurance brokers and marketing organizations. We are pursuing a strategy to increase the efficiency of our distribution network by strengthening our relationships with key national and regional marketing organizations and are alert for opportunities to establish relationships with organizations not presently associated with us. These organizations typically recruit agents for us by advertising our products and our commission structure through direct mail advertising or seminars for insurance agents and brokers. These organizations bear most of the cost incurred in marketing our products. We compensate marketing organizations by paying them a percentage of the commissions earned on new annuity policy sales generated by the agents recruited by such organizations. We also conduct incentive programs for marketing organizations and agents from time to time, including equity-based programs for our leading national marketers and those agents qualifying for our Gold Eagle program. We believe the Gold Eagle program has been effective as evidenced by the increase in Gold Eagle agents to 890 in 2009 as compared to 566 in 2008. For additional information regarding our equity-based programs for our leading national marketers and independent agents, see note 11 to our audited consolidated financial statements. We generally do not enter into exclusive arrangements with these marketing organizations.

One of our national marketing organizations accounted for more than 10% of the annuity deposits collected during 2009 and we expect this organization to continue as a marketer for American Equity

Life with a focus on selling our products. The states with the largest share of direct premiums collected during 2009 were: Florida (12.1%), Texas (9.2%), California (8.5%), Illinois (7.0%) and Ohio (4.7%).

Competition and Ratings

We operate in a highly competitive industry. Many of our competitors are substantially larger and enjoy substantially greater financial resources, higher ratings by rating agencies, broader and more diversified product lines and more widespread agency relationships. Our annuity products compete with index, fixed rate and variable annuities sold by other insurance companies and also with mutual fund products, traditional bank investments and other investment and retirement funding alternatives offered by asset managers, banks, and broker-dealers. Our insurance products compete with products of other insurance companies, financial intermediaries and other institutions based on a number of features, including crediting rates, policy terms and conditions, service provided to distribution channels and policyholders, ratings, reputation and broker compensation.

The sales agents for our products use the ratings assigned to an insurer by independent rating agencies as one factor in determining which insurer's annuity to market. In recent years, the market for annuities has been dominated by those insurers with the highest ratings. Following is a summary of American Equity Life's financial strength ratings:

	Financial Strength Rating	Outlook Statement
A.M. Best Company		
November 2008 current	A-	Negative
August 2006 October 2008	A-	Stable
July 2002 July 2006	B++	Stable
Standard & Poor's		
July 2008 current	BBB+	Negative
July 2002 June 2008	BBB+	Stable

The degree to which ratings adjustments have affected sales and persistency is unknown. We believe the rating upgrade from A.M. Best Company in 2006 enhanced our competitive position and improved our sales. However, the degree to which this rating will affect future sales and persistency is unknown.

Financial strength ratings generally involve quantitative and qualitative evaluations by rating agencies of a company's financial condition and operating performance. Generally, rating agencies base their ratings upon information furnished to them by the insurer and upon their own investigations, studies and assumptions. Ratings are based upon factors of concern to policyholders, agents and intermediaries and are not directed toward the protection of investors and are not recommendations to buy, sell or hold securities.

In addition to the financial strength ratings, rating agencies use an "outlook statement" to indicate a medium or long-term trend which, if continued, may lead to a rating change. A positive outlook indicates a rating may be raised and a negative outlook indicates a rating may be lowered. A stable outlook is assigned when ratings are not likely to be changed. Outlooks should not be confused with expected stability of the issuer's financial or economic performance. A rating may have a "stable" outlook to indicate that the rating is not expected to change, but a "stable" outlook does not preclude a rating agency from changing a rating at any time without notice.

Throughout 2009, A.M. Best Company and Standard & Poor's maintained its outlook for the U.S. life insurance sector as negative. We believe the rating agencies have heightened the level of scrutiny they apply to insurance companies, increased the frequency and scope of their credit reviews, and may adjust upward the capital and other requirements employed in the rating agency models for maintenance of certain ratings levels.

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A.M. Best Company ratings currently range from "A++" (Superior) to "F" (In Liquidation), and include 16 separate ratings categories. Within these categories, "A++" (Superior) and "A+" (Superior) are the highest, followed by "A" (Excellent) and "A-" (Excellent) then followed by "B++" (Good) and "B+" (Good). Publications of A.M. Best Company indicate that the "A-" rating is assigned to those companies that, in A.M. Best Company's opinion, have demonstrated an excellent ability to meet their ongoing obligations to policyholders.

Standard & Poor's insurer financial strength ratings currently range from "AAA (extremely strong)" to "R (under regulatory supervision)", and include 21 separate ratings categories, while "NR" indicates that Standard & Poor's has no opinion about the insurer's financial strength. Within these categories, "AAA" and "AA" are the highest, followed by "A" and "BBB". Publications of Standard & Poor's indicate that an insurer rated "BBB" is regarded as having good financial security characteristics, but is more likely to be affected by adverse business conditions than are higher rated insurers.

A.M. Best Company and Standard & Poor's review their ratings of insurance companies from time to time. There can be no assurance that any particular rating will continue for any given period of time or that it will not be changed or withdrawn entirely if, in their judgment, circumstances so warrant. If our ratings were to be adjusted again for any reason, we could experience a material decline in the sales of our products and the persistency of our existing business.

Reinsurance

Coinsurance

American Equity Life has entered into two coinsurance agreements with EquiTrust Life Insurance Company ("EquiTrust"), covering 70% of certain of our fixed index and fixed rate annuities issued from August 1, 2001 through December 31, 2001, 40% of those contracts issued during 2002 and 2003, and 20% of those contracts issued from January 1, 2004 to July 31, 2004, when the agreement was suspended by mutual consent of the parties. As a result of the suspension, new business is no longer ceded to EquiTrust. The business reinsured under these agreements is not eligible for recapture before the expiration of 10 years. Coinsurance deposits (aggregate policy benefit reserves transferred to EquiTrust under these agreements) were $1.4 billion and $1.5 billion at December 31, 2009 and 2008, respectively. We remain liable to policyholders with respect to the policy liabilities ceded to EquiTrust should EquiTrust fail to meet the obligations it has coinsured. EquiTrust has received a financial strength rating of "B+" (Good) with a negative outlook from A.M. Best Company. None of the coinsurance deposits with EquiTrust are deemed by management to be uncollectible.

Effective July 1, 2009, we entered into two funds withheld coinsurance agreements with Athene Life Re Ltd. ("Athene"), an unauthorized life reinsurer domiciled in Bermuda. One agreement cedes 20% of certain of our fixed index annuities issued in 2009. We agreed to extend this agreement to cede 20% of our fixed index annuities to those issued through March 31, 2010. The business reinsured under this agreement is not eligible for recapture until the end of the month following seven years after the date of issuance of the policy. The other agreement cedes 80% of our multi-year rate guaranteed annuities issued on or after July 1, 2009. The business reinsured under this agreement may not be recaptured. Coinsurance deposits (aggregate policy benefit reserves transferred to Athene under these agreements) were $834.2 million at December 31, 2009. We remain liable to policyholders with respect to the policy liabilities ceded to Athene should Athene fail to meet the obligations it has coinsured. The annuity deposits that have been ceded to Athene are being held in a trust on a funds withheld basis. American Equity Life is named as the sole beneficiary of the trust. The funds withheld are required to remain at a value that is sufficient to support the current balance of policy benefit liabilities of the ceded business on a statutory basis. If the value of the funds withheld account would ever reach a point where it is less than the amount of the ceded policy benefit liabilities on a statutory basis, Athene is required to either establish a letter of credit or deposit securities in a trust for the amount of any shortfall. At December 31, 2009, Athene has adequate capital reserves and a significant capital

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commitment from its equity investor. None of the coinsurance deposits with Athene are deemed by management to be uncollectible.

Financing Arrangements

American Equity Life has two reinsurance transactions with Hannover Life Reassurance Company of America, ("Hannover"), which are treated as reinsurance under statutory accounting practices and as financing arrangements under U.S. generally accepted accounting principles ("GAAP"). The statutory surplus benefits under these agreements are eliminated under GAAP and the associated charges are recorded as risk charges and included in other operating costs and expenses in the consolidated statements of operations. Hannover has received a financial strength rating of "A" (Excellent) with a stable outlook from A.M. Best Company. The transactions became effective October 1, 2005 (the "2005 Hannover Transaction") and December 31, 2008 (the "2008 Hannover Transaction").

The 2008 Hannover Transaction is a coinsurance and yearly renewable term reinsurance agreement for statutory purposes and provided $29.5 million in net pretax statutory surplus benefit in 2008. Pursuant to the terms of this agreement, pretax statutory surplus was reduced by $6.6 million in 2009 and is expected to be reduced as follows: 2010 $6.7 million; 2011 $6.7 million; 2012 $6.8 million; 2013 $6.9 million. These amounts include risk charges equal to 5.0% of the pretax statutory surplus benefit as of the end of each calendar quarter.

The 2005 Hannover Transaction is a yearly renewable term reinsurance agreement for statutory purposes covering 47% of waived surrender charges related to penalty free withdrawals and deaths on certain business. The agreement was amended in 2009 to include policy forms that were not in existence at the time this agreement became effective. We may recapture the risks reinsured under this agreement as of the end of any quarter beginning October 1, 2008. The amendment includes a provision that makes it punitive for us not to recapture the business ceded prior to January 1, 2013. The reserve credit recorded on a statutory basis by American Equity Life was $106.8 million and $59.8 million at December 31, 2009 and 2008, respectively. We pay quarterly reinsurance premiums under this agreement with an experience refund calculated on a quarterly basis resulting in a risk charge equal to approximately 6.0% of the weighted average statutory reserve credit.

Indemnity Reinsurance

Consistent with the general practice of the life insurance industry, American Equity Life enters into agreements of indemnity reinsurance with other insurance companies in order to reinsure portions of the coverage provided by its annuity, life and accident and health insurance products. Indemnity reinsurance agreements are intended to limit a life insurer's maximum loss on a large or unusually hazardous risk or to diversify its risks. Indemnity reinsurance does not discharge the original insurer's primary liability to the insured.

The maximum loss retained by us on all life insurance policies we have issued was $0.1 million or less as of December 31, 2009. American Equity Life's reinsured business under indemnity reinsurance agreements is primarily ceded to two reinsurers. Reinsurance related to life and accident and health insurance that was ceded by us to these reinsurers was immaterial.

During 2007, American Equity Life entered into reinsurance agreements with Ace Tempest Life Reinsurance Ltd and Hannover to cede to each 50% of the risk associated with our living income benefit rider on certain fixed index annuities issued in 2007. The amounts ceded under these agreements were immaterial as of and for the years ended December 31, 2009 and 2008.

We believe the assuming companies will be able to honor all contractual commitments, based on our periodic review of their financial statements, insurance industry reports and reports filed with state insurance departments.

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Regulation

Life insurance companies are subject to regulation and supervision by the states in which they transact business. State insurance laws establish supervisory agencies with broad regulatory authority, including the power to:

- grant and revoke licenses to transact business;
- regulate and supervise trade practices and market conduct;
- establish guaranty associations;
- license agents;
- approve policy forms;
- approve premium rates for some lines of business;
- establish reserve requirements;
- prescribe the form and content of required financial statements and reports;
- determine the reasonableness and adequacy of statutory capital and surplus;
- perform financial, market conduct and other examinations;
- define acceptable accounting principles for statutory reporting;
- regulate the type and amount of permitted investments; and
- limit the amount of dividends and surplus note payments that can be paid without obtaining regulatory approval.

Our life subsidiaries are subject to periodic examinations by state regulatory authorities. In 2009, an examination of American Equity Life as of December 31, 2008, was performed for the Iowa Insurance Division by its examiners under the authority granted to the Iowa Insurance Commissioner . There were no adjustments to American Equity Life's 2008 statutory financial statements as a result of this examination. In 2009, the New York Insurance Department completed an examination of American Equity Investment Life Insurance Company of New York as of December 31, 2007. There were no adjustments to American Equity Investment Life Insurance Company of New York's 2007 statutory financial statements required as a result of this examination; however, it consented to a prospective change in its cash flow testing (asset adequacy) analysis which resulted in a $7.3 million increase in December 31, 2009 statutory reserves.

The payment of dividends or the distributions, including surplus note payments, by our life subsidiaries is subject to regulation by each subsidiary's state of domicile's insurance department. Currently, American Equity Life may pay dividends or make other distributions without the prior approval of the Iowa Insurance Commissioner, unless such payments, together with all other such payments within the preceding twelve months, exceed the greater of (1) American Equity Life's statutory net gain from operations for the preceding calendar year, or (2) 10%

of American Equity Life's statutory surplus at the preceding December 31. For 2010, up to $167.5 million can be distributed as dividends by American Equity Life without prior approval of the Iowa Insurance Commissioner. In addition, dividends and surplus note payments may be made only out of earned surplus, and all surplus note payments are subject to prior approval by regulatory authorities. American Equity Life had $270.3 million of statutory earned surplus at December 31, 2009.

Most states have also enacted regulations on the activities of insurance holding company systems, including acquisitions, extraordinary dividends, the terms of surplus notes, the terms of affiliate transactions and other related matters. We are registered pursuant to such legislation in Iowa. A number of state legislatures have also considered or have enacted legislative proposals that alter and, in many cases, increase the authority of state agencies to regulate insurance companies and holding company systems.

Most states, including Iowa and New York where our life subsidiaries are domiciled, have enacted legislation or adopted administrative regulations affecting the acquisition of control of insurance companies as well as transactions between insurance companies and persons controlling them. The nature and extent of such legislation and regulations currently in effect vary from state to state. However, most states require administrative approval of the direct or indirect acquisition of 10% or more of the outstanding voting securities of an insurance company incorporated in the state. The acquisition of 10% of such securities is generally deemed to be the acquisition of "control" for the purpose of the holding company statutes and requires not only the filing of detailed information concerning the acquiring parties and the plan of acquisition, but also administrative approval prior to the acquisition. In many states, the insurance authority may find that "control" in fact does not exist in circumstances in which a person owns or controls more than 10% of the voting securities.

Although the federal government does not directly regulate the business of insurance, federal legislation and administrative policies in several areas, including pension regulation, age and sex discrimination, financial services regulation, securities regulation and federal taxation can significantly affect the insurance business. In addition, legislation has been passed which could result in the federal government assuming some role in regulating insurance companies and which allows combinations between insurance companies, banks and other entities.

In recent years, the SEC has questioned whether fixed index annuities, such as those sold by us, should be treated as securities under the federal securities laws rather than as insurance products exempted from such laws. Treatment of these products as securities would require additional registration and licensing of these products and the agents selling them, as well as cause us to seek additional marketing relationships for these products. In 2008, the SEC requested comments in Release No. 33-8933 regarding whether and how to apply federal securities laws to fixed index annuities and certain other insurance contracts. In this release, the SEC proposed Rule 151A under the Securities Act of 1933, as amended ("Rule 151A"), to clarify the status under the federal securities laws of fixed index annuities, under which payments to the purchaser are dependent on the performance of a securities index. Subsequently, on December 17, 2008, the SEC voted to approve Rule 151A and apply federal securities oversight to fixed index annuities issued on or after January 12, 2011. Along with several other parties we filed a petition for judicial review of this rule and sought to have it overturned. The court issued its decision in this case on July 21, 2009, and remanded Rule 151A to the SEC for further consideration of the effect of Rule 151A on efficiency, capital formation and competition. However, the court upheld the SEC's authority under the Securities Act of 1933 to regulate our fixed index products if the SEC sufficiently considers such effects. The court has not yet ruled on a petition that Rule 151A be vacated pending the SEC's consideration of the effect of Rule 151A on efficiency, capital formation and conpetition. In response to this petition, the SEC recently consented to an additional two-year extension on the effectiveness of Rule 151A following the date of any re-issuance of the Rule. Whether or when Rule 151A will be vacated or if it will be re-issued is not yet known. In addition, legislation has been introduced in the U.S. House of Representatives and the U.S. Senate that would negate Rule 151A. Whether and when such bills may be enacted into law is also uncertain. Should the legal challenge to Rule 151A be unsuccessful, costs of compliance with Rule 151A will be substantial and may include, among other things: (i) the costs of registering one or more fixed index annuities; (ii) the annual costs of printing and mailing prospectuses to policyholders; (iii) the costs of expanding the operations of our broker-dealer subsidiary; (iv) the costs of establishing relationships with other broker-dealers; and (v) the costs of compensating broker-dealers in connection with product

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sales. In addition, we believe that certain of our sales agents would choose not to become licensed to sell SEC registered products, which could lead to a substantial decline in new annuity deposits unless we are successful in developing new insurance products they are permitted to and want to sell.

State insurance regulators and the National Association of Insurance Commissioners ("NAIC") are continually reexamining existing laws and regulations and developing new legislation for the passage by state legislatures and new regulations for adoption by insurance authorities. Proposed laws and regulations or those still under development pertain to insurer solvency and market conduct and in recent years have focused on:

- insurance company investments;
- risk-based capital ("RBC") guidelines, which consist of regulatory targeted surplus levels based on the relationship of statutory capital and surplus, with prescribed adjustments, to the sum of stated percentages of each element of a specified list of company risk exposures;
- the implementation of non-statutory guidelines and the circumstances under which dividends may be paid;
- principles-based reserving;
- product approvals;
- agent licensing;
- underwriting practices; and
- insurance and annuity sales practices.

The NAIC's RBC requirements are intended to be used by insurance regulators as an early warning tool to identify deteriorating or weakly capitalized insurance companies for the purpose of initiating regulatory action. The RBC formula defines a minimum capital standard which supplements low, fixed minimum capital and surplus requirements previously implemented on a state-by-state basis. Such requirements are not designed as a ranking mechanism for adequately capitalized companies.

The NAIC's RBC requirements provide for four levels of regulatory attention depending on the ratio of a company's total adjusted capital to its RBC. Adjusted capital is defined as the total of statutory capital, surplus, asset valuation reserve and certain other adjustments. Calculations using the NAIC formula at December 31, 2009, indicated that American Equity Life's ratio of total adjusted capital to the highest level at which regulatory action might be initiated was 337%.

Our life subsidiaries also may be required, under the solvency or guaranty laws of most states in which they do business, to pay assessments up to certain prescribed limits to fund policyholder losses or liabilities of insolvent insurance companies. These assessments may be deferred or forgiven under most guaranty laws if they would threaten an insurer's financial strength and, in certain instances, may be offset against future premium taxes. Assessments related to business reinsured for periods prior to the effective date of the reinsurance are the responsibility of the ceding companies.

Federal Income Tax

The annuity and life insurance products that we market generally provide the policyholder with a federal income tax advantage, as compared to certain other savings investments such as certificates of deposit and taxable bonds, in that federal income taxation on any increases in the contract values (i.e., the "inside build-up") of these products is deferred until it is received by the policyholder. With other savings investments, the increase in value is generally taxed each year as it is realized. Additionally, life insurance death benefits are generally exempt from income tax.

From time to time, various tax law changes have been proposed that could have an adverse effect on our business, including the elimination of all or a portion of the income tax advantage described

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above for annuities and life insurance. If legislation were enacted to eliminate the tax deferral for annuities, such a change would have an adverse effect on our ability to sell non-qualified annuities. Non-qualified annuities are annuities that are not sold to an individual retirement account or other qualified retirement plan.

Under current law, nearly all of the tax cuts which were contained in the Economic Growth and Tax Relief Reconciliation Act of 2001 (the "2001 Act") and accelerated by the provisions of the Jobs and Growth Tax Reconciliation Act of 2003 (the "2003 Act") are due to expire at the end of 2010. These tax cuts included a temporary reduction in individual tax rates which can lower the present value of the tax deferred advantage of annuities and life insurance products for some individuals. This in turn might hinder our ability to sell such products and/or increase the rate at which our current policyholders surrender their policies. However, when the tax cut provisions expire at the end of 2010, under current law the individual tax rates in effect prior to 2001 will be reinstated. In addition, the current administration's federal budget proposals include provisions for raising the top two individual tax rates back to their pre-2001 levels, changing the income threshold for the next-to-highest rate, reinstating the personal exemption phaseout and the limitation on itemized deductions, and imposing a 20 percent tax rate on long-term capital gains and qualified dividends. A return to pre-2001 individual tax rates and/or an increase in the higher individual tax rates after 2010 may in turn increase the demand for tax advantaged insurance products. However, there is no assurance that pre-2001 tax rates will be reinstated or that the other federal budget proposals will be approved.

Our life subsidiaries are taxed under the life insurance company provisions of the Internal Revenue Code of 1986, as amended (the "Code"). Provisions in the Code require a portion of the expenses incurred in selling insurance products to be capitalized and deducted over a period of years, as opposed to being immediately deducted in the year incurred. This provision increases the current income tax expense charged to gain from operations for statutory accounting purposes which reduces statutory net income and surplus and, accordingly, may decrease the amount of cash dividends that may be paid by our life subsidiaries.

Employees

As of December 31, 2009, we had approximately 360 full-time employees. We have experienced no work stoppages or strikes and consider our relations with our employees to be excellent. None of our employees are represented by a union.

ITEM 1A. RISK FACTORS

The recent financial crisis resulted in unprecedented levels of market volatility and deteriorated debt and equity markets which adversely affected us. Continued difficult conditions in the global capital markets and economy may not improve in the near future and any subsequent downturn will further adversely affect us if conditions deteriorate in 2010.

Markets in the United States and elsewhere have experienced extreme volatility and disruption since the second half of 2007, due in part to the financial stresses affecting the liquidity of the banking system and the financial markets. This volatility and disruption reached unprecedented levels in late 2008 and early 2009. The United States entered a severe recession and economists have predicted that any recovery will probably be slow and long-term. These circumstances exerted downward pressure on stock prices and have reduced access to the equity and debt markets for certain issuers. The unprecedented market volatility and general decline in the debt and equity markets has directly and materially affected our investment portfolio. The prolonged and severe disruptions in the public debt and equity markets (including, among other things, widening of credit spreads, bankruptcies and government intervention in a number of large financial institutions) have resulted in us recognizing significant other than temporary impairment losses, counterparty defaults on derivative instruments (call options) purchased from one of our counterparties to fund annual index credits on our fixed index annuities, impairments of commercial mortgage loans and continuing credit rating downgrades of our residential mortgage backed securities.

Due to the other than temporary impairments recognized on our investments during 2009 and 2008, there may be pressure on our capital position during 2010 if market conditions deteriorate resulting in additional other than temporary impairments and impairments on our commercial mortgage loans. This may result in us needing to raise additional capital to sustain our current business in force and new sales of our annuity products, which may be difficult under current market conditions. If capital is available, it may be at terms that are not favorable to us. If we are unable to raise adequate capital, we may be required to limit growth in sales of our annuity products.

Additionally, if market conditions occurred that would subsequently effect our liquidity we could be forced to limit our operations and our business could suffer. We need liquidity to pay our policyholder benefits, operating expenses, dividends on our capital stock, and to service our debt obligations. The principal sources of our liquidity are annuity deposits, investment income and proceeds from the sale, maturity and call of investments. Additional sources of liquidity in normal markets also include a variety of short and long-term instruments, including long-term debt and capital securities.

Governmental initiatives intended to alleviate the financial crisis that have been adopted may not be effective and, in any event, may be accompanied by other initiatives, including new capital requirements or other regulations, that could materially affect our results of operations, financial condition and liquidity in ways that we cannot predict.

We are subject to extensive laws and regulations that are administered and enforced by a number of different regulatory authorities including state insurance regulators, the NAIC, the SEC and the New York Stock Exchange. In light of the financial crisis, some of these authorities are or may in the future consider enhanced or new regulatory requirements intended to prevent future crises or otherwise assure the stability of institutions under their supervision. These authorities may also seek to exercise their supervisory or enforcement authority in new or more robust ways. All of these possibilities, if they occurred, could affect the way we conduct our business and manage our capital, and may require us to satisfy increased capital requirements, any of which in turn could materially affect our results of operations, financial condition and liquidity.

The markets in the United States and elsewhere have experienced unprecedented levels of market volatility and disruption. We are exposed to significant financial and capital risk, including changing interest rates, credit spreads and equity prices which may have an adverse affect on sales of our products, profitability, investment portfolio and reported book value per share.

Future changes in interest rates, credit spreads and equity and bond indices may result in fluctuations in the income derived from our investments. These and other factors due to the current economic uncertainty could have a material adverse effect on our financial condition, results of operations or cash flows.

Interest rate and credit spread risk

Our interest rate risk is related to market price and changes in cash flow. Substantial and sustained increases and decreases in market interest rates can materially and adversely affect the profitability of our products, our ability to earn predictable returns, the fair value of our investments and the reported value of stockholders' equity. A rise in interest rates, in the absence of other countervailing changes, will increase the unrealized loss position of our investment portfolio. With respect to our available for sale fixed maturity securities, such declines in value (net of income taxes and certain adjustments for assumed changes in amortization of deferred policy acquisition costs and deferred sales inducements) reduce our reported stockholders' equity and book value per share. We have a portfolio of held for investment securities, which consists principally of long duration bonds issued by United States government agencies, the value of which is also sensitive to interest rate changes.

Our exposure to credit spreads is related to market price and changes in cash flows related to changes in credit spreads. The widening of credit spreads during the financial crisis contributed to the increase in the net unrealized loss position of our investment portfolio at December 31, 2008. If credit spreads had continued to widen significantly it would have probably led to additional other than temporary impairments. If credit spreads tighten significantly it could result in reduced net investment income associated with new purchases of fixed maturity securities.

Disintermediation risk

Disintermediation risk is the risk that our policyholders may surrender all or part of their contracts in a rising interest rate environment, which may require us to sell assets in an unrealized loss position. Sustained declines in long-term interest rates may result in increased redemptions of our fixed income securities that have call features. We have reinvestment risk related to these redemptions to the extent we cannot reinvest the net proceeds in assets with credit quality and yield characteristics similar to or better than those of the redeemed bonds. We have a certain ability to mitigate this risk by lowering crediting rates on our products subject to certain restrictions as discussed below. At December 31, 2009, 50% ($6.3 billion) of our fixed income securities have call features and are subject to redemption currently or in the near future.

Credit risk

We are subject to the risk that the issuers of our fixed maturity securities and other debt securities and borrowers on our commercial mortgages, will default on principal and interest payments, particularly if a major downturn in economic activity occurs. An increase in defaults on our fixed maturity securities and commercial mortgage loan portfolios could harm our financial strength and reduce our profitability.

Credit and cash flow assumption risk is the risk that issuers of securities, mortgagees on mortgage loans or other parties, including reinsurers and derivatives counterparties, default on their contractual obligations or experience adverse changes to their contractual cash flow streams. We attempt to minimize the adverse impact of this risk by monitoring portfolio diversification by asset class, creditor, industry, and by complying with investment limitations governed by state insurance laws and regulations as applicable. We also consider all relevant objective information available in estimating the cash flows related to residential mortgage backed securities. We monitor and manage exposures to determine whether securities are impaired or loans are deemed uncollectible.

We use derivative instruments to fund the annual credits on our fixed index annuities. We purchase derivative instruments, consisting primarily of one-year call options, from a number of counterparties. Our policy is to acquire such options only from counterparties rated "A-"or better by a nationally recognized rating agency and the maximum credit exposure to any single counterparty is subject to concentration limits. If our counterparties fail to honor their obligations under the derivative instruments, our revenues may not be sufficient to fund the annual index credits on our fixed index annuities. Any such failure could harm our financial strength and reduce our profitability.

Liquidity risk

We may also have difficulty selling our commercial mortgage loans because they are less liquid than our publicly traded securities. As of December 31, 2009, our commercial mortgage loans represented approximately 15.9% of the value of our invested assets. If we require significant amounts of cash on short notice, we may have difficulty selling these loans at attractive prices or in a timely manner, or both.

Fluctuations in interest rates and investment spread could adversely affect our financial condition, results of operations and cash flows.

A key component of our net income is the investment spread. A narrowing of investment spreads may adversely affect operating results. Although we have the right to adjust interest crediting rates (cap, participation or asset fee rates for fixed index annuities) on most products, changes to crediting rates may not be sufficient to maintain targeted investment spreads in all economic and market environments. In general, our ability to lower crediting rates is subject to minimum crediting rates filed with and approved by state regulators. In addition, competition and other factors, including the potential for increases in surrenders and withdrawals, may limit our ability to adjust or maintain crediting rates at levels necessary to avoid the narrowing of spreads under certain market conditions. Our policy structure generally provides for resetting of policy crediting rates at least annually and imposes withdrawal penalties for withdrawals during the first 3 to 17 years a policy is in force.

Managing the investment spread on our fixed index annuities is more complex than it is for fixed rate annuity products. We manage the index-based risk component of our fixed index annuities by purchasing call options on the applicable indices to fund the annual index credits on these annuities and by adjusting the caps, participation rates and asset fees on policy anniversary dates to reflect changes in the cost of such options which varies based on market conditions. The price of such options generally increases with increases in the volatility in the indices and interest rates, which may either narrow the spread or cause us to lower caps or participation rates. Thus, the volatility of the indices adds an additional degree of uncertainty to the profitability of the index products. We attempt to mitigate this risk by resetting caps, participation rates and asset fees annually on the policy anniversaries.

Our valuation of fixed maturity and equity securities may include methodologies, estimates and assumptions which are subject to differing interpretations and could result in changes to investment valuations that may materially adversely affect our results of operations or financial condition.

Fixed maturity securities and equity securities are reported at fair value in our consolidated balance sheets. During periods of market disruption including periods of significantly rising or high interest rates, rapidly widening credit spreads or illiquidity, it may be difficult to value certain of our securities if trading becomes less frequent and/or market data becomes less observable. Prices provided by independent broker quotes or independent pricing services that are used in the determination of fair value can vary significantly for a particular security. There may be certain asset classes that were in active markets with significant observable data that become illiquid due to the current financial environment. As such, valuations may include inputs and assumptions that are less observable or require greater judgment as well as valuation methods that require greater judgment. Further, rapidly changing and unprecedented credit and equity market conditions could materially impact the valuation of securities as reported in our consolidated financial statements and the period-to-period changes in value could vary significantly. Decreases in value may have a material adverse effect on our results of operations or financial condition.

Defaults on commercial mortgage loans and volatility in performance may adversely affect our business, financial condition and results of operations.

Commercial mortgage loans face heightened delinquency and default risk due to recent economic conditions which have had a negative impact on the performance of the underlying collateral, resulting in declining values and an adverse impact on the obligors of such instruments. An increase in the default rate of our commercial mortgage loan investments could have an adverse effect on our business, financial condition and results of operations.

In addition, the carrying value of commercial mortgage loans is negatively impacted by such factors. The carrying value of commercial mortgage loans is stated at outstanding principal less any specific loan loss allowances recognized. Considerations in determining allowances include, but are not limited to, the following: (i) declining debt service coverage ratios and increasing loan to value ratios (which have been impacted by, among other things, significant changes in the occupancy level of the underlying property and/or significant changes in the rental rates); (ii) bankruptcy filings of major tenants or affiliates of the borrower on the property; (iii) catastrophic events at the property; and (iv) other subjective events or factors, including whether the terms of the debt will be restructured. There can be no assurance that management's assessment of loan loss allowances on commercial mortgage loans will not change in future periods, which could lead to investment losses.

For additional information on our mortgage loan portfolio, see Management's Discussion and Analysis of Financial Condition and Results of Operations Financial Condition Investments Mortgage Loans.

We face competition from companies that have greater financial resources, broader arrays of products, higher ratings and stronger financial performance, which may impair our ability to retain existing customers, attract new customers and maintain our profitability and financial strength.

We operate in a highly competitive industry. Many of our competitors are substantially larger and enjoy substantially greater financial resources, higher ratings by rating agencies, broader and more diversified product lines and more widespread agency relationships. Our annuity products compete with index, fixed rate and variable annuities sold by other insurance companies and also with mutual fund products, traditional bank investments and other retirement funding alternatives offered by asset managers, banks and broker-dealers. Our insurance products compete with those of other insurance companies, financial intermediaries and other institutions based on a number of factors, including premium rates, policy terms and conditions, service provided to distribution channels and policyholders, ratings by rating agencies, reputation and commission structures. While we compete with numerous other companies, we view the following as our most significant competitors:

- Allianz Life Insurance Company of North America;
- Aviva USA;
- Midland National Life Insurance Company;
- ING USA Annuity & Life Insurance Company; and
- North American Company for Life and Health Insurance.

Our ability to compete depends in part on rates of interest credited to policyholder account balances or the parameters governing the determination of index credits which is driven by our investment performance. We will not be able to accumulate and retain assets under management for our products if our investment results underperform the market or the competition, since such under performance likely would result in asset withdrawals and reduced sales.

We compete for distribution sources for our products. We believe that our success in competing for distributors depends on factors such as our financial strength, the services we provide to, and the relationships we develop with these distributors and offering competitive commission structures. Our distributors are generally free to sell products from whichever providers they wish, which makes it important for us to continually offer distributors products and services they find attractive. If our products or services fall short of distributors' needs, we may not be able to establish and maintain satisfactory relationships with distributors of our annuity and life insurance products. Our ability to compete in the past has also depended in part on our ability to develop innovative new products and bring them to market more quickly than our competitors. In order for us to compete in the future, we will need to continue to bring innovative products to market in a timely fashion. Otherwise, our revenues and profitability could suffer.

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National banks, with pre-existing customer bases for financial services products, may increasingly compete with insurers, as a result of legislation removing restrictions on bank affiliations with insurers. This legislation, the Gramm-Leach-Bliley Act of 1999, permits mergers that combine commercial banks, insurers and securities firms under one holding company. Until passage of the Gramm-Leach-Bliley Act, prior legislation had limited the ability of banks to engage in securities-related businesses and had restricted banks from being affiliated with insurance companies. The ability of banks to increase their securities-related business or to affiliate with insurance companies may materially and adversely affect sales of all of our products by substantially increasing the number and financial strength of our potential competitors.

Our reinsurance program involves risks because we remain liable with respect to the liabilities ceded to reinsurers if the reinsurers fail to meet the obligations assumed by them.

Our life insurance subsidiaries cede certain policies to other insurance companies through reinsurance agreements. In 2009, we entered into two funds withheld coinsurance agreements with Athene Life Re Ltd. ("Athene"), an unauthorized life reinsurer domiciled in Bermuda, covering $834.2 million of policy benefit reserves at December 31, 2009. In prior years, American Equity Life has entered into two coinsurance agreements with EquiTrust covering $1.4 billion of policy benefit reserves at December 31, 2009. New business is no longer ceded to EquiTrust. EquiTrust has been assigned a financial strength rating of "B+" with a negative outlook by A.M. Best Company. We remain liable with respect to the policy liabilities ceded to EquiTrust and Athene should either fail to meet the obligations assumed by them. Since Athene is an unauthorized reinsurer, the annuity deposits that have been ceded to Athene are held in a trust on a funds withheld basis. The funds withheld are required to remain at a value that is sufficient to support the current balance of policy benefit liabilities of the ceded business on a statutory basis. If the value of the funds withheld would ever reach a point where it is less than the amount of the ceded policy benefit liabilities on a statutory basis, Athene is required to either establish a letter of credit or pledge securities to the funds withheld for the amount of any shortfall. At December 31, 2009, Athene has adequate capital reserves and a significant capital commitment from its equity investor.

In addition, we have entered into other types of reinsurance contracts including indemnity reinsurance and financing arrangements. Should any of these reinsurers fail to meet the obligations assumed under such contracts, we remain liable with respect to the liabilities ceded. For further information regarding our reinsurance program, see Business Reinsurance.

We may experience volatility in net income due to the application of fair value accounting to our derivative instruments.

All of our derivative instruments, including certain derivative instruments embedded in other contracts, are recognized in the balance sheet at their fair values and changes in fair value are recognized immediately in earnings. This impacts certain revenues and expenses we report for our fixed index annuity business as follows:

We must present the call options purchased to fund the annual index credits on our fixed index annuity products at fair value. The fair value of the call options is based upon the amount of cash that would be required to settle the call options obtained from the counterparties adjusted for the nonperformance risk of the counterparty. The nonperformance risk for each counterparty is based upon its one-year credit default swap rate. The counterparty one-year credit default swap rates are added to a three-month, six-month or twelve-month London Interbank Offered Rate (LIBOR) rate that best matches the remaining time to maturity of each call option. We record the change in fair value of these options as a component of our revenues. The change in fair value of derivatives includes the gains or losses recognized at expiration of the option term or upon early termination and changes in fair value for open positions.

The contractual obligations for future annual index credits are treated as a "series of embedded derivatives" over the expected life of the applicable contracts. Increases or decreases in the fair value of embedded derivatives generally correspond to increases or decreases in equity market performance and changes in the interest rates used to discount the excess of the projected policy contract values over the projected minimum guaranteed contract values. We record the change in fair value of these embedded derivatives as a component of our benefits and expenses in our consolidated statements of operations. For further information regarding the determination of fair value of our embedded derivatives, see Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies.

The application of fair value accounting for derivatives and embedded derivatives in future periods to our fixed index annuity business may cause substantial volatility in our reported net income.

We may face unanticipated losses if there are significant deviations from our assumptions regarding the probabilities that our annuity contracts will remain in force from one period to the next.

The expected future profitability of our annuity products is based in part upon expected patterns of premiums, expenses and benefits using a number of assumptions, including those related to the probability that a policy or contract will remain in force, or persistency, and mortality. Since no insurer can precisely determine persistency or mortality, actual results could differ significantly from assumptions, and deviations from estimates and assumptions could have a material adverse effect on our business, financial condition or results of operations. For example actual persistency that is lower than our assumptions could have an adverse impact on future profitability, especially in the early years of a policy or contract primarily because we would be required to accelerate the amortization of expenses we deferred in connection with the acquisition of the policy.

In addition, we set initial crediting rates for our annuity products based upon expected claims and payment patterns, using assumptions for, among other factors, mortality rates of our policyholders. The long-term profitability of these products depends upon how our actual experience compares with our pricing assumptions. For example, if mortality rates are lower than our pricing assumptions, we could be required to make more payments under certain annuity contracts in addition to what we had projected.

If our estimated gross profits change significantly from initial expectations we may be required to expense our deferred policy acquisition costs and deferred sales inducements in an accelerated manner, which would reduce our profitability.

Deferred policy acquisition costs represent costs that vary with and primarily relate to the acquisition of new business. Deferred sales inducements are contract enhancements such as first-year premium and interest bonuses that are credited to policyholder account balances. These costs are capitalized when incurred and are amortized over the life of the contracts. Current amortization of these costs is generally in proportion to expected gross profits from interest margins and, to a lesser extent, from surrender charges. Unfavorable experience with regard to expected expenses, investment returns, mortality or withdrawals may cause acceleration of the amortization of these costs resulting in an increase of expenses and lower profitability.

If we do not manage our growth effectively, our financial performance could be adversely affected; our historical growth rates may not be indicative of our future growth.

We have experienced rapid growth since our formation in December 1995. For the year ended December 31, 2009, our deposits from sales of new annuities were $3.7 billion. We intend to continue to grow by recruiting new independent agents, increasing the productivity of our existing agents, expanding our insurance distribution network, developing new products, expanding into new product lines, and continuing to develop new incentives for our sales agents. Future growth will impose

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significant added responsibilities on our management, including the need to identify, recruit, maintain and integrate additional employees, including management. There can be no assurance that we will be successful in expanding our business or that our systems, procedures and controls will be adequate to support our operations as they expand. In addition, due to our rapid growth and resulting increased size, it may be necessary to expand the scope of our investing activities to asset classes in which we historically have not invested or have not had significant exposure. If we are unable to adequately manage our investments in these classes, our financial condition or operating results in the future could be less favorable than in the past. Further, we have utilized reinsurance in the past to support our growth. The future availability and cost of reinsurance is uncertain. Our failure to manage growth effectively, or our inability to recruit, maintain and integrate additional qualified employees and independent agents, could have a material adverse effect on our business, financial condition or results of operations. In addition, due to our rapid growth, our historical growth rates are not likely to accurately reflect our future growth rates or our growth potential. We cannot assure you that our future revenues will increase or that we will continue to be profitable.

We must retain and attract key employees or else we may not grow or be successful.

We are dependent upon our executive management for the operation and development of our business. Our executive management team includes:

David J. Noble, Executive Chairman;

Wendy C. Waugaman, President and Chief Executive Officer;

John M. Matovina, Vice Chairman, Chief Financial Officer and Treasurer;

Debra J. Richardson, Executive Vice President and Secretary;

Ronald J. Grensteiner, President of American Equity Life;

James R. Gerlach, Executive Vice President;

Terry A. Reimer, Executive Vice President;

Ted M. Johnson, Vice President-Controller; and

Jeff D. Lorenzen, Sr. Vice President-Investments.

Although we have change in control agreements with certain members of our executive management team, we do not have employment contracts with any of the members of our executive management team. Although none of our executive management team has indicated that they intend to terminate their employment with us, there can be no assurance that these employees will remain with us for any particular period of time. Also, we do not maintain "key person" life insurance for any of our personnel.

If we are unable to attract and retain national marketing organizations and independent agents, sales of our products may be reduced.

We distribute our annuity products through a variable cost distribution network which included over 50 national marketing organizations and 41,000 independent agents as of December 31, 2009. We must attract and retain such marketers and agents to sell our products. Insurance companies compete vigorously for productive agents. We compete with other life insurance companies for marketers and agents primarily on the basis of our financial position, support services, compensation and product features. Such marketers and agents may promote products offered by other life insurance companies that may offer a larger variety of products than we do. Our competitiveness for such marketers and agents also depends upon the long-term relationships we develop with them. If we are unable to attract and retain sufficient marketers and agents to sell our products, our ability to compete and our revenues would suffer.

We may require additional capital to support our business and sustained future growth which may not be available when needed or may be available only on unfavorable terms.

Our long-term strategic capital requirements will depend on many factors including the accumulated statutory earnings of our life insurance subsidiaries and the relationship between the statutory capital and surplus of our life insurance subsidiaries and various elements of required capital. To support long-term capital requirements, we may need to increase or maintain the statutory capital and surplus of our life insurance subsidiaries through additional financings, which could include debt, equity, financing arrangements and/or other surplus relief transactions. Adverse market conditions have affected and continue to affect the availability and cost of capital. Such financings, if available at all, may be available only on terms that are not favorable to us. If we cannot maintain adequate capital, we may be required to limit growth in sales of new annuity products, and such action could adversely affect our business, financial condition or results of operations.

Changes in state and federal regulation may affect our profitability.

We are subject to regulation under applicable insurance statutes, including insurance holding company statutes, in the various states in which our life insurance subsidiaries transact business. Our life insurance subsidiaries are domiciled in New York and Iowa. We are currently licensed to sell our products in 50 states and the District of Columbia. Insurance regulation is intended to provide safeguards for policyholders rather than to protect shareholders of insurance companies or their holding companies. As increased scrutiny has been placed upon the insurance regulatory framework, a number of state legislatures have considered or enacted legislative proposals that alter, and in many cases increase, state authority to regulate insurance companies and holding company systems.

Regulators oversee matters relating to trade practices, policy forms, claims practices, guaranty funds, types and amounts of investments, reserve adequacy, insurer solvency, minimum amounts of capital and surplus, transactions with related parties, changes in control and payment of dividends.

State insurance regulators and the NAIC continually reexamine existing laws and regulations and may impose changes in the future.

Our life insurance subsidiaries are subject to the NAIC's RBC requirements which are intended to be used by insurance regulators as an early warning tool to identify deteriorating or weakly capitalized insurance companies for the purpose of initiating regulatory action. Our life insurance subsidiaries also may be required, under solvency or guaranty laws of most states in which they do business, to pay assessments up to certain prescribed limits to fund policyholder losses or liabilities for insolvent insurance companies.

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Although the federal government does not directly regulate the insurance business, federal legislation and administrative policies in several areas, including pension regulation, age and sex discrimination, financial services regulation, securities regulation and federal taxation, can significantly affect the insurance business. In addition, legislation has been introduced in Congress which could result in the federal government assuming some role in the regulation of the insurance industry.

On December 17, 2008, the SEC voted to approve Rule 151A, which would apply federal securities oversight to fixed index annuities issued on or after January 12, 2011. Along with several other parties, we filed a petition for judicial review of this rule seeking to have it overturned. The court issued its decision in this case on July 21, 2009 and remanded Rule 151A to the SEC for further consideration of the effect of Rule 151A on efficiency, capital formation and competition. However, the court upheld the SEC's authority under the Securities Act of 1933 to regulate our fixed index products if the SEC sufficiently considers such effects. Further steps in this litigation are uncertain at this time. In addition, legislation has been introduced in the U.S. House of Representatives and the U.S. Senate that would negate Rule 151A. Whether and when such bills may be enacted into law is also uncertain. Should this legal challenge to Rule 151A be unsuccessful, costs of compliance with Rule 151A will be substantial and will include, among other things: (i) the costs of registering one or more fixed index annuities; (ii) the annual costs of printing and mailing prospectuses to policyholders; (iii) the costs of expanding the operations of our broker-dealer subsidiary; (iv) the costs of establishing relationships with other broker-dealers; and (v) the costs of compensating broker-dealers in connection with product sales. In addition, we believe a portion of our sales agents would choose not to become licensed to sell SEC registered products, which could lead to a substantial decline in new annuity deposits unless we are successful in developing new insurance products they want to sell. In a brief filed in the court proceedings challenging Rule 151A, the SEC recently consented to an additional two-year extension on the effectiveness of Rule 151A following the date any re-issuance of the Rule. Whether or when such re-issuance may occur is not yet known.

The regulatory framework at the state and federal level applicable to our insurance products is evolving. The changing regulatory framework could affect the design of such products and our ability to sell certain products. Any changes in these laws and regulations could materially and adversely affect our business, financial condition or results of operations.

Changes in federal income taxation laws, including any reduction in individual income tax rates, may affect sales of our products and profitability.

The annuity and life insurance products that we market generally provide the policyholder with certain federal income tax advantages. For example, federal income taxation on any increases in non-qualified annuity contract values (i.e. the "inside build-up") is deferred until it is received by the policyholder. With other savings investments, such as certificates of deposit and taxable bonds, the increase in value is generally taxed each year as it is realized. Additionally, life insurance death benefits are generally exempt from income tax.

From time to time, various tax law changes have been proposed that could have an adverse effect on our business, including the elimination of all or a portion of the income tax advantages described above for annuities and life insurance. If legislation were enacted to eliminate the tax deferral for annuities, such a change would have an adverse effect on our ability to sell non-qualified annuities. Non-qualified annuities are annuities that are not sold to a qualified retirement plan.

Under current law, nearly all of the tax cuts which were contained in the 2001 Act and accelerated by the provisions of the 2003 Act are due to expire at the end of 2010. These tax cuts included a temporary reduction in individual tax rates which can lower the present value of the tax deferred advantage of annuities and life insurance products for some individuals. This in turn might hinder our

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ability to sell such products and/or increase the rate at which our current policyholders surrender their policies.

We face risks relating to litigation, including the costs of such litigation, management distraction and the potential for damage awards, which may adversely impact our business.

We are occasionally involved in litigation, both as a defendant and as a plaintiff. In addition, state regulatory bodies, such as state insurance departments, the SEC, the Financial Industry Regulatory Authority, Inc. ("FINRA"), the Department of Labor and other regulatory bodies regularly make inquiries and conduct examinations or investigations concerning our compliance with, among other things, insurance laws, securities laws, the Employee Retirement Income Security Act of 1974, as amended, and laws governing the activities of broker-dealers. Companies in the life insurance and annuity business have faced litigation, including class action lawsuits, alleging improper product design, improper sales practices and similar claims. We are currently a defendant in several purported class action lawsuits alleging improper sales practices. In these lawsuits, the plaintiffs are seeking returns of premiums and other compensatory and punitive damages. Although we do not believe that these lawsuits will have a material adverse effect on our business, financial condition or results of operations, there can be no assurance that such litigation, or any future litigation, will not have such an effect, whether financially, through distraction of our management or otherwise. For additional information, see Legal Proceedings and note 13 to our audited consolidated financial statements.

A downgrade in our credit or financial strength ratings may increase our future cost of capital and may reduce new sales, adversely affect relationships with distributors and increase policy surrenders and withdrawals.

Currently, our senior unsecured indebtedness carries a "bbb-" rating from A.M. Best Company and a "BB+" rating from Standard & Poor's. Our ability to maintain such ratings is dependent upon the results of operations of our subsidiaries and our financial strength. If we fail to preserve the strength of our balance sheet and to maintain a capital structure that rating agencies deem suitable, it could result in a downgrade of the ratings applicable to our senior unsecured indebtedness. A downgrade would likely reduce the fair value of the common stock and may increase our future cost of capital.

Financial strength ratings are important factors in establishing the competitive position of life insurance and annuity companies. In recent years, the market for annuities has been dominated by those insurers with the highest ratings. A ratings downgrade, or the potential for a ratings downgrade, could have a number of adverse effects on our business. For example, distributors and sales agents for life insurance and annuity products use the ratings as one factor in determining which insurer's annuities to market. A ratings downgrade could cause those distributors and agents to seek alternative carriers. In addition, a ratings downgrade could materially increase the number of policy or contract surrenders we experience, as well as our ability to obtain reinsurance or obtain reasonable pricing on reinsurance.

Financial strength ratings are measures of an insurance company's ability to meet contractholder and policyholder obligations and generally involve quantitative and qualitative evaluations by rating agencies of a company's financial condition and operating performance. Generally, rating agencies base their ratings upon information furnished to them by the insurer and upon their own investigations, studies and assumptions. Ratings are based upon factors of concern to agents, policyholders and intermediaries and are not directed toward the protection of investors and are not recommendations to buy, sell or hold securities.

American Equity Life has received financial strength ratings of "A-" (Excellent) with a negative outlook from A.M. Best Company and "BBB+" with a negative outlook from Standard & Poor's.

A.M. Best Company and Standard & Poor's review their ratings of insurance companies from time to time. There can be no assurance that any particular rating will continue for any given period of time or that it will not be changed or withdrawn entirely if, in their judgment, circumstances so warrant. If our ratings were to be downgraded for any reason, we could experience a material decline in the sales of our products and the persistency of our existing business. For additional information, see Business Competition and Ratings.

Our system of internal control ensures the accuracy or completeness of our disclosures and a loss of public confidence in the quality of our internal controls or disclosures could have a negative impact on us.

Section 404 of the Sarbanes-Oxley Act of 2002 requires us to provide an annual report on our internal control over financial reporting, including an assessment as to whether or not our internal control over financial reporting is effective. We are also required to have our auditors opine on the effectiveness of our internal control over financial reporting. We have discovered, and may in the future discover deficiencies in our internal control that need remediation. If we determine that our remediation has been ineffective, or we identify additional material weaknesses in our internal control over financial reporting, we could be subjected to additional regulatory scrutiny, future delays in filing our financial statements and a loss of public confidence in the reliability of our financial statements, which could have a negative impact on our liquidity, access to capital markets, and financial condition.

In addition, we do not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent all errors and all fraud. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Based on the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been or will be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple errors or mistakes. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events. Therefore, a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Also, while we document our assumptions and review financial disclosures with the audit committee of our board of directors, the regulations and literature governing our disclosures are complex and reasonable persons may disagree as to their application to a particular situation or set of circumstances.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We lease commercial office space in one building in West Des Moines, Iowa, for our principal offices under an operating lease that expires on November 21, 2021. We also lease our office in Pell City, Alabama, pursuant to an operating lease that expires on December 31, 2010. We are fully utilizing these facilities and believe both locations to be sufficient to house our operations for the foreseeable future.

Item 3. Legal Proceedings

We are occasionally involved in litigation, both as a defendant and as a plaintiff. In addition, state regulatory bodies, such as state insurance departments, the SEC, FINRA, the Department of Labor,

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and other regulatory bodies regularly make inquiries and conduct examinations or investigations concerning our compliance with, among other things, insurance laws, securities laws, the Employee Retirement Income Security Act of 1974, as amended, and laws governing the activities of broker-dealers.

On March 3, 2010, the SEC filed a civil complaint in the United States District Court for the Southern Division of Iowa in connection with the previously disclosed SEC investigation into proxy statement disclosures of certain transactions between American Equity and American Equity Investment Service Company ("Service Company") in 2003, 2004 and 2005 and the acquisition of the Service Company by us in 2005. In the complaint, the SEC charged us, our Executive Chairman and our Chief Executive Officer and President with violating Section 14(a) of the Securities Exchange Act of 1934, as amended, and Rules 14a-3 and 14a-9 thereunder. The complaint made no allegations of fraud or financial statement inaccuracies. As previously disclosed by us in a Current Report on Form 8-K on March 3, 2010, we and our executive officers charged in the SEC's complaint entered into settlements with the SEC in which the parties consented, without admitting or denying the allegations in the complaint, to an entry of judgment enjoining the parties from violating the aforementioned federal securities laws, and in the case of the individuals, the payment of civil monetary penalties. We also agreed to maintain certain remedial corporate governance measures initiated during the SEC inquiry. The settlement did not require us to pay a monetary penalty. The court approved the settlements in final judgments entered on March 4, 2010.

In recent years, companies in the life insurance and annuity business have faced litigation, including class action lawsuits, alleging improper product design, improper sales practices and similar claims. We are currently a defendant in two class action lawsuits alleging improper sales practices and similar claims as described below. It is often not possible to determine the ultimate outcome of pending legal proceedings or to provide reasonable ranges of potential losses with any degree of certainty. The lawsuits referred to below are in various stages. We do not have sufficient information to make an assessment of the plaintiffs' claims for liability or damages as plaintiffs have not provided any damage or restitution model. The plaintiffs are seeking undefined amounts of damages or other relief, including punitive damages, which are difficult to quantify and cannot be estimated based on the information currently available. We do not believe that these lawsuits, including those discussed below, will have a material adverse effect on our financial position, results of operations or cash flows. However, there can be no assurance that such litigation, or any future litigation, will not have a material adverse effect on our business, financial condition, or results of operations.

We are a defendant in two class actions, including (i) *Stephens v. American Equity Investment Life Insurance Company, et. al.*, in the San Luis Obispo Superior Court, California (complaint filed November 29, 2004) (the "SLO Case") and (ii) *McCormack, et al. v. American Equity Investment Life Insurance Company, et al.*, in the United States District Court for the Central District of California, Western Division and *Anagnostis v. American Equity, et al.*, coordinated in the Central District, entitled, *In re American Equity Annuity Practices and Sales Litigation* (complaint filed September 7, 2005) (the "Los Angeles Case").

The plaintiffs in the SLO Case represent a class of individuals who are California residents and who either purchased their annuity from us through a co-defendant marketing organization or who purchased one of a defined set of particular annuities issued by us. The named plaintiffs in this case are: Chalys M. Stephens and John P. Stephens. Plaintiffs seek injunctive relief and restitution on behalf of all class members under California Business & Professions Code section 17200 et seq.; compensatory damages for breach of contract and breach of fiduciary duty; other pecuniary damages under California Civil Code section 1750 and California Welfare & Institutions Codes section 15600 et seq.; and punitive damages under common law causes of action for fraud and breach of the covenant of good faith and fair dealing. On November 3, 2008, the court issued an order certifying the class. We are vigorously defending the underlying allegations. The case is set for trial September 30, 2010, and we may seek to decertify the entire class after further discovery into the merits of the case.

The Los Angeles Case is a consolidated action involving several lawsuits filed by individuals, and the individuals are seeking class action status for a national class of purchasers of annuities issued by us. The named plaintiffs in this consolidated case are Bernard McCormack, Gust Anagnostis by and through Gary S. Anagnostis and Robert C. Anagnostis, Regina Bush by and through Sharon Schipiour, Lenice Mathews by and through Mary Ann Maclean and George Miller. The allegations generally attack the suitability of sales of deferred annuity products to persons over the age of 65. The plaintiffs seek recessionary and injunctive relief including restitution and disgorgement of profits on behalf of all class members under California Business & Professions Code section 17200 et seq. and Racketeer Influenced and Corrupt Organizations Act; compensatory damages for breach of fiduciary duty and aiding and abetting of breach of fiduciary duty; unjust enrichment and constructive trust; and other pecuniary damages under California Civil Code section 1750 and California Welfare & Institutions Codes section 15600 et seq. This action is effectively stayed while the court determines whether plaintiffs' experts' opinions are admissable. We are vigorously defending against both class action status as well as the underlying claims.

Item 4. Reserved

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is traded on the New York Stock Exchange ("NYSE") under the symbol AEL. The following table sets forth the high and low prices of our common stock as quoted on the NYSE.

2009	**High**	**Low**
First Quarter	$ 7.40	$ 2.96
Second Quarter	$ 8.86	$ 4.01
Third Quarter	$ 8.65	$ 5.24
Fourth Quarter	$ 8.40	$ 6.10
2008		
First Quarter	$ 10.21	$ 6.82
Second Quarter	$ 11.63	$ 7.61
Third Quarter	$ 10.75	$ 7.27
Fourth Quarter	$ 7.75	$ 3.65

On August 20, 2009, we entered into distribution agreements with Fox-Pitt Kelton Cochran Caronia Waller (USA) LLC ("FPK") and Sandler O'Neill & Partners, L.P. ("Sandler O'Neill"). On December 3, 2009 Macquarie Capital (USA) Inc. ("Macquarie Capital") assumed all of FPK's rights and obligations under our distribution agreement with FPK. Under the distribution agreements, we can offer and sell shares of our common stock up to an aggregate offering price of $50.0 million. From October 1, 2009 through December 31, 2009, we did not sell any of our common stock pursuant to these distribution agreements. From August 20, 2009 through September 30, 2009, we sold 132,300 shares of our common stock at an average price of $8.26 per share, resulting in gross proceeds to us of $1.1 million. The aggregate net proceeds from such sales were $1.0 million after deducting related expenses, including $0.04 million in gross sales commissions paid to FPK. All of the net proceeds have been used for working capital and general corporate purposes. The offering of shares of our common stock pursuant to the distribution agreements will terminate upon the earlier of (1) the sale of all shares of common stock subject to the distribution agreements and (2) the termination of the distribution agreements by us or by Macquarie Capital or Sandler O'Neill.

As of February 26, 2010, there were approximately 6,000 holders of our common stock. In 2009 and 2008, we paid an annual cash dividend of $0.08 and $0.07, respectively, per share on our common stock. We intend to continue to pay an annual cash dividend on such shares so long as we have sufficient capital and/or future earnings to do so. However, we anticipate retaining most of our future earnings, if any, for use in our operations and the expansion of our business. Any further determination as to dividend policy will be made by our board of directors and will depend on a number of factors, including our future earnings, capital requirements, financial condition and future prospects and such other factors as our board of directors may deem relevant.

Since we are a holding company, our ability to pay cash dividends depends in large measure on our subsidiaries' ability to make distributions of cash or property to us. Iowa insurance laws restrict the amount of distributions American Equity Life can pay to us without the approval of the Iowa Insurance Commissioner. See Management's Discussion and Analysis of Financial Condition and Results of Operations and note 12 to our audited consolidated financial statements.

Issuer Purchases of Equity Securities

There were no issuer purchases of equity securities for the quarter ended December 31, 2009.

We have a Rabbi Trust, the NMO Deferred Compensation Trust, which purchases our common shares to fund the amount of shares earned by our agents and vested under the NMO Deferred Compensation Plan. At December 31, 2009, agents had earned 81,745 shares which had vested but had not yet been purchased and contributed to the Rabbi Trust.

In addition, we have a share repurchase program under which we are authorized to purchase up to 10,000,000 shares of our common stock. As of December 31, 2009 we have repurchased 3,845,296 shares of our common stock under this program. We suspended the repurchase of our common stock under this program in August of 2008.

The maximum number of shares that may yet be purchased under these plans is 6,236,449 at December 31, 2009.

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Item 6. Selected Consolidated Financial Data

The summary consolidated financial and other data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our audited consolidated financial statements and related notes appearing elsewhere in this report. The results for past periods are not necessarily indicative of results that may be expected for future periods.

	Year ended December 31,				
	2009	2008	2007	2006	2005
	(Dollars in thousands, except per share data)				
		(As Adjusted)	(As Adjusted)	(As Adjusted)	(As Adjusted)
Consolidated Statements of Operations Data:					
Revenues					
Annuity product charges	$ 63,358	$ 52,671	$ 45,828	$ 39,472	$ 25,686
Net investment income	932,172	822,077	719,916	677,638	554,118
Change in fair value of derivatives	216,896	(372,009)	(59,985)	183,783	(18,029)
Net realized gains on investments, excluding other than temporary impairment ("OTTI") losses	51,279	5,555	501	2,682	1,827
Net OTTI losses recognized in operations	(86,771)	(192,648)	(4,383)	(1,337)	(9,462)
Total revenues	1,188,913	337,904	714,500	915,860	567,718
Benefits and expenses					
Interest sensitive and index product benefits	347,883	205,131	560,209	404,269	299,254
Change in fair value of embedded derivatives	529,508	(210,753)	(67,902)	151,057	31,087
Amortization of deferred sales inducements and policy acquisition costs	128,008	157,443	68,038	119,716	80,334
Interest expense on notes payable and subordinated debentures	30,672	39,218	43,436	42,632	34,627
Interest expense on amounts due under repurchase agreements	534	8,207	15,926	32,931	11,280
Other operating costs and expenses	57,255	52,633	48,230	40,418	35,896
Total benefits and expenses	1,102,749	260,851	676,356	799,831	500,982
Income before income taxes	86,164	77,053	38,144	116,029	66,736
Income tax expense	17,634	61,106	11,914	41,068	23,676
Net income	68,530	15,947	26,230	74,961	40,559
Per Share Data:					
Earnings per common share	$ 1.22	$ 0.30	$ 0.46	$ 1.33	$ 1.03
Earnings per common share assuming dilution	1.18	0.30	0.46	1.26	0.94
Dividends declared per common share	0.08	0.07	0.06	0.05	0.04
Non-GAAP Financial Measure (a):					

Operating income	$	101,778	$	72,472	$	61,532	$	69,977	$	54,670
Reconciliation to net income:										
Net income	$	68,530	$	15,947	$	26,229	$	74,961	$	40,559
Net realized gains and net OTTI losses on investments, net of offsets		(1,339)		92,524		1,688		(427)		2,653
Convertible debt retirement, net of income taxes		687		(5,702)						
Net effect of derivatives, embedded derivatives and other index annuity, net of offsets		33,900		(30,297)		33,615		(4,557)		7,760
Variable interest entity consolidation and income tax contingency										3,698
Operating income	$	101,778	$	72,472	$	61,532	$	69,977	$	54,670
Operating income per common share	$	1.81	$	1.35	$	1.08	$	1.24	$	1.39
Operating income per common share assuming dilution		1.75		1.30		1.05		1.18		1.26

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	As of and for the Year Ended December 31,				
	2009	2008	2007	2006	2005
	(Dollars in thousands, except per share data)				
		(As Adjusted)	(As Adjusted)	(As Adjusted)	(As Adjusted)
Consolidated Balance Sheet Data:					
Total investments	$ 15,374,110	$ 12,719,605	$ 12,610,895	$ 11,385,464	$ 10,492,346
Total assets	21,312,004	17,081,740	16,384,690	14,979,198	14,027,739
Policy benefit reserves	19,336,221	15,809,539	14,711,780	13,207,931	12,237,988
Notes payable	316,468	247,750	248,968	243,022	328,039
Subordinated debentures	268,347	268,209	268,330	268,489	230,658
Accumulated other comprehensive loss ("AOCL")	(30,456)	(147,376)	(38,929)	(38,769)	(27,306)
Total stockholders' equity	754,623	496,844	621,324	607,502	457,307
Other Data:					
Life subsidiaries' statutory capital and surplus and asset valuation reserve	1,239,651	1,011,682	1,013,845	1,009,192	702,278
Life subsidiaries' statutory net gain from operations before income taxes and realized capital gains (losses)	253,146	129,046	41,473	95,217	112,498
Life subsidiaries' statutory net income (loss)	116,895	(7,073)	17,010	89,875	40,534
Book value per share (b)	$ 13.08	$ 9.46	$ 11.11	$ 10.82	$ 8.24
Book value per share, excluding AOCL (b)	13.61	12.27	11.81	11.51	8.73

(a)

In addition to net income, we have consistently utilized operating income, operating income per common share and operating income per common share assuming dilution, non-GAAP financial measures commonly used in the life insurance industry, as economic measures to evaluate our financial performance. Operating income equals net income adjusted to eliminate the impact of net realized gains on investments, including net OTTI losses recognized in operations and related deferred tax asset valuation allowance, (gain) loss on retirement of debt, fair value changes in derivatives and embedded derivatives, the Lehman counterparty default on expired call options, minority interest of variable interest entity and income tax contingency. Because these items fluctuate from year to year in a manner unrelated to core operations, we believe measures excluding their impact are useful in analyzing operating trends. We believe the combined presentation and evaluation of operating income together with net income, provides information that may enhance an investor's understanding of our underlying results and profitability.

(b)

Book value per share and book value per share excluding AOCL is calculated as total stockholders' equity and total stockholders' equity excluding AOCL divided by the total number of common stock outstanding. AOCL fluctuates from year to year due to unrealized changes in the fair value of available for sale investments. Shares outstanding include shares held by the NMO Deferred Compensation Trust and exclude unallocated shares held by our employee stock ownership plan see note 11 to our audited consolidated financial statements.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's discussion and analysis reviews our consolidated financial position at December 31, 2009 and 2008, and our consolidated results of operations for the three years in the period ended December 31, 2009, and where appropriate, factors that may affect future financial performance. This discussion should be read in conjunction with our audited consolidated financial statements, notes thereto and selected consolidated financial data appearing elsewhere in this report.

Cautionary Statement Regarding Forward-Looking Information

All statements, trend analyses and other information contained in this report and elsewhere (such as in filings by us with the SEC, press releases, presentations by us or our management or oral statements) relative to markets for our products and trends in our operations or financial results, as well as other statements including words such as "anticipate", "believe", "plan", "estimate", "expect", "intend" and other similar expressions, constitute forward-looking statements. We caution that these statements may and often do vary from actual results and the differences between these statements and actual results can be material. Accordingly, we cannot assure you that actual results will not differ materially from those expressed or implied by the forward-looking statements. Factors that could contribute to these differences include, among other things:

- general economic conditions and other factors, including prevailing interest rate levels and stock and credit market performance which may affect (among other things) our ability to sell our products, our ability to access capital resources and the costs associated therewith, the fair value of our investments, which could result in impairments and other than temporary impairments, and certain liabilities, and the lapse rate and profitability of policies;
- customer response to new products and marketing initiatives;
- changes in the Federal income tax laws and regulations which may affect the relative income tax advantages of our products;
- increasing competition in the sale of annuities;
- regulatory changes or actions, including those relating to regulation of financial services affecting (among other things) bank sales and underwriting of insurance products and regulation of the sale, underwriting and pricing of products; and
- the risk factors or uncertainties listed from time to time in our filings with the SEC.

For a detailed discussion of these and other factors that might affect our performance, see Item 1A of this report.

Overview

We specialize in the sale of individual annuities (primarily deferred annuities) and, to a lesser extent, we also sell life insurance policies. Under U.S. generally accepted accounting principles ("GAAP"), premium collections for deferred annuities are reported as deposit liabilities instead of as revenues. Similarly, cash payments to policyholders are reported as decreases in the liabilities for policyholder account balances and not as expenses. Sources of revenues for products accounted for as deposit liabilities are net investment income; surrender and other charges deducted from the account balances of policyholders; net realized gains on investments, excluding other than temporary impairment losses; and changes in fair value of derivatives. Components of expenses for products accounted for as deposit liabilities are interest sensitive and index product benefits (primarily interest credited to account balances), changes in fair value of embedded derivatives, amortization of deferred sales inducements and deferred policy acquisition costs, other operating costs and expenses, and income taxes.

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Earnings from products accounted for as deposit liabilities are primarily generated from the excess of net investment income earned over the interest credited or the cost of providing index credits to the policyholder, or the "investment spread". Our investment spread is summarized as follows:

	Year Ended December 31,		
	2009	2008	2007
Average yield on invested assets	6.30%	6.20%	6.11%
Cost of money:			
Aggregate	3.26%	3.43%	3.50%
Cost of money for fixed index annuities	3.24%	3.43%	3.51%
Average crediting rate for fixed rate annuities:			
Annually adjustable	3.26%	3.26%	3.28%
Multi-year rate guaranteed	3.88%	3.88%	4.14%
Investment spread:			
Aggregate	3.04%	2.77%	2.61%
Fixed index annuities	3.06%	2.77%	2.60%
Fixed rate annuities:			
Annually adjustable	3.04%	2.94%	2.83%
Multi-year rate guaranteed	2.42%	2.32%	1.97%

The cost of money for fixed index annuities and average crediting rates for fixed rate annuities are computed based upon policyholder account balances and do not include the impact of amortization of deferred sales inducements. See Critical Accounting Policies Deferred Policy Acquisition Costs and Deferred Sales Inducements. With respect to our fixed index annuities, the cost of money includes the average crediting rate on amounts allocated to the fixed rate strategy, expenses we incur to fund the annual index credits and where applicable, minimum guaranteed interest credited. Proceeds received upon expiration or early termination of call options purchased to fund annual index credits are recorded as part of the change in fair value of derivatives, and are largely offset by an expense for interest credited to annuity policyholder account balances. See Critical Accounting Policies Policy Liabilities for Fixed Index Annuities and Financial Condition Derivative Instruments.

Our profitability depends in large part upon the amount of assets under our management, investment spreads we earn on our policyholder account balances, our ability to manage our investment portfolio to maximize returns and minimize risks such as interest rate changes and defaults or impairment of investments, our ability to manage interest rates credited to policyholders and costs of the options purchased to fund the annual index credits on our fixed index annuities, our ability to manage the costs of acquiring new business (principally commissions to agents and bonuses credited to policyholders) and our ability to manage our operating expenses.

Critical Accounting Policies

The increasing complexity of the business environment and applicable authoritative accounting guidance require us to closely monitor our accounting policies. We have identified five critical accounting policies that are complex and require significant judgment. The following summary of our critical accounting policies is intended to enhance your ability to assess our financial condition and results of operations and the potential volatility due to changes in estimates.

Valuation of Investments

Our fixed maturity securities (bonds and redeemable preferred stocks maturing more than one year after issuance) and equity securities (common and perpetual preferred stocks) classified as available for sale are reported at fair value. Unrealized gains and losses, if any, on these securities are included directly in stockholders' equity as a component of Accumulated Other Comprehensive Loss, net of income taxes and certain adjustments for assumed changes in amortization of deferred policy acquisition costs and deferred sales inducements. Unrealized gains and losses represent the difference between the amortized cost or cost basis and the fair value of these investments. We use significant judgment within the process used to determine fair value of these investments.

GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability (exit price) in an orderly transaction between market participants at the measurement date. We categorize our investments into three levels of fair value hierarchy based on the priority for use of inputs in determining fair value. The hierarchy defines the highest priority inputs (Level 1) as quoted prices in active markets for identical assets. The lowest priority inputs (Level 3) are our own assumptions about what a market participant would use in determining fair value such as estimated future cash flows. We categorize financial assets and liabilities recorded at fair value in the consolidated balance sheets as follows:

Level 1 Quoted prices are available in active markets for identical financial instruments as of the reporting date. We do not adjust the quoted price for these financial instruments, even in situations where we hold a large position and a sale could reasonably impact the quoted price.

Level 2 Quoted prices in active markets for similar financial instruments, quoted prices for identical or similar financial instruments in markets that are not active; and models and other valuation methodologies using inputs other than quoted prices that are observable.

Level 3 Models and other valuation methodologies using significant inputs that are unobservable for financial instruments and include situations where there is little, if any, market activity for the financial instrument. The inputs into the determination of fair value require significant management judgment or estimation. Financial instruments that are included in Level 3 are securities for which no market activity or data exists and for which we used discounted expected future cash flows with our own assumptions about what a market participant would use in determining fair value.

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The following table presents the fair value of fixed maturity and equity securities, available for sale, by pricing source and hierarchy level as of December 31, 2009 and 2008, respectively:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(Dollars in thousands)			
December 31, 2009				
Priced via third party pricing services	$ 154,035	$ 610,195	$	$ 764,230
Priced via independent broker quotations	2,545	9,945,634		9,948,179
Priced via matrices		53,647		53,647
Priced via other methods		13,243	17,918	31,161
	$ 156,580	$ 10,622,719	$ 17,918	$ 10,797,217
% of Total	1.5%	98.4%	0.2%	100.0%
December 31, 2008				
Priced via third party pricing services	$ 169,499	$ 1,839,770	$	$ 2,009,269
Priced via independent broker quotations	2,733	4,633,011		4,635,744
Priced via matrices		51,199		51,199
Priced via other methods		12,304	20,082	32,386
	$ 172,232	$ 6,536,284	$ 20,082	$ 6,728,598
% of Total	2.6%	97.1%	0.3%	100.0%

Management's assessment of all available data when determining fair value of our investments is necessary to appropriately apply fair value accounting.

Fair values of available for sale fixed maturity and equity securities are obtained primarily from a broker who starts by obtaining a price from an independent pricing source and adjusts for observable data. These prices from the independent broker undergo evaluation by our internal investment professionals. We generally obtain one price per security, which is compared to relevant credit information, perceived market movements and sector news. Market indices of similar rated asset class spreads are considered for valuations and broker indications of similar securities are compared. Inputs used by both the broker and the pricing service include market information, such as yield data and other factors relating to instruments or securities with similar characteristics. If the issuer has had trades in similar debt outstanding but not necessarily the same rank in the capital structure, spread information is used to support fair value. If discrepancies are identified, additional quotes are obtained and the quote that best reflects a fair value exit price at the reporting date is selected. In the case of private placement bonds, the broker typically starts with a price of a publicly traded bond of an entity that is comparable to size and financial position of the issuer of the private bond. The broker adjusts the price for factors such as marketability and risk factors specific to each security.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the investment.

We review the prices received from the independent brokers to ensure that the prices represent a reasonable estimate of fair value. This process involves quantitative and qualitative analysis and is administered by our investment department. This review process includes, but is not limited to, initial and on-going review of methodologies used by the independent broker, review of pricing statistics and

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trends, back testing recent trades, comparing prices to those obtained from other third party pricing services, reviewing cash flow activity in the subsequent period, monitoring credit rating upgrades and downgrades and monitoring of trading volumes. Most all of the information used by the pricing service and the independent broker can be corroborated by our procedures of investigating market data and tying that data to the facts utilized by the broker.

Evaluation of Other Than Temporary Impairments

The evaluation of investments for other than temporary impairments involves significant judgment and estimates by management. We review and analyze all investments on an ongoing basis for changes in market interest rates and credit deterioration. This review process includes analyzing our ability to recover the amortized cost or cost basis of each investment that has a fair value that is lower than its amortized cost or cost and requires a high degree of management judgment and involves uncertainty. The evaluation of securities for other than temporary impairments is a quantitative and qualitative process, which is subject to risks and uncertainties.

We have a policy and process in place to identify securities that could potentially have an impairment that is other than temporary. This process involves monitoring market events and other items that could impact issuers. The evaluation includes but is not limited to such factors as:

- the length of time and the extent to which the fair value has been less than amortized cost or cost;
- whether the issuer is current on all payments and all contractual payments have been made as agreed;
- the remaining payment terms and the financial condition and near-term prospects of the issuer;
- the lack of ability to refinance due to liquidity problems in the credit market;
- the fair value of any underlying collateral;
- the existence of any credit protection available;
- our intent to sell and whether it is more likely than not we would be required to sell debt securities prior to recovery;
- our assessment, in the case of equity securities including perpetual preferred stocks with credit deterioration, that the security cannot recover to cost in a reasonable period of time;
- our intent and ability to retain equity securities for a period of time sufficient to allow for recovery;
- consideration of rating agency actions; and
- changes in estimated cash flows of and residential mortgage and asset backed securities.

We determine whether other than temporary impairment losses should be recognized for debt and equity securities by assessing all facts and circumstances surrounding each security. Where the decline in market value of debt securities is attributable to changes in market interest rates or to factors such as market volatility, liquidity and spread widening, and we anticipate recovery of all contractual or expected cash flows, we do not consider these investments to be other than temporarily impaired because we do not intend to sell these investments and it is not more likely than not we will be required to sell these investments before a recovery of amortized cost, which may be maturity. For equity securities, we recognize an impairment charge in the period in which we do not have the intent and ability to hold the securities until recovery of cost or we determine that the security will not recover to book value within a reasonable period of time. We determine what constitutes a reasonable period of time on a security-by-security basis by considering all the evidence available to us, including the magnitude of any unrealized loss and its duration. In any event, this period does not exceed 18 months from the date of impairment for perpetual preferred securities for which there is evidence of deterioration in credit of the issuer and common equity securities. For perpetual preferred securities absent evidence of a deterioration in credit of the issuer we apply an impairment model, including an anticipated recovery period, similar to a debt security.

Other than temporary impairment losses on equity securities are recognized in operations. If we intend to sell a debt security or if it is more likely than not that we will be required to sell a debt security before recovery of its amortized cost basis, other than temporary impairment has occurred and the difference between amortized cost and fair value will be recognized as a loss in operations.

If we do not intend to sell and it is not more likely than not we will be required to sell the debt security but also do not expect to recover the entire amortized cost basis of the security, an impairment loss would be recognized in operations in the amount of the expected credit loss. We determine the amount of expected credit loss by calculating the present value of the cash flows expected to be collected. The difference between the present value of expected future cash flows and the amortized cost basis of the security is the amount of credit loss recognized in operations. The remaining amount of the other than temporary impairment is recognized in other comprehensive income.

The determination of the credit loss component of a residential mortgage backed security is based on a number of factors. The primary consideration in this evaluation process is the issuer's ability to meet current and future interest and principal payments as contractually stated at time of purchase. Our review of these securities includes an analysis of the cash flow modeling under various default scenarios considering independent third party benchmarks, the seniority of the specific tranche within the structure of the security, the composition of the collateral and the actual default, loss severity and prepayment experience exhibited. With the input of third party assumptions for default projections, loss severity and prepayment expectations, we evaluate the cash flow projections to determine whether the security is performing in accordance with its contractual obligation.

We utilize the models from a leading structured product software specialist serving institutional investors. These models incorporate each security's seniority and cash flow structure. In circumstances where the analysis implies a potential for principal loss at some point in the future, we use our "best estimate" cash flow projection discounted at the security's effective yield at acquisition to determine the amount of our potential credit loss associated with this security. The discounted expected future cash flows equates to our expected recovery value. Any shortfall of the expected recovery when compared to the amortized cost of the security will be recorded as the credit loss component of other than temporary impairment.

The cash flow modeling is performed on a security-by-security basis and incorporates actual cash flows on the residential mortgage backed securities through the current period, as well as the projection of remaining cash flows using a number of assumptions including default rates, prepayment rates and loss severity rates. The default curves we use are tailored to the Prime or Alt-A residential mortgage backed securities that we own, which assume lower default rates and loss severity for Prime securities versus Alt-A securities. These default curves are scaled higher or lower depending on factors such as current underlying mortgage loan performance, rating agency loss projections, loan to value ratios, geographic diversity, as well as other appropriate considerations. The default curves generally assume lower loss levels for older vintage securities versus more recent vintage securities, which reflects the decline in underwriting standards over the years.

The determination of the credit loss component of a corporate bond (including redeemable preferred stocks) is based on the underlying financial performance of the issuer and their ability to meet their contractual obligations. Considerations in our evaluation include, but are not limited to, credit rating changes, financial statement and ratio analysis, changes in management, large changes in credit spreads, breaches of financial covenants and a review of the economic outlook for the industry

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and markets in which they trade. In circumstances where an issuer appears unlikely to meet its future obligation, or the security's price decline is deemed other than temporary, an estimate of credit loss is determined. Credit loss is calculated using default probabilities as derived from the credit default swaps markets in conjunction with recovery rates derived from independent third party analysis or a best estimate of credit loss. This credit loss rate is then incorporated into a present value calculation based on an expected principal loss in the future discounted at the yield at the date of purchase and compared to amortized cost to determine the amount of credit loss associated with the security.

In addition, for debt securities which we do not intend to sell and it is not more likely than not we will be required to sell, but our intent changes due to changes or events that could not have been reasonably anticipated, an other than temporary impairment charge is recognized. Once an impairment charge has been recorded, we then continue to review the other than temporarily impaired securities for appropriate valuation on an ongoing basis. Unrealized losses may be recognized in future periods through a charge to earnings, should we later conclude that the decline in fair value below amortized cost is other than temporary pursuant to our accounting policy described above. The use of different methodologies and assumptions to determine the fair value of investments and the timing and amount of impairments may have a material effect on the amounts presented in our consolidated financial statements.

Policy Liabilities for Fixed Index Annuities

We offer a variety of fixed index annuities with crediting strategies linked to the S&P 500 Index and other equity and bond market indices. We purchase call options on the applicable indices as an investment to provide the income needed to fund the annual index credits on the index products. See Financial Condition Derivative Instruments. Certain derivative instruments embedded in the fixed index annuity contracts are recognized in the consolidated balance sheet at their fair values and changes in fair value are recognized immediately in our consolidated statements of operations in accordance with accounting standards for derivative instruments and hedging activities.

Accounting for derivatives prescribes that the contractual obligations for future annual index credits are treated as a "series of embedded derivatives" over the expected life of the applicable contracts. Policy liabilities for fixed index annuities are equal to the sum of the "host" (or guaranteed) component and the embedded derivative component for each fixed index annuity policy. The host value is established at inception of the contract and accreted over the policy's life at a constant rate of interest. We estimate the fair value of the embedded derivative component at each valuation date by (i) projecting policy contract values and minimum guaranteed contract values over the expected lives of the contracts and (ii) discounting the excess of the projected contract value amounts at the applicable risk free interest rates adjusted for our nonperformance risk related to those liabilities. The projections of policy contract values are based on our best estimate assumptions for future policy growth and future policy decrements. Our best estimate assumptions for future policy growth include assumptions for the expected index credit on the next policy anniversary date which are derived from the fair values of the underlying call options purchased to fund such index credits and the expected costs of annual call options we will purchase in the future to fund index credits beyond the next policy anniversary. The projections of minimum guaranteed contract values include the same best estimate assumptions for policy decrements as were used to project policy contract values. The amounts reported in the consolidated statements of operations as "Interest sensitive and index product benefits" represent amounts credited to policy liabilities pursuant to accounting by insurance companies for certain long-duration contracts which include index credits through the most recent policy anniversary. The amounts reported in the consolidated statements of operations as "Changes in fair value of embedded derivatives" equal the change in the difference between policy benefit reserves for fixed index annuities computed under the derivative accounting standard and the long-duration contracts accounting standard at each balance sheet date.

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In general, the change in the fair value of the embedded derivatives will not correspond to the change in fair value of the purchased call options because the purchased call options are one year options while the options valued in the embedded derivatives represent the rights of the contract holder to receive index credits over the entire period the fixed index annuities are expected to be in force, which typically exceeds 10 years.

The most sensitive assumption in determining policy liabilities for fixed index annuities is the rates used to discount the excess projected contract values. As indicated above, the discount rate reflects our nonperformance risk. If the discount rates used to discount the excess projected contract values at December 31, 2009 were to increase by 100 basis points, our reserves for fixed index annuities would decrease by $81.1 million recorded through operations as a decrease in the change in fair value of embedded derivatives and there would be a corresponding decrease of $50.1 million to our combined balance for deferred policy acquisition costs and deferred sales inducements recorded through operations as an increase in amortization of deferred policy acquisition costs and deferred sales inducements. A decrease by 100 basis points in the discount rate used to discount the excess projected contract values would increase our reserves for fixed index annuities by $90.0 million recorded through operations as a increase in the change in fair value of embedded derivatives and increase our combined balance for deferred policy acquisition costs and deferred sales inducements by $56.1 million recorded through operations as a decrease in amortization of deferred policy acquisition costs and deferred sales inducements.

Deferred Policy Acquisition Costs and Deferred Sales Inducements

Costs relating to the production of new business are not expensed when incurred but instead are capitalized as deferred policy acquisition costs or deferred sales inducements. Only costs which are expected to be recovered from future policy revenues and gross profits may be deferred. Deferred policy acquisition costs and deferred sales inducements are subject to loss recognition testing on a quarterly basis or when an event occurs that may warrant loss recognition. Deferred policy acquisition costs consist principally of commissions and certain costs of policy issuance. Deferred sales inducements consist of premium and interest bonuses credited to policyholder account balances.

For annuity products, these costs are being amortized generally in proportion to expected gross profits from interest margins and, to a lesser extent, from surrender charges. Current and future period gross profits/margins for fixed index annuities also include the impact of amounts recorded for the change in fair value of derivatives and the change in fair value of embedded derivatives. Current period amortization is adjusted retrospectively through an unlocking process when estimates of current or future gross profits/margins (including the impact of realized investment gains and losses) to be realized from a group of products are revised. Our estimates of future gross profits/margins are based on actuarial assumptions related to the underlying policies terms, lives of the policies, yield on investments supporting the liabilities and level of expenses necessary to maintain the polices over their entire lives. Revisions are made based on historical results and our best estimates of future experience.

The impact of unlocking during 2008 was a $1.3 million increase in the amortization of deferred sales inducements and a $14.6 million increase in amortization of deferred policy acquisition costs. The impact of unlocking during 2008 was primarily due to actual index credits to policies being lower than what was estimated due to the lack of performance of the indices upon which the index credits are based. There were no changes in our estimated future gross profits in 2009 and 2007 that resulted in unlocking adjustments to the deferred policy acquisition costs and deferred sales inducements balances.

Estimated future gross profits vary based on a number of sources including investment spread margins, surrender charge income, policy persistency, policy administrative expenses and realized gains and losses on investments including credit related other than temporary impairment losses. Estimated future gross profits are most sensitive to changes in investment spread margins which are the most significant component of gross profits. If estimated gross profits for all future years on business in force at December 31, 2009 were to increase by 10%, our combined balance for deferred policy acquisition costs and deferred sales inducements at December 31, 2009 would increase by $51.5 million recorded through operations as a decrease to amortization of deferred policy acquisition costs and deferred sales inducements. Correspondingly, a 10% decrease in estimated gross profits for all future years would result in a $57.7 million decrease in the combined December 31, 2009 balances recorded through operations as an increase to amortization of deferred policy acquisition costs and deferred sales inducements.

Deferred Income Taxes

We account for income taxes using the liability method. This method provides for the tax effects of transactions reported in the consolidated financial statements for both taxes currently due and deferred. Deferred income taxes reflect the impact of temporary differences between the amount of assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. A temporary difference is a transaction, or amount of a transaction, that is recognized currently for financial reporting purposes but will not be recognized for tax purposes until a future tax period, or is recognized currently for tax purposes but will not be recognized for financial reporting purposes until a future reporting period. Deferred income taxes are measured by applying enacted tax rates for the years in which the temporary differences are expected to be recovered or settled to the amount of each temporary difference.

The realization of deferred income tax assets is primarily based upon management's estimates of future taxable income. Valuation allowances are established when management estimates, based on available information, that it is more likely than not that deferred income tax assets will not be realized. Significant judgment is required in determining whether valuation allowances should be established, as well as the amount of such allowances. When making such determination, consideration is given to, among other things, the following:

- future taxable income of the necessary character exclusive of reversing temporary differences and carryforwards;
- future reversals of existing taxable temporary differences;
- taxable income in prior carryback years; and
- tax planning strategies.

Actual realization of deferred income tax assets and liabilities may materially differ from these estimates as a result of changes in tax laws as well as unanticipated future transactions impacting related income tax balances.

The realization of deferred income tax assets related to unrealized losses on our available for sale fixed maturity securities is also based upon our intent to hold these securities for a period of time sufficient to allow for a recovery in fair value and not realize the unrealized loss.

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Results of Operations for the Three Years Ended December 31, 2009

Annuity deposits by product type collected during 2009, 2008 and 2007, were as follows:

Product Type	Year Ended December 31, 2009	2008	2007
	(Dollars in thousands)		
Fixed index annuities:			
Index strategies	$ 1,535,477	$ 1,303,871	$ 1,578,347
Fixed strategy	1,849,833	937,227	515,229
	3,385,310	2,241,098	2,093,576
Fixed rate annuities:			
Single-year rate guaranteed	113,511	28,930	45,948
Multi-year rate guaranteed	178,737	18,978	5,158
	292,248	47,908	51,106
Total before coinsurance ceded	3,677,558	2,289,006	2,144,682
Coinsurance ceded	749,260	1,310	1,779
Net after coinsurance ceded	$ 2,928,298	$ 2,287,696	$ 2,142,903

Annuity deposits before coinsurance ceded increased 61% during 2009 compared to 2008 and 7% during 2008 compared to 2007. We attribute these increases to several factors, including our continued strong relationships with our national marketing organizations and field force of licensed, independent insurance agents, the increased attractiveness of safe money products in volatile markets, lower interest rates on competing products such as bank certificates of deposit and product enhancements including a new generation of guaranteed income withdrawal benefit riders. In addition, we have benefitted during 2009 from the actions of several significant competitors who have restricted their capacity to accept new business. The extent to which this trend will be sustained in future periods is uncertain. While we have the capital resources to accept more business, our capacity is not unlimited and sales growth must be matched with available capital resources to maintain desired financial strength ratings from credit rating agencies and in particular, A.M. Best Company. Toward this end, effective June 1, 2009, we restructured our payment of commissions to agents on new sales by reducing the amount of commission paid at the time of sale but providing for additional commission payments on the first and second anniversaries of the date a policy was issued. This change will initially increase our statutory earnings and capital and surplus and our capacity to accept new business. It is uncertain what impact the change will have on the agents' willingness to sell business for us. During 2009 we also amended one of our reinsurance agreements with Hannover Life Reassurance Company of America to include certain policy forms that were not in existence in 2005 when the agreement was executed. Effective July 1, 2009 we entered into two reinsurance arrangements with a newly formed reinsurance company to reinsure on a funds withheld coinsurance basis 20% of the annuity deposits received in 2009 from our two top selling fixed index annuity products and 80% of the annuity deposits received after June 30, 2009 from a multi-year rate guaranteed fixed annuity product. Our objective with these agreements is to manage our retained new business growth (net annuity deposits after coinsurance ceded) to a maximum of $3 billion for 2009. These reinsurance arrangements resulted in the significant increase in coinsurance ceded annuity deposits for 2009 in the table above. We have extended the 2009 agreement to cede 20% of our fixed index annuities to those issued through March 31, 2010.

Net income increased 330% to $68.5 million in 2009 and decreased 39% to $15.9 million in 2008 from $26.2 million in 2007. Net income for 2009 includes the impact of applying the FASB guidance for recognition and presentation of other than temporary impairments that was released in April 2009 as discussed below. Net income for 2008 includes the impact of the adoption of fair value measurement accounting standards as discussed below.

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Net income has been positively impacted by the growth in the volume of business in force and the investment spread earned on this business. Average annuity account values outstanding increased 14% for the year ended December 31, 2009 compared to 2008 and 13% for the year ended December 31, 2008 compared to 2007. Our investment spread measured on a percentage basis was 3.04%, 2.77% and 2.61% for the years ended December 31, 2009, 2008 and 2007, respectively. The increase in investment spread resulted from a higher investment yield earned on average assets due to higher yields on investments purchased subsequent to 2007 and a lower aggregate cost of money on our fixed index annuities. The lower cost of money for fixed index annuities during 2009 and 2008 was due to adjustments we made throughout 2007 to caps, participation rates and asset fees to manage the cost of options purchased to fund the annual index credits. The benefit from these adjustments was not fully recognized until the fourth quarter of 2008.

The comparability of the amounts is significantly impacted by net realized gains on investments and net impairment losses on investments recognized in operations, gain (loss) on retirement of debt, the impact of fair value accounting for fixed index annuity derivatives and embedded derivatives and the impact of a counterparty default on expired derivatives contracts. We estimate that these items increased (decreased) net income as follows:

	Year Ended December 31,		
	2009	2008	2007
	(Dollars in thousands)		
Net realized gains and net impairment losses on investments recognized in operations	$ 1,339	$ (92,524)	$ (1,688)
Gain (loss) on retirement of debt	(687)	5,702	
Change in fair value of fixed index annuity derivatives and embedded derivatives	(29,945)	31,125	(33,615)
Effect of counterparty default	(3,948)	(741)	

Net realized gains on investments and net impairment losses recognized in operations fluctuate from year to year based upon changes in the interest rate and economic environment and the timing of the sale of investments or the recognition of other than temporary impairments. We adopted the FASB guidance for recognition and presentation of other than temporary impairments that was released in April 2009 on January 1, 2009, which amended the determination of the amount of other than temporary impairments recognized in the statement of operations resulting in the noncredit portion of other than temporary impairments being recognized in other comprehensive income for debt securities that we do not intend to sell and it is not more likely than not we will be required to sell but also do not expect to recover the entire amortized cost basis of the security. The amounts disclosed above are net of related reductions in amortization of deferred sales inducements and deferred policy acquisition costs and income taxes. Income tax benefits related to net realized gains on investments and net other than temporary impairment losses recognized in operations were reduced by $34.5 million in 2008 for the establishment of a deferred tax valuation allowance related to the other than temporary impairments and capital loss carryforwards. Net income for 2009 includes a benefit of $11.9 million for the reduction of the deferred tax valuation allowance related to other than temporary impairments and capital loss carryforwards.

Amounts attributable to the fair value accounting for fixed index annuity derivatives and embedded derivatives fluctuate from year to year based upon changes in the fair values of call options purchased to fund the annual index credits for fixed index annuities and changes in the interest rates used to discount the embedded derivative liability. The amounts disclosed above are net of related adjustments to amortization of deferred sales inducements and deferred policy acquisition costs and income taxes. The significant changes in the impact from this item disclosed above relate primarily to changes in the interest rates used to discount the embedded derivative liabilities. Pursuant to fair value measurements accounting standards adopted prospectively on January 1, 2008, the discount rates are based on risk-free interest rates adjusted for our nonperformance risk. These rates decreased materially during the year ended December 31, 2009 resulting in decreases in net income for the year. Prior to the adoption of the fair value measurements accounting standards, the discount rates used were risk-free interest rates without adjustment for our nonperformance risk. The change to discount rates including our nonperformance risk resulted in a decrease in policy benefit reserves on January 1, 2008 of $150.6 million. The net income impact of this decrease in reserves net of the related adjustments to amortization of deferred sales inducements and deferred policy acquisition costs and income taxes was $40.7 million.

Annuity product charges (surrender charges assessed against policy withdrawals and fees deducted from policyholder account balances for living income benefit riders) increased 20% to $63.4 million in 2009 and 15% to $52.7 million in 2008 from $45.8 million in 2007. Product charges for the year ended December 31, 2009 include $4.5 million of fees deducted from policyholder account balances for living income benefit riders. Surrender charges fluctuate from year to year based upon policyholder behavior and have generally increased during 2009 and 2008 consistent with growth in the volume of business in force.

Net investment income increased 13% to $932.2 million in 2009 and 14% to $822.1 million in 2008 from $719.9 million in 2007. These increases were principally attributable to the growth in our annuity business and corresponding increases in our invested assets and the average yield earned on investments. Average invested assets (on an amortized cost basis) excluding derivative instruments increased 12% to $14.8 billion at December 31, 2009 and 6% to $13.2 billion at December 31, 2008 compared to $12.5 billion at December 31, 2007. The average yield earned on average invested assets was 6.30%, 6.20% and 6.11% for 2009, 2008 and 2007, respectively. The increase in the yield earned on average invested assets for 2009 and 2008 was attributable to higher yields on investments purchased subsequent to 2007.

Change in fair value of derivatives (principally call options purchased to fund annual index credits on fixed index annuities) is affected by the performance of the indices upon which our options are based and the aggregate cost of options purchased. The components of change in fair value of derivatives are as follows:

	Year Ended December 31,		
	2009	**2008**	**2007**
		(Dollars in thousands)	
Call options:			
Gain (loss) on option expiration	$ (196,000)	$ (270,361)	$ 183,488
Change in unrealized gain (loss)	415,276	(100,453)	(242,199)
Interest rate swaps	(2,380)	(1,195)	(1,274)
	$ 216,896	$ (372,009)	$ (59,985)

The differences between the change in fair value of derivatives between years are primarily due to the performance of the indices upon which our call options are based. A substantial portion of our call options are based upon the S&P 500 Index with the remainder based upon other equity and bond market indices. The range of index appreciation for options expiring during the years ended December 31, 2009, 2008 and 2007 is as follows:

	Year Ended December 31,					
	2009		2008		2007	
S&P 500 Index						
Point-to-point strategy	0.0%	45.1%	0.0%	2.6%	6.9%	24.4%
Monthly average strategy	0.0%	22.9%	0.0%	6.4%	1.2%	14.1%
Monthly point-to-point strategy	0.0%	9.9%	0.0%	0.0%	0.0%	18.8%
Lehman Brothers U.S. Aggregate and U.S. Treasury indices	0.0%	13.8%	0.3%	7.0%	2.6%	8.8%

Actual amounts credited to policyholder account balances may be less than the index appreciation due to contractual features in the fixed index annuity policies (caps, participation rates, and asset fees) which allow us to manage the cost of the options purchased to fund the annual index credits. The change in fair value of derivatives is also influenced by the aggregate costs of options purchased. The aggregate cost of options has increased primarily due to an increased amount of fixed index annuities in force. The aggregate cost of options is also influenced by the amount of policyholder funds allocated to the various indices and market volatility which affects option pricing. Costs for options purchased during the year ended December 31, 2009 and 2008 decreased compared to prior years due to adjustments to caps, participation rates, and asset fees.

We had unsecured counterparty exposure in connection with options purchased from affiliates of Lehman which declared bankruptcy during the third quarter of 2008, and at December 31, 2008, all options purchased from affiliates of Lehman carried a fair value of zero. Except for a few options involving immaterial amounts, all options purchased from affiliates of Lehman have expired as of December 31, 2009. The amount of option proceeds due on expired options purchased from affiliates of Lehman that we did not receive payment on was $12.0 million and $2.1 million for the year ended December 31, 2009 and 2008, respectively. No amount has been recognized for any recovery of these amounts that may result from our claim in Lehman's bankruptcy proceedings.

Net realized gains on investments, excluding OTTI losses include gains and losses on the sale of securities and impairment losses on mortgage loans on real estate which fluctuate from year to year due to changes in the interest rate and economic environment and the timing of the sale of investments. The components of net realized gains on investments for the years ended December 31, 2009, 2008 and 2007 are set forth in the table that follows:

	Year Ended December 31,		
	2009	2008	2007
	(Dollars in thousands)		
Available for sale fixed maturity securities:			
Gross realized gains	$ 54,401	$ 5,852	$ 931
Gross realized losses	(2,162)	(589)	(88)
	52,239	5,263	843
Equity securities:			
Gross realized gains	5,620	292	232
Gross realized losses	(96)		(574)
	5,524	292	(342)
Mortgage loans on real estate:			
Impairment losses	(6,484)		
	$ 51,279	$ 5,555	$ 501

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Gross realized gains have increased in 2009 due to tax planning strategies to generate taxable capital gains that will permit deduction of capital losses for income tax purposes. Gross realized losses in 2009 primarily relate to three securities that experienced credit events during 2009 resulting in the decision to sell the securities at a loss. See Financial Condition Investments for additional discussion of impairment losses recognized on mortgage loans on real estate.

Net OTTI losses recognized in operations decreased to $86.8 million in 2009 and increased to $192.6 million in 2008 from $4.4 million in 2007. See Financial Condition Investments for additional discussion of write downs of securities for other than temporary impairments.

Gain (loss) on retirement of debt for 2009 includes a $3.1 million gain on an exchange of five million shares of our common stock for $37.2 million principal amount of our 5.25% contingent convertible senior notes due in December 2024 (the "2024 notes") and a $3.8 million loss on an exchange of $63.6 million principal amount of our 5.25% contingent convertible senior notes due in December 2029 for the same principal amount of the 2024 notes. The fair value of the common stock issued was $31.3 million and the 2024 notes retired in the common stock for debt exchange carried unamortized debt discount and debt issue costs totaling $2.8 million. The 2024 notes retired in the debt for debt exchange carried unamortized debt discount and debt issue costs totaling $3.8 million. The $9.7 million gain on retirement of debt in 2008 resulted from the purchase of $78.1 million principal amount of the 2024 notes for $61.4 million in cash, of which $0.4 million was assigned to the reacquisition of the equity component of the 2024 notes. The 2024 notes retired in 2008 carried unamortized debt discount and debt issue costs totaling $7.4 million.

Interest sensitive and index product benefits increased 70% to $347.9 million in 2009 and decreased 63% to $205.1 million in 2008 from $560.2 million in 2007. The components of interest credited to account balances are summarized as follows:

	Year Ended December 31,		
	2009	2008	2007
	(Dollars in thousands)		
Index credits on index policies	$ 94,601	$ 33,337	$ 403,416
Interest credited (including changes in minimum guaranteed interest for fixed index annuities)	249,015	171,794	156,793
Living income benefit rider	4,267		
	$ 347,883	$ 205,131	$ 560,209

The changes in index credits were attributable to changes in the appreciation of the underlying indices (see discussion above under change in fair value of derivatives) and the amount of funds allocated by policyholders to the respective index options. Total proceeds received upon expiration of the call options purchased to fund the annual index credits were $70.6 million, $26.2 million and $392.1 million for the years ended December 31, 2009, 2008 and 2007, respectively. Proceeds for 2009 were adversely affected by the Lehman defaults as discussed above. The increases in interest credited for 2009 and 2008 was due to an increase in the average amount of annuity liabilities outstanding receiving a fixed rate of interest and an increase in minimum guaranteed interest for fixed index annuities. The increase in minimum guaranteed interest for fixed index annuities is directly attributable to the weak equity market performance during prior periods which resulted in smaller index credits. The increase in interest credited for 2008 included an immaterial correction to single premium annuity reserves in the fourth quarter of 2008 which reduced interest credited by $2.2 million. The average amount of annuity liabilities outstanding (net of annuity liabilities ceded under coinsurance agreements) increased 14% to $15.4 billion in 2009 and 13% to $13.5 billion in 2008 from $11.9 billion in 2007.

Amortization of deferred sales inducements increased 30% to $40.0 million in 2009 and 162% to $30.7 million in 2008 from $11.7 million in 2007. The 2008 increase includes the $1.3 million impact of unlocking discussed above. In general, amortization of deferred sales inducements has been increasing each year due to growth in our annuity business and the deferral of sales inducements incurred with respect to sales of premium bonus annuity products. Bonus products represented 94%, 93% and 86% of our total annuity deposits during 2009, 2008 and 2007, respectively. The anticipated increase in amortization from these factors has been affected by amortization associated with fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business and amortization associated with the net realized gains on investments and net OTTI losses recognized in operations.

Fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business creates differences in the recognition of revenues and expenses from derivative instruments including the embedded derivative liabilities in our fixed index annuity contracts. The change in fair value of the embedded derivatives will not correspond to the change in fair value of the derivatives (purchased call options) because the purchased call options are one-year options while the options valued in the fair value of embedded derivatives cover the expected life of the contracts which typically exceeds ten years. The gross profit adjustments resulting from fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business decreased amortization by $29.2 million, increased amortization by $13.9 million, and decreased amortization by $23.4 million in 2009, 2008 and 2007, respectively. The gross profit adjustments from net realized gains on investments and net OTTI losses recognized in operations decreased amortization by $6.8 million, $35.6 million and $0.3 million in 2009, 2008 and 2007, respectively. Excluding the amortization amounts attributable to fair value accounting for derivatives and embedded derivatives and realized gains on investments and net OTTI losses recognized in operations, amortization would have been $76.0 million, $52.4 million and $35.4 million for 2009, 2008 and 2007, respectively. See Critical Accounting Policies Deferred Policy Acquisition Costs and Deferred Sales Inducements.

Change in fair value of embedded derivatives was an increase of $529.5 million during 2009 compared to decreases of $210.8 million in 2008 and $67.9 million in 2007. These changes resulted from (i) changes in the expected index credits on the next policy anniversary dates, which are related to the change in fair value of the call options acquired to fund these index credits discussed above in change in fair value of derivatives; (ii) changes in discount rates used in estimating our liability for policy growth; (iii) changes in estimates of expected costs of annual call options that will be purchased in the future to fund index credits beyond the next policy anniversary; and (iv) the growth in the host component of the policy liability. See Critical Accounting Policies Policy Liabilities for Fixed Index Annuities. The primary reasons for the significant increases in the fair values of embedded derivatives for 2009 were decreases in the discount rates used in estimating our liability for policy growth and increases in the expected index credits on the next policy anniversary dates which correlated with the change in fair value of derivatives discussed above. The primary reasons for the significant decrease in the fair value of the embedded derivatives for 2008 were increases in the discount rates used in estimating our liability for policy growth and a decrease in our estimate of the expected future cost of annual call options. The increase in the discount rates to reflect our nonperformance risk upon the adoption of the fair value measurements accounting requirements on January 1, 2008 as discussed above decreased the fair value of embedded derivatives by $150.6 million and the decrease in the estimate of future option costs decreased the fair value of the embedded derivatives for 2008 by $51.6 million.

Interest expense on notes payable decreased 25% to $14.9 million in 2009 and decreased 5% to $19.8 million in 2008 from $20.9 million in 2007. These decreases were primarily attributable to the retirement of $78.1 million principal amount of our 2024 notes during 2008 and retirement of $37.2 million principal amount of our 2024 notes through the exchange of five million shares of our common stock in the second quarter of 2009. This decrease in interest expense on notes payable was offset in part by interest on borrowings under our revolving line of credit, which had a weighted average interest rate of 1.49% and 4.15% for the year ended December 31, 2009 and 2008, respectively.

The average borrowings outstanding under the line of credit were $113.3 million and $35.9 million for the years ended December 31, 2009 and 2008, respectively. Absent any further retirements of the 2024 notes, interest expense on notes payable will increase in 2010 due to the December 2009 issuance of convertible senior notes that carry an effective interest rate of 11.8%, offset in part by a decrease in interest for the 2024 notes that were retired in December 2009. See note 9 to our audited consolidated financial statements.

Interest expense on subordinated debentures decreased 19% to $15.8 million in 2009 and 14% to $19.4 million in 2008 from $22.5 million in 2007. These decreases were primarily due to decreases in the weighted average interest rates on the outstanding subordinated debentures which were 5.82%, 7.15% and 8.32% for 2009, 2008 and 2007, respectively. The weighted average interest rates have decreased because $149.0 million principal amount of the subordinated debentures have a floating rate of interest based upon the three month London Interbank Offered Rate plus an applicable margin. See Financial Condition Liabilities.

Interest expense on amounts due under repurchase agreements decreased 93% to $0.5 million in 2009 and 48% to $8.2 million in 2008 from $15.9 million in 2007. These decreases were principally due to decreases in the borrowings outstanding and decreases in the weighted average interest rates on amounts borrowed. Weighted average interest rates were 0.35%, 2.28% and 5.27% for 2009, 2008 and 2007, respectively, and average borrowings outstanding were $150.7 million, $359.9 million and $301.9 million during 2009, 2008 and 2007, respectively. The decrease in the average borrowings outstanding for 2009 was due to the high level of calls on investment securities during the year. See Financial Condition Investments.

Amortization of deferred policy acquisition costs decreased 31% to $88.0 million in 2009 and increased 125% to $126.7 million in 2008 from $56.3 million in 2007. The 2008 increase includes the $14.6 million impact of unlocking discussed above. In general, amortization of deferred policy acquisition costs has been increasing each year due to the growth in our annuity business and the deferral of policy acquisition costs incurred with respect to sales of annuity products. The anticipated increase in amortization from these factors has been affected by amortization associated with fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business and amortization associated with net realized gains on investments and net OTTI losses recognized in operations.

As discussed above, fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business creates differences in the recognition of revenues and expenses from derivative instruments including the embedded derivative liabilities in our fixed index annuity contracts. The gross profit adjustments resulting from fair value accounting for derivatives and embedded derivatives utilized in our fixed index annuity business decreased amortization by $60.6 million, increased amortization by $44.2 million, and decreased amortization by $52.3 million in 2009, 2008 and 2007, respectively. The gross profit adjustments from net realized gains on investments and net OTTI losses recognized in operations decreased amortization by $12.2 million, $61.6 million and $0.9 million for 2009, 2008 and 2007, respectively. Excluding the amortization amounts attributable to fair value accounting for derivatives and net realized gains on investments and net OTTI losses recognized in operations, amortization would have been $160.9 million, $144.2 million and $109.5 million for 2009, 2008 and 2007, respectively.

Other operating costs and expenses increased 9% to $57.3 million in 2009 and 9% to $52.6 million in 2008 from $48.2 million in 2007. The increase in 2009 was principally attributable to an increase in salaries and benefits of $3.3 million, increase in risk charges on reinsurance of $3.7 million, increase in general overhead of $1.0 million offset by a decrease in legal expense of $3.1 million. The increase in salaries and benefits for 2009 was primarily due to an increase in the number of employees due to the growth in our business. Also, we recorded post employment benefit expense of $1.2 million during the second quarter of 2009 related to a post employment benefit agreement with our Executive Chairman, David J. Noble which was approved by our board of directors on June 4, 2009. The increase in risk charges on reinsurance was due to a reinsurance treaty entered into on December 31, 2008 and the expansion of the inforce business covered under an existing reinsurance treaty during the second quarter of 2009. The increase in general overhead costs was due to the growth in our business from increased sales. The decreases in legal expense were primarily related to a decrease in the cost of defense related to ongoing litigation. The increase in 2008 was principally attributable to increases in salaries and benefits of $4.3 million and $1.0 million in general overhead due to the growth in our business from increased sales, offset by a decrease in legal expense of $0.8 million due to a decrease in the cost of defense related to ongoing litigation.

Income tax expense decreased 71% to $17.6 million in 2009 and increased 413% to $61.1 million in 2008 from $11.9 million in 2007. These changes were primarily related to changes in income before income taxes and the impact of changes in the valuation allowance for deferred income tax assets related to capital loss carryforwards and other than temporary impairments on investment securities. The effective tax rates were 20.5%, 79.3% and 31.2% for 2009, 2008 and 2007, respectively. The effective tax rate for 2009 was less than the applicable statutory federal income tax rate of 35% primarily due to a decrease in the deferred income tax asset valuation allowance established in 2008 for capital loss carryforwards and other than temporary impairments which decreased income tax expense in 2009 by $11.9 million. This decrease was primarily due to current year taxable income from capital gain sources which resulted from the recognition of net realized gains on available for sale fixed maturity and equity securities that were sold as part of a tax planning strategy to generate capital gains to offset capital losses as discussed above. The effective tax rate for 2008 was more than the applicable statutory federal income tax rate of 35% primarily due to the establishment of a valuation allowance for deferred income tax assets related to capital loss carryforwards and other than temporary impairments on investment securities. See note 8 to our consolidated financial statements. The effective tax rate for 2007 was less than the applicable statutory federal income tax rate of 35% primarily due to state income tax benefits attributable to losses in the non-life subgroup.

Financial Condition

Investments

Our investment strategy is to maintain a predominantly investment grade fixed income portfolio, provide adequate liquidity to meet our cash obligations to policyholders and others and maximize current income and total investment return through active investment management. Consistent with this strategy, our investments principally consist of fixed maturity securities, mortgage loans on real estate and short-term investments.

Insurance statutes regulate the type of investments that our life subsidiaries are permitted to make and limit the amount of funds that may be used for any one type of investment. In light of these statutes and regulations and our business and investment strategy, we generally seek to invest in United States government and government-sponsored agency securities and corporate securities rated investment grade by established nationally recognized rating organizations or in securities of comparable investment quality, if not rated and commercial mortgage loans on real estate.

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The composition of our investment portfolio is summarized as follows:

	December 31,					
	2009			2008		
	Carrying Amount		Percent	Carrying Amount		Percent
	(Dollars in thousands)					
Fixed maturity securities:						
United States Government full faith and credit	$	3,310		$	22,050	0.2%
United States Government sponsored agencies		5,557,971	36.2%		6,633,481	52.1%
U.S. states, territories and political subdivisions		355,634	2.3%			
Corporate securities		3,933,198	25.6%		1,777,821	14.0%
Residential mortgage backed securities		2,489,101	16.2%		1,799,843	14.2%
Total fixed maturity securities		12,339,214	80.3%		10,233,195	80.5%
Equity securities		93,086	0.6%		99,552	0.8%
Mortgage loans on real estate		2,449,778	15.9%		2,329,824	18.3%
Derivative instruments		479,272	3.1%		56,588	0.4%
Other investments		12,760	0.1%		446	
	$	15,374,110	100.0%	$	12,719,605	100.0%

During 2009 and 2008, we received $4.2 billion and $2.8 billion, respectively, in net redemption proceeds related to calls of our callable United States Government sponsored agency securities, of which $2.1 billion and $2.0 billion, respectively, were classified as held for investment. We reinvested the proceeds from these redemptions primarily in United States Government sponsored agencies, corporate fixed maturity securities and residential mortgage backed securities classified as available for sale. At December 31, 2009, 50% of our fixed income securities have call features and 8% of those securities were subject to call redemption. Another 38% of our fixed income securities will become subject to call redemption during 2010.

Fixed Maturity Securities

Our fixed maturity portfolio is managed to minimize risks such as interest rate changes and defaults or impairments while earning a sufficient return on our investments. We have over 36% of our fixed maturities invested in U.S. federal government sponsored agency securities (Federal Home Loan Mortgage Corporation and Federal National Mortgage Association make up the majority), which are an excellent source of dependable income and are of high credit quality. Since 2007 we have built a portfolio of residential mortgage backed securities ("RMBS") that provide our portfolio a source of regular cash flow and higher yielding assets than our agency securities. The remainder of our fixed maturity portfolio is mostly made up of publicly traded and privately placed bonds and redeemable preferred stocks.

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The table below presents our total fixed maturity securities by Nationally Recognized Statistical Rating Organization ("NRSRO") ratings:

	December 31,			
	2009		2008	
Rating Agency Rating	Carrying Amount	Percent	Carrying Amount	Percent
	(Dollars in thousands)			
Aaa/Aa/A	$ 8,666,467	70.2%	$ 8,510,772	83.2%
Baa	2,442,897	19.8%	1,292,303	12.6%
Total investment grade	11,109,364	90.0%	9,803,075	95.8%
Ba	367,427	3.0%	225,594	2.2%
B	358,288	2.9%	135,989	1.3%
Caa and lower	481,389	3.9%	31,375	0.3%
In or near default	22,746	0.2%	37,162	0.4%
Total below investment grade	1,229,850	10.0%	430,120	4.2%
	$ 12,339,214	100.0%	$ 10,233,195	100.0%

The NAIC's Securities Valuation Office ("SVO") is responsible for the day-to-day credit quality assessment and valuation of securities owned by state regulated insurance companies. Insurance companies report ownership of securities to the SVO when such securities are eligible for regulatory filings. The SVO conducts credit analysis on these securities for the purpose of assigning an NAIC designation and/or unit price. Typically, if a security has been rated by an NRSRO, the SVO utilizes that rating and assigns an NAIC designation based upon the following system:

NAIC Designation	NRSRO Equivalent Rating
1	Aaa/Aa/A
2	Baa
3	Ba
4	B
5	Caa and lower
6	In or near default

In November 2009, the NAIC membership approved a process to assess non-agency RMBS for the 2009 filing year that does not rely on NRSRO ratings. The NAIC retained the services of PIMCO Advisory to model each non-agency RMBS owned by U.S. insurers at year-end 2009. PIMCO Advisory has provided 5 prices for each security for life insurance companies to utilize in determining the NAIC designation for each RMBS based on each insurer's statutory book value price. This process results in a more appropriate level of RBC requirements for non-agency RMBS.

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The table below presents our total fixed maturity securities at December 31, 2009 by NAIC designation:

NAIC Designation	Amortized Cost	Fair Value	Carrying Amount	Percentage of Total Carrying Amount
	(Dollars in thousands)			
1	$ 9,495,015	$ 9,370,647	$ 9,374,900	76.0%
2	2,571,815	2,555,826	2,555,826	20.7%
3	409,860	315,948	344,914	2.8%
4	24,375	20,799	20,799	0.2%
5	21,013	20,749	20,749	0.1%
6	25,685	22,026	22,026	0.2%
	$ 12,547,763	$ 12,305,995	$ 12,339,214	100.0%

A summary of our RMBS by collateral type and split by NAIC designation, as well as a separate summary of securities for which we have recognized OTTI and those which we have not yet recognized any OTTI is as follows as of December 31, 2009:

Collateral Type	NAIC Designation	Principal Amount	Amortized Cost	Fair Value
		(Dollars in thousands)		
OTTI has not been recognized				
Government agency	1	$ 69,496	$ 68,715	$ 72,306
Prime	1	1,713,391	1,595,502	1,585,337
	2	127,951	127,210	106,395
	3	1,474	1,471	977
Alt-A	1	93,963	87,071	70,749
	2	46,456	47,301	38,030
		$ 2,052,731	$ 1,927,270	$ 1,873,794
OTTI has been recognized				
Prime	1	$ 173,149	$ 156,108	$ 126,301
	2	223,473	212,221	156,522
	3	60,965	58,965	44,853
Alt-A	1	194,682	164,402	127,341
	2	111,673	96,700	75,557
	3	134,085	115,522	81,922
	6	5,394	4,701	2,811
		$ 903,421	$ 808,619	$ 615,307
Total by collateral type				
Government agency		$ 69,496	$ 68,715	$ 72,306
Prime		2,300,403	2,151,477	2,020,385
Alt-A		586,253	515,697	396,410
		$ 2,956,152	$ 2,735,889	$ 2,489,101
Total by NAIC designation				
	1	$ 2,244,681	$ 2,071,798	$ 1,982,034
	2	509,553	483,432	376,504
	3	196,524	175,958	127,752
	6	5,394	4,701	2,811
		$ 2,956,152	$ 2,735,889	$ 2,489,101

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The amortized cost and fair value of fixed maturity securities by contractual maturity are shown below. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. All of our residential mortgage and asset backed securities provide for periodic payments throughout their lives and are shown below as a separate line.

	Available for sale		Held for investment	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
December 31, 2009				
Due in one year or less	$ 18,948	$ 18,656	$	$
Due after one year through five years	446,487	467,458		
Due after five years through ten years	1,333,196	1,446,348		
Due after ten years through twenty years	1,449,264	1,450,402	555,000	549,461
Due after twenty years	4,928,896	4,832,166	1,080,083	1,052,403
	8,176,791	8,215,030	1,635,083	1,601,864
Residential mortgage and asset backed securities	2,735,889	2,489,101		
	$ 10,912,680	$ 10,704,131	$ 1,635,083	$ 1,601,864
December 31, 2008				
Due in one year or less	$ 5,010	$ 4,996	$	$
Due after one year through five years	318,003	287,405		
Due after five years through ten years	797,903	728,597		
Due after ten years through twenty years	2,264,953	2,215,863	805,170	801,384
Due after twenty years	1,692,043	1,592,343	2,798,979	2,786,730
	5,077,912	4,829,204	3,604,149	3,588,114
Residential mortgage and asset backed securities	2,081,375	1,799,842		
	$ 7,159,287	$ 6,629,046	$ 3,604,149	$ 3,588,114

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Unrealized Losses

At December 31, 2009 and 2008, the amortized cost and fair value of fixed maturity securities and equity securities that were in an unrealized loss position were as follows:

	Number of Securities	Amortized Cost	Unrealized Losses	Fair Value
		(Dollars in thousands)		
December 31, 2009				
Fixed maturity securities, available for sale:				
United States Government full faith and credit	2	$ 338	$ (6)	$ 332
United States Government sponsored agencies	27	3,026,593	(118,388)	2,908,205
U.S. states, territories and political subdivisions	32	114,232	(2,263)	111,969
Corporate securities:				
Finance, insurance and real estate	68	443,859	(50,555)	393,304
Manufacturing, construction and mining	28	178,642	(10,462)	168,180
Utilities and related sectors	36	226,604	(13,156)	213,448
Wholesale/retail trade	17	80,599	(5,423)	75,176
Services, media and other	17	113,308	(5,324)	107,984
Residential mortgage backed securities	109	1,719,481	(306,372)	1,413,109
	336	$ 5,903,656	$ (511,949)	$ 5,391,707
Fixed maturity securities, held for investment:				
United States Government sponsored agencies	4	$ 365,000	$ (5,900)	$ 359,100
Corporate security:				
Finance, insurance and real estate	1	75,649	(28,966)	46,683
	5	$ 440,649	$ (34,866)	$ 405,783
Equity securities, available for sale:				
Finance, insurance and real estate	14	$ 41,948	$ (3,269)	$ 38,679
December 31, 2008				
Fixed maturity securities, available for sale:				
United States Government full faith and credit	1	$ 18,774	$ (129)	$ 18,645
United States Government sponsored agencies	9	360,533	(1,133)	359,400
Corporate securities:				
Finance, insurance and real estate	68	447,692	(92,418)	355,274
Manufacturing, construction and mining	57	425,573	(65,567)	360,006
Utilities and related sectors	61	363,406	(55,123)	308,283
Wholesale/retail trade	26	158,118	(26,237)	131,881
Services, media and other	41	238,173	(39,212)	198,961
Residential mortgage backed securities	100	1,698,973	(287,458)	1,411,515
	363	$ 3,711,242	$ (567,277)	$ 3,143,965
Fixed maturity securities, held for investment:				
United States Government sponsored agencies	4	$ 365,000	$ (4,984)	$ 360,016
Corporate security:				
Finance, insurance and real estate	1	75,521	(17,472)	58,049
	5	$ 440,521	$ (22,456)	$ 418,065
Equity securities, available for sale:				
Finance, insurance and real estate	26	$ 76,429	$ (25,978)	$ 50,451

Unrealized losses decreased $65.6 million from $615.7 million at December 31, 2008 to $550.1 million at December 31, 2009. On January 1, 2009, we increased unrealized losses by

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$83.9 million due to the cumulative adjustment to reclassify the noncredit portion of OTTI recognized at December 31, 2008, by adopting the FASB's guidance issued in April 2009 for bifurcating credit and noncredit portions of OTTI between earnings and other comprehensive income/(loss). We have decreased unrealized losses by $86.8 million by recognizing OTTI losses on equity securities totaling $21.2 million and by recognizing $65.6 million of credit OTTI losses on debt securities for the year ended December 31, 2009. The remaining decrease in unrealized losses was due to improving market conditions resulting in higher fair values of many of our corporate securities; however, continued uncertainty in the RMBS market has increased the unrealized loss position of those assets over the year. The decline in fair value of these RMBS is due to imbalances in supply and demand for RMBS, increased foreclosures and bankruptcies and projections of potential future losses.

The following table sets forth the composition by credit quality (NAIC designation) of fixed maturity securities with gross unrealized losses:

	Carrying Value of Securities with Gross Unrealized Losses	Percent of Total	Gross Unrealized Losses	Percent of Total
	(Dollars in thousands)			
December 31, 2009				
1	$ 4,577,573	78.5%	$ (295,280)	54.0%
2	904,027	15.5%	(147,214)	26.9%
3	302,630	5.2%	(94,679)	17.3%
4	20,799	0.4%	(3,576)	0.7%
5	14,499	0.2%	(467)	0.1%
6	12,828	0.2%	(5,599)	1.0%
	$ 5,832,356	100.0%	$ (546,815)	100.0%
December 31, 2008				
1	$ 2,235,159	62.3%	$ (289,300)	49.0%
2	1,110,279	31.0%	(223,225)	37.9%
3	224,003	6.2%	(68,397)	11.6%
4	7,953	0.2%	(4,765)	0.8%
5	5,472	0.2%	(4,016)	0.7%
6	1,620	0.1%	(30)	
	$ 3,584,486	100.0%	$ (589,733)	100.0%

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The following tables show our investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities (consisting of 355 and 394 securities, respectively) have been in a continuous unrealized loss position, at December 31, 2009 and 2008:

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(Dollars in thousands)			
December 31, 2009						
Fixed maturity securities:						
Available for sale:						
United States Government full faith and credit	$ 332	$ (6)	$	$	$ 332	$ (6)
United States Government sponsored agencies	2,908,205	(118,388)			2,908,205	(118,388)
U.S. states, territories and political subdivisions	111,969	(2,263)			111,969	(2,263)
Corporate securities:						
Finance, insurance and real estate	154,093	(10,560)	239,211	(39,995)	393,304	(50,555)
Manufacturing, construction and mining	93,922	(2,032)	74,258	(8,430)	168,180	(10,462)
Utilities and related sectors	149,515	(5,046)	63,933	(8,110)	213,448	(13,156)
Wholesale/retail trade	35,629	(623)	39,547	(4,800)	75,176	(5,423)
Services, media and other	46,625	(512)	61,359	(4,812)	107,984	(5,324)
Residential mortgage backed securities	226,567	(22,781)	1,186,542	(283,591)	1,413,109	(306,372)
	$ 3,726,857	$ (162,211)	$ 1,664,850	$ (349,738)	$ 5,391,707	$ (511,949)
Held for investment:						
United States Government sponsored agencies	$ 359,100	$ (5,900)	$	$	$ 359,100	$ (5,900)
Corporate security:						
Finance, insurance and real estate			46,683	(28,966)	46,683	(28,966)
	$ 359,100	$ (5,900)	$ 46,683	$ (28,966)	$ 405,783	$ (34,866)
Equity securities, available for sale:						
Finance, insurance and real estate	$ 9,802	$ (147)	$ 28,877	$ (3,122)	$ 38,679	$ (3,269)
December 31, 2008						
Fixed maturity securities:						
Available for sale:						
United States Government full faith and credit	$	$	$ 18,645	$ (129)	$ 18,645	$ (129)
United States Government sponsored agencies	60,475	(57)	298,925	(1,076)	359,400	(1,133)
Corporate securities:						
Finance, insurance and real estate	209,048	(45,657)	146,226	(46,761)	355,274	(92,418)
Manufacturing, construction and mining	294,428	(37,589)	65,578	(27,978)	360,006	(65,567)
Utilities and related sectors	192,110	(22,816)	116,173	(32,307)	308,283	(55,123)
Wholesale/retail trade	120,056	(16,557)	11,825	(9,680)	131,881	(26,237)
Services, media and other	119,297	(22,425)	79,664	(16,787)	198,961	(39,212)
	1,114,073	(220,301)	297,442	(67,157)	1,411,515	(287,458)

Residential mortgage backed securities						
	$ 2,109,487	$ (365,402)	$ 1,034,478	$ (201,875)	$ 3,143,965	$ (567,277)
Held for investment:						
United States Government sponsored agencies	$	$	$ 360,016	$ (4,984)	$ 360,016	$ (4,984)
Corporate security:						
Finance, insurance and real estate			58,049	(17,472)	58,049	(17,472)
	$	$	$ 418,065	$ (22,456)	$ 418,065	$ (22,456)
Equity securities, available for sale:						
Finance, insurance and real estate	$ 30,093	$ (14,360)	$ 20,358	$ (11,618)	$ 50,451	$ (25,978)

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The following is a description of the factors causing the unrealized losses by investment category as of December 31, 2009:

United States Government sponsored agencies and U.S. states, territories and political subdivisions: These securities are relatively long in duration, making the value of such securities sensitive to changes in market interest rates. During the last twelve months spreads on agency securities have improved; however, long term interest rates have risen by a greater amount. These securities carry yields less than those available at December 31, 2009 as the result of these rising interest rates.

Corporate securities: The unrealized losses in these securities are due partially to a rise in interest rates in 2009 as well as the continuation of wider than historic credit spreads in certain industries of the corporate bond market. While credit spreads narrowed throughout the year, several industries remain at spreads wider than pre-crisis levels, such as financials and economic sensitive issuers. As the result of wider spreads, these issues carry yields less than those available in the market as of December 31, 2009.

Residential mortgage backed securities: At December 31, 2009, we had no exposure to subprime residential mortgage backed securities. All of our residential mortgage backed securities are pools of first-lien residential mortgage loans. Substantially all of the securities that we own are in the most senior tranche of the securitization in which they are structured and are not subordinated to any other tranche. Our "Alt-A" residential mortgage backed securities are comprised of 37 securities with a total amortized cost basis of $515.7 million and a fair value of $396.4 million. Despite recent improvements in the capital markets, the fair values of RMBS continue at prices below amortized cost. RMBS prices will likely remain below our cost basis until the housing market is able to absorb current and future foreclosures.

Equity securities: The unrealized loss on equity securities, which are primarily investment grade perpetual preferred stocks with exposure to REITS, investment banks and finance companies, are due to the ongoing concerns relating to capital, asset quality and earnings stability due to the financial crisis. All of the equity securities in an unrealized loss position for 12 months or more are investment grade perpetual preferred stocks that are absent credit deterioration. A prolonged recession due to tight credit markets and a continued difficult housing market have raised concerns in regard to earnings and dividend stability in many companies which directly affect the values of these securities.

Where the decline in market value of debt securities is attributable to changes in market interest rates or to factors such as market volatility, liquidity and spread widening, and we anticipate recovery of all contractual or expected cash flows, we do not consider these investments to be other than temporarily impaired because we do not intend to sell these investments and it is not more likely than not we will be required to sell these securities before a recovery of amortized cost, which may be maturity. For equity securities, we recognize an impairment charge in the period in which we do not have the intent and ability to hold the securities until a recovery of cost or we determine that the security will not recover to book value within a reasonable period of time. We determine what constitutes a reasonable period of time on a security-by-security basis based upon consideration of all the evidence available to us, including the magnitude of an unrealized loss and its duration. In any event, this period does not exceed 18 months from the date of impairment for perpetual preferred securities for which there is evidence of deterioration in credit of the issuer and common equity securities. For perpetual preferred securities absent evidence of a deterioration in credit of the issuer we apply an impairment model, including an anticipated recovery period, similar to a debt security. For equity securities we measure impairment charges based upon the difference between the book value of a security and its fair value.

At December 31, 2009 and 2008, the amortized cost and fair value of fixed maturity securities and equity securities in an unrealized loss position and the number of months in an unrealized loss position

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with fixed maturity securities that carry an NRSRO rating of BBB/Baa or higher considered investment grade were as follows:

	Number of Securities	Amortized Cost	Fair Value	Gross Unrealized Losses
		(Dollars in thousands)		
December 31, 2009				
Fixed maturity securities:				
Investment grade:				
Less than six months	120	$ 2,516,264	$ 2,463,732	$ (52,532)
Six months or more and less than twelve months	26	1,591,620	1,500,847	(90,773)
Twelve months or greater	95	883,552	777,079	(106,473)
Total investment grade	241	4,991,436	4,741,658	(249,778)
Below investment grade:				
Less than six months	3	60,580	57,220	(3,360)
Six months or more and less than twelve months	12	85,605	64,159	(21,446)
Twelve months or greater	85	1,206,684	934,453	(272,231)
Total below investment grade	100	1,352,869	1,055,832	(297,037)
Equity securities:				
Less than six months	2	7,291	7,242	(49)
Six months or more and less than twelve months	1	2,658	2,561	(97)
Twelve months or greater	11	32,000	28,877	(3,123)
Total equity securities	14	41,949	38,680	(3,269)
	355	$ 6,386,254	$ 5,836,170	$ (550,084)
December 31, 2008				
Fixed maturity securities				
Investment grade:				
Less than six months	101	$ 923,551	$ 856,068	$ (67,483)
Six months or more and less than twelve months	135	1,397,314	1,132,871	(264,443)
Twelve months or greater	104	1,532,113	1,351,515	(180,598)
Total investment grade	340	3,852,978	3,340,454	(512,524)
Below investment grade:				
Less than six months	4	27,862	23,377	(4,485)
Six months or more and less than twelve months	13	126,163	97,172	(28,991)
Twelve months or greater	11	144,760	101,027	(43,733)
Total below investment grade	28	298,785	221,576	(77,209)
Equity securities:				
Less than six months	10	23,454	17,635	(5,819)
Six months or more and less than twelve months	8	21,000	12,459	(8,541)
Twelve months or greater	8	31,975	20,357	(11,618)
Total equity securities	26	76,429	50,451	(25,978)

394	$	4,228,192	$	3,612,481	$	(615,711)

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At December 31, 2009 and 2008, the amortized cost and fair value of fixed maturity securities (excluding United States Government and United States Government sponsored agency securities) segregated by investment grade (NRSRO rating of BBB/Baa or higher) and below investment grade and equity securities that had unrealized losses greater than 20% and the number of months in an unrealized loss position greater than 20% were as follows:

	Number of Securities	Amortized Cost	Carrying Value	Gross Unrealized Losses
		(Dollars in thousands)		
December 31, 2009				
Investment grade:				
Less than six months	2	$ 34,271	$ 30,198	$ (4,073)
Six months or more and less than twelve months				
Twelve months or greater	2	11,940	8,601	(3,339)
Total investment grade	4	46,211	38,799	(7,412)
Below investment grade:				
Less than six months	13	118,198	101,805	(16,393)
Six months or more and less than twelve months	9	158,359	111,878	(46,481)
Twelve months or greater	27	365,706	252,062	(113,644)
Total below investment grade	49	642,263	465,745	(176,518)
	53	$ 688,474	$ 504,544	$ (183,930)
December 31, 2008				
Investment grade:				
Less than six months	98	$ 840,309	$ 614,000	$ (226,309)
Six months or more and less than twelve months	18	99,216	65,679	(33,537)
Twelve months or greater				
Total investment grade	116	939,525	679,679	(259,846)
Below investment grade:				
Less than six months	17	152,936	104,729	(48,207)
Six months or more and less than twelve months	2	10,497	4,159	(6,338)
Twelve months or greater				
Total below investment grade	19	163,433	108,888	(54,545)
Equity securities:				
Less than six months	17	44,321	27,562	(16,759)
Six months or more and less than twelve months	3	8,000	4,642	(3,358)
Twelve months or greater				
Total equity securities	20	52,321	32,204	(20,117)
	155	$ 1,155,279	$ 820,771	$ (334,508)

The amortized cost and fair value of fixed maturity securities at December 31, 2009 and 2008, by contractual maturity, that were in an unrealized loss position are shown below. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations

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with or without call or prepayment penalties. All of our residential mortgage and asset backed securities provide for periodic payments throughout their lives, and are shown below as a separate line.

	Available for sale		Held for investment	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
December 31, 2009				
Due in one year of less	$ 12,000	$ 11,707	$	$
Due after one year through five years	82,754	75,462		
Due after five years through ten years	100,597	95,678		
Due after ten years through twenty years	707,824	682,247	365,000	359,100
Due after twenty years	3,281,000	3,113,504	75,649	46,683
	4,184,175	3,978,598	440,649	405,783
Residential mortgage and asset backed securities	1,719,481	1,413,109		
	$ 5,903,656	$ 5,391,707	$ 440,649	$ 405,783
December 31, 2008				
Due in one year or less	$ 4,990	$ 4,977	$	$
Due after one year through five years	265,271	232,651		
Due after five years through ten years	616,498	540,629		
Due after ten years through twenty years	564,674	505,442	365,000	360,016
Due after twenty years	560,837	448,751	75,521	58,049
	2,012,270	1,732,450	440,521	418,065
Residential mortgage and asset backed securities	1,698,973	1,411,515		
	$ 3,711,243	$ 3,143,965	$ 440,521	$ 418,065

Watch List

At each balance sheet date, we identify invested assets which have characteristics (i.e. significant unrealized losses compared to amortized cost and industry trends) creating uncertainty as to our future assessment of an other than temporary impairment. As part of this assessment we review not only a change in current price relative to its amortized cost but the issuer's current credit rating and the probability of full recovery of principal based upon the issuer's financial strength. Specifically for corporate issues we evaluate the financial stability and quality of asset coverage for the securities relative to the term to maturity for the issues we own. A security which has a 25% or greater change in market price relative to its amortized cost and a possibility of a loss of principal will be included on a list which is referred to as our watch list. We exclude from this list securities with unrealized losses which are related to market movements in interest rates and which have no factors indicating that such unrealized losses may be other than temporary as we do not intend to sell these securities and it is more likely than not we will not have to sell these securities before a recovery is realized. In addition, we exclude our RMBS as we monitor all of our RMBS on a quarterly basis for changes in default rates, loss severities and expected cash flows for the purpose of assessing potential other than temporary impairments and related credit losses to be recognized in operations. At December 31, 2009, the amortized cost and fair value of securities on the watch list are as follows:

General Description	Number of Securities	Amortized Cost	Unrealized Gains/ (Losses)	Fair Value	Months in Continuous Unrealized Loss Position	Months Unrealized Losses Greater Than 20%
		(Dollars in thousands)				
Investment grade						
Corporate fixed maturity securities:						
Finance	1	$ 9,987	$ (787)	$ 9,200	20	
Insurance	1	3,765	(1,237)	2,528	31	19
Perpetual preferred stocks:						
Insurance	1	3,000	(625)	2,375	23	19
	3	16,752	(2,649)	14,103		
Below investment grade						
Corporate fixed maturity securities:						
Finance	4	22,186	(2,683)	19,503	20 33	0 23
Insurance	1	13,523	(3,622)	9,901	52	29
Retail	1	10,488	(1,988)	8,500	55	
	6	46,197	(8,293)	37,904		
	9	$ 62,949	$ (10,942)	$ 52,007		

Our analysis of these securities that we have determined are temporarily impaired and their credit performance at December 31, 2009 is as follows:

Finance and Insurance: The decline in value of these corporate bonds and preferred stocks is due to the continued wide spreads as a result of the ongoing concerns relating to capital, asset quality and earnings stability due to the financial crisis. While these issuers have had their financial position and profitability weakened by the credit and liquidity crisis, we have determined that these securities were not other than temporarily impaired due to our evaluation of the operating performance and the credit worthiness of each individual issuer.

Retail: The decline in value of this bond relates to a debt-financed share repurchase combined with a weakening economy which has led to a decrease in sales. We have determined that this security was not other than temporarily impaired due to the issuer's very strong market position and a consistent history of strong operating performance.

The securities on the watch list are current with respect to payments of principal and interest. We do not intend to sell these securities and it is more likely than not we will not have to sell these securities before recovery of their amortized cost and, as such, there were no other than temporary impairments on these securities at December 31, 2009.

Other Than Temporary Impairments

We have a policy and process in place to identify securities in our investment portfolio for which we should recognize impairments. See Critical Accounting Policies Evaluation of Other Than Temporary Impairments.

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We recognized other than temporary impairments and credit losses as follows:

General Description	Year Ended December 31, 2009 Number of Securities	2009 Other Than Temporary Impairments	2009 Portion Recognized In Comprehensive Income	2009 Net Impairment Losses Recognized in Operations	2008 Number of Securities	2008 Other Than Temporary Impairments	2007 Number of Securities	2007 Other Than Temporary Impairments
			(Dollars in thousands)					
United States Government full faith and credit	1	$ (245)	$	$ (245)		$		$
Corporate bonds:								
Finance	3	(8,388)	(1,521)	(9,909)	3	(13,462)		
Insurance	2	(766)	(421)	(1,187)	2	(10,662)		
Home building	3	(5,242)	(814)	(6,056)	3	(7,009)		
Media					1	(5,325)	1	(3,948)
Residential mortgage backed securities	54	(184,590)	136,400	(48,190)	15	(76,171)		
Common & preferred stocks:								
Finance	7	(18,292)		(18,292)	9	(49,763)		
Insurance	2	(1,492)		(1,492)	3	(7,093)		
Real estate	2	(1,400)		(1,400)	14	(23,163)	1	(435)
	74	$ (220,415)	$ 133,644	$ (86,771)	50	$ (192,648)	2	$ (4,383)

Several factors have led us to believe that full recovery of amortized cost will not be expected. These include, but are not limited to: (i) a change in the operating performance of an issuer; (ii) a change in ratings as defined by the NRSRO; and (iii) the time frame in which a recovery to amortized cost may occur.

Deterioration of the issuers' credit worthiness and liquidity profile were major factors in leading us to make the determination that other than temporary impairments were present in our corporate bonds and common and preferred stocks. Our analysis demonstrated that we could not expect a recovery of our cost basis within our expected holding period for debt securities or within a reasonable period of time for equity securities.

In the case of residential mortgage backed securities, we considered the ratings downgrades, increased default projections, actual defaults, and expected cash flow projections to determine that other than temporary impairments were present. We continue to monitor the cash flows and economics surrounding these securities to determine changes in expected future cash flows. The following table presents the range of significant assumptions used to determine the credit loss component of other than temporary impairments we have recognized on residential mortgage backed securities which are all senior level tranches within the structure of the securities:

		Discount Rate		Default Rate		Loss Severity	
Sector	Vintage	Min	Max	Min	Max	Min	Max
Prime	2006	6.5%	6.5%	7%	7%	55%	55%
	2007	6.1%	7.9%	11%	18%	40%	50%
Alt-A	2004	5.8%	5.8%	11%	11%	40%	40%
	2005	6.2%					