JACKSON NATIONAL LIFE INSURANCE COMPANY

Jackson National Life Insurance Company and Subsidiaries

Consolidated Financial Statements

December 31, 2006

Jackson National Life Insurance Company and Subsidiaries

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December 31, 2006

KPMG LLP
303 East Wacker Drive
Chicago, IL 60601-5212

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholder of
Jackson National Life Insurance Company:

We have audited the accompanying consolidated balance sheets of Jackson National Life Insurance Company and Subsidiaries as of December 31, 2006 and 2005, and the related consolidated income statements and the consolidated statements of stockholder's equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Jackson National Life Insurance Company and Subsidiaries as of December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2006 in conformity with U.S. generally accepted accounting principles.

As discussed more fully in note 2 to the consolidated financial statements, effective January 1, 2004, Jackson National Life Insurance Company adopted Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" issued by the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants.

KPMG LLP

Chicago, Illinois
March 7, 2007

Jackson National Life Insurance Company and Subsidiaries
Consolidated Financial Statements

Consolidated Balance Sheets
(In thousands, except per share information)

	December 31, 2006	December 31, 2005
Assets		
Investments:		
Cash and short-term investments	$ 946,386	$ 729,695
Investments available for sale, at fair value:		
Fixed maturities (amortized cost: 2006, $38,022,986; 2005, $39,633,811)	38,239,906	40,249,207
Equities (cost: 2006, $107,750; 2005, $313,498)	121,593	326,478
Trading securities, at fair value	549,300	138,685
Mortgage loans	5,290,788	4,989,516
Policy loans	815,725	804,009
Other invested assets	1,168,929	1,414,720
Total investments	47,132,627	48,652,310
Accrued investment income	533,887	553,120
Deferred acquisition costs	3,065,327	2,548,473
Deferred sales inducements	297,051	253,083
Reinsurance recoverable	886,967	943,738
Value of acquired insurance	-	23,578
Income taxes receivable from Parent	53,799	50,633
Deferred income taxes	16,160	-
Other assets	220,016	83,180
Separate account assets	22,243,997	14,720,596
Total assets	$ 74,449,831	$ 67,828,711
Liabilities and Stockholder's Equity		
Liabilities		
Policy reserves and liabilities:		
Reserves for future policy benefits and claims payable	$ 2,485,338	$ 2,551,779
Deposits on investment contracts	34,634,715	35,273,715
Guaranteed investment contracts	1,995,013	1,983,693
Trust instruments supported by funding agreements	5,204,275	5,609,059
Federal Home Loan Bank advances	601,397	100,209
Notes payable	402,262	486,939
Securities lending payable	235,888	428,032
Deferred income taxes	-	40,583
Other liabilities	1,402,440	1,760,763
Separate account liabilities	22,243,997	14,720,596
Total liabilities	69,205,325	62,955,368
Minority interest	148,495	7,186
Stockholder's Equity		
Common stock, $1.15 par value; authorized 50,000 shares; issued and outstanding 12,000 shares	13,800	13,800
Additional paid-in capital	2,904,276	2,854,533
Accumulated other comprehensive income, net of tax of $59,665 in 2006 and $141,725 in 2005	110,807	263,203
Retained earnings	2,067,128	1,734,621
Total stockholder's equity	5,096,011	4,866,157
Total liabilities and stockholder's equity	$ 74,449,831	$ 67,828,711

See accompanying notes to consolidated financial statements.

Consolidated Income Statements
(In thousands)

	Years Ended December 31, 2006	2005	2004
Revenues			
Premiums	$ 196,201	$ 199,061	$ 162,342
Net investment income	2,904,787	2,879,440	2,689,945
Net realized gains (losses) on investments	(57,710)	12,984	138,656
Risk management activity	(105,227)	169,827	90,814
Fee income	711,584	509,376	387,386
Other income	62,532	38,815	84,451
Total revenues	3,712,167	3,809,503	3,553,594
Benefits and Expenses			
Death and other policy benefits	490,527	428,162	379,175
Interest credited on deposit liabilities	1,450,048	1,434,807	1,364,803
Interest expense on trust instruments supported by funding agreements	269,577	217,917	143,317
Interest expense on Federal Home Loan Bank advances, notes and reverse repurchase agreements	52,817	50,249	42,376
Increase (decrease) in reserves, net of reinsurance	(37,266)	19,466	19,340
Commissions	663,176	537,303	483,005
General and administrative expenses	387,011	341,793	290,863
Deferral of policy acquisition costs	(675,098)	(556,564)	(507,660)
Deferral of sales inducements	(101,525)	(92,381)	(86,430)
Amortization of acquisition costs:			
Attributable to operations	318,443	364,907	419,048
Attributable to risk management activity	(3,302)	64,962	4,674
Attributable to net realized gains (losses) on investments	(10,501)	2,671	12,208
Amortization of deferred sales inducements:			
Attributable to operations	109,043	55,639	38,039
Attributable to risk management activity	(35,058)	7,632	9,087
Attributable to net realized gains (losses) on investments	(2,576)	459	2,902
Amortization of acquired insurance	23,578	22,190	20,882
Total benefits and expenses	2,898,894	2,899,212	2,635,629
Pretax income from continuing operations before minority interest	813,273	910,291	917,965
Minority interest	(17,236)	(922)	(49,041)
Pretax income from continuing operations	796,037	909,369	868,924
Federal income tax expense	263,416	315,295	304,076
Income from continuing operations before extraordinary gain and cumulative effect of change in accounting principle	532,621	594,074	564,848
Income from discontinued operations, net of tax	-	-	56,776
Income before extraordinary gain and cumulative effect of change in accounting principle	532,621	594,074	621,624
Extraordinary gain, net of tax benefit of $908	8,944	-	-
Income before cumulative effect of change in accounting principle	541,565	594,074	621,624
Cumulative effect of change in accounting principle, net of tax	-	-	8,912
Net income	$ 541,565	$ 594,074	$ 630,536
Pro forma net income assuming the change in accounting principle is applied retroactively			$ 621,624

See accompanying notes to consolidated financial statements.

Consolidated Statements of Stockholder's Equity and Comprehensive Income
(In thousands)

	Years Ended December 31, 2006	2005	2004
Common stock, beginning and end of year	$ 13,800	$ 13,800	$ 13,800
Additional paid-in-capital			
Beginning of year	2,854,533	2,562,214	2,533,535
Capital contributions	49,743	292,319	28,679
End of year	2,904,276	2,854,533	2,562,214
Accumulated other comprehensive income			
Beginning of year	263,203	745,430	814,102
Net unrealized investment losses, net of reclassification adjustment and net of tax	(152,396)	(482,227)	(68,672)
End of year	110,807	263,203	745,430
Retained Earnings			
Beginning of year	1,734,621	1,551,347	1,040,811
Net income	541,565	594,074	630,536
Dividends paid to stockholder	(209,058)	(410,800)	(120,000)
End of year	2,067,128	1,734,621	1,551,347
Total stockholder's equity	$ 5,096,011	$ 4,866,157	$ 4,872,791

	Years Ended December 31, 2006	2005	2004
Net income	$ 541,565	$ 594,074	$ 630,536
Net unrealized holding losses arising during the period, net of tax of $(86,061) in 2006; $(243,143) in 2005 and $(11,016) in 2004	(159,828)	(451,661)	(19,721)
Reclassification adjustment for losses (gains) included in net income, net of tax of $4,001 in 2006; $(16,459) in 2005 and $(26,358) in 2004	7,432	(30,566)	(48,951)
Comprehensive income	$ 389,169	$ 111,847	$ 561,864

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows
(In thousands)

	Years Ended December 31, 2006	2005	2004
Cash flows from operating activities:			
Net income	$ 541,565	$ 594,074	$ 630,536
Less income from discontinued operations	-	-	(56,776)
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:			
Net realized (gains) losses on investments	57,710	(12,984)	(138,656)
Unrealized gains on trading portfolio	(10,937)	(565)	(8,360)
Risk management activity	105,227	(169,827)	(90,814)
Interest credited on deposit liabilities	1,450,048	1,434,807	1,364,803
Interest expense on trust instruments supported by funding agreements	269,577	217,917	143,317
Interest expense on Federal Home Loan Bank advances	18,147	209	-
Other charges	(282,931)	(245,877)	(216,383)
Amortization of discount and premium on investments	76,919	(72,853)	34,514
Deferred income tax provision	22,558	141,115	216,880
Change in (net of effects of contribution of subsidiary):			
Accrued investment income	19,233	(7,630)	(29,741)
Deferred sales inducements and acquisition costs	(401,934)	(154,653)	(124,385)
Trading portfolio activity, net	(25,082)	(13,522)	(15,726)
Value of acquired insurance	23,578	22,190	20,882
Income taxes receivable from Parent	(3,166)	(22,523)	(19,485)
Other assets and liabilities, net	50,624	348,543	370,851
Net cash provided by operating activities of discontinued operations	-	-	28,671
Net cash provided by operating activities	1,911,136	2,058,421	2,110,128
Cash flows from investing activities:			
Sales of fixed maturities and equities available for sale	5,384,731	2,889,975	3,536,656
Principal repayments, maturities, calls and redemptions:			
Fixed maturities available for sale	2,593,502	2,956,801	2,836,775
Mortgage loans	770,151	914,758	804,356
Purchases of:			
Fixed maturities and equities available for sale	(6,300,678)	(6,676,587)	(7,551,922)
Mortgage loans	(1,067,685)	(1,278,434)	(1,111,534)
Other investing activities	(543,162)	(419,823)	(256,443)
Proceeds from sale of discontinued operations	-	-	260,051
Net cash provided by (used in) investing activities of discontinued operations	-	-	376,480
Net cash provided by (used in) investing activities	836,859	(1,613,310)	(1,105,581)
Cash flows from financing activities:			
Policyholders' account balances:			
Deposits	11,232,706	9,355,451	8,300,160
Withdrawals	(8,095,806)	(6,598,525)	(6,180,543)
Net transfers to separate accounts	(5,363,753)	(3,564,891)	(2,394,722)
Proceeds from notes	-	-	26,264
Payments on notes	(119,543)	(3,747)	(44,784)
Payment of cash dividends to Parent	(209,058)	(410,800)	(120,000)
Capital contribution	24,150	86,670	-
Net cash used in financing activities of discontinued operations	-	-	(426,055)
Net cash used in financing activities	(2,531,304)	(1,135,842)	(839,680)
Net increase (decrease) in cash and short-term investments	216,691	(690,731)	164,867
Cash and short-term investments, beginning of year	729,695	1,420,426	1,255,559
Total cash and short-term investments, end of period	$ 946,386	$ 729,695	$ 1,420,426

See accompanying notes to consolidated financial statements.

1. Nature of Operations

Jackson National Life Insurance Company (the "Company" or "Jackson") is wholly owned by Brooke Life Insurance Company ("Brooke Life" or the "Parent") which is ultimately a wholly owned subsidiary of Prudential plc ("Prudential"), London, England. Jackson, together with its New York life insurance subsidiary, is licensed to sell group and individual annuity products (including immediate, index linked and deferred fixed annuities and variable annuities), guaranteed investment contracts ("GICs") and individual life insurance products, including variable universal life, in all 50 states and the District of Columbia.

The consolidated financial statements include the accounts of the following:

- Life insurers: Jackson and its wholly owned subsidiaries Jackson National Life Insurance Company of New York, Jackson National Life (Bermuda) LTD and Life Insurance Company of Georgia ("Life of Georgia") from May 31, 2005 to December 31, 2005, when it was merged with Jackson;
- Wholly owned broker-dealer, investment management and investment advisor subsidiaries: Jackson National Life Distributors, LLC, Jackson National Asset Management, LLC, Curian Clearing, LLC and Curian Capital, LLC;
- Wholly owned insurance agency: JNL Southeast Agency, LLC;
- PPM America Special Investments Fund, L.P. ("SIF I") and PPM America Special Investments CBO II, L.P. ("CBO II"), (collectively, "PPMA Funds"). Jackson has effective managerial control of the PPMA Funds. Jackson owns a 72.0% interest in SIF I and a 15.1% interest in CBO II;
- Tuscany CDO, Limited ("Tuscany"), a variable interest entity created in 2001 to securitize certain fixed maturities owned by Jackson. Jackson is the primary beneficiary of Tuscany;
- Other partnerships, limited liability companies and variable interest entities in which Jackson has a controlling interest or is deemed the primary beneficiary;
- The discontinued operations of Jackson Federal Bank ("Jackson Federal") through October 28, 2004. See note 4 for additional information.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). All significant intercompany accounts and transactions have been eliminated in consolidation.

The preparation of the consolidated financial statements in conformity with GAAP requires the use of estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results may differ from those estimates. Significant estimates or assumptions, as further discussed in the notes, include: 1) valuation of investments, including fair values of securities without readily ascertainable market values and the determination of when an unrealized loss is other-than-temporary; 2) assessments as to whether certain entities are variable interest entities and which party, if any, should consolidate the entity; 3) assumptions impacting future gross profits, including lapse and mortality rates, expenses, investment returns and policy crediting rates, used in the calculation of amortization of deferred acquisition costs and deferred sales inducements; 4) assumptions used in calculating policy reserves and liabilities, including lapse and mortality rates, expenses and investment returns; 5) assumptions as to future earnings levels being sufficient to realize deferred tax benefits; and 6) estimates related to establishment of loan loss reserves, liabilities for lawsuits and the liability for state guaranty fund assessments.

Changes in Accounting Principles

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("FAS") No. 157, "Fair Value Measurements" ("FAS 157"), which establishes a framework for measuring fair value under current accounting pronouncements that require or permit fair value measurement. FAS 157 retains the exchange price notion, but clarifies that exchange price is the price in an orderly transaction between market participants to sell the asset or transfer the liability in the most advantageous market for that asset or liability. Fair value measurement is based on assumptions used by market participants in

2. Summary of Significant Accounting Policies (continued)

pricing the asset or liability, which may include inherent risk, restrictions on the sale or use of an asset, or nonperformance risk which would include the reporting entity's own credit risk. FAS 157 establishes a three-level fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value. The highest priority is given to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs in situations where there is little or no market activity for the asset or liability. In addition, FAS 157 expands the disclosure requirements for annual and interim reporting to focus on the inputs used to measure fair value, including those measurements using significant unobservable inputs, and the effects of the measurements on earnings. FAS 157 will be applied prospectively and is effective for fiscal years beginning after November 15, 2007. Retrospective application is required for certain financial instruments as a cumulative effect adjustment to the opening balance of retained earnings. Jackson has not yet quantified the impact of adoption on the Company's consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements. FIN 48 requires companies to determine whether it is "more likely than not" that a tax position will be sustained upon examination by the appropriate taxing authorities before any part of the benefit can be recorded in the financial statements. It also provides guidance on the recognition, measurement and classification of income tax uncertainties, along with any related interest and penalties. Previously recorded income tax benefits that no longer meet this standard are required to be charged to earnings in the period that such determination is made. FIN 48 will also require additional disclosures and is effective for fiscal years beginning after December 15, 2006. Jackson does not expect adoption to have a material impact on the Company's consolidated financial statements.

In April 2006, the FASB issued FASB Staff Position ("FSP") on Interpretation 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)" ("FIN 46(R)-6"). The FSP affects the identification of which entities are Variable Interest Entities ("VIE") through a "by design" approach in identifying and measuring the variable interests of the variable interest entity and its primary beneficiary. The requirements became effective beginning in the third quarter of 2006 and are to be applied to all new variable interest entities. The new requirements need not be applied to entities that have previously been analyzed under FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" (revised) ("FIN 46R") unless a reconsideration event occurs. The adoption of this guidance did not have a material effect on the Company's consolidated financial statements.

In February 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments" ("FAS 155"). This statement, effective for financial instruments acquired or issued after the beginning of an entity's first fiscal year after September 15, 2006, allows companies to include changes in fair value of certain hybrid financial instruments in earnings on an instrument-by-instrument basis. Further guidance issued in October 2006 provided an exemption from the provisions of FAS No. 133 for certain financial instruments that would have otherwise been required to recognize embedded derivatives arising as a result of prepayment risk in certain structured securities. As a result, adoption of FAS 155 is not expected to have a material impact on the Company's consolidated financial statements.

In September 2005, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" ("SOP 05-1"). SOP 05-1 addresses the accounting for deferred acquistion costs on internal replacements other than those described in FAS No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments." An internal replacement is defined by SOP 05-1 as a modification in product benefits, features, rights or coverages that occurs by (a) exchanging the contract for a new contract, (b) amending, endorsing or attaching a rider to the contract, or (c) electing a feature or coverage within a contract. Contract modifications that result in a substantially changed contract should be accounted for as an extinguishment of the replaced contract, and any unamortized deferred acquisition costs, unearned revenue and deferred sales inducements must be written-off. SOP 05-1 is to be applied prospectively and is effective for

2. Summary of Significant Accounting Policies (continued)

internal replacements occurring in fiscal years beginning after December 15, 2006. Jackson does not expect adoption to have a material impact on the Company's consolidated financial statements.

In May 2005, the FASB issued Statement of Financial Accounting Standards No. 154, "Accounting Changes and Error Corrections" ("FAS 154"). FAS 154 requires that, unless impracticable or absent explicit transition requirements specific to the newly adopted accounting principle, companies apply changes in accounting principles on a retrospective basis. FAS 154 is effective for accounting changes and corrections or errors made in fiscal years beginning after December 15, 2005. The adoption of FAS 154 did not have a material impact on the Company's consolidated financial statements.

In March 2004, the Emerging Issues Task Force ("EITF") reached a consensus on Issue No. 03-01, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments" ("EITF 03-01"). EITF 03-01 provides more specific guidance on how to determine when an investment is considered impaired, whether the impairment is other-than-temporary, and how to measure an impairment loss. On September 30, 2004, the FASB issued FASB Staff Position EITF Issue 03-1-1, "Effective Date of Paragraphs 10-20 of EITF Issue No. 03-01, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" delaying the effective date of paragraphs 10-20 of EITF 03-01 until the FASB has resolved certain implementation issues. On June 29, 2005, the FASB concluded that the current guidance included in EITF 03-01 was adequate and that further clarification was not necessary. Jackson adopted the requirements of EITF 03-01 for the year ended December 31, 2004, with no material impact on the Company's consolidated financial statements.

Effective January 1, 2004, Jackson adopted the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants' Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" ("SOP 03-1"). SOP 03-1 addresses separate account presentation, transfers of assets from the general account to the separate account, valuation of certain insurance liabilities and policy features such as guaranteed minimum death benefits and annuitization benefits and accounting for sales inducements. At January 1, 2004, the Company recorded an $8.9 million gain, net of increased deferred acquisition cost amortization of $16.2 million and federal income tax expense of $4.8 million, as a cumulative effect of change in accounting principle. The gain resulted from reduced reserving requirements for annuitization benefits on two-tiered annuities offset by additional reserves for certain life products with secondary guarantees. See note 9 for additional information.

Comprehensive Income
Comprehensive income includes all changes in stockholder's equity (except those arising from transactions with owners/stockholders) and, in the Company's case, includes net income and net unrealized gains or losses on securities.

Investments
Cash and short-term investments, which primarily include commercial paper and money market instruments, are carried at amortized cost. These investments have maturities of three months or less and are considered cash equivalents for reporting cash flows.

Fixed maturities consist primarily of bonds, notes, redeemable preferred stocks, asset-backed securities and structured securities. Acquisition discounts and premiums on fixed maturities are amortized into investment income through call or maturity dates using the interest method. Asset-backed and structured securities are amortized over the estimated redemption period. With regard to structured securities that are considered to be other than high quality or otherwise deemed to be high-risk, meaning the Company might not recover substantially all of its recorded investment due to unanticipated prepayment events, changes in investment yields due to changes in estimated future cash flows are accounted for on a prospective basis. The carrying value of such securities was $504.9 million and $542.4 million as of December 31, 2006 and 2005, respectively.

All fixed maturities are classified as available for sale and are carried at fair value. For declines in fair value considered to be other-than-temporary, the amortized cost basis of fixed maturities is reduced to fair value through an impairment charge included in net realized gains (losses) on investments. In determining whether an other-

2. Summary of Significant Accounting Policies (continued)

than-temporary impairment has occurred, the Company considers a security's forecasted cash flows as well as the severity and duration of depressed fair values.

Equities, which include common stocks and non-redeemable preferred stocks, are generally carried at fair value. Equities are reduced to estimated net realizable value for declines in fair value considered to be other than temporary. Any impairment charges are included in net realized gains (losses) on investments.

Trading securities primarily consist of private equity securities, investments in mutual funds that support liabilities of the Company's non-qualified voluntary deferred compensation plans and seed money that supports newly established variable funds. During 2004, the Company transferred its investment in mutual funds from available for sale to a trading portfolio and recognized a loss of $9.3 million. Trading securities are carried at fair value with changes in value included in net investment income. During 2006, 2005 and 2004, $26.3 million, $5.4 million and $8.4 million of investment income was recognized on trading securities held at December 31, 2006, 2005 and 2004, respectively.

Mortgage loans are carried at aggregate unpaid principal balances, net of unamortized discounts and premiums and an allowance for loan losses. The allowance for loan losses represents the estimated risk of loss for individual mortgages in the portfolio.

Policy loans are carried at the unpaid principal balances.

Real estate is carried at the lower of depreciated cost or fair value.

Limited partnership investments are accounted for using the equity method.

The consolidated financial statements include the PPMA Funds, which are limited life partnerships. Upon termination of the partnerships, the assets will be sold and proceeds distributed to the partners in accordance with their respective partnership interests. The assets of the PPMA Funds are marketable securities, which are carried at fair value, with an appropriate adjustment to minority interest, in the accompanying financial statements. Accordingly, the minority interest related to the PPMA Funds is reflected at fair value in the accompanying consolidated balance sheets.

Pursuant to the guidance provided by FIN 46R, the Company has concluded that it owns interests in VIEs that represent primary beneficial interests. These VIEs are included in the consolidated financial statements and include entities structured to hold and manage investments, including real estate properties and interests in commercial loans. In addition, Jackson had an investment of $72.7 million and $47.5 million as of December 31, 2006 and 2005, respectively, in debt issued by a VIE structured to hold and manage investments in commercial loans, for which it is not the primary beneficiary.

Realized gains and losses on sales of investments are recognized in income at the date of sale and are determined using the specific cost identification method. The changes in unrealized gains and losses on investments classified as available for sale, net of tax and the effect of the adjustment for deferred acquisition costs and sales inducements, are excluded from net income and included as a component of other comprehensive income and stockholder's equity.

Determination of Fair Value for Illiquid Distressed Securities

Fair values for illiquid distressed securities are primarily determined based on internally derived estimates of discounted future cash flows or expected recovery values. Liquidation values for these illiquid distressed securities would generally be lower, and in many cases significantly lower, than internally derived fair values. The amortized cost and fair value of illiquid distressed securities valued internally were $343.7 million and $344.4 million, respectively, at December 31, 2006 and $379.2 million and $387.5 million, respectively, at December 31, 2005.

2. Summary of Significant Accounting Policies (continued)

Derivative Instruments, Embedded Derivatives and Risk Management Activity

The Company enters into financial derivative transactions, including swaps, forwards, put-swaptions, futures and options to reduce and manage business risks. These transactions manage the risk of a change in the value, yield, price, cash flows, credit quality or degree of exposure with respect to assets, liabilities, or future cash flows, which the Company has acquired or incurred. The Company manages the potential credit exposure for over-the-counter derivative contracts through careful evaluation of the counterparty credit standing, collateral agreements, and master netting agreements. The Company is exposed to credit-related losses in the event of nonperformance by counterparties, however, it does not anticipate nonperformance.

The Company generally uses free-standing derivative instruments for hedging purposes. Additionally, certain liabilities, primarily trust instruments supported by funding agreements, index linked annuities and guarantees offered in connection with variable annuities issued by the Company, contain embedded derivatives as defined by Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("FAS 133"). The Company generally does not account for such derivatives as either fair value or cash flow hedges as might be permitted if specific hedging documentation requirements of FAS 133 were followed. Financial derivatives, including derivatives embedded in certain host liabilities that have been separated for accounting and financial reporting purposes, are carried at fair value. The results from derivative financial instruments and embedded derivatives, including net payments, realized gains and losses and changes in value, are reported in risk management activity.

Interest rate swap agreements generally involve the exchange of fixed and floating payments over the life of the agreement without an exchange of the underlying principal amount and are used for hedging purposes. Interest rate swaps are included in other invested assets or other liabilities.

Forwards consist of interest rate spreadlock agreements, in which the Company locks in the forward interest rate differential between a swap and the corresponding U.S. Treasury security. The forwards are held for investment purposes and are included in other invested assets. The Company had no forwards at December 31, 2006 or 2005.

Put-swaption contracts provide the purchaser with the right, but not the obligation, to require the writer to pay the present value of a long duration interest rate swap at future exercise dates. The Company purchases and writes put-swaptions with maturities up to 10 years. On a net basis, put-swaptions hedge against significant upward movements in interest rates. Written put-swaptions are entered into in conjunction with associated put-swaptions purchased with identical strike prices and notional amounts ("linked put-swaptions") and are presented as a net position included in other liabilities. Non-linked put-swaptions purchased are included in other invested assets.

Equity index futures contracts and equity index call and put options, which are used to hedge the Company's obligations associated with its index linked annuities and guarantees in variable annuity products, are included in other invested assets or other liabilities. These annuities contain embedded options whose fair value is included in deposits on investment contracts.

Credit default swaps, with maturities up to five years, represent agreements under which the Company has purchased default protection on certain underlying corporate bonds held in its portfolio. These contracts allow the Company to sell the protected bonds at par value to the counterparty in the event of their default in exchange for periodic payments made by the Company for the life of the agreement. Credit default swaps are carried at fair value and included in other liabilities.

Total return swaps, in which the Company receives equity returns or returns based on reference pools of assets in exchange for short-term floating rate payments based on notional amounts, are held for both hedging and investment purposes, and are included in other invested assets or other liabilities.

Cross-currency swaps, which embody spot and forward currency swaps and additionally, in some cases, interest rate swaps and equity index swaps, are entered into for the purpose of hedging the Company's foreign currency denominated trust instruments supported by funding agreements. Cross-currency swaps serve to hedge derivatives embedded in the funding agreements and are included in other invested assets or other liabilities. The

2. Summary of Significant Accounting Policies (continued)

fair value of derivatives embedded in funding agreements, as well as foreign currency transaction gains and losses, are included in the carrying value of the trust instruments supported by funding agreements. Foreign currency transaction gains and losses associated with funding agreements hedging activities are included in risk management activity.

Deferred Acquisition Costs
Certain costs of acquiring new business, principally commissions and certain costs associated with policy issue and underwriting, which vary with and are primarily related to the production of new business, have been capitalized as deferred acquisition costs. Deferred acquisition costs are increased by interest thereon and amortized in proportion to anticipated premium revenues for traditional life policies and in proportion to estimated gross profits for annuities and interest-sensitive life products. As certain fixed maturities and equities available for sale are carried at fair value, an adjustment is made to deferred acquisition costs equal to the change in amortization that would have occurred if such securities had been sold at their stated fair value and the proceeds reinvested at current yields. The change in this adjustment is included with the change in fair value of fixed maturities and equities available for sale, net of tax, that is credited or charged directly to stockholder's equity and is a component of other comprehensive income. Deferred acquisition costs have been decreased by $43.2 million and $188.3 million at December 31, 2006 and 2005, respectively, to reflect this adjustment.

Deferred Sales Inducements
Bonus interest on deferred fixed annuities and contract enhancements on index linked annuities and variable annuities have been capitalized as deferred sales inducements. Deferred sales inducements are increased by interest thereon and amortized in proportion to estimated gross profits. As certain fixed maturities and equities available for sale are carried at fair value, an adjustment is made to deferred sales inducements equal to the change in amortization that would have occurred if such securities had been sold at their stated fair value and the proceeds reinvested at current yields. The change in this adjustment is included with the change in fair value of fixed maturities and equities available for sale, net of tax, that is credited or charged directly to stockholder's equity and is a component of other comprehensive income. Deferred sales inducements have been decreased by $16.5 million and $30.4 million at December 31, 2006 and 2005, respectively, to reflect this adjustment.

Value of Acquired Insurance
The value of acquired insurance in-force at acquisition date represents the present value of anticipated profits of the business in-force on November 25, 1986 (the date the Company was acquired by Prudential) net of amortization. The value of acquired insurance in-force is amortized in proportion to anticipated premium revenues for traditional life insurance contracts and estimated gross profits for annuities and interest-sensitive life products over a period of 20 years and was fully amortized as of December 31, 2006.

Federal Income Taxes
The Company provides deferred income taxes on the temporary differences between the tax and financial statement basis of assets and liabilities.

Jackson files a consolidated federal income tax return with Brooke Life, Jackson National Life Insurance Company of New York and Life Insurance Company of Georgia (for the period from May 19, 2005 through December 31, 2005). The PPMA Funds file as limited partnerships and pass through the appropriate portion of their income and deductions to their partners. Jackson National Life (Bermuda) LTD is taxed as a controlled foreign corporation of Jackson. The other affiliated subsidiary entities are limited liability companies with all of their interests owned by Jackson. Accordingly, they are not considered separate entities for income tax purposes; and therefore, are taxed as part of the operations of Jackson. Jackson Federal Bank filed a separate income tax return during the period it was owned by Jackson. Income tax expense is calculated on a separate company basis.

Policy Reserves and Liabilities
Reserves for future policy benefits and claims payable:
For traditional life insurance contracts, reserves for future policy benefits are determined using the net level premium method and assumptions as of the issue date or acquisition date as to mortality, interest, policy lapsation and expenses plus provisions for adverse deviations. Mortality assumptions range from 25% to 160% of the

2. Summary of Significant Accounting Policies (continued)

1975-1980 Basic Select and Ultimate tables depending on policy duration. Interest rate assumptions range from 4.0% to 8.0%. Lapse and expense assumptions are based on Company experience.

Deposits on investment contracts:
For the Company's interest-sensitive life contracts, liabilities approximate the policyholder's account value. For deferred annuities, the fixed option on variable annuities, guaranteed investment contracts and other investment contracts, the liability is the policyholder's account value. The liability for index linked annuities is based on two components, 1) the imputed value of the underlying guaranteed host contract, and 2) the fair value of the embedded option component of the contract. Obligations in excess of the guaranteed contract value are hedged through the use of futures contracts and call options.

Trust Instruments Supported by Funding Agreements
Jackson and Jackson National Life Funding, LLC have established a European Medium Term Note program, with up to $6 billion in aggregate principal amount outstanding at any one time. Jackson National Life Funding, LLC was formed as a special purpose vehicle solely for the purpose of issuing instruments to institutional investors, the proceeds of which are deposited with Jackson and secured by the issuance of funding agreements. Carrying values totaled $1.7 billion and $2.2 billion at December 31, 2006 and 2005, respectively.

Jackson and Jackson National Life Global Funding have established an $8 billion aggregate Global Medium Term Note program. Jackson National Life Global Funding was formed as a statutory business trust, solely for the purpose of issuing instruments to institutional investors, the proceeds of which are deposited with Jackson and secured by the issuance of Funding Agreements. The carrying values at December 31, 2006 and 2005 totaled $3.5 billion and $3.4 billion, respectively.

Instruments issued representing obligations denominated in a foreign currency have been hedged for changes in exchange rates using cross-currency swaps. The fair value of derivatives embedded in funding agreements, as well as foreign currency transaction gains and losses, are included in the carrying value of the trust instruments supported by funding agreements.

Trust instrument liabilities are adjusted to reflect the effects of foreign currency transaction gains and losses using exchange rates as of the reporting date. Foreign currency transaction gains and losses are included in risk management activity.

Federal Home Loan Bank Advances
In 2005, Jackson, as an eligible institution, became a member of the regional Federal Home Loan Bank of Indianapolis ("FHLBI") primarily for the purpose of participating in its mortgage-collateralized loan advance program. Membership requires the Company to purchase and hold a minimum amount of FHLBI capital stock plus additional stock based on outstanding advances. Advances are in the form of funding agreements issued to FHLBI. At December 31, 2006 and 2005, Jackson held $30.0 million and $30.2 million, respectively, in FHLBI capital stock.

Separate Account Assets and Liabilities
The assets and liabilities resulting from individual variable life and annuity contracts, which aggregated $22,113.5 million and $14,613.2 million at December 31, 2006 and 2005, respectively, are segregated in separate accounts. The Company receives administrative fees for managing the funds and other fees for assuming mortality and certain expense risks. Such fees are recorded as earned and included in fee income in the consolidated income statements.

The Company has issued a group variable annuity contract designed for use in connection with and issued to the Company's Defined Contribution Retirement Plan. These deposits are allocated to the Jackson National Separate Account - II and aggregated $130.5 million and $107.4 million at December 31, 2006 and 2005, respectively. The Company receives administrative fees for managing the funds. These fees are recorded as earned and included in fee income in the consolidated income statements.

2. Summary of Significant Accounting Policies (continued)

Revenue and Expense Recognition

Premiums for traditional life insurance are reported as revenues when due. Benefits, claims and expenses are associated with earned revenues in order to recognize profit over the lives of the contracts. This association is accomplished by provisions for future policy benefits and the deferral and amortization of acquisition costs.

Deposits on interest-sensitive life products and investment contracts, principally deferred annuities and guaranteed investment contracts, are treated as policyholder deposits and excluded from revenue. Revenues consist primarily of the investment income and charges assessed against the policyholder's account value for mortality charges, surrenders and administrative expenses. Fee income also includes revenues related to asset management and 12b-1 service fees. Surrender benefits are treated as repayments of the policyholder account. Annuity benefit payments are treated as reductions to the policyholder account. Death benefits in excess of the policyholder account are recognized as an expense when incurred. Expenses consist primarily of the interest credited to policyholder deposits. Underwriting and other acquisition expenses are associated with gross profit in order to recognize profit over the life of the business. This is accomplished by deferral and amortization of acquisition costs and sales inducements. Expenses not related to policy acquisition are recognized as incurred.

Investment income is not accrued on securities in default and otherwise where the collection is uncertain. Subsequent receipts of interest on such securities are generally used to reduce the cost basis of the securities.

In 2006, the Company was awarded $16.0 million from a class action settlement against certain underwriters of WorldCom securities. Also, in 2004, the Company received cash proceeds of $51.9 million from a judgment award in a legal action involving LePages, Inc., a company in which Jackson had a controlling interest. These settlements were recorded in other income.

3. Acquisitions

On May 18, 2005, Brooke Life purchased, in exchange for $260.7 million in cash, 100% of the interest in Life of Georgia, a life insurance company domiciled in Georgia, from ING Groep, N.V. ("ING"). Direct costs of $4.4 million were capitalized in connection with the acquisition. On May 31, 2005, Brooke Life contributed 100% of its interest in Life of Georgia to Jackson. The acquisition expanded Jackson's life insurance base while taking advantage of Jackson's low cost structure. The results of Life of Georgia's operations have been included in these consolidated financial statements since acquisition. On December 31, 2005, Life of Georgia was merged into Jackson.

The preliminary purchase price was subject to post-closing adjustments and was initially allocated to the assets acquired and liabilities assumed using management's best estimate of fair value as of the acquisition date. In 2006, an arbitrator ruled in Jackson's favor on certain purchase price adjustments. As a result of this determination and other previously settled amounts, the purchase price was reduced by $11.7 million within the purchase price allocation period.

As of December 31, 2005, Jackson recorded in other assets the value of business acquired totaling $1.1 million. As a result of purchase price adjustments, this asset was reversed in 2006 and the remaining adjustment resulted in negative goodwill, which was recorded as an extraordinary gain of $8.9 million.

3. Acquisitions (continued)

The following table summarizes the fair value of the assets acquired and liabilities assumed, as adjusted (in thousands):

	Opening Balance Sheet
Cash and short-term investments	$ 86,670
Fixed maturities	1,612,767
Other invested assets	78,129
Accrued investment income	21,516
Deferred income taxes	7,868
Other assets	12,609
Total assets acquired	$ 1,819,559
Reserves for future policy benefits and claims payable	$ 881,083
Deposits on investment contracts	656,161
Other liabilities	20,820
Total liabilities assumed	$ 1,558,064
Net assets acquired	$ 261,495
Adjusted purchase price	$ 253,459
Extraordinary gain on purchase, net of tax benefit	$ 8,944

The following table summarizes Jackson's unaudited pro forma results of operations assuming the business acquisition had occurred at the beginning of 2004 (in thousands):

	Unaudited Pro Forma	
	Years ended December 31,	
	2005	2004
Revenues	$ 4,013,031	$ 3,729,228
Total benefits and expenses	2,976,945	2,799,273
Pretax income from continuing operations	1,035,164	880,914
Net income	675,841	638,330

The 2005 pro forma amounts include the effects of certain non-recurring restructuring transactions effected by Life of Georgia prior to the acquisition. These transactions included transferring certain assets and liabilities to ING affiliates, resulting in revenue of $120.8 million, expenses of $17.0 million, pretax income from operations of $103.8 million and net income of $67.5 million.

4. Discontinued Operations

On October 28, 2004, the Company completed the sale of Jackson Federal, a wholly owned thrift headquartered in Southern California, to Union BanCal Corporation for $305.0 million in cash and stock. On October 27, 2004, Jackson made a capital contribution of $4.6 million to Jackson Federal prior to closing to fund certain expenses incurred by Jackson Federal related to the sale. The gain on disposal and results of operations of Jackson Federal for all periods presented are included in income from discontinued operations on the consolidated income statements.

4. Discontinued Operations (continued)

The following table summarizes certain components of the results of the discontinued operations (in thousands):

		Period ended October 28, 2004
Revenues	$	79,813
Realized gains	$	1,700
Income from discontinued operations, net of tax of $11,064	$	20,658
Gain on disposal of discontinued operations, net of tax of $29,580	$	36,118

Interest expense on savings deposits, which is included in discontinued operations, totaled $19.5 million in 2004.

Interest paid on credit programs offered by the Federal Home Loan Bank, which is included in discontinued operations, totaled $7.0 million in 2004.

5. Fair Value of Financial Instruments

Disclosure is required of the fair value of financial instruments for which it is practicable to estimate that value. In cases where quoted market prices are not available, and for illiquid distressed securities, fair values are based on estimates using discounted cash flows or other valuation techniques. Such values are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent market quotes and, in many cases, could not be realized in immediate settlement of the instrument.

The following summarizes the basis used by the Company in estimating fair values for financial instruments:

Cash and Short-Term Investments:
Carrying value is considered to be a reasonable estimate of fair value.

Fixed Maturities:
Fair values for fixed maturity securities are based principally on quoted market prices, if available. For securities that are not actively traded, fair values are estimated using independent pricing services or are analytically determined. Fair values for illiquid distressed securities are primarily determined based on internally derived estimates of discounted future cash flows or expected recovery values.

Equities and Trading Securities:
Fair values for common and non-redeemable preferred stock are based principally on quoted market prices, if available. For securities that are not actively traded, fair values are estimated using independent pricing services or are analytically determined. Fair values of investments in mutual funds are based on quoted net asset values. Certain public stock positions are fair valued at a discount to their exchange-traded price due to lock-up trading restrictions imposed in connection with initial public offerings. Discounts of 10% and 15% are applied to two positions at December 31, 2006, totaling $3.3 million. A discount of 15% for a single issue at December 31, 2005 totaled $1.5 million.

Mortgage Loans:
Fair values are determined by discounting the future cash flows at current market rates. The fair value of mortgages approximated $5,373.1 million and $5,134.1 million at December 31, 2006 and 2005, respectively.

Policy Loans:
Fair value approximates carrying value since policy loan balances reduce the amount payable at death or surrender of the contract.

5. Fair Value of Financial Instruments (continued)

Derivative Instruments:
Fair values for interest rate swaps, cross-currency swaps, put-swaptions, forwards and total return swaps are determined using estimates of future cash flows discounted at current market rates. Fair values for futures are based on exchange-traded prices. Fair values for equity index call and put options are determined using Black-Scholes option valuation methodologies. Fair values for credit default swaps are based on quoted market prices.

The fair value of the Company's guaranteed minimum withdrawal benefit embedded derivative liability has been calculated based on actuarial assumptions related to the projected cash flows, including benefits and related contract charges, over the expected lives of the contracts, incorporating expectations regarding policyholder behavior in varying economic conditions.

The Company reinsures essentially 100% of its guaranteed minimum income benefit on a net settled basis. The net settlement is considered an embedded derivative and the Company determines the fair value using actuarial assumptions related to the projected cash flows, including reinsurance premiums and related benefit reimbursements, over the expected lives of the contracts, incorporating expectations regarding policyholder behavior in varying economic conditions.

The nature of these embedded derivative cash flows can be quite varied. Therefore, stochastic techniques are used to generate a variety of market return scenarios for evaluation. The generation of these scenarios and the assumptions as to policyholder behavior involve numerous estimates and subjective judgments including those regarding expected market volatility, correlations of market returns and discount rates, utilization of the benefit by policyholders under varying conditions and policyholder lapsation. At each valuation date, the Company assumes expected returns based on risk-free rates as represented by the LIBOR forward curve rates as of that date and market volatility as determined with reference to implied volatility data and evaluations of historical volatilities for various indices. The risk-free spot rates as represented by the LIBOR spot curve as of the valuation date are used to determine the present value of expected future cash flows produced in the stochastic process.

Separate Account Assets:
Separate account assets are carried at the fair value of the underlying securities.

Annuity Reserves:
Fair values for immediate annuities, without mortality features, are derived by discounting the future estimated cash flows using current interest rates for similar maturities. For deferred annuities, fair value is based on surrender value. For index linked annuities, fair value includes the fair value of the embedded options. The carrying value and fair value of the annuity reserves approximated $28.5 billion and $27.7 billion, respectively, at December 31, 2006 and $29.2 billion and $28.3 billion, respectively, at December 31, 2005.

Reserves for Guaranteed Investment Contracts:
Fair value is based on the present value of future cash flows at current pricing rates. The fair value approximated $2.0 billion at both December 31, 2006 and 2005.

Trust Instruments Supported by Funding Agreements:
Fair value is based on the present value of future cash flows at current pricing rates, plus the fair value of embedded derivatives. The fair value approximated $5.2 billion and $5.6 billion at December 31, 2006 and 2005, respectively.

Federal Home Loan Bank Advances:
Fair value is based on future cash flows discounted at current interest rates. The fair value approximated $597.4 million and $99.6 million at December 31, 2006 and 2005, respectively.

Reverse Repurchase Agreements:
Carrying value of reverse repurchase agreements is considered to be a reasonable estimate for fair value.

5. Fair Value of Financial Instruments (continued)

Notes Payable:
Fair value of notes payable is based on future cash flows discounted at current interest rates. The fair value approximated $461.5 million and $552.0 million at December 31, 2006 and 2005, respectively.

Separate Account Liabilities:
Fair value of contracts in the accumulation phase is based on account value less surrender charges. Fair value of contracts in the payout phase is based on the present value of future cash flows at assumed investment rates. The aggregate fair value approximated $20.9 billion and $13.8 billion at December 31, 2006 and 2005, respectively.

6. Investments

Investments are comprised primarily of fixed-income securities, primarily publicly-traded industrial, asset-backed, utility and government bonds, and mortgage loans. Asset-backed securities include mortgage-backed and other structured securities. The Company generates the majority of its deposits from interest-sensitive individual annuity contracts, life insurance products and guaranteed investment contracts on which it has committed to pay a declared rate of interest. The Company's strategy of investing in fixed-income securities and loans aims to ensure matching of the asset yield with the interest-sensitive liabilities and to earn a stable return on its investments.

Fixed Maturities
The following table sets forth fixed maturity investments at December 31, 2006, classified by rating categories as assigned by nationally recognized statistical rating organizations, the National Association of Insurance Commissioners (“NAIC”), or if not rated by such organizations, the Company’s affiliated investment advisor. At December 31, 2006, the carrying value of investments rated by the Company’s affiliated investment advisor totaled $503.0 million. For purposes of the table, if not otherwise rated higher by a nationally recognized statistical rating organization, NAIC Class 1 investments are included in the A rating; Class 2 in BBB; Class 3 in BB and Classes 4 through 6 in B and below.

Investment Rating	Percent of Total Fixed Maturities December 31, 2006
AAA	20.5%
AA	8.4
A	26.9
BBB	38.4
Investment grade	94.2
BB	5.0
B and below	0.8
Below investment grade	5.8
Total fixed maturities	100.0%

The amortized cost and carrying value of fixed maturities in default that were anticipated to be income producing when purchased were $4.0 million and $4.1 million, respectively, at December 31, 2006. The amortized cost and carrying value of fixed maturities that have been non-income producing for the 12 months preceding December 31, 2006 were $4.0 million and $4.1 million, respectively, and for the 12 months preceding December 31, 2005 were $4.0 million and $5.3 million, respectively.

6. Investments (continued)

The cost or amortized cost, gross unrealized gains and losses and fair value of available for sale fixed maturities and equities were as follows (in thousands):

December 31, 2006	**Cost or Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Fixed Maturities				
U.S. Treasury securities	$ 11,693	$ -	$ 281	$ 11,412
Foreign governments	1,341	314	-	1,655
Public utilities	2,753,801	62,651	26,298	2,790,154
Corporate securities	25,220,870	530,472	351,648	25,399,694
Asset-backed securities	10,035,281	122,647	120,937	10,036,991
Total fixed maturities	$ 38,022,986	$ 716,084	$ 499,164	$ 38,239,906
Equities	$ 107,750	$ 13,843	$ -	$ 121,593

December 31, 2005	**Cost or Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Fixed Maturities				
U.S. Treasury securities	$ 39,561	$ 22	$ 756	$ 38,827
Foreign governments	32,331	281	770	31,842
Public utilities	2,937,225	103,964	16,353	3,024,836
Corporate securities	27,984,571	867,709	308,982	28,543,298
Asset-backed securities	8,640,123	95,291	125,010	8,610,404
Total fixed maturities	$ 39,633,811	$ 1,067,267	$ 451,871	$ 40,249,207
Equities	$ 313,498	$ 14,736	$ 1,756	$ 326,478

At December 31, 2006 and 2005, available for sale securities without a readily ascertainable market value having an amortized cost of $5.7 billion and $5.9 billion, respectively, had estimated fair values of $5.7 billion and $6.0 billion, respectively.

The amortized cost and fair value of fixed maturities at December 31, 2006, by contractual maturity, are shown below (in thousands). Expected maturities may differ from contractual maturities where securities can be called or prepaid with or without early redemption penalties.

	Amortized Cost	**Fair Value**
Due in 1 year or less	$ 1,189,966	$ 1,192,368
Due after 1 year through 5 years	8,538,615	8,726,446
Due after 5 years through 10 years	13,791,038	13,766,996
Due after 10 years through 20 years	2,954,442	2,979,718
Due after 20 years	1,513,644	1,537,387
Asset-backed securities	10,035,281	10,036,991
Total	$ 38,022,986	$ 38,239,906

U.S. Treasury securities with a carrying value of $10.7 million and $13.5 million at December 31, 2006 and 2005, respectively, were on deposit with regulatory authorities, as required by law in various states in which business is conducted.

6. Investments (continued)

The fair value and the amount of gross unrealized losses included in accumulated other comprehensive income in stockholder's equity were as follows (in thousands):

	Less than 12 months		12 months or longer		Total	
December 31, 2006	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**
U.S. Treasury securities	$ 27	$ 3,063	$ 254	$ 7,280	$ 281	$ 10,343
Foreign governments	-	-	-	-	-	-
Public utilities	2,182	513,145	24,116	964,937	26,298	1,478,082
Corporate securities	48,919	3,869,151	302,729	10,212,760	351,648	14,081,911
Asset-backed securities	8,642	2,129,328	112,295	3,740,046	120,937	5,869,374
Subtotal - fixed maturities	59,770	6,514,687	439,394	14,925,023	499,164	21,439,710
Equities	-	-	-	-	-	-
Total temporarily impaired securities	$ 59,770	$ 6,514,687	$ 439,394	$14,925,023	$ 499,164	$ 21,439,710

	Less than 12 months		12 months or longer		Total	
December 31, 2005	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**
U.S. Treasury securities	$ 756	$ 35,717	$ -	$ -	$ 756	$ 35,717
Foreign governments	671	28,285	99	2,039	770	30,324
Public utilities	15,125	1,055,007	1,228	42,302	16,353	1,097,309
Corporate securities	250,414	12,914,442	58,568	927,820	308,982	13,842,262
Asset-backed securities	44,837	3,303,743	80,173	2,190,168	125,010	5,493,911
Subtotal - fixed maturities	311,803	17,337,194	140,068	3,162,329	451,871	20,499,523
Equities	1,756	24,198	-	-	1,756	24,198
Total temporarily impaired securities	$ 313,559	$ 17,361,392	$ 140,068	$ 3,162,329	$ 453,627	$ 20,523,721

The Company periodically reviews its fixed maturities and equities on a case-by-case basis to determine if any decline in fair value to below amortized cost is other-than-temporary. Factors considered in determining whether a decline is other-than-temporary include the length of time a security has been in an unrealized loss position, reasons for the decline in value, expectations for the amount and timing of a recovery in value and the Company's ability and intent to hold a security to recovery in value or of contractual cash flows. If it is determined that a decline in value of an investment is temporary, the decline is recorded as an unrealized loss in accumulated other comprehensive income in stockholder's equity. If the decline is considered to be other-than-temporary, a realized loss is recognized in the consolidated income statements.

Generally, securities with fair values that are less than 80% of amortized cost and other securities the Company determines are underperforming or potential problem securities are subject to regular review. To facilitate the review, securities with significant declines in value, or where other objective criteria evidencing credit deterioration have been met, are included on a watch list. Among the criteria for securities to be included on a watch list are: credit deterioration that has led to a significant decline in value of the security; a significant covenant related to the security has been breached; or an issuer has filed or indicated a possibility of filing for bankruptcy, has missed or announced it intends to miss a scheduled interest or principal payment, or has experienced a specific material adverse change that may impair its creditworthiness.

In performing these reviews, the Company considers the relevant facts and circumstances relating to each investment and must exercise considerable judgment in determining whether a security is other than temporarily

6. Investments (continued)

impaired. Assessment factors include judgments about an obligor's current and projected financial position, an issuer's current and projected ability to service and repay its debt obligations, the existence of, and realizable value of, any collateral backing obligations, the macro-economic outlook and micro-economic outlooks for specific industries and issuers. Assessing the duration of asset-backed securities can also involve assumptions regarding underlying collateral such as prepayment rates, default and recovery rates, and third-party servicing capabilities.

Among the specific factors considered are whether the decline in fair value results from a change in the credit quality of the security itself, or from a downward movement in the market as a whole, the likelihood of recovering the carrying value based on the near term prospects of the issuer and the Company's ability and intent to hold the security until such a recovery may occur. Unrealized losses that are considered to be primarily the result of market conditions are usually determined to be temporary, e.g., minor increases in interest rates, unusual market volatility or industry-related events, and where the Company also believes there exists a reasonable expectation for recovery in the near term and, furthermore, has the intent and ability to hold the investment until maturity or the market recovery. To the extent factors contributing to impairment losses recognized affect other investments, such investments are also reviewed for other-than-temporary impairment and losses are recorded when appropriate.

The Company applies the provisions of EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets" ("EITF 99-20") when evaluating whether impairments on its other than high quality structured securities, including certain asset-backed securities and collateralized debt obligations, are other than temporary. The Company regularly reviews future cash flow assumptions and, in accordance with EITF 99-20, if there has been an adverse change in estimated cash flows to be received on a security, an impairment is recognized in the consolidated income statements. For privately placed structured securities, impairment amounts are based on discounted cash flows.

There are inherent uncertainties in assessing the fair values assigned to the Company's investments and in determining whether a decline in market value is other-than-temporary. The Company's review of fair value involves several criteria including economic conditions, credit loss experience, other issuer-specific developments and future cash flows. These assessments are based on the best available information at the time. Factors such as market liquidity, the widening of bid/ask spreads and a change in the cash flow assumptions can contribute to future price volatility. If actual experience differs negatively from the assumptions and other considerations used in the consolidated financial statements, unrealized losses currently in accumulated other comprehensive income may be recognized in the consolidated income statement in future periods.

The Company currently intends to hold available for sale securities with unrealized losses not considered other than temporary until they mature or recover in value. However, if the specific facts and circumstances surrounding an individual security, or the outlook for its industry sector change, the Company may sell the security prior to its maturity and realize a loss.

Of the total carrying value for fixed maturities in an unrealized loss position at December 31, 2006, 84.3% were investment grade, 4.9% were below investment grade and 10.8% were not rated. Unrealized losses from fixed maturities that were below investment grade or not rated represented approximately 20.9% of the aggregate gross unrealized losses on available for sale fixed maturities.

Corporate securities in an unrealized loss position were diversified across industries. As of December 31, 2006, the industries representing the larger unrealized losses included energy (12.6% of fixed maturities gross unrealized losses) and financial services (11.7%). The Company had no material unrealized losses on individual fixed maturities or equities at December 31, 2006.

6. Investments (continued)

The amount of gross unrealized losses for fixed maturities in a loss position by maturity date of the fixed maturities as of December 31, 2006 were as follows (in thousands):

Less than one year	$	1,672
One to five years		56,851
Five to ten years		221,130
More than ten years		98,574
Asset-backed securities		120,937
Total gross unrealized losses	$	499,164

Mortgage Loans
Commercial mortgage loans are net of allowance for loan losses of $13.1 million and $17.6 million at December 31, 2006 and 2005, respectively. At December 31, 2006, mortgage loans were collateralized by properties located in 38 states and Canada.

Securitizations
In November 2003, Jackson executed the Piedmont CDO Trust ("Piedmont") securitization transaction. In this transaction, Jackson contributed $1,159.6 million of asset-backed securities, ultimately to Piedmont, which issued several classes of debt to acquire such securities. The transaction was recorded as a sale; however, Jackson retained beneficial interests in the contributed asset-backed securities of approximately 80% by acquiring certain securities issued by Piedmont. Piedmont is a Qualified Special Purpose Entity and accordingly, is not consolidated in the accompanying financial statements. Jackson's carrying value in securities issued by Piedmont totaled $636.6 million and $795.9 million at December 31, 2006 and 2005, respectively, and was included in asset-backed securities.

Other Invested Assets
Other invested assets primarily include investments in 1) limited partnerships, 2) derivative instruments with positive fair values and 3) real estate. Investments in limited partnerships have carrying values of $479.9 million and $710.3 million at December 31, 2006 and 2005, respectively. Real estate totaling $109.0 million and $142.4 million at December 31, 2006 and 2005, respectively, includes foreclosed properties with a book value of $10.5 million and $19.6 million at December 31, 2006 and 2005, respectively. Limited partnership income recognized by the Company was $133.0 million, $162.5 million and $105.2 million in 2006, 2005 and 2004, respectively.

The fair value of free-standing derivative instruments reflects the estimated amounts, net of payment accruals, that the Company would receive or pay upon sale or termination of the contracts at the reporting date. With respect to swaps and put-swaptions, the notional amount represents the stated principal balance used as a basis for calculating payments. With respect to futures and options, the contractual amount represents the market exposure of open positions.

6. Investments (continued)

A summary of the aggregate contractual or notional amounts and fair values of freestanding derivative instruments outstanding is as follows (in thousands):

December 31, 2006

	Other Invested Assets		Other Liabilities		
	Contractual/ Notional Amount	Fair Value	Contractual/ Notional Amount	Fair Value	Net Fair Value
Cross-currency swaps	$ 1,051,577	$ 215,382	$ 50,000	$ (1,789)	$ 213,593
Credit default swaps	-	-	36,000	(59)	(59)
Equity index call options	1,140,750	108,472	22,718	(5,446)	103,026
Equity index put options	5,300,000	32,837	-	-	32,837
Put-swaptions	26,500,000	9,559	23,000,000	(459)	9,100
Futures	-	-	535,650	(1,238)	(1,238)
Total return swaps	450,000	24,632	127,000	(13,470)	11,162
Interest rate swaps	4,710,105	104,899	3,890,000	(156,495)	(51,596)
Total	$ 39,152,432	$ 495,781	$ 27,661,368	$ (178,956)	$ 316,825

December 31, 2005

	Other Invested Assets		Other Liabilities		
	Contractual/ Notional Amount	Fair Value	Contractual/ Notional Amount	Fair Value	Net Fair Value
Cross-currency swaps	$ 947,735	$ 189,383	$ 672,653	$ (45,278)	$ 144,105
Equity index call options	1,365,850	108,085	22,718	(3,566)	104,519
Equity index put options	2,450,000	45,758	-	-	45,758
Put-swaptions	16,000,000	11,634	25,000,000	(1,746)	9,888
Futures	313,700	6,825	-	-	6,825
Total return swaps	1,050,000	66,248	206,272	(32,297)	33,951
Interest rate swaps	4,063,566	107,330	6,092,000	(224,103)	(116,773)
Total	$ 26,190,851	$ 535,263	$ 31,993,643	$ (306,990)	$ 228,273

Securities Lending

The Company has entered into securities lending agreements with an agent bank whereby blocks of securities are loaned to third parties, primarily major brokerage firms. As of December 31, 2006 and 2005, the estimated fair value of loaned securities was $306.5 million and $436.8 million, respectively. The agreements require a minimum of 102 percent of the fair value of the loaned securities to be held as collateral, calculated on a daily basis. To further minimize the credit risks related to this program, the financial condition of counterparties is monitored on a regular basis. Cash collateral received, in the amount of $235.9 million and $428.0 million at December 31, 2006 and 2005, respectively, was invested by the agent bank and included in short-term investments of the Company. A securities lending payable is included in liabilities for cash collateral received. Other collateral received, generally in the form of securities, totaled $89.2 million and $29.4 million at December 31, 2006 and 2005, respectively. Securities lending transactions are used to generate income. Income and expenses associated with these transactions are reported as net investment income.

7. Investment Income, Risk Management Activity and Realized Gains and Losses

The sources of net investment income by major category were as follows (in thousands):

	Years ended December 31, 2006	2005	2004
Fixed maturities	$ 2,363,953	$ 2,340,984	$ 2,270,233
Other investment income	619,864	626,967	492,210
Total investment income	2,983,817	2,967,951	2,762,443
Less investment expenses	(79,030)	(88,511)	(72,498)
Net investment income	$ 2,904,787	$ 2,879,440	$ 2,689,945

Risk management activity, including gains (losses) and change in fair value of derivative instruments and embedded derivatives, was as follows (in thousands):

	Years ended December 31, 2006	2005	2004
Interest rate swaps	$ 106,907	$ 160,250	$ 16,618
Forwards	-	6,891	4,024
Put-swaptions	(10,572)	(3,093)	8,390
Futures	(40,993)	4,086	708
Equity index call options	33,460	4,548	48,870
Equity index put options	(64,046)	(19,757)	-
Total return swaps	10,486	-	21,701
Fixed index annuity embedded derivatives	(154,696)	(20,247)	(30,024)
Credit default swaps	1,447	-	-
Variable annuity embedded derivatives	12,780	37,149	20,527
Risk management activity	$ (105,227)	$ 169,827	$ 90,814

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

	Years ended December 31, 2006	2005	2004
Sales of fixed maturities			
Gross gains	$ 96,911	$ 85,648	$ 263,685
Gross losses	(113,800)	(53,395)	(67,352)
Sales of equities			
Gross gains	7,796	25,243	33,037
Gross losses	(1,562)	(93)	(685)
Sales of real estate			
Gross gains	-	19	-
Transfers to trading securities	-	-	(9,300)
Impairment losses	(47,055)	(44,438)	(80,729)
Total	$ (57,710)	$ 12,984	$ 138,656

Net realized gains (losses) on investments, net of amounts allocated to minority interest, totaled $(66.7) million, $12.0 million and $92.8 million in 2006, 2005 and 2004, respectively.

8. Value of Acquired Insurance

The value of acquired insurance in-force at acquisition date represents the present value of anticipated profits of the business in-force on November 25, 1986 (the date the Company was acquired by Prudential). The value of acquired insurance in-force was determined by using assumptions as to interest, persistency and mortality. Profits were then discounted to arrive at the value of the insurance in-force.

The amortization of acquired insurance was as follows (in thousands):

	2006	2005	2004
Value of acquired insurance:			
Balance, beginning of year	$ 23,578	$ 45,768	$ 66,650
Interest, at rates varying from 6.5% to 9.5%	1,108	3,258	5,277
Amortization	(24,686)	(25,448)	(26,159)
Balance, end of year	$ -	$ 23,578	$ 45,768

9. Certain Nontraditional Long-Duration Contracts and Variable Annuity Guarantees

The Company issues variable contracts through its separate accounts for which investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities). The Company also issues variable annuity and life contracts through separate accounts where the Company contractually guarantees to the contract holder (variable contracts with guarantees) either a) return of no less than total deposits made to the contract adjusted for any partial withdrawals, b) total deposits made to the contract adjusted for any partial withdrawals plus a minimum return, or c) the highest contract value on a specified anniversary date adjusted for any withdrawals following the contract anniversary. These guarantees include benefits that are payable in the event of death (guaranteed minimum death benefit (“GMDB”)), annuitization (guaranteed minimum income benefit (“GMIB”)), or at specified dates during the accumulation period (guaranteed minimum withdrawal benefit (“GMWB”)).

The assets supporting the variable portion of both traditional variable annuities and variable contracts with guarantees are carried at fair value and reported as summary total separate account assets with an equivalent summary total reported for liabilities. Amounts assessed against the contract holders for mortality, administrative, and other services are included in revenue. Changes in liabilities for minimum guarantees are included in increase in reserves, net of reinsurance in the consolidated income statement, with the exception of changes in embedded derivatives, which are included in risk management activity. Separate account net investment income, net investment gains and losses, and the related liability changes are offset within the same line item in the consolidated income statements.

9. Certain Nontraditional Long-Duration Contracts and Variable Annuity Guarantees (continued)

At December 31, 2006 and 2005, the company had variable contracts with guarantees, where net amount at risk is the amount of guaranteed benefit in excess of current account value, as follows (dollars in millions):

December 31, 2006	Minimum Return	Account Value	Net Amount at Risk	Weighted Average Attained Age	Average Period until Expected Annuitization
Return of net deposits plus a minimum return					
GMDB	0% - 5%	$ 17,036	$ 1,218	63.3 years	
GMIB	0% - 6%	$ 2,522	$ 21		7.4 years
GMWB - Premium only		$ 4,928	$ -		
GMWB - For life	0% - 5%	$ 997	$ -		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		$ 3,266	$ 45	61.6 years	
GMWB - Highest anniversary only		$ 1,854	$ 1		
GMWB - For life		$ 543	$ -		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0% - 5%	$ 1,786	$ 5	63.8 years	
GMWB - For life	0% - 5%	$ 962	$ -		

December 31, 2005	Minimum Return	Account Value	Net Amount at Risk	Weighted Average Attained Age	Average Period until Expected Annuitization
Return of net deposits plus a minimum return					
GMDB	0% - 5%	$ 11,471	$ 1,411	63.4 years	
GMIB	0% - 6%	$ 2,000	$ 21		8.1 years
GMWB		$ 4,380	$ 1		
Highest specified anniversary account value minus withdrawals post-anniversary - GMDB		$ 1,886	$ 47	61.2 years	
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary - GMDB	0% - 5%	$ 1,243	$ 5	63.7 years	

Account balances of contracts with guarantees were invested in variable separate accounts as follows (in millions):

	December 31,	
Fund type:	**2006**	**2005**
Equity	$ 18,937	$ 12,388
Bond	1,508	1,156
Balanced	1,373	903
Money market	269	160
Total	$ 22,087	$ 14,607

9. Certain Nontraditional Long-Duration Contracts and Variable Annuity Guarantees (continued)

GMDB liabilities, before reinsurance, reflected in the general account are as follows (in millions):

	2006	2005	2004
Balance at January 1	$ 37.0	$ 42.0	$ 50.1
Incurred guaranteed benefits	43.6	21.2	19.1
Paid guaranteed benefits	(24.0)	(26.2)	(27.2)
Balance at December 31	$ 56.6	$ 37.0	$ 42.0
Balance at December 31, net of reinsurance	$ 1.9	$ 0.8	$ 0.9

The GMDB liability is determined at each period end by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. The Company regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

The following assumptions and methodology were used to determine the GMDB liability at December 31, 2006 and 2005:

1) Use of a series of deterministic investment performance scenarios.
2) Mean investment performance assumption of 8.4% after investment management fees, but before investment advisory fees and mortality and expense charges.
3) Mortality equal to 80% of the Annuity 2000 table.
4) Lapse rates varying by contract type and duration and ranging from 2% to 50%, with an average of 7% during the surrender charge period and 13% thereafter at December 31, 2006 and from 2% to 40%, with an average of 5% during the surrender charge period and 12% thereafter at December 31, 2005.
5) Discount rate of 8.4%.

Most GMWB reserves are considered to be derivatives under FAS 133 and are recognized at fair value, with the change in fair value included in risk management activity. As the nature of the cash flows used to derive the fair value of these reserves may be quite varied, the fair value is calculated as the average of the results from 1,000 stochastic scenarios. These scenarios incorporate assumptions regarding expected market volatility, correlations of market returns and discount rates, utilization of the benefit by policyholders under varying conditions and policyholder lapsation. At each valuation date, the Company assumes expected returns based on risk-free rates as represented by the LIBOR forward curve as of that date and market volatility as determined with reference to implied volatility data and evaluations of historical volatilities for various indices. The risk-free spot rates as represented by the LIBOR spot curve as of the valuation date are used to determine the present value of expected future cash flows produced in the stochastic process. The negative GMWB reserve at December 31 2006 and 2005 totaled $56.0 million and $26.5 million, respectively, and is included in other assets.

Since October 2004, Jackson has issued certain GMWB products that guarantee payments over a lifetime. Reserves for these lifetime benefits are calculated as required by SOP 03-1. At December 31, 2006 and 2005, these SOP 03-1 reserves are immaterial.

The direct GMIB liability is determined at each period end by estimating the expected value of the annuitization benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. The Company regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised. The assumptions used for calculating the direct GMIB liability at December 31, 2006 and 2005, are consistent with those used for calculating the GMDB liability. These GMIB SOP 03-1 reserves are minimal at December 31, 2006 and 2005.

9. Certain Nontraditional Long-Duration Contracts and Variable Annuity Guarantees (continued)

Other Liabilities – Insurance and Annuitization Benefits

The Company has established additional reserves for life insurance business due to: universal life ("UL") plans with secondary guarantees, interest-sensitive life ("ISWL") plans that exhibit "profits followed by loss" patterns and account balance adjustments to tabular guaranteed cash values on one interest sensitive life plan. The Company also has a small closed block of two-tier annuities, where different crediting rates are used for annuitization and surrender benefit calculations, for which a liability was established to cover future annuitization benefits in excess of surrender values. The Company also has a small closed block of two-tier annuities, where different crediting rates are used for annuitization and surrender benefit calculations. The total liability for this block is the low tier funding using the lower credited rate associated with surrenders, plus the SOP 03-1 annuitization reserve.

Liabilities for these benefits have been established according to the methodology prescribed in SOP 03-1, as follows:

	December 31, 2006			December 31, 2005		
Benefit Type	Liability (in millions)	Net Amount at Risk (in millions)*	Weighted Average Attained Age	Liability (in millions)	Net Amount at Risk (in millions)*	Weighted Average Attained Age
UL insurance benefit	$ 57	$ 4,992	54.5 years	$ 58	$ 4,620	54.6 years
Two-tier annuitization	$ 7	$ 37	60.7 years	$ 7	$ 39	59.4 years
ISWL account balance adjustment	$ 40	n/a	n/a	$ 34	n/a	n/a

* Net amount at risk ("NAR") for the UL benefits is for the total of the plans containing any policies having projected non-zero excess benefits, and thus may include NAR for some policies with zero excess benefits.

The following assumptions and methodology were used to determine the UL insurance benefit liability at December 31, 2006 and 2005:

1) Use of a series of deterministic premium persistency scenarios.
2) Other experience assumptions similar to those used in amortization of deferred acquisition costs.
3) Discount rates equal to the credited interest rates, approximately 4%-5% projected.

The following assumptions and methodology were used to determine the two-tier annuitization benefit liability at December 31, 2006 and 2005:

1) Use of a series of deterministic scenarios, varying by surrender rate and annuitization rate.
2) Other experience assumptions similar to those used in amortization of deferred acquisition costs.
3) Discount rates are equal to credited interest rates, approximately, 3%-4% projected at December 31, 2006 and 3% - 5% projected at December 31, 2005.

10. Notes Payable

The aggregate carrying value and fair value of notes payable at December 31, 2006 and 2005 were as follows (in thousands):

	December 31,			
	2006		2005	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Surplus notes	$ 249,265	$ 308,550	$ 249,251	$ 314,350
Tuscany notes	114,381	114,381	224,712	224,712
Mortgage loans	34,866	34,866	4,226	4,226
VIE equity classes	3,750	3,750	8,750	8,750
Total	$ 402,262	$ 461,547	$ 486,939	$ 552,038

Surplus notes
On March 15, 1997, the Company issued 8.15% Surplus Notes (the "Notes") in the principal amount of $250.0 million due March 15, 2027. The Notes were issued pursuant to Rule 144A under the Securities Act of 1933, and are unsecured and subordinated to all present and future indebtedness, policy claims and other creditor claims.

Under Michigan Insurance law, for statutory reporting purposes, the Notes are not part of the legal liabilities of the Company and are considered capital and surplus. Payments of interest or principal may only be made with the prior approval of the Commissioner of Insurance of the State of Michigan and only out of surplus earnings which the Commissioner determines to be available for such payments under Michigan Insurance law. The Notes may not be redeemed at the option of the Company or any holder prior to maturity.

Interest is payable semi-annually on March 15 and September 15 of each year. Interest paid on the Notes was $20.4 million in each of 2006, 2005 and 2004.

Tuscany notes
On December 19, 2001, Tuscany CDO, Limited, a VIE in which Jackson is the primary beneficiary, issued $900.0 million of senior and subordinated notes. At issuance, the most senior notes, initially totaling $450.0 million, due February 25, 2010 were sold to unrelated parties with the remaining senior and subordinated notes retained by the Company. The most senior notes were paid in full by August 2006. In 2003, the second most senior notes, initially totaling $129.0 million, due February 25, 2015 were sold to unrelated parties. The most senior notes bore interest at LIBOR plus .38% and the second most senior notes bear interest at LIBOR plus .47% (collectively, "Tuscany Notes"). At December 31, 2006 and 2005, the weighted average rate on the Tuscany Notes was 5.93% and 4.48%, respectively. Interest paid totaled $11.0 million, $6.8 million and $3.7 million in 2006, 2005 and 2004, respectively.

Mortgage loans
Certain consolidated real estate VIEs, including certain entities that were newly consolidated in 2006, have outstanding mortgage loans at a weighted average interest rate of 6.53% and 8.55% at December 31, 2006 and 2005, respectively, with maturities through 2016. Interest paid totaled $2.8 million, $273 thousand and $160 thousand in 2006, 2005 and 2004, respectively.

VIE equity classes
Certain of the VIEs have "equity" classes issued in the form of non-investment grade debt with maturities through November 2013. Accordingly, these equity classes are classified as notes payable rather than minority interest in the consolidated balance sheets. These notes accrue contingent interest in addition to the stated coupon. The outstanding principal amounts accrued interest at a weighted average interest rate of 7.12% and 8.31% at December 31, 2006 and 2005, respectively. Interest paid on the notes in 2006, 2005 and 2004 totaled $20.0 million, $664 thousand and $456 thousand, respectively.

11. Reverse Repurchase Agreements

During 2006 and 2005, the Company entered into reverse repurchase and dollar roll repurchase agreements whereby the Company agreed to sell and repurchase securities. These activities have been accounted for as financing transactions, with the assets and associated liabilities included in the consolidated balance sheets. Short-term borrowings under such agreements averaged $33.9 million and $17.4 million during 2006 and 2005, respectively, at weighted average interest rates of 4.53% and 2.25%, respectively. There was no outstanding balance as of December 31, 2006. The outstanding balance totaled $300.0 million at December 31, 2005 and was included in other liabilities. Interest paid totaled $1.5 million, $0.4 million and $0.2 million in 2006, 2005 and 2004, respectively. The highest level of short-term borrowings at any month end was $230.0 million in 2006 and $300.0 million in 2005.

12. Reinsurance

The Company assumes and cedes reinsurance from and to other insurance companies in order to limit losses from large exposures; however, if the reinsurer is unable to meet its obligations, the originating issuer of the coverage retains the liability. The maximum amount of life insurance risk retained by the Company on any one life is generally $2.0 million. Amounts not retained are ceded to other companies on a yearly renewable-term or a coinsurance basis.

In connection with the purchase of Life of Georgia, Jackson acquired certain lines of business that were wholly ceded to non-affiliates. These include both direct and assumed accident and health business, direct and assumed life insurance business, and certain institutional annuities.

With the approval of the Michigan Commissioner of Insurance, Jackson cedes the guaranteed minimum death benefit coverage associated with certain variable annuities issued prior to 2002 to an affiliate, Prudential Atlantic Reinsurance Company, Dublin, Ireland ("PARC"). PARC is a wholly owned subsidiary of Prudential. The income statement impact of the treaty is negligible, as the reinsurance premium, net of claims, approximates the change in the GMDB reserve.

The effect of reinsurance on premiums was as follows (in thousands):

	Years ended December 31,		
	2006	**2005**	**2004**
Direct premiums:			
Life	$ 361,016	$ 347,831	$ 314,168
Accident and health	22,297	14,855	-
Plus reinsurance assumed:			
Life	3,984	12,629	6
Accident and health	2,113	1,232	-
Less reinsurance ceded:			
Life	(134,251)	(134,258)	(126,778)
Accident and health	(24,410)	(16,087)	-
Guaranteed annuity benefits	(34,548)	(27,141)	(25,054)
Total net premiums	$ 196,201	$ 199,061	$ 162,342

Premiums ceded for guaranteed annuity benefits included $24.5 million, $19.4 million and $20.2 million premiums ceded to PARC during 2006, 2005 and 2004, respectively.

12. Reinsurance (continued)

Components of the reinsurance recoverable asset were as follows (in thousands):

	December 31, 2006	December 31, 2005
Reserves:		
Life	$ 735,904	$ 681,765
Accident and health	32,560	39,047
Guaranteed annuity benefits	70,675	171,310
Claims liability	37,997	41,254
Other	9,831	10,362
Total	$ 886,967	$ 943,738

Reserves reinsured through Brooke Life were $56.8 million and $59.4 million at December 31, 2006 and 2005, respectively. Reserves reinsured through PARC were $54.7 million and $36.3 million at December 31, 2006 and 2005, respectively.

13. Federal Income Taxes

The components of the provision for federal income taxes were as follows (in thousands):

	Years ended December 31,		
	2006	2005	2004
Current tax expense	$ 240,858	$ 174,180	$ 87,196
Deferred tax expense	22,558	141,115	216,880
Federal income tax expense	$ 263,416	$ 315,295	$ 304,076

Federal income tax expense reported for discontinued operations totaled $40.6 million in 2004.

The federal income tax provisions differ from the amounts determined by multiplying pretax income by the statutory federal income tax rate of 35% for 2006, 2005 and 2004 as follows (in thousands):

	Years ended December 31,		
	2006	2005	2004
Income taxes at statutory rate	$ 278,612	$ 318,279	$ 304,123
Dividends received deduction	(15,156)	(3,437)	-
Other	(40)	452	(47)
Provision for federal income taxes	$ 263,416	$ 315,294	$ 304,076
Effective tax rate	33.1%	34.7%	35.0%

Federal income taxes paid were $214.0 million, $165.1 million and $105.5 million in 2006, 2005 and 2004, respectively.

13. Federal Income Taxes (continued)

The tax effects of significant temporary differences that give rise to deferred tax assets and liabilities were as follows (in thousands):

	December 31, 2006	December 31, 2005
Gross deferred tax asset		
Difference between financial reporting and the tax basis of:		
Policy reserves and other insurance items	$ 860,143	$ 745,761
Investments	138,758	163,076
Deferred compensation	56,866	47,550
Other, net	48,543	48,715
Total gross deferred tax asset	1,104,310	1,005,102
Gross deferred tax liability		
Difference between financial reporting and the tax basis of:		
Deferred acquisition costs and sales inducements	(976,968)	(786,538)
Value of the insurance in-force	-	(8,252)
Other assets	(3,354)	(24,469)
Net unrealized gains on available for sale securities	(80,579)	(218,250)
Other, net	(27,249)	(8,176)
Total gross deferred tax liability	(1,088,150)	(1,045,685)
Net deferred tax asset (liability)	$ 16,160	$ (40,583)

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the gross deferred tax asset.

At December 31, 2006, the Company had no federal tax capital loss carryforwards available for future use.

14. Commitments and Contingencies

The Company and its subsidiaries are involved in litigation arising in the ordinary course of business. It is the opinion of management that the ultimate disposition of such litigation will not have a material adverse affect on the Company's financial condition or results of operations. Jackson has been named in civil litigation proceedings which appear to be substantially similar to other class action litigation brought against many life insurers alleging misconduct in the sale of insurance products. The Company accrues for legal contingencies once the contingency is deemed to be probable and estimable. Accordingly, at December 31, 2006 and 2005, Jackson had recorded accruals totaling $11.0 million and $7.1 million, respectively. Additionally, in connection with the purchase of Life of Georgia, Jackson assumed a $9.4 million liability related to a class action lawsuit. This liability has been fully indemnified by ING Groep, N.V. and an indemnification receivable of $9.4 million has been included in other assets.

State guaranty funds provide payments for policyholders of insolvent life insurance companies. These guaranty funds are financed by assessments to solvent insurance companies based on location, volume and types of business. The Company estimated its reserve for future state guaranty fund assessments based on data received from the National Organization of Life and Health Insurance Guaranty Associations. Based on data received at the end of 2006 and 2005, the Company’s reserve for future state guaranty fund assessments was $18.0 million and $19.3 million, respectively. The Company believes the reserve is adequate for all anticipated payments for known insolvencies.

14. Commitments and Contingencies (continued)

The Company had unfunded commitments related to its investments in limited partnerships totaling $339.7 million and $389.1 million at December 31, 2006 and 2005, respectively.

The Company leases office space, land and equipment under several operating leases that expire at various dates through 2051. Certain leases include escalating lease rates, lease abatements and other incentives and, as a result, at December 31, 2006, Jackson recorded a liability of $2.0 million for future lease payments. Lease expense was $23.0 million, $28.5 million and $27.9 million in 2006, 2005 and 2004, respectively. Future minimum payments under these noncancellable operating leases are as follows (in thousands):

2007	$ 7,124
2008	6,980
2009	4,172
2010	3,408
2011	3,400
Thereafter	28,167
Total	$ 53,251

Jackson subleased office space under several operating leases that expire at various dates through 2008. Total future lease income to be received on the subleased property is $1.5 million. Lease income for the subleased property totaled $0.7 million per year in 2006, 2005 and 2004.

15. Stockholder's Equity

Under Michigan Insurance Law, dividends on capital stock can only be distributed out of earned surplus, unless the Commissioner approves the dividend prior to payment. Furthermore, without the prior approval of the Commissioner, dividends cannot be distributed if all dividends made within the preceding 12 months exceed the greater of statutory net income less realized gains or 10% of the Company's statutory surplus for the prior year. In 2007, the maximum amount of dividends that can be paid by the Company without prior approval of the Commissioner under this limitation approximates $412.3 million.

The Company received capital contributions from its parent of $49.7 million, $292.3 million and $28.7 million in 2006, 2005 and 2004, respectively. Contributions received in 2006 included the transfer of $6.9 million in net assets of an affiliate. Contributions received in 2005 included common stock of $260.7 million in Life of Georgia. The capital contributions also included $29.1 million, $31.6 million and $28.7 million in 2006, 2005 and 2004, respectively, from Brooke Life's forgiveness of an intercompany tax liability. Dividend payments were $209.1 million, $410.8 million and $120.0 million in 2006, 2005 and 2004, respectively. Dividends paid in 2005 include $260.8 million paid to Brooke Life to fund the purchase of Life of Georgia.

Statutory capital and surplus of the Company, as reported in its Annual Statement, was $3.7 billion and $3.4 billion at December 31, 2006 and 2005, respectively. Statutory net income of the Company, as reported in its Annual Statement, was $412.3 million, $565.1 million and $624.5 million in 2006, 2005 and 2004, respectively. Statutory net income included pre-acquisition Life of Georgia net income of $112.1 million and $8.2 million in 2005 and 2004, respectively, in accordance with statutory guidelines.

16. Other Related Party Transactions

The Company's investment portfolio is managed by PPM America, Inc. (“PPMA”), a registered investment advisor, and PPM Finance, Inc. (collectively, “PPM”). PPM is ultimately a wholly owned subsidiary of Prudential. The Company paid $35.9 million, $35.6 million and $33.2 million to PPM for investment advisory services during 2006, 2005 and 2004, respectively.

In 2006, Jackson issued $125.6 million in loans to an affiliate, Brooke Holdings, LLC. The loans were unsecured and were repaid in full during the year. Interest on these loans (ranging from 4.60% per annum to 5.50% per annum) totaled $4.3 million during 2006. In December 2006, Jackson issued an additional $16.0 million loan to Brooke Holdings, LLC. This loan is also unsecured and matures December 31, 2007. Interest on this loan, at a rate of 5.00% per annum, totaled $38 thousand in 2006.

Also in 2006, Jackson issued a $5.0 million loan to an affiliate, Brooke GP. The loan was unsecured and repaid in September 2006. Interest on this loan, at a rate of 5.44% per annum, totaled $39 thousand in 2006.

In 2004, Jackson issued $13.0 million in loans to Brooke Holdings, Inc. The loans were unsecured and were repaid in 2005. Interest on these loans (at a rate of 2.75% per annum in 2005 and 1.75% per annum in 2004) totaled $309.7 thousand and $223.6 thousand in 2005 and 2004, respectively.

Included in notes payable is debt in the amount of $1.5 million and $3.5 million payable to affiliates PPM Holdings, Inc. (“PPMH”) and PPMA at December 31, 2006 and 2005, respectively. Interest accrued on this debt, including contingent interest, of $5.0 million and $15.2 million is included in other liabilities at December 31, 2006 and 2005, respectively. Outstanding principal amounts accrued interest at a weighted average interest rate of 7.12% and 8.31% at December 31, 2006 and 2005, respectively. Interest paid to PPMH and PPMA totaled $8.0 million and $266 thousand in 2006 and 2005, respectively.

Jackson has entered into shared services administrative agreements with affiliates PPMA and National Planning Holdings, Inc. (“NPH”). Under the shared services administrative agreements, Jackson allocated $5.2 million, $5.0 million and $6.3 million of certain management and corporate services expenses to affiliates in 2006, 2005 and 2004, respectively.

Jackson provides a $40.0 million revolving credit facility to PPMA. The loan is unsecured, matures on September 9, 2008, accrues interest at LIBOR plus 2% per annum, and has a commitment fee of 0.25% per annum. There was no balance outstanding at December 31, 2006 or 2005. The highest outstanding loan balance during 2006 and 2005 was $11.5 million and $20.0 million, respectively. Interest and commitment fees totaled $175 thousand, $306 thousand and $124 thousand during 2006, 2005 and 2004, respectively.

In 2003, Jackson provided a $20.0 million revolving credit facility to Investment Centers of America, Inc., a wholly owned subsidiary of NPH. The loan was unsecured and was scheduled to mature on November 14, 2008, accruing interest at LIBOR plus 2% per annum with a commitment fee of 0.10% per annum. There was no balance outstanding at December 31, 2005. The highest outstanding loan balance during 2005 was $14.2 million. Interest and commitment fees totaled $10 thousand, $52 thousand and $24 thousand in 2006, 2005 and 2004, respectively. No borrowings were made against this credit facility during 2006 and the facility was terminated in July 2006.

17. Benefit Plans

The Company has a defined contribution retirement plan covering substantially all employees. To be eligible to participate in the Company's contribution, an employee must have attained the age of 21, have completed at least 1,000 hours of service in a 12-month period and passed their 12-month employment anniversary. In addition, the employee must be employed on the applicable January 1 or July 1 entry date. The Company's annual contributions, as declared by the board of directors, are based on a percentage of eligible compensation paid to participating employees during the year. In addition, the Company matches up to 6 percent of a participant's elective contribution to the plan during the year. The Company's expense related to this plan was $8.9 million, $7.2 million and $7.8 million in 2006, 2005 and 2004, respectively.

The Company maintains non-qualified voluntary deferred compensation plans for certain agents and employees. At December 31, 2006 and 2005, the liability for such plans totaled $162.4 million and $135.9 million, respectively. Jackson invests general account assets in selected mutual funds in amounts similar to participant elections as a hedge against significant movement in the payout liability. The Company's expense related to these plans, including a match of elective deferrals for the agents' deferred compensation plan, was $21.5 million, $18.6 million and $20.7 million in 2006, 2005 and 2004, respectively.