



Jackson National Life Insurance
Company and Subsidiaries

Consolidated Financial Statements
December 31, 2017 and 2016



Jackson National Life Insurance Company and Subsidiaries

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KPMG LLP
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Report of Independent Registered Public Accounting Firm

The stockholders and board of directors
Jackson National Life Insurance Company and Subsidiaries:

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Jackson National Life Insurance Company and Subsidiaries (the Company) as of December 31, 2017 and 2016, the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the years in the three-year period ended December 31, 2017, and the related notes (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2017, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

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 are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

KPMG LLP

We have served as the Company's auditor since 1999.

Columbus, Ohio
March 8, 2018

Jackson National Life Insurance Company and Subsidiaries
Consolidated Balance Sheets
(In thousands, except per share information)

	December 31,	
Assets	2017	2016
Investments:		
Securities available for sale, at fair value:		
Fixed maturities (amortized cost: 2017, \$45,867,015; 2016, \$49,163,580, including \$115,997 and \$138,598 at fair value under the fair value option at December 31, 2017 and 2016, respectively)	\$ 47,457,154	\$ 49,938,751
Trading securities, at fair value	137,756	415,122
Commercial mortgage loans, net of allowance	8,435,440	7,482,233
Policy loans (includes \$3,397,764 and \$3,301,038 at fair value under the fair value option at December 31, 2017 and 2016, respectively)	4,591,132	4,546,161
Derivative instruments	2,178,969	1,030,133
Other invested assets (includes \$1,141,123 and \$1,219,887 at fair value under the fair value option at December 31, 2017 and 2016, respectively)	1,369,895	1,455,449
Total investments	64,170,346	64,867,849
Cash and cash equivalents	1,617,934	1,265,041
Accrued investment income	595,370	673,144
Deferred acquisition costs	10,540,588	9,678,063
Reinsurance recoverable	8,702,090	8,927,559
Deferred income taxes, net	484,224	1,226,465
Receivables from affiliates	312,049	344,100
Other assets	1,467,163	1,173,468
Separate account assets	176,578,848	148,791,796
Total assets	\$ 264,468,612	\$ 236,947,485
Liabilities and Equity		
Liabilities		
Reserves for future policy benefits and claims payable	\$ 12,714,534	\$ 13,467,949
Other contract holder funds	60,742,599	60,864,343
Funds held under reinsurance treaties, at fair value under the fair value option	3,604,525	3,523,106
Debt	647,718	685,949
Securities lending payable	69,785	119,608
Derivative instruments	6,448	78,802
Other liabilities	3,165,252	2,783,473
Separate account liabilities	176,578,848	148,791,796
Total liabilities	257,529,709	230,315,026
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	3,816,079	3,816,079
Shares held in trust	(18,851)	(22,686)
Equity compensation reserve	10,249	5,785
Accumulated other comprehensive income, net of tax expense (benefit)		
of \$140,872 in 2017 and \$(75,888) in 2016	1,092,974	597,122
Retained earnings	2,024,652	2,222,359
Total stockholder's equity	6,938,903	6,632,459
Total liabilities and equity	\$ 264,468,612	\$ 236,947,485

See accompanying Notes to Consolidated Financial Statements.

Jackson National Life Insurance Company and Subsidiaries
Consolidated Income Statements
(In thousands)

	Years Ended December 31,		
	2017	2016	2015
Revenues			
Fee income	\$ 5,734,935	\$ 5,151,117	\$ 4,981,941
Premium	169,079	229,611	266,409
Net investment income	2,654,542	2,914,947	2,939,362
Net realized losses on investments:			
Total other-than-temporary impairments	(3,070)	(68,511)	(77,662)
Portion of other-than-temporary impairments included in other comprehensive income	18	9,562	15,024
Net other-than-temporary impairments	(3,052)	(58,949)	(62,638)
Other net investment losses	(3,424,277)	(3,600,152)	(1,524,877)
Total net realized losses on investments	(3,427,329)	(3,659,101)	(1,587,515)
Other income	68,395	70,786	97,945
Total revenues	<u>5,199,622</u>	<u>4,707,360</u>	<u>6,698,142</u>
Benefits and Expenses			
Death, other policy benefits and change in policy reserves, net of deferrals	1,128,340	1,000,280	997,746
Interest credited on other contract holder funds, net of deferrals	1,547,561	1,558,400	1,516,522
Interest expense	54,342	41,589	38,104
Operating costs and other expenses, net of deferrals	1,817,455	1,601,004	1,724,590
Amortization of deferred acquisition and sales inducement costs	(58,231)	(159,852)	660,860
Total benefits and expenses	<u>4,489,467</u>	<u>4,041,421</u>	<u>4,937,822</u>
Pretax income before noncontrolling interests	710,155	665,939	1,760,320
Income tax expense (benefit)	307,375	(106,500)	346,339
Net income	<u>402,780</u>	<u>772,439</u>	<u>1,413,981</u>
Less: Net income attributable to noncontrolling interests	-	-	13,101
Net income attributable to Jackson	<u>\$ 402,780</u>	<u>\$ 772,439</u>	<u>\$ 1,400,880</u>

See accompanying Notes to Consolidated Financial Statements.

Jackson National Life Insurance Company and Subsidiaries
Consolidated Statements of Comprehensive Income
(In thousands)

	Years Ended December 31,		
	2017	2016	2015
Net income	\$ 402,780	\$ 772,439	\$ 1,413,981
Other comprehensive income, net of tax:			
Net unrealized gains (losses) on securities not other-than-temporarily impaired (net of tax expense (benefit) of: 2017 \$168,816; 2016 \$40,243; 2015 \$(447,191))	406,815	74,735	(846,010)
Net unrealized losses on other-than-temporarily impaired securities (net of tax benefit of: 2017 \$4; 2016 \$3,080; 2015 \$4,469)	(8)	(5,719)	(8,299)
Reclassification adjustment for gains (losses) included in net income (net of tax expense (benefit) of: 2017 \$47,948; 2016 \$(10,959); 2015 \$(49,168))	89,045	(20,352)	(91,310)
Total other comprehensive income (loss)	<u>495,852</u>	<u>48,664</u>	<u>(945,619)</u>
Comprehensive income	898,632	821,103	468,362
Less: Comprehensive loss attributable to noncontrolling interests	-	-	(2,411)
Comprehensive income attributable to Jackson	<u>\$ 898,632</u>	<u>\$ 821,103</u>	<u>\$ 470,773</u>

See accompanying Notes to Consolidated Financial Statements.

Jackson National Life Insurance Company and Subsidiaries
Consolidated Statements of Equity
(In thousands)

	Common Stock	Additional Paid-In Capital	Shares Held In Trust	Equity Compensation Reserve	Accumulated Other Comprehensive Income	Retained Earnings	Total Stockholder's Equity	Non- Controlling Interests	Total Equity
Balances as of December 31, 2014	\$ 13,800	\$ 3,816,079	\$ (27,084)	\$ 14,130	\$ 1,478,565	\$ 1,311,175	\$ 6,606,665	\$ 34,971	\$ 6,641,636
Net income	-	-	-	-	-	1,400,880	1,400,880	13,101	1,413,981
Change in unrealized investment gains and losses, net of tax	-	-	-	-	(930,107)	-	(930,107)	(15,512)	(945,619)
Dividends to stockholder	-	-	-	-	-	(711,413)	(711,413)	-	(711,413)
Shares acquired at cost	-	-	(19,438)	-	-	-	(19,438)	-	(19,438)
Shares distributed at cost	-	-	14,584	-	-	-	14,584	-	14,584
Reserve for equity compensation plans	-	-	-	4,187	-	-	4,187	-	4,187
Fair value of shares issued under equity compensation plans	-	-	-	(15,054)	-	-	(15,054)	-	(15,054)
Balances as of December 31, 2015	<u>13,800</u>	<u>3,816,079</u>	<u>(31,938)</u>	<u>3,263</u>	<u>548,458</u>	<u>2,000,642</u>	<u>6,350,304</u>	<u>32,560</u>	<u>6,382,864</u>
Net income	-	-	-	-	-	772,439	772,439	-	772,439
Change in unrealized investment gains and losses, net of tax	-	-	-	-	48,664	-	48,664	-	48,664
Deconsolidation of variable interest entities	-	-	-	-	-	-	-	(32,560)	(32,560)
Dividends to stockholder	-	-	-	-	-	(550,722)	(550,722)	-	(550,722)
Shares acquired at cost	-	-	(2,272)	-	-	-	(2,272)	-	(2,272)
Shares distributed at cost	-	-	11,524	-	-	-	11,524	-	11,524
Reserve for equity compensation plans	-	-	-	2,522	-	-	2,522	-	2,522
Balances as of December 31, 2016	<u>13,800</u>	<u>3,816,079</u>	<u>(22,686)</u>	<u>5,785</u>	<u>597,122</u>	<u>2,222,359</u>	<u>6,632,459</u>	<u>-</u>	<u>6,632,459</u>
Net income	-	-	-	-	-	402,780	402,780	-	402,780
Change in unrealized investment gains and losses, net of tax	-	-	-	-	495,852	-	495,852	-	495,852
Dividends to stockholder	-	-	-	-	-	(600,487)	(600,487)	-	(600,487)
Shares acquired at cost	-	-	(2,392)	-	-	-	(2,392)	-	(2,392)
Shares distributed at cost	-	-	6,227	-	-	-	6,227	-	6,227
Reserve for equity compensation plans	-	-	-	4,464	-	-	4,464	-	4,464
Balances as of December 31, 2017	<u>\$ 13,800</u>	<u>\$ 3,816,079</u>	<u>\$ (18,851)</u>	<u>\$ 10,249</u>	<u>\$ 1,092,974</u>	<u>\$ 2,024,652</u>	<u>\$ 6,938,903</u>	<u>\$ -</u>	<u>\$ 6,938,903</u>

See accompanying Notes to Consolidated Financial Statements.

Jackson National Life Insurance Company and Subsidiaries
Consolidated Statements of Cash Flows
(In thousands)

	Years Ended December 31,		
	2017	2016	2015
Cash flows from operating activities:			
Net income	\$ 402,780	\$ 772,439	\$ 1,413,981
Adjustments to reconcile net income to net cash provided by operating activities:			
Net realized losses (gains) on investments	50,663	(349,204)	(34,191)
Net losses on derivatives	3,130,445	3,713,938	1,339,369
Interest credited on other contract holder funds, gross	1,558,057	1,570,709	1,529,137
Mortality, expense and surrender charges	(671,593)	(704,343)	(730,782)
Amortization of discount and premium on investments	16,539	28,037	39,713
Deferred income tax expense (benefit)	525,481	(771,586)	33,701
Share-based compensation	70,810	30,012	50,083
Change in:			
Accrued investment income	77,774	12,655	1,704
Deferred sales inducements and acquisition costs	(912,250)	(1,083,309)	(465,937)
Trading portfolio activity, net	281,664	(129,968)	245,264
Income tax accruals	(204,405)	330,807	(452,016)
Other assets and liabilities, net	705,115	(570,959)	295,502
Net cash provided by operating activities	5,031,080	2,849,228	3,265,528
Cash flows from investing activities:			
Sales, maturities and repayments of:			
Fixed maturities	9,771,562	11,005,017	7,941,581
Commercial mortgage loans	1,401,641	1,151,212	1,159,080
Purchases of:			
Fixed maturities	(6,546,920)	(10,841,032)	(8,720,419)
Commercial mortgage loans	(2,358,647)	(2,196,376)	(1,596,503)
Other investing activities	(4,532,283)	(3,706,102)	(816,079)
Net cash used in investing activities	(2,264,647)	(4,587,281)	(2,032,340)
Cash flows from financing activities:			
Policyholders' account balances:			
Deposits	21,854,967	21,747,583	27,030,772
Withdrawals	(17,948,260)	(15,178,565)	(14,530,207)
Net transfers to separate accounts	(5,406,328)	(5,991,929)	(11,886,621)
Net (payments on) proceeds from repurchase agreements	(411,857)	411,857	(289,625)
Net proceeds from (payments on) Federal Home Loan Bank notes	99,999	500,000	(200,000)
Net (payments on) proceeds from debt	(5,896)	(5,039)	18,191
Shares held in trust at cost, net	3,835	9,252	(4,854)
Payment of cash dividends to Parent	(600,000)	(550,000)	(710,000)
Net cash (used in) provided by financing activities	(2,413,540)	943,159	(572,344)
Net increase (decrease) in cash and cash equivalents	352,893	(794,894)	660,844
Cash and cash equivalents, beginning of year	1,265,041	2,059,935	1,399,091
Cash and cash equivalents, end of year	\$ 1,617,934	\$ 1,265,041	\$ 2,059,935
Supplemental Cash Flow Information			
Income tax (received) paid	\$ (13,212)	\$ 335,000	\$ 766,000
Interest paid	\$ 21,237	\$ 20,816	\$ 20,943

See accompanying Notes to Consolidated Financial Statements.

Jackson National Life Insurance Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2017 and 2016

1. Business and Basis of Presentation

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 accounts, after the elimination of intercompany accounts and transactions, of the following:

- Life insurers: Jackson and its wholly owned subsidiaries Jackson National Life Insurance Company of New York (“JNY”), Squire Reassurance Company LLC (“Squire Re”), Squire Reassurance Company II, Inc. (“Squire Re II”), VFL International Life Company SPC, LTD and Jackson National Life (Bermuda) LTD;
- Wholly owned broker-dealer, investment management and investment advisor subsidiaries: Jackson National Life Distributors, LLC, Jackson National Asset Management, LLC, Curian Clearing, LLC (“Curian Clearing”), and Curian Capital, LLC (“Curian Capital”);
- PGDS (US One) LLC (“PGDS”), a wholly owned subsidiary that provides information technology services to Jackson and certain affiliates;
- Other insignificant wholly owned subsidiaries; and
- Other insignificant partnerships, limited liability companies and variable interest entities (“VIEs”) in which Jackson is deemed the primary beneficiary.

In 2015, Jackson announced that Curian Capital would no longer accept new business effective July 31, 2015. Curian Capital continued to actively manage existing accounts into early 2016 to accommodate financial professionals and clients in their transition. The Curian Capital separately managed account program terminated on February 19, 2016 and Curian Capital de-registered as a Securities and Exchange Commission (“SEC”) regulated investment advisor in October 2016. Curian Clearing, which had served exclusively as the clearing broker-dealer for the Curian Capital separately managed account program, de-registered as a SEC regulated broker-dealer on September 13, 2017.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”). Intercompany accounts and transactions have been eliminated upon consolidation. Certain amounts in the 2016 notes to the consolidated financial statements have been reclassified to conform to the 2017 presentation.

The preparation of the consolidated financial statements in conformity with GAAP requires the use of estimates and assumptions about future events that affect the amounts reported in the consolidated financial statements and the accompanying notes. Significant estimates or assumptions, as further discussed in the notes, include: 1) valuation of investments and derivative instruments, including fair values of securities deemed to be in an illiquid market and the determination of when an impairment is other-than-temporary; 2) assessments as to whether certain entities are variable interest entities, the existence of reconsideration events and the determination of which party, if any, should consolidate the entity; 3) assumptions impacting estimated future gross profits, including but not limited to, policyholder behavior, 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 but not limited to, policyholder behavior, mortality rates, expenses, investment returns and policy crediting rates; 5) assumptions as to future earnings levels being sufficient to realize deferred tax benefits; 6) estimates related to establishment of loan loss reserves, allowances on receivables, liabilities for lawsuits and state guaranty fund assessments; 7) assumptions and estimates associated with the Company’s tax positions which impact the amount of recognized tax benefits recorded by the Company; 8) value of guaranteed benefits; and 9) value of business acquired, its recoverability and amortization. These estimates and assumptions are based on management’s best estimates and judgments. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors deemed appropriate. As facts and circumstances dictate, these estimates and assumptions may be adjusted. Since future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in estimates, including those resulting from continuing changes in the economic environment, will be reflected in the consolidated financial statements in the periods the estimates are changed.

Jackson National Life Insurance Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2017 and 2016

2. Summary of Significant Accounting Policies

Changes in Accounting Principles – Adopted in Current Year

In October 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Updates (“ASU”) No. 2016-17, “Consolidation: Interests held through Related Parties that are under Common Control.” Under ASU No. 2016-17, if a decision maker is required to evaluate whether it is the primary beneficiary of a VIE, it will need to consider only its proportionate indirect interest in the VIE held through a common control party. The previous guidance directed the decision maker to treat the common control party’s interest in the VIE as if the decision maker held the interest itself. Effective January 1, 2017, the Company adopted ASU No. 2016-17 with no material impact on the Company’s consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation – Stock Compensation: Improvements to Employee Share-Based Payment Accounting,” which simplifies employee share-based payment accounting. These amendments require all income tax effects of awards to be recognized in the income statement when the awards vest or are settled rather than through additional paid-in capital. The amendments also permit an employer to repurchase an employee’s shares at the maximum statutory tax rate in the employee’s applicable jurisdiction for tax withholding purposes without triggering liability accounting. In addition, the amendments permit entities to make a one-time accounting policy election to account for forfeitures as they occur. Effective January 1, 2017, the Company adopted ASU No. 2016-09 prospectively with no material impact on the Company’s consolidated financial statements.

In January 2015, the FASB issued ASU No. 2015-01, “Extraordinary and Unusual Items: Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items,” which eliminates the concept of extraordinary items. Effective January 1, 2017, the Company adopted ASU No. 2015-01 with no impact on the Company’s consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, “Presentation of Financial Statements – Going Concern,” which defines management’s responsibility to evaluate whether there is substantial doubt about the organization’s ability to continue as a going concern and to provide related disclosures in the footnotes. Management is required to evaluate for each annual period whether it is probable that the entity will not be able to meet its obligations as they become due within one year after the date that financial statements are issued, or available to be issued. Effective January 1, 2017, the Company adopted ASU No. 2014-15 with no impact on the Company’s consolidated financial statements.

Changes in Accounting Principles – Issued but Not Yet Adopted

In February 2018, the FASB issued ASU No. 2018-02, “Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,” which provides an option to reclassify stranded tax effects within accumulated other comprehensive income (“AOCI”) to retained earnings in each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act (the “Tax Act”) is recorded. ASU No. 2018-02 is effective for fiscal years beginning after December 15, 2018, and should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the Tax Act is recognized. Early adoption is permitted. The Company expects to adopt ASU No. 2018-02 effective January 1, 2018, which will result in the retrospective reclassification of \$141.0 million of stranded tax effects from AOCI to retained earnings within the Company’s consolidated financial statements and disclosures.

In August 2017, the FASB issued ASU No. 2017-12, “Derivatives and Hedging – Targeted Improvements to Accounting for Hedging Activities,” which changes the recognition and presentation requirements of hedge accounting. ASU No. 2017-12 is effective for annual periods beginning after December 15, 2018. Early adoption is permitted. The adoption of ASU No. 2017-12 is not expected to have an impact on the Company’s consolidated financial statements, as the Company does not intend to elect hedge accounting.

In March 2017, the FASB issued ASU No. 2017-08, “Receivables – Nonrefundable Fees and Other Costs: Premium Amortization on Purchased Callable Debt Securities,” which requires that certain premiums on callable debt securities be amortized to the earliest call date. ASU No. 2017-08 is effective for annual periods beginning after December 15, 2018. Early adoption is permitted. The adoption of ASU No. 2017-08 is not expected to have a material impact on the Company’s consolidated financial statements.

Jackson National Life Insurance Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2017 and 2016

In November 2016, the FASB issued ASU No. 2016-18, “Statement of Cash Flows – Restricted Cash,” which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU No. 2016-18 is effective for annual periods beginning after December 15, 2018, and should be applied retrospectively for all periods presented. Early adoption is permitted. The adoption of ASU No. 2016-18 is not expected to have a material impact on the Company’s consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows – Classification of Certain Cash Receipts and Cash Payments,” which clarifies the classification of eight specific cash flow issues in an entity’s statement of cash flows where it was determined there is diversity in practice. ASU No. 2016-15 is effective for annual periods beginning after December 15, 2018, and should be applied retrospectively for all periods presented. Early adoption is permitted. The adoption of ASU No. 2016-15 is not expected to have a material impact on the Company’s consolidated financial statements, as the requirements are presentational only within the statement of cash flows.

In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments,” which provides a new current expected credit loss model to account for credit losses on certain financial assets and off-balance sheet exposures. The model requires an entity to estimate lifetime credit losses related to such financial assets and exposures based on relevant information about past events, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The guidance also modifies the current other-than-temporary impairment guidance for available-for-sale debt securities to require the use of an allowance rather than a direct write down of the investment, and replaces existing guidance for purchased credit deteriorated loans and debt securities. ASU No. 2016-13 is effective for annual reporting periods beginning after December 15, 2020. Early adoption is permitted for annual periods beginning after December 15, 2018. The Company is currently assessing the impact of the guidance on the Company’s consolidated financial statements and disclosures.

In February 2016, the FASB issued ASU No. 2016-02, “Leases,” which establishes a new accounting model for leases. Lessees will recognize most leases on the balance sheet as a right-of-use asset and a related lease liability. The lease liability is measured as the present value of the lease payments over the lease term with the right-of-use asset measured at the lease liability amount and includes adjustments for certain lease incentives and initial direct costs. Lease expense recognition will continue to differentiate between finance leases and operating leases resulting in a similar pattern of lease expense recognition as under current guidance. ASU No. 2016-02 is effective for annual periods beginning after December 15, 2018, and a modified retrospective transition approach is required for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the consolidated financial statements. Early adoption is permitted. The Company is currently assessing the impact of the guidance on the Company’s consolidated financial statements and disclosures.

In January 2016, the FASB issued ASU No. 2016-01, “Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities,” which revises an entity’s accounting related to the classification and measurement of certain equity investments and the presentation of certain fair value changes for financial liabilities measured at fair value. The guidance also amends certain disclosure requirements associated with the fair value of financial instruments. ASU No. 2016-01 is effective for annual periods beginning after December 15, 2017, and should be adopted in the financial statements through a cumulative effect adjustment to the beginning balance of retained earnings. Early adoption is generally not permitted, except as defined in the ASU. The adoption of ASU No. 2016-01 will not have a material impact on the Company’s consolidated financial statements and disclosures.

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers,” which specifies the accounting treatment for all revenue arising from contracts with customers, and creates a new Topic 606 in the FASB Accounting Standards Codification. This standard, together with subsequent amendments to Topic 606, establishes the core principle of recognizing revenue to depict the transfer of promised goods or services in an amount that reflects the consideration the entity expects to be entitled in exchange for those goods or services. The FASB defines a five-step process which systematically identifies the various components of the revenue recognition process, culminating with the recognition of revenue upon satisfaction of an entity’s performance obligation. The guidance also requires additional disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from cost incurred to obtain or fulfill a contract. This guidance does not apply to contracts within the scope of Accounting Standards Codification Topic 944, “Financial Services – Insurance.” ASU No. 2014-09 is effective retrospectively for periods beginning after December 15,

Jackson National Life Insurance Company and Subsidiaries
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2017. For those revenue streams within the scope of this Standard, there is no change to the timing of revenue recognition and, therefore, there is no impact on the Company's financial statements. Upon adoption, the Company will include the required additional disclosures, where applicable.

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 available for sale securities.

Investments

Fixed maturities consist primarily of bonds, notes, and asset-backed securities. Acquisition discounts and premiums on fixed maturities are amortized into investment income through call or maturity dates using the effective interest method. Discounts and premiums on asset-backed securities are amortized over the estimated redemption period. Certain asset-backed securities 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. For these securities, 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 \$365.7 million and \$415.4 million as of December 31, 2017 and 2016, respectively.

Fixed maturities are generally classified as available for sale and are carried at fair value. For declines in fair value considered to be other-than-temporary, an impairment charge reflecting the difference between the amortized cost basis and fair value is included in net realized losses on investments. If management believes the Company does not intend to sell the security and is not more likely than not to be required to sell the security prior to recovery of its amortized cost basis, an amount representing the non-credit related portion of a loss is reclassified out of net realized losses on investments and into other comprehensive income. In determining whether an other-than-temporary impairment has occurred, and in calculating the non-credit related component of the total impairment loss, the Company considers a number of factors, which are further described in Note 3.

Equity securities are classified as trading. Trading securities are carried at fair value with changes in value included in net investment income.

Commercial mortgage loans are carried at the aggregate unpaid principal balance, adjusted for any applicable unamortized discount or premium, impairments or allowance for loan losses.

On a periodic basis, the Company assesses the commercial mortgage loan portfolio for the need for an allowance for loan losses. In determining its allowance for loan losses, the Company evaluates each loan to determine if it is probable that amounts due according to the contractual terms of the loan agreement will not be collected. The allowance includes loan specific reserves for loans that are determined to be non-performing as a result of this loan review process and a portfolio reserve for probable incurred but not specifically identified losses for performing loans. The loan specific portion of the loss allowance is based on the Company's assessment as to ultimate collectability of loan principal and interest, or other value expected in lieu of loan principal and interest. This review contemplates a variety of factors which may include, but are not limited to, current economic conditions, the physical condition of the property, the financial condition of the borrower, and the near and long-term prospects for change in these conditions. In determining the portfolio reserve for incurred but not specifically identified losses, Jackson considers the current credit composition of the portfolio based on the results of its loan modeling analysis, which considers property type, default statistics, historical losses and other relevant factors to determine probability of default and other default loss estimates. Model assumptions are updated each quarter and, based upon actual loan experience, are considered together with other relevant qualitative factors in making the final portfolio reserve calculations. The valuation allowance for commercial mortgage loans can increase or decrease from period to period based on these factors. Changes in the allowance for loan losses are recorded in net investment income.

Separately, the Company also reviews individual loans in the portfolio for impairment based on an assessment of the factors identified above. Impairment charges recognized are recorded initially against the established loan loss allowance and, if necessary, any additional amounts are recorded as realized losses. As deemed necessary based on cash flow expectations and other factors, Jackson may place loans on non-accrual status. In this case, all cash received is applied against the carrying value of the loan.

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Policy loans are loans the Company issues to contract holders that use the cash surrender value of their life insurance policy or annuity contract as collateral. The Company elected the fair value option upon acquisition of policy loans held as collateral for reinsurance, further described below. At December 31, 2017 and 2016, \$3.4 billion and \$3.3 billion, respectively, of these loans were carried at fair value, which the Company believes is equal to the unpaid principal balances plus accrued investment income. At both December 31, 2017 and 2016, the Company had \$1.2 billion of policy loans not held as collateral for reinsurance, which were carried at the unpaid principal balances.

Other invested assets primarily include investments in limited partnerships and real estate. The Company has elected the fair value option for limited partnerships, which is consistent with the role of these investments within the investment portfolio. Carrying values for limited partnership investments are determined by using the proportion of the Company's investment in each fund (Net Asset Value ("NAV") equivalent) as a practical expedient for fair value.

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

In 2015, the Company held interests in VIEs that represented primary beneficial interests. These consolidated VIEs were comprised of entities structured to hold and manage investments. Upon adoption of ASU No. 2015-02 in 2016, these VIEs were deconsolidated.

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 Company elected the fair value option for certain assets which are held as collateral for reinsurance, as further described below. Accordingly, the Company established a funds held liability, for which the Company also elected the fair value option. The value of the funds held liability is equal to the fair value of the assets held as collateral. The income and any changes in unrealized gains and losses on these assets and the corresponding funds held liability are included in net investment income and have no impact on the Company's consolidated income statements.

The changes in unrealized gains and losses on certain investments that are classified as available for sale and the non-credit related portion of other-than-temporary impairment charges are excluded from net income and included as a component of other comprehensive income and total equity, net of tax and the effect of the adjustment for deferred acquisition costs and deferred sales inducements. The changes in unrealized gains and losses on investments for which Jackson elected the fair value option are included in net investment income.

Derivative Instruments and Embedded Derivatives

The Company enters into financial derivative transactions, including, but not limited to, swaps, 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. There were no charges due to nonperformance by derivative counterparties in 2017, 2016, or 2015.

The Company generally uses freestanding derivative instruments for hedging purposes. Additionally, certain liabilities, primarily trust instruments supported by funding agreements, fixed index annuities and guarantees offered in connection with variable annuities issued by the Company, may contain embedded derivatives. Further details regarding Jackson's derivative positions are included in Note 4. The Company generally does not account for freestanding derivatives as either fair value or cash flow hedges as might be permitted if specific hedging documentation requirements 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 freestanding derivative instruments and embedded derivatives, including net payments, realized gains and losses and changes in value, are reported in net income, as further detailed in Note 4.

Cash and Cash Equivalents

Cash and cash equivalents primarily include money market instruments and bank deposits.

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Fair Value Measurement

Fair value measurements are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's view of market assumptions in the absence of observable market information. The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. All financial assets and liabilities measured at fair value are required to be classified into one of the following categories:

- Level 1 Observable inputs that reflect quoted prices for identical assets or liabilities in active markets that the Company has the ability to access at the measurement date. Level 1 securities include U.S. Treasury securities and exchange traded equity securities and derivative instruments.

- Level 2 Observable inputs, other than quoted prices included in Level 1, for the asset or liability or prices for similar assets and liabilities. Most fixed maturity securities that are model priced using observable inputs are classified within Level 2. Also included are freestanding and embedded derivative instruments that are priced using models with observable market inputs.

- Level 3 Valuations that are derived from techniques in which one or more of the significant inputs are unobservable (including assumptions about risk). Embedded derivatives that are valued using unobservable inputs are included in Level 3. Because Level 3 fair values, by their nature, contain unobservable market inputs, considerable judgment may be used to determine the Level 3 fair values. Level 3 fair values represent the Company's best estimate of an amount that could be realized in a current market exchange absent actual market exchanges.

In many situations, inputs used to measure the fair value of an asset or liability may fall into different levels of the fair value hierarchy. In these situations, the Company determines the level in which the fair value falls based upon the lowest level input that is significant to the determination of the fair value. As a result, both observable and unobservable inputs may be used in the determination of fair values that the Company has classified within Level 3.

The Company determines the fair values of certain financial assets and liabilities based on quoted market prices, where available. The Company may also determine fair value based on estimated future cash flows discounted at the appropriate current market rate. When appropriate, fair values reflect adjustments for counterparty credit quality, the Company's credit standing, liquidity and risk margins on unobservable inputs.

Where quoted market prices are not available, fair value estimates are made at a point in time, based on relevant market data, as well as the best information about the individual financial instrument. At times, illiquid market conditions may result in inactive markets for certain of the Company's financial instruments. In such instances, there may be no or limited observable market data for these assets and liabilities. Fair value estimates for financial instruments deemed to be in an illiquid market are based on judgments regarding current economic conditions, liquidity discounts, currency, credit and interest rate risks, loss experience and other factors. These fair values are estimates and involve considerable uncertainty and variability as a result of the inputs selected and may differ materially from the values that would have been used had an active market existed. As a result of market inactivity, such calculated fair value estimates may not be realizable in an immediate sale or settlement of the instrument. In addition, changes in the underlying assumptions used in the fair value measurement technique could significantly affect these fair value estimates.

Refer to Note 5 for further discussion of the methodologies used to determine fair values of the Company's financial instruments.

Deferred Acquisition Costs

Under current accounting guidance, certain costs that are directly related to the successful acquisition of new or renewal insurance business can be capitalized as deferred acquisition costs. These costs primarily pertain to commissions and certain costs associated with policy issuance and underwriting. All other acquisition costs are expensed as incurred.

Deferred acquisition costs are increased by interest thereon and amortized into income in proportion to anticipated premium revenues for traditional life policies and in proportion to estimated gross profits, including realized gains and losses and derivative movements, for annuities and interest-sensitive life products. Due to volatility of certain factors that affect gross profits, including realized capital gains and losses and derivative movements, amortization may be a benefit

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or a charge in any given period. In the event of negative amortization, the related deferred acquisition cost balance is capped at the initial amount capitalized, plus interest. Unamortized deferred acquisition costs are written off when a contract is internally replaced and substantially changed.

As certain fixed maturities 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. This adjustment, along with the change in net unrealized gains (losses) on fixed maturities available for sale, net of applicable tax, is credited or charged directly to equity as a component of other comprehensive income. At December 31, 2017 and 2016, deferred acquisition costs decreased by \$301.3 million and \$216.4 million, respectively, to reflect this adjustment.

For variable annuity business, the Company employs a mean reversion methodology that is applied with the objective of adjusting the amortization of deferred acquisition costs that would otherwise be highly volatile due to fluctuations in the level of future gross profits arising from changes in equity market levels. The mean reversion methodology achieves this objective by applying a dynamic adjustment to the assumption for short-term future investment returns. Under this methodology, the projected returns for the next five years are set such that, when combined with the actual returns for the current and preceding two years, the average rate of return over the eight-year period is 7.4% for both 2017 and 2016, after investment management fees. The mean reversion methodology does, however, include a cap and a floor of 15% and 0% per annum, respectively, on the projected return for each of the next five years. At December 31, 2017 and 2016, projected returns under mean reversion were within the range bound by the 15% cap and 0% floor. At December 31, 2017 and 2016, projected returns after the next five years were set at 7.4%.

Deferred acquisition costs are reviewed periodically to ensure that the unamortized portion does not exceed the expected recoverable amounts. Any amount deemed unrecoverable is written off with a charge through deferred acquisition costs amortization. No such write-offs were required for 2017, 2016, and 2015. During 2016, and 2015, certain amounts related to life products were adjusted, resulting in an additional \$20 million, and \$75 million, respectively, in deferred acquisition cost amortization.

Deferred Sales Inducements

Under current accounting guidance, certain sales inducement costs that are directly related to the successful acquisition of new or renewal insurance business can be capitalized as deferred sales inducement costs. Bonus interest on deferred fixed annuities and contract enhancements on fixed index annuities and variable annuities are capitalized as deferred sales inducements and included in other assets. Deferred sales inducements are increased by interest thereon and amortized into income in proportion to estimated gross profits, including realized capital gains and losses and derivative movements. Due to volatility of certain factors that affect gross profits, including realized capital gains and losses and derivative movements, amortization may be a benefit or a charge in any given period. In the event of negative amortization, the related deferred sales inducements balance is capped at the initial amount capitalized, plus interest. Unamortized deferred sales inducements are written off when a contract is internally replaced and substantially changed.

As certain fixed maturities 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. This adjustment, along with the change in net unrealized gains (losses) on fixed maturities available for sale, net of applicable tax, is credited or charged directly to equity as a component of other comprehensive income. At December 31, 2017 and 2016, deferred sales inducements decreased by \$55.0 million and \$37.5 million, respectively, to reflect this adjustment.

For variable annuity business, the Company employs the same mean reversion methodology as is employed for deferred acquisition costs as described above.

Deferred sales inducements are reviewed periodically to ensure that the unamortized portion does not exceed the expected recoverable amounts. Any amount deemed unrecoverable is written off with a charge through deferred sales inducements amortization. No such write-offs were required for 2017, 2016, and 2015.

Actuarial Assumption Changes (Unlocking)

Annually, or as circumstances warrant, the Company conducts a comprehensive review of the assumptions used for its estimates of future gross profits underlying the amortization of deferred acquisition costs and deferred sales inducements,

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as well as the valuation of the embedded derivatives and reserves for life insurance and annuity products with living benefit and death benefit guarantees. These assumptions include, but may not be limited to, policyholder behavior, mortality rates, expenses, investment returns and policy crediting rates. Based on this review, the cumulative balances of deferred acquisition costs, deferred sales inducements and life and annuity guaranteed benefit reserves are adjusted with a corresponding benefit or charge to net income. Additionally, in 2017, the Company implemented an enhancement to the method for incorporating own credit risk in the discounting of embedded derivative cash flows. The impact of the enhancement reduced reserves by \$558 million, net of deferred acquisition costs.

Reinsurance and Funds Held Under Reinsurance Treaties

The Company enters into assumed and ceded reinsurance agreements with other companies in the normal course of business. Ceded reinsurance agreements are reported on a gross basis on the Company's consolidated balance sheets as an asset for amounts recoverable from reinsurers or as a component of other assets or liabilities for amounts, such as premiums, owed to or due from reinsurers. Reinsurance assumed and ceded premiums and benefits paid or provided are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premium income and benefit expenses are reported net of reinsurance assumed and ceded.

The Company has three retrocession reinsurance agreements ("retro treaties") with Swiss Reinsurance Company Ltd. ("SRZ"). Pursuant to these retro treaties, the Company ceded to SRZ on a 100% coinsurance basis, subject to pre-existing reinsurance with other parties, certain blocks of business.

As a result of these retro treaties, the Company holds certain assets, primarily in the form of policy loans and fixed maturities, as collateral for the reinsurance recoverable. Investment income and realized gains or losses earned on assets held as collateral are paid by the Company to SRZ, pursuant to the terms of the treaties. Investment income and realized gains and losses are reported net of investment income and realized gains and losses on funds held under reinsurance treaties, with no net impact on the Company's consolidated income statements.

The income credited to SRZ on the funds held for the retro treaties is based on the income earned on those assets, which results in an embedded derivative (total return swap). However, the Company elected the fair value option for the funds held liability, which is carried at fair value with changes in fair value reported in net investment income. Accordingly, the embedded derivative is not bifurcated or separately valued.

Receivables from Affiliates

Effective December 30, 2016, the Company executed a reserve financing transaction, whereby, for statutory reporting, the risk on \$319.0 million of statutory basis redundant term life reserves was transferred to a third-party reinsurer. In conjunction with the transaction, Squire Re II financed the excess reserves through a surplus note (the "Squire Surplus Note") issued to an affiliate, Brier Capital LLC ("Brier"), in return for a note receivable from Brier (the "Financing Note"). Quarterly interest payments due under the Financing Note and the Squire Surplus Note are offset against each other and only the net amounts are due. The outstanding principal on the Financing Note and the Squire Surplus Note, each initially \$344 million, are expected to increase or decrease in relation to changes in the excess reserves financed. The Financing Note, reported in Receivables from Affiliates, matures December 30, 2031 and bears interest at 4.00%. The outstanding balance of both the Financing Note and the Squire Surplus Note was \$307.4 million at December 31, 2017.

Jackson provides a revolving credit facility to Jackson Holdings, LLC, an upstream holding company. The outstanding balance at December 31, 2017 and 2016 was \$1.5 million and \$0.1 million, respectively.

Value of Business Acquired

The Company has an intangible asset representing the value of business acquired ("VOBA"), which is included in other assets. In connection with the acquisition of insurance policies and investment contracts, a portion of the purchase price is assigned to the right to receive future gross profits from the acquired insurance policies and investment contracts. This intangible asset, or VOBA, represents the actuarially estimated present value of future cash flows from the acquired policies. The Company established a VOBA intangible asset for previously acquired traditional life insurance products and deferred annuity contracts. This intangible asset is amortized over the life of the business, which approximates 20 years. The unamortized VOBA balance is subject to recoverability testing at the end of each reporting period to ensure that the balance does not exceed the present value of anticipated gross profits.

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Income Taxes

The Company files income tax returns with the U.S. federal government and various state and local jurisdictions, as well as certain foreign jurisdictions.

Jackson files a consolidated federal income tax return with Brooke Life, Jackson National Life Insurance Company of New York and, beginning in 2016, Squire Re II. Jackson National Life (Bermuda) LTD and VFL International Life Company SPC, LTD are taxed as controlled foreign corporations of Jackson. With the exception of several insignificant wholly owned subsidiaries that are not included in the Jackson consolidated tax return, all other subsidiaries 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. Income tax expense is the lesser of the amount calculated on a separate company basis or Jackson's pro-rata share of the actual liability as determined under the consolidated return taking into account only Jackson and Brooke Life.

Deferred federal income taxes arise from the recognition of temporary differences between the basis of assets and liabilities determined for financial reporting purposes and the basis determined for income tax purposes. Such temporary differences are principally related to the effects of recording certain invested assets at market value, the deferral of acquisition costs and sales inducements and the provisions for future policy benefits and expenses. Deferred tax assets and liabilities are measured using the tax rates expected to be in effect when such benefits are realized. Jackson is required to test the value of deferred tax assets for realizability. Deferred tax assets are reduced by a valuation allowance if, based on the weight of available positive and negative evidence, it is more likely than not that some portion, or all, of the deferred tax assets will not be realized. In determining the need for a valuation allowance, the Company considers the carryback eligibility of losses, reversal of existing temporary differences, estimated future taxable income and tax planning strategies.

The determination of the valuation allowance for Jackson's deferred tax assets requires management to make certain judgments and assumptions regarding future operations that are based on historical experience and expectations of future performance. In order to recognize a tax benefit in the consolidated financial statements, there must be a greater than fifty percent chance of success of the Company's position being sustained by the relevant taxing authority with regard to that tax position. Management's judgments are potentially subject to change given the inherent uncertainty in predicting future performance, which is impacted by such factors as policyholder behavior, competitor pricing and other specific industry and market conditions.

The Company recognizes accrued interest and penalties, if any, related to unrecognized tax benefits as a component of tax expense.

Reserves for Future Policy Benefits and Claims Payable and Other Contract Holder Funds

For traditional life insurance contracts, which include term and whole life, 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, persistency and expenses, plus provisions for adverse deviations. These assumptions are not unlocked unless the reserve is determined to be deficient. Interest rate assumptions range from 2.5% to 6.0%. Lapse, mortality, and expense assumptions are based primarily on Company experience. The Company's liability for future policy benefits also includes net liabilities for guaranteed benefits related to certain nontraditional long-duration life and annuity contracts, which are further discussed in Note 9.

In conjunction with a prior acquisition, the Company recorded a fair value adjustment related to certain annuity and interest sensitive liability blocks of business to reflect the cost of the interest guarantees within the inforce liabilities, based on the difference between the guaranteed interest rate and an assumed new money guaranteed interest rate. This adjustment was recorded in reserves for future policy benefits and claims payable. This component of the acquired reserves is reassessed at the end of each period, taking into account changes in the inforce block. Any resulting change in the reserve is recorded as a change in policy reserve through the consolidated income statements.

For the Company's interest-sensitive life contracts, liabilities approximate the policyholder's account value, plus the remaining balance of the fair value adjustment related to previously acquired business. For fixed deferred annuities, the liability is the policyholder's account value, plus the unamortized balance of the above mentioned fair value adjustment. For the fixed option on variable annuities, guaranteed investment contracts and other investment contracts, the liability is the policyholder's account value. The liability for fixed index annuities is based on three components, 1) the imputed

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value of the underlying guaranteed host contract, 2) the fair value of the embedded option component of the contract and 3) the liability for guaranteed benefits related to the optional lifetime income rider.

The Company has formed both a special purpose vehicle and a statutory business trust, solely for the purpose of issuing Medium Term Note instruments to institutional investors, the proceeds of which are deposited with the Company and secured by the issuance of funding agreements.

Those Medium Term Note instruments issued in a foreign currency have been economically hedged for changes in exchange rates using cross-currency swaps. The fair value of derivatives embedded in funding agreements, including unrealized foreign currency 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 gains and losses using exchange rates as of the reporting date. Foreign currency gains and losses are included in other net investment losses.

Jackson and Squire Re are members of the Federal Home Loan Bank of Indianapolis ("FHLBI") primarily for the purpose of participating in the bank's mortgage-collateralized loan advance program with short-term and long-term funding facilities. Members are required to purchase and hold a minimum amount of FHLBI capital stock, plus additional stock based on outstanding advances. Advances are in the form of short-term or long-term notes or funding agreements issued to FHLBI.

The Company's institutional products business is comprised of the guaranteed investment contracts, funding agreements and FHLBI funding agreement advances described above.

Contingent Liabilities

The Company is a party to legal actions and, at times, regulatory investigations. Given the inherent unpredictability of these matters, it is difficult to estimate their impact on the Company's financial position. A reserve is established for contingent liabilities if it is probable that a loss has been incurred and the amount is reasonably estimable. It is possible that an adverse outcome in certain of the Company's contingent liabilities, or the use of different assumptions in the determination of amounts recorded, could have a material effect upon the Company's financial position. However, it is the opinion of management that the ultimate disposition of contingent liabilities is unlikely to have a material adverse effect on the Company's financial position.

Separate Account Assets and Liabilities

The Company maintains separate account assets, which are reported at fair value. The related liabilities are reported at an amount equivalent to the separate account assets. At December 31, 2017 and 2016, the assets and liabilities associated with variable life and annuity contracts were \$176.6 billion and \$148.8 billion, respectively. Investment risks associated with market value changes are borne by the contract holders, except to the extent of minimum guarantees made by the Company. Refer to Note 9 for additional information regarding the Company's contractual guarantees. Separate account net investment income, net investment realized and unrealized gains and losses, and the related liability changes are offset within the same line item in the consolidated income statements. Amounts assessed against the contract holders for mortality, variable annuity benefit guarantees, administrative, and other services are reported in revenue as fee income.

Included in the above mentioned assets and liabilities is a Company issued 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, which had balances of \$267.7 million and \$264.7 million at December 31, 2017 and 2016, 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.

Debt

Liabilities for the Company's debt are primarily carried at an amount equal to the unpaid principal balance. Original issuance discount or premium and any debt issue costs, if applicable, are recognized as a component of interest expense over the period the debt is expected to be outstanding. Refer to Note 10 for further information regarding the Company's debt.

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Share-Based Compensation

As more fully described in Note 14, the Company has certain share award plans that are either equity settled or liability settled. The Company recognizes compensation expense based on a grant-date award fair value, ratably over the requisite service period of each individual grant, which generally equals the vesting period. Additional compensation expense is recognized based on the change in fair value of the award at the end of each reporting period.

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 through provisions for future policy benefits and the deferral and amortization of certain 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 investment income and charges assessed against the account value for mortality charges, surrenders, variable annuity benefit guarantees and administrative expenses. Fee income also includes revenues related to asset management fees and certain 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 direct acquisition expenses are associated with gross profit in order to recognize profit over the life of the business. This is accomplished through deferral and amortization of acquisition costs and sales inducements. Expenses not related to policy acquisition are recognized when incurred.

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

Subsequent Events

The Company has evaluated events through March 8, 2018, which is the date the consolidated financial statements were available to be issued.

3. Investments

Investments are comprised primarily of fixed-income securities and loans, primarily publicly-traded corporate and government bonds, asset-backed securities and commercial mortgage loans. Asset-backed securities include mortgage-backed and other structured securities. The Company generates the majority of its general account 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 amounts credited to the interest-sensitive liabilities and to earn a stable return on its investments.

Fixed Maturities

The following table sets forth the composition of the fair value of fixed maturities at December 31, 2017, classified by rating categories as assigned by nationally recognized statistical rating organizations ("NRSRO"), the National Association of Insurance Commissioners ("NAIC"), or if not rated by such organizations, the Company's affiliated investment advisor. At December 31, 2017, the carrying value of investments rated by the Company's affiliated investment advisor totaled \$381.2 million. For purposes of the table, if not otherwise rated higher by a NRSRO, 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.

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<u>Investment Rating</u>	<u>Percent of Total Fixed Maturities Carrying Value December 31, 2017</u>
AAA	19.7%
AA	6.2%
A	35.7%
BBB	35.0%
Investment grade	96.6%
BB	2.2%
B and below	1.2%
Below investment grade	3.4%
Total fixed maturities	100.0%

At December 31, 2017, based on ratings by NRSROs, of the total carrying value of fixed maturities in an unrealized loss position, 79% were investment grade, 4% were below investment grade and 17% were not rated. Unrealized losses on fixed maturities that were below investment grade or not rated were approximately 25% 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, 2017, the industries accounting for the larger percentage of unrealized losses included telecom (14% of corporate gross unrealized losses) and consumer goods (12%). The largest unrealized loss related to a single corporate obligor was \$7.0 million at December 31, 2017.

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At December 31, 2017 and 2016, the amortized cost, gross unrealized gains and losses, fair value and non-credit other-than-temporary impairment (“OTTI”) of available for sale fixed maturities, including \$116.0 million and \$138.6 million in securities carried at fair value under the fair value option, were as follows (in thousands):

	Amortized Cost ⁽¹⁾	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Non-credit OTTI ⁽²⁾
December 31, 2017					
Fixed Maturities					
U.S. government securities	\$ 5,652,866	\$ 52,180	\$ 20,373	\$ 5,684,673	\$ -
Other government securities	842,781	18,105	6,321	854,565	-
Public utilities	4,459,077	314,480	10,424	4,763,133	-
Corporate securities	30,675,364	1,234,667	79,721	31,830,310	-
Residential mortgage-backed	865,339	53,643	5,580	913,402	(26,533)
Commercial mortgage-backed	2,077,960	41,356	6,787	2,112,529	204
Other asset-backed securities	1,293,628	20,938	16,024	1,298,542	(17,635)
Total fixed maturities	<u>\$ 45,867,015</u>	<u>\$ 1,735,369</u>	<u>\$ 145,230</u>	<u>\$ 47,457,154</u>	<u>\$ (43,964)</u>
December 31, 2016					
Fixed Maturities					
U.S. government securities	\$ 6,796,612	\$ 278	\$ 509,340	\$ 6,287,550	\$ -
Other government securities	965,661	1,084	21,016	945,729	-
Public utilities	4,465,064	277,588	31,633	4,711,019	-
Corporate securities	31,719,821	1,202,727	221,512	32,701,036	-
Residential mortgage-backed	1,220,368	57,655	9,484	1,268,539	(30,029)
Commercial mortgage-backed	2,690,258	56,603	17,469	2,729,392	296
Other asset-backed securities	1,305,796	19,694	30,004	1,295,486	(17,635)
Total fixed maturities	<u>\$ 49,163,580</u>	<u>\$ 1,615,629</u>	<u>\$ 840,458</u>	<u>\$ 49,938,751</u>	<u>\$ (47,368)</u>

⁽¹⁾ Amortized cost, apart from the carrying value for securities carried at fair value under the fair value option.

⁽²⁾ Represents the amount of non-credit OTTI gains (losses) recognized in other comprehensive income on securities for which credit impairments have been recorded.

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The amortized cost, gross unrealized gains and losses, and fair value of fixed maturities at December 31, 2017, by contractual maturity, are shown below (in thousands). Actual maturities may differ from contractual maturities where securities can be called or prepaid with or without early redemption penalties.

	Amortized⁽¹⁾ Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Due in 1 year or less	\$ 1,298,022	\$ 15,556	\$ 129	\$ 1,313,449
Due after 1 year through 5 years	12,040,633	483,555	9,594	12,514,594
Due after 5 years through 10 years	17,014,638	487,119	54,302	17,447,455
Due after 10 years through 20 years	3,042,808	250,757	16,366	3,277,199
Due after 20 years	8,233,987	382,445	36,448	8,579,984
Residential mortgage-backed	865,339	53,643	5,580	913,402
Commercial mortgage-backed	2,077,960	41,356	6,787	2,112,529
Other asset-backed securities	1,293,628	20,938	16,024	1,298,542
Total	<u>\$ 45,867,015</u>	<u>\$ 1,735,369</u>	<u>\$ 145,230</u>	<u>\$ 47,457,154</u>

⁽¹⁾ Amortized cost, apart from the carrying value for securities carried at fair value under the fair value option.

Securities with a carrying value of \$110.7 million and \$134.3 million at December 31, 2017 and 2016, respectively, were on deposit with regulatory authorities, as required by law in various states in which business is conducted.

At December 31, 2017 and 2016, fixed maturities include \$116.0 million and \$124.6 million, respectively, held in trust pursuant to the retro treaties with SRZ.

Residential mortgage-backed securities ("RMBS") include certain RMBS, which are collateralized by residential mortgage loans and are neither explicitly nor implicitly guaranteed by U.S. government agencies ("non-agency RMBS"). The Company's non-agency RMBS include investments in securities backed by prime, Alt-A, and subprime loans as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2017				
Prime	\$ 171,016	\$ 11,846	\$ 965	\$ 181,897
Alt-A	147,140	23,218	410	169,948
Subprime	143,865	7,861	774	150,952
Total non-agency RMBS	<u>\$ 462,021</u>	<u>\$ 42,925</u>	<u>\$ 2,149</u>	<u>\$ 502,797</u>
December 31, 2016				
Prime	\$ 228,216	\$ 10,894	\$ 2,109	\$ 237,001
Alt-A	200,077	18,438	1,856	216,659
Subprime	216,120	8,243	2,674	221,689
Total non-agency RMBS	<u>\$ 644,413</u>	<u>\$ 37,575</u>	<u>\$ 6,639</u>	<u>\$ 675,349</u>

The Company defines its exposure to non-agency residential mortgage loans as follows. Prime loan-backed securities are collateralized by mortgage loans made to the highest rated borrowers. Alt-A loan-backed securities are collateralized by mortgage loans made to borrowers who lack credit documentation or necessary requirements to obtain prime borrower rates. Subprime loan-backed securities are collateralized by mortgage loans made to borrowers that have a FICO score of 680 or lower.

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The following table summarizes the number of securities, fair value and the related amount of gross unrealized losses aggregated by investment category and length of time that individual fixed maturities have been in a continuous loss position (dollars in thousands):

	December 31, 2017			December 31, 2016		
	Less than 12 months			Less than 12 months		
	Gross Unrealized Losses	Fair Value	# of securities	Gross Unrealized Losses	Fair Value	# of securities
U.S. government securities	\$ 6,730	\$ 819,187	6	\$ 509,340	\$ 6,254,301	23
Other government securities	541	50,975	7	20,419	644,616	26
Public utilities	3,909	325,474	26	30,033	901,185	86
Corporate securities	36,783	2,923,660	285	162,756	6,893,553	567
Residential mortgage-backed	533	66,969	31	2,686	205,296	59
Commercial mortgage-backed	2,479	412,621	33	12,632	665,513	54
Other asset-backed securities	2,477	409,700	58	6,006	487,424	72
Total temporarily impaired securities	<u>\$ 53,452</u>	<u>\$ 5,008,586</u>	<u>446</u>	<u>\$ 743,872</u>	<u>\$ 16,051,888</u>	<u>887</u>
	12 months or longer			12 months or longer		
	Gross Unrealized Losses	Fair Value	# of securities	Gross Unrealized Losses	Fair Value	# of securities
U.S. government securities	\$ 13,643	\$ 894,138	8	\$ -	\$ -	-
Other government securities	5,780	97,883	4	597	7,126	1
Public utilities	6,515	294,916	26	1,600	19,439	6
Corporate securities	42,938	1,513,801	123	58,756	840,610	89
Residential mortgage-backed	5,047	172,512	74	6,798	124,372	52
Commercial mortgage-backed	4,308	148,107	22	4,837	46,937	7
Other asset-backed securities	13,547	250,724	46	23,998	103,207	25
Total temporarily impaired securities	<u>\$ 91,778</u>	<u>\$ 3,372,081</u>	<u>303</u>	<u>\$ 96,586</u>	<u>\$ 1,141,691</u>	<u>180</u>
	Total			Total		
	Gross Unrealized Losses	Fair Value	# of securities	Gross Unrealized Losses	Fair Value	# of securities
U.S. government securities	\$ 20,373	\$ 1,713,325	14	\$ 509,340	\$ 6,254,301	23
Other government securities	6,321	148,858	11	21,016	651,742	27
Public utilities	10,424	620,390	52	31,633	920,624	92
Corporate securities	79,721	4,437,461	408	221,512	7,734,163	656
Residential mortgage-backed	5,580	239,481	105	9,484	329,668	111
Commercial mortgage-backed	6,787	560,728	55	17,469	712,450	61
Other asset-backed securities	16,024	660,424	104	30,004	590,631	97
Total temporarily impaired securities	<u>\$ 145,230</u>	<u>\$ 8,380,667</u>	<u>749</u>	<u>\$ 840,458</u>	<u>\$ 17,193,579</u>	<u>1,067</u>

Other-Than-Temporary Impairments on Available For Sale Securities

The Company periodically reviews its available for sale fixed maturities on a case-by-case basis to determine if any decline in fair value to below cost or 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, the severity of the unrealized loss and the reasons for the decline in value and expectations for the amount and timing of a recovery in fair value.

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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 fair 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 exercises considerable judgment in determining whether a security is other-than-temporarily 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 the obligations and the macro-economic and micro-economic outlooks for specific industries and issuers. This assessment may 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, and the likelihood of recovering the carrying value based on the near-term prospects of the issuer. Unrealized losses that are considered to be primarily the result of market conditions (e.g., minor increases in interest rates, temporary market illiquidity or volatility, or industry-related events) and where the Company also believes there exists a reasonable expectation for recovery in the near term are usually determined to be temporary. To the extent that 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.

In addition to the review procedures described above, investments in asset-backed securities where market prices are depressed are subject to a review of their future estimated cash flows, including expected and stress case scenarios, to identify potential shortfalls in contractual payments. These estimated cash flows are developed using available performance indicators from the underlying assets including current and projected default or delinquency rates, levels of credit enhancement, current subordination levels, vintage, expected loss severity and other relevant characteristics. These estimates reflect a combination of data derived by third parties and internally developed assumptions. Where possible, this data is benchmarked against third-party sources.

Even in the case of severely depressed market values on asset-backed securities, the Company places significant reliance on the results of its cash flow testing and its lack of an intent to sell these securities until their fair values recover when reaching other-than-temporary impairment conclusions with regard to these securities. Other-than-temporary impairment charges are recorded on asset-backed securities when the Company forecasts a contractual payment shortfall.

The Company recognizes other-than-temporary impairments on debt securities in an unrealized loss position when any of the following circumstances exists:

- The Company does not expect full recovery of the amortized cost based on the discounted cash flows estimated to be collected;
- The Company intends to sell a security; or,
- It is more likely than not that the Company will be required to sell a security prior to recovery.

For mortgage-backed securities, credit impairment is assessed using a cash flow model that estimates the cash flows on the underlying mortgages, using the security-specific collateral characteristics and transaction structure. The model estimates cash flows from the underlying mortgage loans and distributes those cash flows to various tranches of securities, considering the transaction structure and any subordination and credit enhancements existing in that structure. The cash flow model incorporates actual cash flows on the mortgage-backed securities through the current period and then projects the remaining cash flows using a number of assumptions, including prepayment speeds, default rates and loss severity.

Specifically for prime and Alt-A RMBS, the assumed default percentage is dependent on the severity of delinquency status, with foreclosures and real estate owned receiving higher rates, but also includes the currently performing loans. As of December 31, 2017 and 2016, assumed default rates for delinquent loans ranged from 15% to 100%. At December 31,

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2017 and 2016, assumed loss severities were applied to generate and analyze cash flows of each security and ranged from 25% to 70%.

These estimates reflect a combination of data derived by third parties and internally developed assumptions. Where possible, this data is benchmarked against other third-party sources. In addition, these estimates are extrapolated along a default timing curve to estimate the total lifetime pool default rate.

Other-than-temporary impairments are calculated as the difference between amortized cost and fair value. For other-than-temporarily impaired securities where Jackson does not intend to sell the security and it is not more likely than not that Jackson will be required to sell the security prior to recovery, total other-than-temporary impairments are reduced by the non-credit portion of the other-than-temporary impairments, which are recognized in other comprehensive income. The resultant net other-than-temporary impairments recorded in net income reflect only the credit loss on the other-than-temporarily impaired securities. The amortized cost of the other-than-temporarily impaired securities is reduced by the amount of this credit loss.

For securities that were deemed to be other-than-temporarily impaired and for which a non-credit loss was recorded in other comprehensive income, the amount recorded as an unrealized gain (loss) represents the difference between the fair value and the new amortized cost basis of the securities. The unrealized gain (loss) on other-than-temporarily impaired securities is recorded in other comprehensive income.

The following table summarizes net realized losses on investments (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Available-for-sale securities			
Realized gains on sale	\$ 152,283	\$ 612,422	\$ 211,198
Realized losses on sale	(201,604)	(205,501)	(128,955)
Impairments:			
Total other-than-temporary impairments	(3,070)	(68,511)	(77,662)
Portion of other-than-temporary impairments included in other comprehensive income	18	9,562	15,024
Net other-than-temporary impairments	(3,052)	(58,949)	(62,638)
Other	1,710	1,232	14,586
Net realized (losses) gains on non-derivative investments	(50,663)	349,204	34,191
Net losses on derivative instruments	(3,376,666)	(4,008,305)	(1,621,706)
Total net realized losses on investments	<u>\$ (3,427,329)</u>	<u>\$ (3,659,101)</u>	<u>\$ (1,587,515)</u>

The net losses on derivative instruments included in the above table are further detailed in Note 4.

The aggregate fair value of securities sold at a loss for the years ended December 31, 2017, 2016, and 2015 was \$4,276.1 million, \$1,662.6 million and \$1,022.1 million, respectively, which was approximately 96%, 89%, and 89% of book value, respectively.

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The following summarizes the current year activity for credit losses recognized in net income on securities where an other-than-temporary impairment was identified and the non-credit portion of the other-than-temporary impairment was included in other comprehensive income (in thousands):

	Years Ended December 31,	
	2017	2016
Cumulative credit loss beginning balance	\$ 250,124	\$ 294,266
Additions:		
New credit losses	2,128	42,048
Incremental credit losses	424	16,901
Reductions:		
Securities sold, paid down or disposed of	(23,758)	(92,578)
Securities where there is intent to sell	(1,655)	(10,513)
Cumulative credit loss ending balance	<u>\$ 227,263</u>	<u>\$ 250,124</u>

There are inherent uncertainties in assessing the fair values assigned to the Company's investments and in determining whether a decline in fair value is other-than-temporary. The Company's reviews of net present value and fair value involve several criteria including economic conditions, credit loss experience, other issuer-specific developments and estimated 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 reported in accumulated other comprehensive income may be recognized in the consolidated income statements in future periods.

The Company currently has no intent to sell securities with unrealized losses considered to be temporary until they mature or recover in value and believes that it has the ability to do so. 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 or recovery and realize a loss.

Commercial Mortgage Loans

Commercial mortgage loans of \$8.4 billion and \$7.5 billion at December 31, 2017 and 2016, respectively, are reported net of an allowance for loan losses of \$6.8 million and \$3.9 million at each date, respectively. At December 31, 2017, commercial mortgage loans were collateralized by properties located in 41 states. Jackson's commercial mortgage loan portfolio does not include single-family residential mortgage loans, and is therefore not exposed to the risk of defaults associated with residential subprime mortgage loans. Jackson periodically reviews these loans for impairment. During 2017, 2016, and 2015, Jackson recognized impairment charges against the allowance for loan losses of \$0.7 million, \$0, and \$0, respectively.

The following table provides a summary of the allowance for losses in the Company's commercial mortgage loan portfolio at December 31, 2017 and 2016 (in thousands):

Allowance for loan losses:	2017	2016
Balance at beginning of year	\$ 3,924	\$ 4,556
Charge-offs	(665)	-
Recoveries	-	-
Net charge-offs	(665)	-
Addition (reduction) to allowance	3,585	(632)
Balance at end of year	<u>\$ 6,844</u>	<u>\$ 3,924</u>

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The following table provides a summary of the allowance for losses in Jackson's commercial mortgage loan portfolio (in thousands):

	<u>December 31, 2017</u>		<u>December 31, 2016</u>	
	<u>Allowance for Loan Losses</u>	<u>Recorded Investment</u>	<u>Allowance for Loan Losses</u>	<u>Recorded Investment</u>
Individually evaluated for impairment	\$ 766	\$ 3,100	\$ -	\$ -
Collectively evaluated for impairment	6,078	8,432,340	3,924	7,482,233
Total	<u>\$ 6,844</u>	<u>\$ 8,435,440</u>	<u>\$ 3,924</u>	<u>\$ 7,482,233</u>

As of December 31, 2017 and 2016, the Company's commercial mortgage loan portfolio is current and accruing interest. Delinquency status is determined from the date of the first missed contractual payment.

Under Jackson's policy for monitoring commercial mortgage loans, all impaired commercial mortgage loans are closely evaluated subsequent to impairment. The table below summarizes the recorded investment, unpaid principal balance, related loan allowance, average recorded investment and investment income recognized on impaired loans (in thousands):

	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Loan Allowance</u>	<u>Average Recorded Investment</u>	<u>Investment Income Recognized</u>
December 31, 2017:					
Impaired Loans with a Valuation					
Allowance					
Retail	\$ 3,100	\$ 3,866	\$ 766	\$ 2,097	\$ 235
Warehouse	-	-	-	-	-
Total	<u>\$ 3,100</u>	<u>\$ 3,866</u>	<u>\$ 766</u>	<u>\$ 2,097</u>	<u>\$ 235</u>
Impaired Loans without a Valuation					
Allowance					
Retail	\$ -	\$ -	\$ -	\$ -	\$ -
Warehouse	-	-	-	1,623	75
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,623</u>	<u>\$ 75</u>
Total Impaired Loans					
Retail	\$ 3,100	\$ 3,866	\$ 766	\$ 2,097	\$ 235
Warehouse	-	-	-	1,623	75
Total	<u>\$ 3,100</u>	<u>\$ 3,866</u>	<u>\$ 766</u>	<u>\$ 3,720</u>	<u>\$ 310</u>

During 2016 there were no impaired commercial mortgage loans.

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The following tables provide information about the credit quality of commercial mortgage loans (in thousands):

December 31, 2017					
	In Good Standing	Restructured	Greater than 90 Days Delinquent	In the Process of Foreclosure	Total Carrying Value
Apartment	\$ 2,861,428	\$ -	\$ -	\$ -	\$ 2,861,428
Hotel	705,077	-	-	-	705,077
Office	879,676	-	-	-	879,676
Retail	1,610,631	-	-	-	1,610,631
Warehouse	2,378,628	-	-	-	2,378,628
Total	\$ 8,435,440	\$ -	\$ -	\$ -	\$ 8,435,440

December 31, 2016					
	In Good Standing	Restructured	Greater than 90 Days Delinquent	In the Process of Foreclosure	Total Carrying Value
Apartment	\$ 2,430,942	\$ -	\$ -	\$ -	\$ 2,430,942
Hotel	630,070	-	-	-	630,070
Office	826,811	-	-	-	826,811
Retail	1,282,917	-	-	-	1,282,917
Warehouse	2,311,493	-	-	-	2,311,493
Total	\$ 7,482,233	\$ -	\$ -	\$ -	\$ 7,482,233

As of December 31, 2017 and 2016, there were no commercial mortgage loans involved in troubled debt restructuring.

Securitizations

In 2001, Jackson executed the Morgan Stanley Dean Witter Capital I, Series 2001-PPM (“MSDW”) securitization transaction, contributing commercial mortgages to MSDW and retaining a beneficial interest. Effective January 1, 2010, as a result of adoption of accounting guidance on certain investment funds, the Company was deemed to be the primary beneficiary of MSDW and, therefore, consolidated MSDW. As such, Jackson’s consolidated financial statements include MSDW assets of \$6.0 million at December 31, 2016. Effective February 13, 2017, Jackson purchased the underlying commercial mortgage loans at fair value, and MSDW was dissolved.

Other Invested Assets

Other invested assets primarily include investments in limited partnerships and real estate. At December 31, 2017 and 2016, investments in limited partnerships had carrying values of \$1,141.1 million and \$1,219.9 million, respectively. At December 31, 2017 and 2016, real estate totaling \$228.8 million and \$235.6 million, respectively, included foreclosed properties with a book value of \$0.7 million in both 2017 and 2016.

In 2017, the Company funded PPM Loan Holding Management Company, LLC, an affiliated investment entity facilitating the issuance of collateralized loan obligations. At December 31, 2017, the Company’s investment in PPM Loan Holding Management Company, LLC had a carrying value of \$7.5 million and was included in other invested assets.

Securities Lending

The Company has entered into securities lending agreements with agent banks whereby blocks of securities are loaned to third parties, primarily major brokerage firms. As of December 31, 2017 and 2016, the estimated fair value of loaned securities was \$67.5 million and \$116.0 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 these programs, the financial condition of counterparties is monitored on a regular basis. At December 31, 2017 and 2016, cash collateral received in the amount of \$69.8 million and \$119.6 million, respectively, was invested by the agent banks and included in cash and cash equivalents of the Company. A securities lending payable for the overnight and continuous loans is included in liabilities in the amount of cash collateral received.

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Securities lending transactions are used to generate income. Income and expenses associated with these transactions are reported as net investment income.

Repurchase Agreements

The Company routinely enters into repurchase agreements whereby the Company agrees to sell and repurchase securities. These agreements are accounted for as financing transactions, with the assets and associated liabilities included in the consolidated balance sheets. During 2017 and 2016, short-term borrowings under such agreements averaged \$474.3 million and \$278.4 million, respectively, with weighted average interest rates of 0.90% and 0.43% during 2017 and 2016, respectively. At December 31, 2017 and 2016, the outstanding repurchase agreement balance was nil and \$411.9 million, respectively, collateralized with US Treasury notes and maturing within 30 days, and was included within other liabilities in the consolidated balance sheets. In the event of a decline in the fair value of the pledged collateral under these agreements, the Company may be required to transfer cash or additional securities as pledged collateral. Interest expense totaled \$4.3 million, \$1.2 million, and \$0.1 million in 2017, 2016, and 2015, respectively. The highest level of short-term borrowings at any month end was \$804.9 million in 2017 and \$857.7 million in 2016.

Investment Income

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

	Years Ended December 31,		
	<u>2017</u>	<u>2016</u>	<u>2015</u>
Fixed maturities	\$ 1,963,569	\$ 2,122,604	\$ 2,172,061
Commercial mortgage loans	305,338	294,243	287,420
Limited partnerships	155,093	179,882	129,470
Derivative instruments	246,221	294,366	282,337
Policy loans	400,788	403,403	398,855
Other investment (loss) income	(2,336)	19,571	41,785
Total investment income	<u>3,068,673</u>	<u>3,314,069</u>	<u>3,311,928</u>
Less: income on funds held under reinsurance treaties	(322,764)	(318,204)	(308,298)
Less: investment expenses	<u>(91,367)</u>	<u>(80,918)</u>	<u>(64,268)</u>
Net investment income	<u>\$ 2,654,542</u>	<u>\$ 2,914,947</u>	<u>\$ 2,939,362</u>

Investment income of \$9.2 million, \$11.2 million, and \$6.7 million was recognized on trading securities held at December 31, 2017, 2016, and 2015, respectively. In addition, investment income of \$0.6 million, \$2.6 million, and \$0.3 million, respectively, was recognized on securities carried at fair value recorded through income.

During 2017, investment income was reduced by \$322.8 million for expense incurred on the liability for funds held under reinsurance treaties, including \$320.1 million on policy loans, \$2.4 million of fixed maturity income, \$0.4 million loss on fixed maturities with fair value recorded through the consolidated income statement, and \$0.7 million of income from other invested assets. During 2016, investment income was reduced by \$318.2 million for expense incurred on the liability for funds held under reinsurance treaties, including \$313.8 million on policy loans, \$2.4 million of fixed maturity income, \$1.7 million gain on fixed maturities with fair value recorded through the consolidated income statement, and \$0.3 million of income from other invested assets. During 2015, investment income was reduced by \$308.3 million for expense incurred on the liability for funds held under reinsurance treaties, including \$305.6 million on policy loans, \$2.4 million of fixed maturity income, \$0.1 million gain on fixed maturities with fair value recorded through the consolidated income statement, and \$0.2 million of income from other invested assets.

4. Derivative Instruments

Jackson's business model includes the acceptance, monitoring and mitigation of risk. Specifically, Jackson considers, among other factors, exposures to interest rate and equity market movements, foreign exchange rates and other asset or liability prices. The Company uses derivative instruments to mitigate or reduce these risks in accordance with established policies and goals. Jackson's derivative holdings, while effective in managing defined risks, are not structured to meet accounting requirements to be designated as hedging instruments. As a result, freestanding derivatives are carried at fair value with changes recorded in other net investment losses.

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Cross-currency swaps, which embody spot and forward currency swaps and, in some cases, interest rate and equity index swaps, are entered into for the purpose of hedging the Company issued foreign currency denominated trust instruments supported by funding agreements. Cross-currency swaps serve to hedge foreign currency exchange risk embedded in the funding agreements and are carried at fair value. The fair value of derivatives embedded in funding agreements, including unrealized foreign currency translation gains and losses, are included in the carrying value of the trust instruments supported by funding agreements. Foreign currency translation gains and losses associated with funding agreement hedging activities are included in other net investment losses.

Credit default swaps, with maturities up to five years, are agreements where 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 if a defined “default event” occurs, in exchange for periodic payments made by the Company for the life of the agreement. Credit default swaps are carried at fair value. The Company does not currently sell default protection using credit default swaps or other similar derivative instruments.

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-term interest rate swap at future exercise dates. The Company purchases and writes put-swaptions for hedging purposes with original maturities of up to 10 years. Put-swaptions hedge against movements in interest rates. Written put-swaptions may be entered into in conjunction with associated put-swaptions purchased from the same counterparties, referred to as linked put-swaptions. Linked put-swaptions have identical notional amounts and strike prices, but have different underlying swap terms. Linked put-swaptions are presented at the fair value of the net position for each pair of contracts. Non-linked put-swaptions are carried at fair value.

Equity index futures contracts and equity index options (including various call and put options, interest rate-contingent options, currency-contingent options, and put spreads), which are used to hedge the Company’s equity risk, including obligations associated with its fixed index annuities and guarantees in variable annuity products, are carried at fair value. These insurance products contain embedded options whose fair values are reported in other contract holder funds and reserves for future policy benefits and claims payable.

Total return swaps, for which the Company receives 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 carried at fair value.

Interest rate swap agreements used for hedging purposes generally involve the exchange of fixed and floating payments based on a notional contract amount over the period for which the agreement remains outstanding without an exchange of the underlying notional amount. Interest rate swaps are carried at fair value.

Treasury futures contracts are used to hedge movements in interest rates, which are carried at fair value.

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

	December 31, 2017				
	Assets		Liabilities		Net Fair Value
	Contractual/ Notional Amount ⁽¹⁾	Fair Value	Contractual/ Notional Amount ⁽¹⁾	Fair Value	
	Amount ⁽¹⁾	Value	Amount ⁽¹⁾	Value	
Cross-currency swaps	\$ 211,816	\$ 19,416	\$ 404,338	\$ (4,335)	
Equity index call options	31,500,000	1,642,827	-	-	1,642,827
Equity index futures	-	-	29,346,663	-	-
Equity index put options	23,750,000	97,062	-	-	97,062
Interest rate swaps	15,500,000	419,662	1,500,000	(2,113)	417,549
Put-swaptions	2,000,000	2	-	-	2
Treasury futures	-	-	502,969	-	-
Total	<u>\$ 72,961,816</u>	<u>\$ 2,178,969</u>	<u>\$ 31,753,970</u>	<u>\$ (6,448)</u>	<u>\$ 2,172,521</u>

	December 31, 2016				
	Assets		Liabilities		Net Fair Value
	Contractual/ Notional Amount ⁽¹⁾	Fair Value	Contractual/ Notional Amount ⁽¹⁾	Fair Value	
	Amount ⁽¹⁾	Value	Amount ⁽¹⁾	Value	
Cross-currency swaps	\$ 156,515	\$ 7,273	\$ 175,782	\$ (14,158)	
Equity index call options	25,500,000	306,692	-	-	306,692
Equity index futures	-	-	24,745,569	-	-
Equity index put options	37,000,000	70,172	5,000,000	(25,782)	44,390
Interest rate swaps	15,000,000	638,332	5,250,000	(38,715)	599,617
Put-swaptions	3,750,000	7,664	500,000	(147)	7,517
Treasury futures	-	-	480,750	-	-
Total	<u>\$ 81,406,515</u>	<u>\$ 1,030,133</u>	<u>\$ 36,152,101</u>	<u>\$ (78,802)</u>	<u>\$ 951,331</u>

⁽¹⁾ The notional amount for swaps and put-swaptions represents the stated principal balance used as a basis for calculating payments. The contractual amount for futures and options represents the market exposure of open positions.

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The following tables reflect the results of the Company's derivatives, including gains (losses) and change in fair value of freestanding derivative instruments and embedded derivatives (in thousands):

Year Ended December 31, 2017			
	Net		
	Derivative	Net Investment	Net Gain (Loss)
	Gains (Losses)	Income	
Equity index call options	\$ 1,892,556	\$ -	\$ 1,892,556
Equity index futures	(5,030,793)	-	(5,030,793)
Equity index put options	(279,592)	-	(279,592)
Fixed index annuity embedded derivatives	(327,420)	-	(327,420)
Interest rate swaps	(182,068)	246,221	64,153
Put-swaptions	(7,515)	-	(7,515)
Treasury futures	34,224	-	34,224
Variable annuity embedded derivatives	523,942	-	523,942
Total	<u>\$ (3,376,666)</u>	<u>\$ 246,221</u>	<u>\$ (3,130,445)</u>

Year Ended December 31, 2016			
	Net		
	Derivative	Net Investment	Net Gain (Loss)
	Gains (Losses)	Income	
Equity index call options	\$ 35,134	\$ -	\$ 35,134
Equity index futures	(2,730,551)	-	(2,730,551)
Equity index put options	(767,258)	-	(767,258)
Fixed index annuity embedded derivatives	(93,455)	-	(93,455)
Interest rate swaps	(348,710)	294,366	(54,344)
Put-swaptions	70,300	-	70,300
Treasury futures	(45,160)	-	(45,160)
Variable annuity embedded derivatives	(128,605)	-	(128,605)
Total	<u>\$ (4,008,305)</u>	<u>\$ 294,366</u>	<u>\$ (3,713,939)</u>

Year Ended December 31, 2015			
	Net		
	Derivative	Net Investment	Net Gain (Loss)
	Gains (Losses)	Income	
Equity index call options	\$ (120,259)	\$ -	\$ (120,259)
Equity index futures	5,347	-	5,347
Equity index put options	(1,044,044)	-	(1,044,044)
Fixed index annuity embedded derivatives	13,555	-	13,555
Interest rate swaps	(36,205)	282,337	246,132
Put-swaptions	8,695	-	8,695
Variable annuity embedded derivatives	(448,795)	-	(448,795)
Total	<u>\$ (1,621,706)</u>	<u>\$ 282,337</u>	<u>\$ (1,339,369)</u>

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All of Jackson's trade agreements for freestanding, over-the-counter derivatives contain credit downgrade provisions that allow a party to assign or terminate derivative transactions if the counterparty's credit rating declines below an established limit. At December 31, 2017 and 2016, the fair value of Jackson's net derivative assets by counterparty were \$2,172.5 million and \$953.7 million, respectively, and held collateral was \$2,574.8 million and \$1,098.6 million respectively, related to these agreements. At December 31, 2017 and 2016, the fair value of Jackson's net derivative liabilities by counterparty was nil and \$2.4 million, respectively, and provided collateral was nil and \$0.9 million, respectively, related to these agreements. If all of the downgrade provisions had been triggered at December 31, 2017 or 2016, in aggregate, Jackson would have had to disburse \$402.2 million and \$146.4 million, respectively, to counterparties, representing the net fair values of derivatives by counterparty, less collateral held.

Offsetting Assets and Liabilities

The Company's derivative instruments, repurchase agreements and securities lending agreements are subject to master netting arrangements and collateral arrangements. A master netting arrangement with a counterparty creates a right of offset for amounts due to and due from that same counterparty that is enforceable in the event of a default or bankruptcy. The Company recognizes amounts subject to master netting arrangements on a gross basis within the consolidated balance sheets.

The following tables present the gross and net information about the Company's financial instruments subject to master netting arrangements (in thousands):

December 31, 2017							
	Gross Amounts Recognized	Gross Amounts Offset in the Consolidated Balance Sheets	Net Amounts Presented in the Consolidated Balance Sheets	Gross Amounts Not Offset in the Consolidated Balance Sheets			Net Amount
				Financial Instruments ⁽¹⁾	Cash Collateral	Securities Collateral ⁽²⁾	
Financial Assets:							
Derivative assets	\$ 2,178,969	\$ -	\$ 2,178,969	\$ 6,448	\$ 905,108	\$ 1,267,413	\$ -
Financial Liabilities:							
Derivative liabilities	\$ 6,448	\$ -	\$ 6,448	\$ 6,448	\$ -	\$ -	\$ -
Securities loaned	69,785	-	69,785	-	69,785	-	-
Total financial liabilities	\$ 76,233	\$ -	\$ 76,233	\$ 6,448	\$ 69,785	\$ -	\$ -
December 31, 2016							
	Gross Amounts Recognized	Gross Amounts Offset in the Consolidated Balance Sheets	Net Amounts Presented in the Consolidated Balance Sheets	Gross Amounts Not Offset in the Consolidated Balance Sheets			Net Amount
				Financial Instruments ⁽¹⁾	Cash Collateral	Securities Collateral ⁽²⁾	
Financial Assets:							
Derivative assets	\$ 1,030,133	\$ -	\$ 1,030,133	\$ 76,431	\$ 115,297	\$ 825,554	\$ 12,851
Financial Liabilities:							
Derivative liabilities	\$ 78,802	\$ -	\$ 78,802	\$ 76,431	\$ -	\$ -	\$ 2,371
Securities loaned	119,608	-	119,608	-	119,608	-	-
Repurchase agreements	411,857	-	411,857	-	-	411,857	-
Total financial liabilities	\$ 610,267	\$ -	\$ 610,267	\$ 76,431	\$ 119,608	\$ 411,857	\$ 2,371

⁽¹⁾ Represents the amount that could be offset under master netting or similar arrangements that management elects not to offset on the consolidated balance sheets.

⁽²⁾ Excludes initial margin amounts for exchange-traded derivatives.

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In the above tables, the amounts of assets or liabilities presented in the Company's consolidated balance sheets are offset first by financial instruments that have the right of offset under master netting or similar arrangements with any remaining amount reduced by the amount of cash and securities collateral. The actual amount of collateral may be greater than amounts presented in the tables. The above tables exclude net embedded derivative liabilities of \$2,896.1 million and \$3,363.6 million for 2017 and 2016, respectively, as these derivatives are not subject to master netting arrangements. In addition, repurchase agreements are presented within other liabilities in the consolidated balance sheets.

5. Fair Value Measurements

The following table summarizes the fair value and carrying value of Jackson's financial instruments (in thousands). The basis for determining the fair value of each instrument is described in Note 2.

	December 31, 2017		December 31, 2016	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Fixed maturities ⁽¹⁾	\$ 47,457,154	\$ 47,457,154	\$ 49,938,751	\$ 49,938,751
Trading securities	137,756	137,756	415,122	415,122
Commercial mortgage loans	8,435,440	8,554,827	7,482,233	7,555,143
Policy loans ⁽¹⁾	4,591,132	4,591,132	4,546,161	4,546,161
Derivative instruments	2,178,969	2,178,969	1,030,133	1,030,133
Limited partnerships	1,141,123	1,141,123	1,219,887	1,219,887
Cash and cash equivalents	1,617,934	1,617,934	1,265,041	1,265,041
GMB reinsurance recoverable	252,138	252,138	304,927	304,927
Receivables from affiliates	312,049	312,049	344,100	344,100
Separate account assets	176,578,848	176,578,848	148,791,796	148,791,796
Liabilities				
Other contract holder funds				
Annuity reserves ⁽²⁾	\$ 38,938,615	\$ 46,156,875	\$ 41,363,500	\$ 46,229,473
Reserves for guaranteed investment contracts	1,698,178	1,699,627	1,875,816	1,876,930
Trust instruments supported by funding agreements	5,752,078	5,841,278	3,836,441	3,879,525
Federal Home Loan Bank funding agreements	1,934,690	1,947,151	1,784,040	1,782,493
Funds held under reinsurance treaties	3,604,525	3,604,525	3,523,106	3,523,106
Debt	647,718	726,322	685,949	766,461
Securities lending payable	69,785	69,785	119,608	119,608
Derivative instruments	6,448	6,448	78,802	78,802
Repurchase agreements	-	-	411,857	411,857
Federal Home Loan Bank advances	600,071	600,071	500,071	500,071
Separate account liabilities	176,578,848	176,578,848	148,791,796	148,791,796

⁽¹⁾ Includes items carried at fair value under the fair value option, for which there is a corresponding liability within funds held under reinsurance treaties.

⁽²⁾ Annuity reserves represent only the components of other contract holder funds and reserves for future policy benefits and claims payable that are considered to be financial instruments.

The following is a discussion of the methodologies used to determine fair values of the financial instruments measured on both a recurring and nonrecurring basis reported in the following tables.

Fixed Maturity and Trading Securities

The fair values for fixed maturity and trading securities are determined using information available from independent pricing services, broker-dealer quotes, or internally derived estimates. Priority is given to publicly available prices from independent sources, when available. Securities for which the independent pricing service does not provide a quotation are either submitted to independent broker-dealers for prices or priced internally. Typical inputs used by these three pricing methods include, but are not limited to, reported trades, benchmark yields, credit spreads, liquidity premiums and/or estimated cash flows based on default and prepayment assumptions.

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As a result of typical trading volumes and the lack of specific quoted market prices for most fixed maturities, independent pricing services will normally derive the security prices through recently reported trades for identical or similar securities, making adjustments through the reporting date based upon available market observable information as outlined above. If there are no recently reported trades, the independent pricing services and broker-dealers may use matrix or pricing model processes to develop a security price where future cash flow expectations are developed based upon collateral performance and discounted at relevant market rates. Certain securities are priced using broker-dealer quotes, which may utilize proprietary inputs and models. Additionally, the majority of these quotes are non-binding.

Included in the pricing of asset-backed securities are estimates of the rate of future prepayments of principal over the remaining life of the securities. Such estimates are derived based on the characteristics of the underlying structure and prepayment assumptions believed to be relevant for the underlying collateral. Actual prepayment experience may vary from these estimates.

Internally derived estimates may be used to develop a fair value for securities for which the Company is unable to obtain either a reliable price from an independent pricing service or a suitable broker-dealer quote. These fair value estimates may incorporate Level 2 and Level 3 inputs and are generally derived using expected future cash flows, discounted at market interest rates available from market sources based on the credit quality and duration of the instrument. For securities that may not be reliably priced using these internally developed pricing models, a fair value may be estimated using indicative market prices. These prices are indicative of an exit price, but the assumptions used to establish the fair value may not be observable or corroborated by market observable information and, therefore, represent Level 3 inputs.

The Company performs a monthly analysis on the prices and credit spreads received from third parties to ensure that the prices represent a reasonable estimate of the fair value. This process involves quantitative and qualitative analysis and is overseen by investment and accounting professionals. Examples of procedures performed include, but are not limited to, initial and ongoing review of third party pricing service methodologies, review of pricing statistics and trends, back testing recent trades and monitoring of trading volumes. In addition, the Company considers whether prices received from independent broker-dealers represent a reasonable estimate of fair value through the use of internal and external cash flow models, which are developed based on spreads and, when available, market indices. As a result of this analysis, if the Company determines there is a more appropriate fair value based upon the available market data, the price received from the third party may be adjusted accordingly.

For those securities that were internally valued at December 31, 2017 and 2016, the pricing model used by the Company utilizes current spread levels of similarly rated securities to determine the market discount rate for the security. Furthermore, appropriate risk premiums for illiquidity and non-performance are incorporated in the discount rate. Cash flows, as estimated by the Company using issuer-specific default statistics and prepayment assumptions, are discounted to determine an estimated fair value.

On an ongoing basis, the Company reviews the independent pricing services' valuation methodologies and related inputs, and evaluates the various types of securities in its investment portfolio to determine an appropriate fair value hierarchy distribution based upon trading activity and the observability of market inputs. Based on the results of this evaluation, each price is classified into Level 1, 2, or 3. Most prices provided by independent pricing services, including broker-dealer quotes, are classified into Level 2 due to their use of market observable inputs.

Commercial Mortgage Loans

Fair values are generally determined by discounting expected future cash flows at current market interest rates, inclusive of a credit spread, for similar quality loans. For loans whose value is dependent upon the underlying property, fair value is determined to be the estimated value of the collateral. Certain characteristics considered significant in determining the spread or collateral value may be based on internally developed estimates. As a result, these investments have been classified as Level 3 within the fair value hierarchy.

Policy Loans

Policy loans are funds provided to policyholders in return for a claim on the policies values and function like demand deposits which are redeemable upon repayment, death or surrender, and there is only one market price at which the transaction could be settled – the then current carrying value. The funds provided are limited to the cash surrender value of the underlying policy. The nature of policy loans is to have a negligible default risk as the loans are fully collateralized by the value of the policy. Policy loans do not have a stated maturity and the balances and accrued interest are repaid

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either by the policyholder or with proceeds from the policy. Due to the collateralized nature of policy loans and unpredictable timing of payments, the Company believes the carrying value of policy loans approximates fair value.

Freestanding Derivative Instruments

Freestanding derivative instruments are reported at fair value, which reflects the estimated amounts, net of payment accruals, which the Company would receive or pay upon sale or termination of the contracts at the reporting date. Changes in fair value are included in other net investment losses. Freestanding derivatives priced using third party pricing services incorporate inputs that are predominantly observable in the market. Inputs used to value derivatives include, but are not limited to, interest rate swap curves, credit spreads, interest rates, counterparty credit risk, equity volatility and equity index levels.

Freestanding derivative instruments classified as Level 1 include futures, which are traded on active exchanges. Freestanding derivative instruments classified as Level 2 include interest rate swaps, cross currency swaps, credit default swaps, put-swaptions and certain equity index call and put options. These derivative valuations are determined by third-party pricing services using pricing models with inputs that are observable in the market or can be derived principally from, or corroborated by, observable market data. Freestanding derivative instruments classified as Level 3 include interest rate contingent options that are valued by third-party pricing services utilizing significant unobservable inputs.

Limited Partnerships

Fair value for limited partnership interests, which are included in other invested assets, is determined using the proportion of Jackson's investment in each fund ("NAV equivalent") as a practical expedient for fair value. No adjustments to these amounts were deemed necessary at December 31, 2017 or 2016. As a result of using the net asset value per share practical expedient, limited partnerships are not classified in the fair value hierarchy.

The Company's limited partnership investments are not redeemable and distributions received are generally the result of liquidation of the underlying assets of the partnerships. The term of Jackson's interest in the partnerships is generally ten years, but may be extended for a period of time under provisions within the partnership agreements, if applicable. The Company generally has the ability under the partnership agreements to sell its interest to another limited partner with the prior written consent of the general partner. It is not probable that Jackson will sell a limited partnership interest for an amount different from its NAV equivalent.

Cash and Cash Equivalents

Cash and cash equivalents primarily include money market instruments and bank deposits. Certain money market instruments are valued using unadjusted quoted prices in active markets and are classified as Level 1.

Receivables from Affiliates

The Company's receivables from affiliates are set equal to the carrying value and are classified as Level 3.

Separate Account Assets and Liabilities

Separate account assets are comprised of investments in mutual funds that transact regularly, but do not trade in active markets as they are not publically available, and are categorized as Level 2 assets. The values of separate account liabilities are set equal to the values of separate account assets.

Other Contract Holder Funds

Fair values for immediate annuities without mortality features are derived by discounting the future estimated cash flows using current market interest rates for similar maturities. Fair values for deferred annuities, including fixed index annuities, are determined using projected future cash flows discounted at current market interest rates.

The fair value of the fixed index annuities embedded option, incorporating such factors as the volatility of returns, the level of interest rates and the time remaining until the option expires, is calculated using the closed form Black-Scholes Option Pricing model or Monte Carlo simulations, as appropriate for the type of option. Additionally, assumed withdrawal rates are used to estimate the expected volume of embedded options that will be realized by policyholders.

Fair values for guaranteed investment contracts are based on the present value of future cash flows discounted at current market interest rates.

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Fair values for trust instruments supported by funding agreements are based on the present value of future cash flows discounted at current market interest rates, plus the fair value of any embedded derivatives that are not required to be reported separately.

Fair values of the FHLBI funding agreements are based on the present value of future cash flows discounted at current market interest rates.

Funds Held Under Reinsurance Treaties

The fair value of the funds held is equal to the fair value of the assets held as collateral, which primarily consist of policy loans and fixed maturities.

Debt

Fair values for the Company's surplus notes and other long-term debt are generally determined by prices obtained from independent broker dealers or discounted cash flow models. Such prices are derived from market observable inputs and are classified as Level 2. The Squire Surplus Note is set equal to the carrying value and is classified as Level 3.

Securities Lending Payable

The Company's securities lending payable is set equal to the cash collateral received. Due to the short-term nature of the loans, carrying value is a reasonable estimate of fair value and is classified as Level 2.

Repurchase Agreements

Carrying value of the Company's repurchase agreements, which are included in other liabilities, is considered a reasonable estimate of fair value due to their short-term maturities and are classified as Level 2.

Federal Home Loan Bank Advances

Carrying value of the Company's Federal Home Loan Bank advances, which are included in other liabilities, is considered a reasonable estimate of fair value due to their short-term maturities and are classified as Level 2.

Certain Guaranteed Benefits

Variable annuity contracts issued by the Company offer various guaranteed minimum death, withdrawal, income and accumulation benefits. Certain benefits, primarily non-life contingent components of guaranteed minimum withdrawal benefits ("GMWB"), guaranteed minimum accumulation benefits ("GMAB") and the reinsurance recoverable on the Company's guaranteed minimum income benefits ("GMIB"), are recorded at fair value. Guaranteed benefits that are not subject to fair value accounting are accounted for as insurance benefits.

Non-life contingent components of GMWBs and GMABs are recorded at fair value with changes in fair value recorded in other net investment losses. The fair value of the reserve is based on the expectations of future benefit payments and certain future fees associated with the benefits. At the inception of the contract, the Company attributes to the embedded derivative a portion of total fees collected from the contract holder, which is then held static in future valuations. Those fees, generally referred to as the attributed fees, are set such that the present value of the attributed fees is equal to the present value of future claims expected to be paid under the guaranteed benefit at the inception of the contract. In subsequent valuations, both the present value of future benefits and the present value of attributed fees are revalued based on current market conditions and policyholder behavior assumptions. The difference between each of the two components represents the fair value of the embedded derivative. Jackson discontinued offering the GMAB in 2011.

Jackson's GMIB book is reinsured through an unrelated party and, due to the net settlement provisions of the reinsurance agreement, this contract meets the definition of a derivative. Accordingly, the GMIB reinsurance agreement is recorded at fair value, with changes in fair value recorded in other net investment losses. Due to the inability to economically reinsure or hedge new issues of the GMIB, the Company discontinued offering the benefit in 2009.

Fair values for GMWB and GMAB embedded derivatives, as well as GMIB reinsurance recoverables, are calculated using internally developed models because active, observable markets do not exist for those guaranteed benefits.

The fair value calculation is based on the present value of future cash flows comprised of future expected benefit payments, less future attributed rider fees, over the lives of the contracts. Estimating these cash flows requires numerous estimates and subjective judgments related to capital market inputs, as well as actuarially determined assumptions related

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to expectations concerning policyholder behavior. Capital market inputs include expected market rates of return, market volatility, correlations of market index returns to funds, fund performance and discount rates. The more significant actuarial assumptions include benefit utilization by policyholders under varying conditions, fund allocation, persistency, mortality, and withdrawal rates. Best estimate assumptions plus risk margins are used as applicable.

At each valuation date, the Company assumes expected returns based on the greater of LIBOR swap rates and constant maturity treasury rates as of that date to determine the value of expected future cash flows produced in a stochastic process. Volatility assumptions are based on a weighting of available market data for implied market volatility for durations up to 10 years, grading to a historical volatility level by year 15, where such long-term historical volatility levels contain an explicit risk margin. Additionally, non-performance risk is incorporated into the calculation through the use of discount rates based on a AA corporate credit curve as an approximation of Jackson's own credit risk. Risk margins are also incorporated into the model assumptions, particularly for policyholder behavior. Estimates of future policyholder behavior are subjective and are based primarily on the Company's experience.

As markets change, mature and evolve and actual policyholder behavior emerges, management continually evaluates the appropriateness of its assumptions for this component of the fair value model.

The use of the models and assumptions described above requires a significant amount of judgment. Management believes the aggregation of each of these components results in an amount that the Company would be required to transfer for a liability, or receive for an asset, to or from a willing buyer or seller, if one existed, for those market participants to assume the risks associated with the guaranteed benefits and the related reinsurance. However, the ultimate settlement amount of the asset or liability, which is currently unknown, could likely be significantly different than this fair value.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following tables summarize the Company's assets and liabilities that are carried at fair value by hierarchy levels (in thousands):

	December 31, 2017			
	Total	Level 1	Level 2	Level 3
Assets				
Fixed maturities				
U.S. government securities	\$ 5,684,673	\$ 5,684,673	\$ -	\$ -
Other government securities	854,565	-	854,565	-
Public utilities	4,763,133	-	4,763,133	-
Corporate securities	31,830,310	-	31,830,310	-
Residential mortgage-backed	913,402	-	913,400	2
Commercial mortgage-backed	2,112,529	-	2,112,529	-
Other asset-backed securities	1,298,542	-	1,298,542	-
Trading securities	137,756	125,434	12,211	111
Policy loans	3,397,764	-	-	3,397,764
Derivative instruments	2,178,969	-	2,173,038	5,931
GMIB reinsurance recoverable	252,138	-	-	252,138
Separate account assets	176,578,848	-	176,578,848	-
Total	<u>\$ 230,002,629</u>	<u>\$ 5,810,107</u>	<u>\$ 220,536,576</u>	<u>\$ 3,655,946</u>
Liabilities				
Embedded derivative liabilities ⁽¹⁾	\$ 2,896,141	\$ -	\$ 1,184,999	\$ 1,711,142
Funds held under reinsurance treaties	3,604,525	-	-	3,604,525
Derivative instruments	6,448	-	6,448	-
Total	<u>\$ 6,507,114</u>	<u>\$ -</u>	<u>\$ 1,191,447</u>	<u>\$ 5,315,667</u>

⁽¹⁾ Includes the embedded derivative liabilities related to GMWB reserves and fixed index annuities.

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	December 31, 2016			
	Total	Level 1	Level 2	Level 3
Assets				
Fixed maturities				
U.S. government securities	\$ 6,287,550	\$ 6,287,550	\$ -	\$ -
Other government securities	945,729	-	945,729	-
Public utilities	4,711,019	-	4,711,019	-
Corporate securities	32,701,036	-	32,701,036	-
Residential mortgage-backed	1,268,539	-	1,268,535	4
Commercial mortgage-backed	2,729,392	-	2,729,392	-
Other asset-backed securities	1,295,486	-	1,295,486	-
Trading securities	415,122	139,930	275,081	111
Policy loans	3,301,038	-	-	3,301,038
Derivative instruments	1,030,133	-	1,011,163	18,970
GMB reinsurance recoverable	304,927	-	-	304,927
Separate account assets	148,791,796	-	148,791,796	-
Total	<u>\$ 203,781,767</u>	<u>\$ 6,427,480</u>	<u>\$ 193,729,237</u>	<u>\$ 3,625,050</u>
Liabilities				
Embedded derivative liabilities ⁽¹⁾	\$ 3,363,639	\$ -	\$ 1,075,766	\$ 2,287,873
Funds held under reinsurance treaties	3,523,106	-	-	3,523,106
Derivative instruments	78,802	-	78,802	-
Total	<u>\$ 6,965,547</u>	<u>\$ -</u>	<u>\$ 1,154,568</u>	<u>\$ 5,810,979</u>

⁽¹⁾ Includes the embedded derivative liabilities related to GMWB reserves and fixed index annuities.

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Assets and Liabilities Measured at Fair Value Using Significant Unobservable Inputs (Level 3)

Level 3 Assets and Liabilities by Price Source

The table below presents the balances of Level 3 assets and liabilities measured at fair value with their corresponding pricing sources (in thousands).

	December 31, 2017		
	Total	Internal	External
Assets			
Fixed Maturities			
Residential mortgage-backed	\$ 2	\$ 2	\$ -
Trading securities	111	111	-
Policy loans	3,397,764	3,397,764	-
Derivative instruments	5,931	-	5,931
GMIB reinsurance recoverable	252,138	252,138	-
Total	<u>\$ 3,655,946</u>	<u>\$ 3,650,015</u>	<u>\$ 5,931</u>
Liabilities			
Embedded derivative liabilities ⁽¹⁾	\$ 1,711,142	\$ 1,711,142	\$ -
Funds held under reinsurance treaties	3,604,525	3,604,525	-
Total	<u>\$ 5,315,667</u>	<u>\$ 5,315,667</u>	<u>\$ -</u>
	December 31, 2016		
	Total	Internal	External
Assets			
Fixed Maturities			
Residential mortgage-backed	\$ 4	\$ 4	\$ -
Trading securities	111	111	-
Policy loans	3,301,038	3,301,038	-
Derivative instruments	18,970	-	18,970
GMIB reinsurance recoverable	304,927	304,927	-
Total	<u>\$ 3,625,050</u>	<u>\$ 3,606,080</u>	<u>\$ 18,970</u>
Liabilities			
Embedded derivative liabilities ⁽¹⁾	\$ 2,287,873	\$ 2,287,873	\$ -
Funds held under reinsurance treaties	3,523,106	3,523,106	-
Total	<u>\$ 5,810,979</u>	<u>\$ 5,810,979</u>	<u>\$ -</u>

⁽¹⁾ Includes the embedded derivatives related to GMWB reserves.

External pricing sources for securities represent unadjusted prices from independent pricing services and independent indicative broker quotes where pricing inputs are not readily available.

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Quantitative Information Regarding Internally-Priced Level 3 Assets and Liabilities

The table below presents quantitative information on significant internally-priced Level 3 assets and liabilities (in thousands):

December 31, 2017					
	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range in bps (Weighted Average)	Impact of Increase in Input on Fair Value
Assets					
Policy loans	\$ 3,397,764	Outstanding balance	N/A	N/A	N/A
GMB reinsurance recoverable	252,138	Discounted cash flow	See below	See below	See below
Total	<u>\$ 3,649,902</u>				
Liabilities					
Embedded derivative liabilities	\$ 1,711,142	Discounted cash flow	See below	See below	See below
Funds held under reinsurance treaties	3,604,525	Carrying value of asset	N/A	N/A	N/A
Total	<u>\$ 5,315,667</u>				
December 31, 2016					
	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range in bps (Weighted Average)	Impact of Increase in Input on Fair Value
Assets					
Policy loans	\$ 3,301,038	Outstanding balance	N/A	N/A	N/A
GMB reinsurance recoverable	304,927	Discounted cash flow	See below	See below	See below
Total	<u>\$ 3,605,965</u>				
Liabilities					
Embedded derivative liabilities	\$ 2,287,873	Discounted cash flow	See below	See below	See below
Funds held under reinsurance treaties	3,523,106	Carrying value of asset	N/A	N/A	N/A
Total	<u>\$ 5,810,979</u>				

Sensitivity to Changes in Unobservable Inputs

The following is a general description of sensitivities of significant unobservable inputs and their impact on the fair value measurement for the assets and liabilities reflected in the table above.

As of December 31, 2017 and 2016, securities of \$113 thousand and \$115 thousand, respectively, are fair valued using techniques incorporating unobservable inputs and are classified in Level 3 of the fair value hierarchy. For these assets, their unobservable inputs and ranges of possible inputs do not materially affect their fair valuations and have been excluded from the quantitative information in the table above.

The GMB reinsurance recoverable fair value calculation is based on the present value of future cash flows comprised of future expected reinsurance benefit receipts, less future attributed premium payments to reinsurers, over the lives of the contracts. Estimating these cash flows requires actuarially determined assumptions related to expectations concerning policyholder behavior and long-term market volatility. The more significant policyholder behavior actuarial assumptions include benefit utilization, fund allocation, persistency, and mortality. In general, an increase (decrease) in assumed benefit utilization would increase (decrease) the fair value of the reinsurance recoverable; an increase (decrease) in allocation to equity funds would increase (decrease) the fair value of the reinsurance recoverable; an increase (decrease) in assumed persistency would increase (decrease) the fair value of the reinsurance recoverable; an increase (decrease) in assumed mortality would decrease (increase) the fair value of the reinsurance recoverable; and an increase (decrease) in long-term market volatility would increase (decrease) the fair value of the reinsurance recoverable.

Embedded derivative liabilities classified in Level 3 represent the fair value of GMWB and GMAB liabilities. These fair value calculations are based on the present value of future cash flows comprised of future expected benefit payments, less future attributed rider fees, over the lives of the contracts. Estimating these cash flows requires actuarially determined assumptions related to expectations concerning policyholder behavior and long-term market volatility. The more significant policyholder behavior actuarial assumptions include benefit utilization, fund allocation, persistency, and mortality. In general, an increase (decrease) in assumed benefit utilization would increase (decrease) the fair value of the

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liabilities; an increase (decrease) in allocation to equity funds would increase (decrease) the fair value of the liabilities; an increase (decrease) in assumed persistency would increase (decrease) the fair value of the liabilities; an increase (decrease) in assumed mortality would decrease (increase) the fair value of the liabilities; and an increase (decrease) in long-term market volatility would increase (decrease) the fair value of the liabilities.

The tables below provide rollforwards for 2017 and 2016 of the financial instruments for which significant unobservable inputs (Level 3) are used in the fair value measurement. Gains and losses in the table below include changes in fair value due partly to observable and unobservable factors. The Company utilizes derivative instruments to manage the risk associated with certain assets and liabilities. However, the derivative instruments hedging the related risks may not be classified within the same fair value hierarchy level as the associated assets and liabilities. Therefore, the impact of the derivative instruments reported in Level 3 may vary significantly from the total income effect of the hedged instruments. Additionally, the Company's policy for determining and disclosing transfers between levels is to recognize transfers using beginning of period balances.

	Total Realized/Unrealized Gains (Losses) Included in					
	Fair Value as of January 1, 2017	Net Income	Other Comprehensive Income	Purchases, Sales, Issuances and Settlements	Transfers in and/or (out of) Level 3	Fair Value as of December 31, 2017
(in thousands)						
Assets						
Fixed maturities						
Residential mortgage-backed	\$ 4	\$ -	\$ -	\$ (2)	\$ -	\$ 2
Other asset-backed securities	-	8	-	(8)	-	-
Trading securities	111	-	-	-	-	111
Policy loans	3,301,038	(3,689)	-	100,415	-	3,397,764
Derivative instruments	18,970	(53,334)	-	40,295	-	5,931
GMB reinsurance recoverable	304,927	(52,789)	-	-	-	252,138
Liabilities						
Embedded derivative liabilities ⁽¹⁾	\$ (2,287,873)	\$ 576,731	\$ -	\$ -	\$ -	\$ (1,711,142)
Funds held under reinsurance treaties	(3,523,106)	2,508	237	(84,164)	-	(3,604,525)

	Total Realized/Unrealized Gains (Losses) Included in					
	Fair Value as of January 1, 2016	Net Income	Other Comprehensive Income	Purchases, Sales, Issuances and Settlements	Transfers in and/or (out of) Level 3	Fair Value as of December 31, 2016
(in thousands)						
Assets						
Fixed maturities						
Residential mortgage-backed	\$ 7	\$ 33	\$ -	\$ (36)	\$ -	\$ 4
Commercial mortgage-backed	186	5,441	(186)	(5,441)	-	-
Other asset-backed securities	6,450	-	-	-	(6,450)	-
Trading securities	33,448	-	-	(33,337)	-	111
Policy loans	3,216,123	2,921	-	81,994	-	3,301,038
Derivative instruments	97,352	(117,105)	-	38,723	-	18,970
GMB reinsurance recoverable	329,753	(24,826)	-	-	-	304,927
Liabilities						
Embedded derivative liabilities ⁽¹⁾	\$ (2,184,096)	\$ (103,777)	\$ -	\$ -	\$ -	\$ (2,287,873)
Funds held under reinsurance treaties	(3,459,645)	(2,975)	(1,846)	(58,640)	-	(3,523,106)

⁽¹⁾ Includes the embedded derivative related to GMWB reserves.

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The components of the amounts included in purchases, sales, issuances, and settlements for years ended December 31, 2017 and 2016 shown above are as follows (in thousands):

	December 31, 2017				
	Purchases	Sales	Issuances	Settlements	Total
Assets					
Fixed maturities					
Residential mortgage-backed	\$ -	\$ (2)	\$ -	\$ -	\$ (2)
Other asset-backed securities	-	(8)	-	-	(8)
Policy loans	-	-	303,216	(202,801)	100,415
Derivative instruments	40,295	-	-	-	40,295
Total	<u>\$ 40,295</u>	<u>\$ (10)</u>	<u>\$ 303,216</u>	<u>\$ (202,801)</u>	<u>\$ 140,700</u>
Liabilities					
Funds held under reinsurance treaties	\$ -	\$ -	\$ (400,433)	\$ 316,269	\$ (84,164)
	December 31, 2016				
	Purchases	Sales	Issuances	Settlements	Total
Assets					
Fixed maturities					
Residential mortgage-backed	\$ -	\$ (36)	\$ -	\$ -	\$ (36)
Commercial mortgage-backed	-	(5,441)	-	-	(5,441)
Trading securities	-	(33,337)	-	-	(33,337)
Policy loans	-	-	248,471	(166,477)	81,994
Derivative instruments	39,573	(850)	-	-	38,723
Total	<u>\$ 39,573</u>	<u>\$ (39,664)</u>	<u>\$ 248,471</u>	<u>\$ (166,477)</u>	<u>\$ 81,903</u>
Liabilities					
Funds held under reinsurance treaties	\$ -	\$ -	\$ (409,532)	\$ 350,892	\$ (58,640)

There were no transfers from Level 3 to Level 2 of the fair value hierarchy during 2017. In 2016, \$6.4 million was transferred from level 3 to Level 2 as a result of the Company being able to obtain pricing from an independent pricing service utilizing significant observable inputs. There were no transfers from Level 2 to Level 3 during 2017 and 2016. There were no transfers between Level 1 and 2 of the fair value hierarchy in 2017 or 2016.

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The portion of gains (losses) included in net income or other comprehensive income attributable to the change in unrealized gains and losses on Level 3 financial instruments still held at December 31, 2017 and 2016 was as follows (in thousands):

	<u>2017</u>	<u>2016</u>
Assets		
Derivative instruments	\$ (34,364)	\$ (73,175)
GMB reinsurance recoverable	(52,789)	(24,826)
Liabilities		
Embedded derivative liabilities	\$ 576,731	\$ (103,777)
Funds held under reinsurance treaties	237	(1,846)

Fair Value of Financial Instruments Carried at Other Than Fair Value

The table below presents the carrying amount and fair value by fair value hierarchy level of certain financial instruments that are not reported at fair value (in thousands).

	Fair Value Hierarchy Level	<u>December 31, 2017</u>		<u>December 31, 2016</u>	
		Carrying Value	Fair Value	Carrying Value	Fair Value
Assets					
Commercial mortgage loans	Level 3	\$ 8,435,440	\$ 8,554,827	\$ 7,482,233	\$ 7,555,143
Policy loans	Level 3	1,193,368	1,193,368	1,245,123	1,245,123
Receivables from affiliates	Level 3	312,049	312,049	344,100	344,100
Liabilities					
Other contract holder funds					
Annuity reserves ⁽¹⁾	Level 3	\$ 36,042,474	\$ 43,260,734	\$ 37,999,861	\$ 42,865,834
Reserves for guaranteed investment contracts	Level 3	1,698,178	1,699,627	1,875,816	1,876,930
Trust instruments supported by funding agreements	Level 3	5,752,078	5,841,278	3,836,441	3,879,525
Federal Home Loan Bank funding agreements	Level 3	1,934,690	1,947,151	1,784,040	1,782,493
Debt - Squire Surplus Note	Level 3	310,776	310,776	344,000	344,000
Debt - all other	Level 2	336,942	415,546	341,949	422,461
Securities lending payable	Level 2	69,785	69,785	119,608	119,608
Repurchase agreements	Level 2	-	-	411,857	411,857
Federal Home Loan Bank advances	Level 2	600,071	600,071	500,071	500,071
Separate account liabilities ⁽²⁾	Level 2	176,578,848	176,578,848	148,791,796	148,791,796

⁽¹⁾ Annuity reserves represent only the components of other contract holder funds that are considered to be financial instruments.

⁽²⁾ The values of separate account liabilities are set equal to the values of separate account assets.

Fair Value Option

The Company elected the fair value option for certain assets, which are held as collateral for reinsurance. Accordingly, the Company established a funds held liability, for which the Company also elected the fair value option. The value of the funds held liability is equal to the fair value of the assets held as collateral. The income and any changes in unrealized gains and losses on these assets and the corresponding funds held liability are included in net investment income and have no impact on the Company's consolidated income statements. Income and changes in unrealized gains and losses on other assets for which the Company has elected the fair value option are immaterial to the Company's consolidated financial statements.

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6. Deferred Acquisition Costs and Deferred Sales Inducements

The balances of and changes in deferred acquisition costs, as of and for the years ended December 31, were as follows (in thousands):

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Balance, beginning of year	\$ 9,678,063	\$ 8,438,804	\$ 7,455,336
Deferrals of acquisition costs	839,143	903,479	1,102,213
Amortization related to:			
Operations	(475,587)	(511,028)	(711,391)
Derivatives	579,923	793,306	171,657
Net realized losses (gains)	3,965	(26,981)	(7,972)
Total amortization	<u>108,301</u>	<u>255,297</u>	<u>(547,706)</u>
Unrealized investment (gains) losses	<u>(84,919)</u>	<u>80,483</u>	<u>428,961</u>
Balance, end of year	<u>\$ 10,540,588</u>	<u>\$ 9,678,063</u>	<u>\$ 8,438,804</u>

The balances of and changes in deferred sales inducements, which are reported in other assets, as of and for the years ended December 31, were as follows (in thousands):

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Balance, beginning of year	\$ 696,636	\$ 754,690	\$ 768,272
Deferrals of sales inducements	14,877	19,978	24,584
Amortization related to:			
Operations	(64,178)	(112,698)	(108,127)
Derivatives	13,483	21,618	(3,727)
Net realized losses (gains)	625	(4,365)	(1,300)
Total amortization	<u>(50,070)</u>	<u>(95,445)</u>	<u>(113,154)</u>
Unrealized investment (gains) losses	<u>(17,437)</u>	<u>17,413</u>	<u>74,988</u>
Balance, end of year	<u>\$ 644,006</u>	<u>\$ 696,636</u>	<u>\$ 754,690</u>

7. 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 Company reinsures certain of its risks to other reinsurers under a coinsurance, modified coinsurance, yearly renewable term, or, with Brooke Life, a monthly renewable term basis. The Company regularly monitors the financial strength rating of its reinsurers.

The Company has also acquired certain lines of business that are 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.

Jackson's GMIBs are reinsured with an unrelated party and, due to the net settlement provisions of the reinsurance agreement, meet the definition of a derivative. Accordingly, the GMIB reinsurance agreement is recorded at fair value on the Company's consolidated balance sheets, with changes in fair value recorded in other net investment losses. GMIB reinsured benefits are subject to aggregate annual claim limits. Deductibles also apply on reinsurance of GMIB business issued since March 1, 2005.

The Company has three retro treaties with SRZ. Pursuant to these retro treaties, the Company ceded to SRZ on a 100% coinsurance basis, subject to pre-existing reinsurance with other parties, certain blocks of business. These blocks of business include disability income and accident and health business, a mix of life and annuity insurance business, and corporate owned life insurance business.

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Pursuant to the retro treaties, the Company holds certain assets, primarily policy loans and fixed maturities, as collateral. This collateral is reported as a liability as funds held under reinsurance treaties on the consolidated balance sheets. This funds held liability was \$3.6 billion and \$3.5 billion at December 31, 2017 and 2016, respectively.

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

	Years Ended December 31,		
	2017	2016	2015
Direct premium:			
Life	\$ 518,819	\$ 578,120	\$ 600,689
Accident and health	49,180	54,900	60,002
Plus reinsurance assumed:			
Life	68,290	56,559	59,069
Accident and health	8,098	9,246	10,514
Less reinsurance ceded:			
Life	(402,803)	(388,949)	(376,283)
Annuity guaranteed benefits	(15,227)	(16,119)	(17,066)
Accident and health	(57,278)	(64,146)	(70,516)
Total premium	<u>\$ 169,079</u>	<u>\$ 229,611</u>	<u>\$ 266,409</u>

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

	Years Ended December 31,		
	2017	2016	2015
Direct benefits:			
Life	\$ 1,261,108	\$ 1,331,018	\$ 1,351,975
Accident and health	132,471	126,525	134,447
Annuity guaranteed benefits	101,326	123,629	93,473
Plus reinsurance assumed:			
Life	248,917	228,129	248,217
Accident and health	26,731	28,136	31,444
Less reinsurance ceded:			
Life	(576,447)	(534,486)	(574,634)
Accident and health	(159,202)	(154,661)	(165,891)
Deferral of contract enhancements	(4,382)	(7,669)	(11,970)
Change in reserves, net of reinsurance	97,818	(140,341)	(109,315)
Total benefits	<u>\$ 1,128,340</u>	<u>\$ 1,000,280</u>	<u>\$ 997,746</u>

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Components of the Company's reinsurance recoverable were as follows (in thousands):

	December 31,	
	2017	2016
Reserves:		
Life	\$ 6,668,525	\$ 6,798,865
Accident and health	600,119	604,827
Guaranteed minimum income benefits	252,138	304,927
Other annuity benefits	207,016	217,361
Claims liability	965,930	994,554
Other	8,362	7,025
Total	<u>\$ 8,702,090</u>	<u>\$ 8,927,559</u>

Included in the reinsurance recoverable were reserves ceded to Brooke Life of \$38.0 million and \$39.4 million at December 31, 2017 and 2016, respectively. At December 31, 2017, the largest amount ceded to any reinsurer totaled \$6.2 billion, which was primarily related to the retro treaties, which are fully collateralized.

The following table sets forth the Company's net life insurance in-force (in millions):

	December 31,	
	2017	2016
Direct life insurance in-force	\$ 188,920	\$ 213,022
Amounts assumed from other companies	20,174	21,288
Amounts ceded to other companies	(131,305)	(145,500)
Net life insurance in-force	<u>\$ 77,789</u>	<u>\$ 88,810</u>

8. Reserves for Future Policy Benefits and Claims Payable and Other Contract Holder Funds

The following table sets forth the Company's reserves for future policy benefits and claims payable balances (in thousands):

	December 31,	
	2017	2016
Traditional life	\$ 5,500,369	\$ 5,876,822
Guaranteed benefits	3,925,663	4,214,555
Claims payable	915,761	933,799
Accident and health	1,362,054	1,394,669
Other	1,010,687	1,048,104
Total	<u>\$ 12,714,534</u>	<u>\$ 13,467,949</u>

For traditional life insurance contracts, which include term and whole life, reserves are determined using the net level premium method and assumptions as of the issue date or acquisition date as to mortality, interest rates, persistency and expenses, plus provisions for adverse deviation. These assumptions are not unlocked unless the reserve is determined to be deficient.

The Company's liability for future policy benefits also includes liabilities for guaranteed benefits related to certain nontraditional long-duration life and annuity contracts, which are further discussed in Note 9.

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The following table sets forth the Company's liabilities for other contract holder funds balances (in thousands):

	December 31,	
	2017	2016
Interest-sensitive life	\$ 12,778,982	\$ 12,964,116
Variable annuity fixed option	8,334,585	9,278,095
Fixed annuity	18,304,874	18,922,387
Fixed index annuity	11,939,212	12,203,448
GICs, funding agreements and FHLB advances	9,384,946	7,496,297
Total	\$ 60,742,599	\$ 60,864,343

For interest-sensitive life contracts, liabilities approximate the policyholder's account value, plus the remaining balance of the fair value adjustment related to previously acquired business, which is further discussed below. The liability for fixed index annuities is based on three components, 1) the imputed value of the underlying guaranteed host contract, 2) the fair value of the embedded option component of the contract, and 3) the liability for guaranteed benefits related to the optional lifetime income rider. For fixed annuities and other investment contracts, as detailed in the above table, the liability is the policyholder's account value, plus the unamortized balance of the fair value adjustment related to previously acquired business. At December 31, 2017, the Company had interest sensitive life business with minimum guaranteed interest rates ranging from 2.5% to 6.0%, with a 4.67% average guaranteed rate and fixed interest rate annuities with minimum guaranteed rates ranging from 1.0% to 5.5% and a 2.36% average guaranteed rate.

The Company recorded a fair value adjustment related to certain annuity and interest sensitive liability blocks of business to reflect the cost of the interest guarantees within the inforce liabilities, based on the difference between the guaranteed interest rate and an assumed new money guaranteed interest rate. This adjustment was recorded in reserves for future policy benefits and claims payable. This component of the reserve is reassessed at the end of each period, taking into account changes in the inforce block. Any resulting change in the reserve is recorded as a change in reserve through the consolidated income statements.

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At both December 31, 2017 and 2016, approximately 88% of the Company's fixed interest rate annuity account values correspond to crediting rates that are at the minimum guaranteed interest rates. The following tables show the distribution of the fixed interest rate annuities' account values within the presented ranges of minimum guaranteed interest rates (in millions):

Minimum Guaranteed Interest Rate	December 31, 2017			
	Account Value			
	Fixed	Fixed Index	Variable	Total
1.0%	\$ 3,158.1	\$ 1,892.9	\$ 4,263.4	\$ 9,314.4
>1.0% - 2.0%	1,033.4	6,969.5	1,970.6	9,973.5
>2.0% - 3.0%	8,141.8	3,076.8	1,749.7	12,968.3
>3.0% - 4.0%	1,720.8	-	-	1,720.8
>4.0% - 5.0%	2,359.5	-	-	2,359.5
>5.0% - 5.5%	297.7	-	-	297.7
Total	<u>\$ 16,711.3</u>	<u>\$ 11,939.2</u>	<u>\$ 7,983.7</u>	<u>\$ 36,634.2</u>

Minimum Guaranteed Interest Rate	December 31, 2016			
	Account Value			
	Fixed	Fixed Index	Variable	Total
1.0%	\$ 2,916.8	\$ 1,912.8	\$ 4,763.6	\$ 9,593.2
>1.0% - 2.0%	1,136.1	7,011.2	2,606.3	10,753.6
>2.0% - 3.0%	8,712.6	3,279.4	1,609.2	13,601.2
>3.0% - 4.0%	1,799.7	-	-	1,799.7
>4.0% - 5.0%	2,414.6	-	-	2,414.6
>5.0% - 5.5%	304.7	-	-	304.7
Total	<u>\$ 17,284.5</u>	<u>\$ 12,203.4</u>	<u>\$ 8,979.1</u>	<u>\$ 38,467.0</u>

At both December 31, 2017 and 2016, approximately 81% of the Company's interest sensitive life business account values correspond to crediting rates that are at the minimum guaranteed interest rates. The following table shows the distribution of the interest sensitive life business account values within the presented ranges of minimum guaranteed interest rates, excluding the business that is subject to the previously mentioned retro treaties (in millions):

Minimum Guaranteed Interest Rate	Account Value - Interest Sensitive Life	
	December 31,	
	2017	2016
>2.0% - 3.0%	\$ 299.2	\$ 299.7
>3.0% - 4.0%	3,166.9	3,305.8
>4.0% - 5.0%	2,785.6	2,882.5
>5.0% - 6.0%	2,233.1	2,272.4
Subtotal	<u>8,484.8</u>	<u>8,760.4</u>
Retro treaties	4,294.2	4,203.7
Total	<u>\$ 12,779.0</u>	<u>\$ 12,964.1</u>

The Company has established a European Medium Term Note program, with up to \$5.8 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 Medium Term Note 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, 2017 and 2016 totaled \$25.6 million and \$3.7 million, respectively.

The Company has established a \$17.0 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 Medium Term Note 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, 2017 and 2016 totaled \$5.7 billion and \$3.8 billion, respectively.

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Those Medium Term Note instruments issued 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 unrealized 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 translation gains and losses using exchange rates as of the reporting date. Foreign currency translation gains and losses are included in other net investment losses.

Jackson and Squire Re are members of the FHLBI primarily for the purpose of participating in the bank's mortgage-collateralized loan advance program with short-term and long-term funding facilities. Advances are in the form of short-term or long-term notes or funding agreements issued to FHLBI. At both December 31, 2017 and 2016, the Company held \$125.4 million of FHLBI capital stock, supporting \$2.6 billion and \$2.4 billion in funding agreements, short-term and long-term borrowing capacity in 2017 and 2016, respectively.

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 account adjusted for any partial withdrawals, b) total deposits made to the account adjusted for any partial withdrawals plus a minimum return, or c) the highest account 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 (GMDB), at annuitization (GMIB), upon the depletion of funds (GMWB) or at the end of a specified period (GMAB).

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 separate account liabilities. Liabilities for guaranteed benefits are general account obligations and are reported in reserves for future policy benefits and claims payable. Amounts assessed against the contract holders for mortality, administrative, and other services are reported in revenue as fee income. Changes in liabilities for minimum guarantees are reported within death, other policy benefits and change in policy reserves within the consolidated income statements with the exception of changes in embedded derivatives, which are included in other net investment losses. Separate account net investment income, net investment realized and unrealized gains and losses, and the related liability changes are offset within the same line item in the consolidated income statements.

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At December 31, 2017 and 2016, the Company provided variable annuity contracts with guarantees, for which the net amount at risk ("NAR") is defined as the amount of guaranteed benefit in excess of current account value, as follows (dollars in millions):

December 31, 2017	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	0-6%	\$ 135,890.3	\$ 2,251.9	66.0 years	
GMWB - Premium only	0%	2,885.7	27.2		
GMWB	0-5%*	318.0	18.2		
GMAB - Premium only	0%	51.3	-		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		12,309.0	129.7	66.5 years	
GMWB - Highest anniversary only		3,310.1	68.4		
GMWB		902.9	64.1		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0-6%	7,703.2	576.2	69.0 years	
GMIB	0-6%	2,007.1	590.3		0.4 years
GMWB	0-8%*	126,118.1	5,942.3		
December 31, 2016					
Return of net deposits plus a minimum return					
GMDB	0-6%	\$ 115,553.0	\$ 3,067.9	65.6 years	
GMWB - Premium only	0%	2,740.0	48.5		
GMWB	0-5%*	316.4	27.7		
GMAB - Premium only	0%	53.9	0.1		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		10,872.2	427.7	66.0 years	
GMWB - Highest anniversary only		3,063.6	154.8		
GMWB		923.0	102.5		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0-6%	6,560.2	864.1	68.7 years	
GMIB	0-6%	1,970.7	734.6		0.5 years
GMWB	0-8%*	105,531.4	11,483.7		

* Ranges shown based on simple interest. The upper limits of 5% or 8% simple interest are approximately equal to 4.1% and 6%, respectively, on a compound interest basis over a typical 10-year bonus period.

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Amounts shown as GMWB above include a ‘not-for-life’ component up to the point at which the guaranteed withdrawal benefit is exhausted, after which benefits paid are considered to be ‘for-life’ benefits. The liability related to this ‘not-for-life’ portion is valued as an embedded derivative, while the ‘for-life’ benefits are valued as an insurance liability (see below). For this table, the net amount at risk of the ‘not-for-life’ component is the undiscounted excess of the guaranteed withdrawal benefit over the account value, and that of the ‘for-life’ component is the estimated value of additional life contingent benefits paid after the guaranteed withdrawal benefit is exhausted.

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

	December 31,	
Fund type:	2017	2016
Equity	\$ 109,363.9	\$ 90,737.7
Bond	18,907.3	18,590.2
Balanced	26,855.4	21,551.2
Money market	921.6	1,228.1
Total	\$ 156,048.2	\$ 132,107.2

GMDB liabilities reflected in the general account were as follows (in millions):

	2017	2016
Balance at January 1	\$ 858.3	\$ 855.1
Incurred guaranteed benefits	286.1	115.9
Paid guaranteed benefits	(93.0)	(112.7)
Balance at December 31	\$ 1,051.4	\$ 858.3

The GMDB liability is determined by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. The Company regularly evaluates estimates used and adjusts the liability balance through the consolidated income statement, within death, other policy benefits and change in policy reserves, 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 both December 31, 2017 and 2016 (except where otherwise noted):

- 1) Use of a series of stochastic investment performance scenarios, based on historical average market volatility.
- 2) Mean investment performance assumption of 7.4% after investment management fees, but before investment advisory fees and mortality and expense charges.
- 3) Mortality equal to 23% to 100% of the Annuity 2000 table (2016: 36% to 100%).
- 4) Lapse rates varying by contract type, duration and degree the benefit is in-the-money and ranging from 0.4% to 27.9% (before application of dynamic adjustments).
- 5) Discount rates: 7.4% on 2013 and later issues, 8.4% on 2012 and prior issues.

Most GMWB reserves are considered to be derivatives under current accounting guidance and are recognized at fair value, as previously defined, with the change in fair value reported in net income. The fair value of these liabilities is determined using stochastic modeling and inputs as further described in Note 5. The fair valued GMWB had a reserve liability of \$1,711.4 million and \$2,288.3 million at December 31, 2017 and 2016, respectively, and was reported in reserves for future policy benefits and claims payable.

Jackson has also issued certain GMWB products that guarantee payments over a lifetime. Reserves for the portion of these benefits after the point where the guaranteed withdrawal balance is exhausted are calculated using assumptions and methodology similar to the GMDB liability. At December 31, 2017 and 2016, these GMWB reserves totaled \$106.9 million and \$91.1 million, respectively, and were reported in reserves for future policy benefits and claims payable.

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GMAB benefits were offered on some variable annuity plans. However, the Company no longer offers these benefits. The GMAB had an asset value that was immaterial to the consolidated financial statements at both December 31, 2017 and 2016, respectively.

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 assumptions used for calculating the direct GMIB liability are consistent with those used for calculating the GMDB liability. At December 31, 2017 and 2016, GMIB reserves before reinsurance totaled \$68.6 million and \$24.2 million, respectively.

Other Liabilities – Insurance and Annuitization Benefits

The Company has established additional reserves for life insurance business for 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.

Liabilities for these benefits have been established according to the methodologies described below:

Benefit Type	December 31, 2017			December 31, 2016		
	Liability	Net Amount	Weighted	Liability	Net Amount	Weighted
	(in millions)	at Risk	Average	(in millions)	at Risk	Average
UL insurance benefit *	\$ 858.7	\$ 23,163.1	61.5 years	\$ 836.0	\$ 24,352.6	60.8 years
ISWL account balance adjustment	118.7	n/a	n/a	111.8	n/a	n/a

* Amounts for the UL benefits are for the total of the plans containing any policies having projected non-zero excess benefits and thus, may include some policies with zero projected excess benefits.

The following assumptions and methodology were used to determine the UL insurance benefit liability at December 31, 2017 and 2016:

- 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 credited interest rates, approximately 4.0% to 5.5%.

The Company also has a small closed block of two-tier annuities, where different crediting rates are used for annuitization and surrender benefit calculations. A liability is established to cover future annuitization benefits in excess of surrender values, and was immaterial to the consolidated financial statements at both December 31, 2017 and 2016. In 2015, the Company began offering an optional lifetime income rider with certain of its fixed index annuities. The liability established for this rider was \$8.2 million and \$3.0 million at December 31, 2017 and 2016.

10. Debt

The aggregate carrying value of borrowings was as follows (in thousands):

	December 31,	
	2017	2016
Surplus notes	\$ 560,297	\$ 593,488
FHLBI bank loans	87,421	92,461
Total	\$ 647,718	\$ 685,949

At December 31, 2017, the above borrowings were all due after five years.

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Surplus notes

Under Michigan Insurance Law, for statutory reporting purposes, the surplus notes are not part of the legal liabilities of the Company and are considered surplus funds. 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.

On March 15, 1997, Jackson issued 8.15% surplus notes in the principal amount of \$250.0 million due March 15, 2027. These surplus 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 and may not be redeemed at the option of the Company or any holder prior to maturity. Interest is payable semi-annually on March 15th and September 15th of each year. Interest expense on the notes was \$20.4 million in 2017, 2016, and 2015.

As described in Note 2, in conjunction with a reserve financing transaction, Squire Re II issued the Squire Surplus Note to an affiliate. The Squire Surplus Note matures December 30, 2031 and bears interest at 4.35%, payable quarterly. Interest expense on the Squire Surplus Note was \$14.0 million in 2017 and nil in 2016.

Federal Home Loan Bank Loans

The Company received loans of \$50.0 million from the FHLBI under its community investment program in both 2015 and 2014, which amortize on a straight line basis over the loan term. The weighted average interest rate on these loans was 0.94% in 2017 and 0.45% in 2016. The outstanding balance on these loans was \$87.4 million and \$92.5 million at December 31, 2017 and 2016, respectively. During 2017, 2016, and 2015, interest expense for these loans totaled \$805 thousand, \$405 thousand, and \$139 thousand, respectively. At December 31, 2017, the loans were collateralized by mortgage-related securities and commercial mortgage loans with a carrying value of \$134.2 million.

11. Federal Home Loan Bank Advances

The Company entered into a short-term advance program with the FHLBI in which interest rates were either fixed or variable based on the FHLBI cost of funds or market rates. Advances of \$600.1 million and \$500.1 million were outstanding at December 31, 2017 and 2016, respectively, and were recorded in other liabilities. The Company paid interest of \$3.4 million, \$594 thousand, and \$53 thousand on such advances in 2017, 2016, and 2015, respectively. At December 31, 2017, advances were collateralized by mortgage related securities and commercial mortgage loans with a carrying value of \$920.8 million.

12. Income Taxes

On December 22, 2017, the Tax Cuts and Jobs Act (the "Tax Act") was signed into law. The Tax Act changed many aspects of the U.S. corporate income tax system, including a reduction of the U.S. federal corporate income tax rate from 35% to 21%, effective January 1, 2018. In accordance with current U.S. GAAP, the effects of changes in tax rates and laws on deferred tax balances are to be recognized in the period in which legislation is enacted. Therefore, the Company remeasured its deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is now 21%. As a result of this reduction, the Company recognized additional tax expense of \$355.4 million in 2017, due to the rescaling of deferred tax assets and liabilities, including a benefit of \$141.0 million due to the impact of the Tax Act on deferred taxes related to unrealized holding gains and losses.

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

	Years Ended December 31,		
	2017	2016	2015
Current tax (benefit) expense	\$ (218,106)	\$ 665,086	\$ 312,638
Deferred tax expense (benefit)	525,481	(771,586)	33,701
Income tax expense (benefit)	<u>\$ 307,375</u>	<u>\$ (106,500)</u>	<u>\$ 346,339</u>

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The federal income tax provisions differ from the amounts determined by multiplying pre-tax income attributable to Jackson by the statutory federal income tax rate of 35% for 2017, 2016, and 2015 as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Income taxes at statutory rate	\$ 248,554	\$ 233,079	\$ 616,111
Dividends received deduction	(346,330)	(314,672)	(250,358)
U.S. federal tax reform impact	355,432	-	-
Provision for uncertain tax benefit	32,178	-	-
Other	17,541	(24,907)	(19,414)
Income tax expense (benefit)	<u>\$ 307,375</u>	<u>\$ (106,500)</u>	<u>\$ 346,339</u>
Effective tax rate	43.3%	-16.0%	19.7%

Federal income taxes (received) paid were \$(13.2) million, \$335.0 million, and \$766.0 million in 2017, 2016, and 2015, respectively.

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

	December 31,	
	2017	2016
Gross deferred tax asset		
Difference between financial reporting and the tax basis of:		
Policy reserves and other insurance items	\$ 2,434,237	\$ 4,208,029
Derivative investments	795,965	922,671
Deferred compensation	76,458	134,711
Net operating loss carryforward	46,204	74,381
Other, net	72,941	54,558
Total gross deferred tax asset	<u>3,425,805</u>	<u>5,394,350</u>
Gross deferred tax liability		
Difference between financial reporting and the tax basis of:		
Deferred acquisition costs and sales inducements	(2,202,104)	(3,319,616)
Other investment items	(405,459)	(586,160)
Net unrealized gains on available for sale securities	(259,110)	(182,432)
Other, net	(74,908)	(79,677)
Total gross deferred tax liability	<u>(2,941,581)</u>	<u>(4,167,885)</u>
Net deferred tax asset	<u>\$ 484,224</u>	<u>\$ 1,226,465</u>

The Company is required to evaluate the recoverability of its deferred tax assets and establish a valuation allowance, if necessary, to reduce its deferred tax asset to an amount that is more likely than not to be realizable. Considerable judgment and the use of estimates are required when determining whether a valuation allowance is necessary and, if so, the amount of such valuation allowance. When evaluating the need for a valuation allowance, the Company considers many factors, including: the nature and character of the deferred tax assets and liabilities; taxable income in prior carryback years; future reversals of temporary differences; the length of time carryovers can be utilized; and any tax planning strategies the Company would employ to avoid a tax benefit from expiring unused. Although realization is not assured, management believes as of December 31, 2017, it is more likely than not that the deferred tax assets will be realized. At December 31, 2017 and 2016, the Company did not have a valuation allowance.

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During 2016, Jackson reached an agreement with the IRS regarding the taxation of hedging activities. This agreement requires the current taxation of all unrealized gains and losses on hedge-related investments, but then defers two-thirds of the amount ratably over the following two years. Accordingly, there is an acceleration of taxes incurred currently and a related offset to the taxes being deferred.

At December 31, 2017, the Company had a federal tax ordinary loss carryforward of \$220.0 million which begins to expire in 2025, that was attributable to a previous acquisition. Section 382 of the Internal Revenue Code imposes limitations on the utilization of net operating loss carryforwards. The Section 382 limitation is an annual limitation on the amount of pre-acquisition net operating losses that a corporation may use to offset post-acquisition income. Section 382 further limits certain unrealized built-in losses at the time of acquisition. The annual limitation is approximately \$21.0 million.

The Company has considered both permanent and temporary positions in determining the unrecognized tax benefit rollforward. As of December 31, 2017, the Company established a reserve related to exclusion of short-term capital gains from the separate account dividends received deduction (“DRD”) calculation. The following table summarizes the changes in the Company’s unrecognized tax benefits, for the year ended December 31, 2017 (in thousands):

	December 31, 2017
Unrecognized tax benefit, beginning of year	\$ -
Additions for tax positions identified	32,178
Reduction of tax positions of closed prior years	-
Reduction of reserve	-
Unrecognized tax benefit, end of year	\$ 32,178

The Company did not have an unrecognized tax benefit at year-end December 31, 2016. The Company has not recorded any amounts for penalties related to unrecognized tax benefits during 2017, 2016, or 2015.

Based on information available as of December 31, 2017, the Company believes that, in the next 12 months, there are no positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease.

13. Commitments, Contingencies, and Guarantees

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. Jackson has been named in civil litigation proceedings, which appear to be substantially similar to other class action litigation brought against many life insurers including allegations of misconduct in the sale of insurance products. The Company accrues for legal contingencies once the contingency is deemed to be probable and reasonably estimable. At December 31, 2017 and 2016, Jackson recorded accruals totaling \$11.3 million and \$1.9 million, respectively.

State guaranty funds provide payments for policyholders of insolvent life insurance companies. These guaranty funds are financed by assessing 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, the Company’s reserve for future state guaranty fund assessments was \$3.5 million and \$3.6 million at the end of 2017 and 2016, respectively. At both December 31, 2017 and 2016, related premium tax offsets were \$1.5 million. While Jackson cannot predict the amount and timing of any future assessments, the Company believes the reserve is adequate for all anticipated payments for known insolvencies.

At December 31, 2017, the Company had unfunded commitments related to its investments in limited partnerships and limited liability companies totaling \$560.2 million. At December 31, 2017, unfunded commitments related to fixed-rate commercial mortgage loans and other fixed maturities totaled \$290.0 million.

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The Company has two separate service agreements with third party administrators to provide policyholder administrative services. These agreements, subject to certain termination provisions, have ten-year terms and expire in 2019 and 2020.

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, 2017, Jackson recorded a liability of \$6.1 million for future lease payments. Lease expense was \$32.7 million, \$31.3 million, and \$33.1 million in 2017, 2016, and 2015, respectively. At December 31, 2017, future minimum payments under these noncancellable operating leases were as follows (in thousands):

2018	\$	17,139
2019		16,380
2020		12,688
2021		9,462
2022		5,777
Thereafter		17,470
Total	<u>\$</u>	<u>78,916</u>

14. Share-Based Compensation

Certain employees participate in various share award plans relating to Prudential shares and/or American Depositary Receipts (“ADRs”) that are tradable on the New York Stock Exchange and are described below.

The Group Performance Share Plan (“GPSP”) was a Prudential incentive plan in which all executive directors of Prudential and other senior executives could participate. Awards were granted in the form of a nil cost option with a vesting period of three years. Participants were entitled to the value of reinvested dividends that would have accrued on the shares that vest. As of December 31, 2015, there were no remaining outstanding shares under this plan.

The Business Unit Performance Plan (“BUPP”) was a Prudential incentive plan created to provide a common framework under which awards were made to Chief Executive Officers of Prudential’s business units. Awards under this nil cost plan for Jackson were based on compound annual growth in Jackson Shareholder Capital Value on a European Embedded Value (“EEV”) basis with performance measured over three years. Awards granted in 2009 and later were settled in ADRs after vesting. Participants were entitled to receive the value of reinvested dividends over the performance period for those shares/ADRs that vest. As of December 31, 2015, there were no remaining outstanding shares under this plan.

At certain times, the Company may grant one-off type retention awards to certain key senior executives within Jackson. These awards are subject to the prior approval of the Jackson Remuneration Committee and are nil cost awards with a contingent right to receive Prudential ADRs. The awards are contingent upon continued employment of the recipient through the award vesting date. There are no performance measurements with these awards.

The Company classifies all of the above plans as equity settled plans and, therefore, reflects the net reserve related to the compensation expense and the value of the shares distributed under this plan within the consolidated statements of equity. At December 31, 2017 and 2016, the Company had \$10.2 million and \$5.8 million, respectively, reserved for future payments under these plans.

The Company either acquires shares/ADRs or reimburses Prudential for the costs of any shares/ADRs that were distributed to participants in the above plans, or may be distributed in the future. The shares/ADRs acquired for all the share-award plans are held at cost in a trust account for future distributions. The Company reflects the costs of shares/ADRs held within the consolidated balance sheet as shares held in trust. At December 31, 2017 and 2016, the Company had \$18.9 million and \$22.7 million of shares/ADRs held at cost in the trust, respectively.

The Company also had a performance-related share award plan which, subject to the prior approval of the Jackson Remuneration Committee, granted share awards to eligible employees in the form of a contingent right to receive Prudential ADRs, or a conditional allocation of Prudential ADRs. These share awards were based on the compound annual EEV imputed growth in shareholder value of the U.S. business, had vesting periods of four years and were at nil cost to the employee. Share awards vested between 0% (less than 8% growth) and 150% (more than 17.5% growth) of the

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grant amounts dependent on the compound annual growth rate attained over the performance period. Award holders did not have any right to dividends or voting rights attached to the ADRs granted during the performance period. In 2013, this plan was replaced by the Prudential Long-Term Incentive Plan (“PLTIP”) as further described below. As of December 31, 2016, there were no remaining outstanding shares under this plan.

The PLTIP is a Prudential incentive plan in which the Company may grant share awards to eligible employees in the form of a contingent right to receive Prudential ADRs, or a conditional allocation of Prudential ADRs, subject to the prior approval of the Jackson Remuneration Committee. These share awards vest based on the achievement of planned International Financial Reporting Standards (“IFRS”) pretax operating income for the U.S. business, have vesting periods of three years and are at nil cost to the employee. Share awards vest between 0% (less than 90% of plan) and 100% (more than 110% of plan) of the grant amounts dependent on IFRS pretax operating income attained over the performance period. Award holders do not have any right to dividends or voting rights attached to the ADRs granted during the performance period. Upon vesting, a number of ADRs equivalent to the value of dividends that otherwise would have been received over the performance period are added to vested awards.

The Company classifies these plans as liability settled plans and, therefore, reflects the accrued compensation expense and the value of the shares distributed under the plans within other liabilities. At December 31, 2017 and 2016, the Company had \$98.6 million and \$74.7 million, respectively, accrued for future payments under these plans.

The Company recognizes share-based compensation expense associated with the above plans based on the grant-date award fair value ratably over the requisite service period of each individual grant, which generally equals the vesting period. Additional compensation expense is recognized based on the change in fair value of the award at the end of each reporting period. The Company estimates forfeitures when calculating share-based compensation expense.

Total expense related to these share-based performance related compensation plans was as follows (in millions):

	Years Ended December 31,		
	2017	2016	2015
Group Performance Share Plan	\$ -	\$ -	\$ 0.5
Business Unit Performance Plan	-	-	0.5
Retention Share Plan	4.5	2.5	3.3
Jackson performance plan	-	(0.8)	0.9
Prudential LTIP	66.3	28.3	44.9
Total compensation expense related to incentive plans	<u>\$ 70.8</u>	<u>\$ 30.0</u>	<u>\$ 50.1</u>
Income tax benefit	\$ 10.7	\$ 10.5	\$ 17.5

The total unrecognized compensation expense related to all share-based plans at December 31, 2017 was \$87.7 million with a weighted average remaining period of 1.37 years.

During 2015, certain one-off type retention awards were issued. There were no new grants under the GPSP, BUPP, or performance plans.

The weighted average share/ADR fair values of share-based awards granted by the PLTIP during 2017, 2016, and 2015 were \$42.12, \$37.27, and \$50.48, respectively.

The weighted average fair value for the Company’s performance awards represents the average Prudential ADR price for the thirty days following Prudential’s unaudited annual earnings release date. The fair value amounts relating to the equity settled plans were determined using either the Black-Scholes or Monte Carlo option-pricing models. These models are used to calculate fair values for options and awards at the grant date based on the quoted market price of the stock at the measurement date, the dividend yield, expected volatility, risk-free interest rates and expected term.

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Outstanding non-vested Prudential ADRs granted were as follows:

	Performance Award Plan		Prudential LTIP	
	ADR's	Weighted Average Grant Date Fair Value	ADR's	Weighted Average Grant Date Fair Value
At December 31, 2015	102,605	\$ 24.24	3,225,838	\$ 41.46
Granted	-	-	1,507,879	37.27
Exercised	102,605	24.24	1,199,794	32.62
Lapsed/Forfeited	-	-	156,688	44.20
At December 31, 2016	<u>-</u>	<u>\$ -</u>	<u>3,377,235</u>	<u>\$ 42.61</u>
Granted	-	-	1,495,495	42.12
Exercised	-	-	920,279	42.89
Lapsed/Forfeited	-	-	261,372	41.62
At December 31, 2017	<u>-</u>	<u>\$ -</u>	<u>3,691,079</u>	<u>\$ 42.41</u>

At December 31, 2017 and 2016, there were 117,814 and 235,620 non-vested Prudential ADR grants related to the one-off retention award plan, with a weighted average grant date price of \$46.68, respectively.

15. Statutory Accounting Capital and Surplus

The Company is required to prepare statutory financial statements in accordance with statutory accounting practices prescribed or permitted by the insurance department of the state of domicile. Statutory accounting practices primarily differ from GAAP by charging policy acquisition costs to expense as incurred and establishing future policy benefit liabilities using different actuarial assumptions, as well as valuing investments and certain assets and accounting for deferred income taxes on a different basis.

Under Michigan Insurance Law, while Jackson must provide notification to the Michigan commissioner of insurance prior to payment of any dividend, ordinary dividends on capital stock may only be distributed out of earned surplus, excluding any unrealized capital gains and the effect of permitted practices (referred to as adjusted earned surplus). At December 31, 2017, the Company had no adjusted earned surplus available for dividends. Ordinary dividends are also limited to the greater of 10% of statutory surplus as of the preceding year-end, excluding any increase arising from the application of permitted practices, or the statutory net income, excluding any net realized investment gains, for the twelve month period ended on the preceding December 31. The commissioner may approve payment of dividends in excess of these amounts, which would be deemed an extraordinary dividend. The maximum amount that would qualify as an ordinary dividend, which would consequently be free from restriction and available for payment of dividends to Brooke Life in 2018, is estimated to be \$366.7 million, subject to the availability of adjusted earned surplus as of the dividend date.

Dividends from the Company to its parent were \$600.5 million, \$550.7 million, and \$711.4 million in 2017, 2016, and 2015, respectively. Jackson's 2017, 2016, and 2015 dividends include \$0.5 million, \$0.7 million, and \$1.4 million, respectively, related to Jackson's forgiveness of Brooke Life's intercompany tax liability.

Statutory capital and surplus of the Company, as reported in its Annual Statement, was \$3.9 billion and \$4.9 billion at December 31, 2017 and 2016, respectively. Statutory net income (loss) of the Company, as reported in its Annual Statement, was \$168.4 million, (\$563.8) million, and \$627.0 million in 2017, 2016, and 2015, respectively.

The commissioner has granted Jackson a permitted practice that allows Jackson to carry interest rate swaps at book value, as if the requirements for statutory hedge accounting were in place, instead of at fair value as would have been otherwise required. Jackson is required to demonstrate the effectiveness of its interest rate swap program pursuant to the Michigan Insurance Code. This permitted practice expires on October 1, 2018. At December 31, 2017 and 2016, the effect of the permitted practice decreased statutory surplus by \$480.2 million and \$413.0 million, net of tax, respectively. The permitted practice had no impact on statutory net income.

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Under Michigan Insurance Law, VOBA is reported as an admitted asset if certain criteria are met. Pursuant to Michigan Insurance Law, the Company reported \$229.3 million and \$278.4 million of statutory basis VOBA at December 31, 2017 and 2016, respectively, which is fully admissible.

The NAIC has developed certain risk-based capital (“RBC”) requirements for life insurance companies. Under those requirements, compliance is determined by a ratio of a company’s total adjusted capital (“TAC”), calculated in a manner prescribed by the NAIC to its authorized control level RBC (“ACL RBC”), calculated in a manner prescribed by the NAIC. Companies below specific trigger points or ratios are classified within certain levels, each of which requires specified corrective action. The minimum level of TAC before corrective action commences is twice ACL RBC (“Company action level RBC”). At December 31, 2017, the Company’s TAC was more than 400% of the Company action level RBC.

In addition, on the basis of statutory financial statements that insurers file with the state insurance regulators, the NAIC annually calculates twelve financial ratios to assist state regulators in monitoring the financial condition of insurance companies. A usual range of results for each ratio is used as a benchmark and departure from the usual range on four or more of the ratios can lead to inquiries from individual state insurance departments. In 2017 and 2016, there were no significant exceptions with any ratios.

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 \$45.8 million, \$47.4 million, and \$45.1 million to PPM for investment advisory services during 2017, 2016, and 2015, respectively.

National Planning Holdings, Inc. (“NPH”), Jackson’s affiliated broker-dealer network, distributes products issued by Jackson and receives commissions and fees from Jackson. Commissions and fees paid by Jackson to NPH during 2017, 2016, and 2015 totaled \$100.2 million, \$107.3 million, and \$144.1 million, respectively. On August 15, 2017, NPH announced the sale of its broker-dealer network to LPL Financial LLC.

Jackson has entered into shared services administrative agreements with both NPH and PPMA. Under the shared services administrative agreements, Jackson charged \$16.6 million, \$12.5 million, and \$13.1 million of certain management and corporate services costs to these affiliates in 2017, 2016, and 2015, respectively.

Jackson provides a \$100.0 million revolving credit facility to Brooke (Holdco1) Inc., an upstream holding company. The loan is unsecured, matures in December 2021, accrues interest at LIBOR plus 2%, and has a commitment fee of 0.10% per annum. There was no outstanding balance at both December 31, 2017 and 2016. The highest outstanding loan balance during both 2017 and 2016 was nil. During 2017, 2016, and 2015, interest and commitment fees totaled \$65.2 thousand, \$40.0 thousand, and \$40.0 thousand, respectively.

Jackson provides a \$40.0 million revolving credit facility to PPMA. The loan is unsecured, matures in September 2018, accrues interest at LIBOR plus 2% per annum and has a commitment fee of 0.25% per annum. There was no outstanding balance at both December 31, 2017 and 2016. The highest outstanding loan balance during both 2017 and 2016 was nil. Interest and commitment fees totaled \$0.1 million each year for 2017, 2016, and 2015.

Jackson provides a \$20.0 million revolving credit facility to Jackson Holdings, LLC, an upstream holding company. The loan is unsecured, matures in June 2019, accrues interest at LIBOR plus 2% per annum and has a commitment fee of 0.25% per annum. The outstanding balance at December 31, 2017 and 2016, was \$1.5 million and \$0.1 million, respectively. The highest outstanding loan balance during 2017 and 2016 was \$1.5 million and \$0.1 million, respectively. Interest and commitment fees totaled \$0.1 million each year for 2017, 2016, and 2015.

Jackson provides, through its PGDS subsidiary, information technology services to certain Prudential affiliates. Jackson recognized \$3.7 million, \$7.3 million, and \$13.6 million of revenue associated with these services during 2017, 2016, and 2015, respectively. This revenue is included in other income in the accompanying consolidated income statements. This revenue is substantially equal to the costs incurred by PGDS to provide the services, which are reported in general and administrative expenses in the consolidated income statements.

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17. Benefit Plans

The Company has a defined contribution retirement plan covering substantially all employees and certain affiliates. To be eligible to participate in the Company's contribution, an employee must have attained the age of 21, 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 a participant's elective contribution, up to 6 percent of eligible compensation, to the plan during the year. The Company's expense related to this plan was \$29.7 million, \$26.0 million, and \$26.4 million in 2017, 2016, and 2015, respectively.

The Company maintains non-qualified voluntary deferred compensation plans for certain agents and employees of Jackson and certain affiliates. At December 31, 2017 and 2016, the liability for such plans totaled \$329.6 million and \$591.9 million, respectively, and is reported in other liabilities. The Company's expense related to these plans, including a match of elective deferrals for the agents' deferred compensation plan and the change in value of participant elected deferrals, was \$41.5 million, \$37.4 million, and \$11.8 million in 2017, 2016, and 2015, respectively. Previously, Jackson invested in selected mutual funds in amounts similar to participant elections as a hedge against significant movement in the payout liability. In December 2015, the Company liquidated its investment in these mutual funds and, instead, is hedging this liability within its overall hedging strategy. During 2015, the investment loss from the mutual funds previously invested in totaled \$1.1 million.

18. Operating Costs and Other Expenses

The following table is a summary of the Company's operating costs and other expenses (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Commission expenses	\$ 1,822,748	\$ 1,741,387	\$ 1,979,537
General and administrative expenses	833,850	763,096	847,265
Deferral of policy acquisition costs	(839,143)	(903,479)	(1,102,212)
Total operating costs and other expenses	\$ 1,817,455	\$ 1,601,004	\$ 1,724,590

19. Reclassifications Out of Accumulated Other Comprehensive Income

The following table represents changes in the balance of AOCI, net of income tax, related to unrealized investment gains (losses) (in thousands):

	December 31,		
	2017	2016	2015
Balance, beginning of year	\$ 597,122	\$ 548,458	\$ 1,478,565
OCI before reclassifications	406,807	69,016	(854,309)
Amounts reclassified from AOCI	89,045	(20,352)	(91,310)
Less: Comprehensive loss attributable to noncontrolling interest	-	-	15,512
Balance, end of year	\$ 1,092,974	\$ 597,122	\$ 548,458

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The following table represents amounts reclassified out of AOCI (in thousands):

<u>AOCI Components</u>	<u>Amounts Reclassified from AOCI</u>			<u>Affected Line Item in the Consolidated Income Statement</u>
	<u>2017</u>	<u>December 31, 2016</u>		
Net unrealized investment loss:				
Net realized loss on investments	\$ 137,686	\$ (3,862)	\$ (121,539)	Other net investment losses
Other-than-temporary impairments	(693)	(27,449)	(18,939)	Total other-than-temporary impairments
Net unrealized loss before income taxes	136,993	(31,311)	(140,478)	
Income tax (expense) benefit	(47,948)	10,959	49,168	
Reclassifications, net of income taxes	<u>\$ 89,045</u>	<u>\$ (20,352)</u>	<u>\$ (91,310)</u>	