Fidelity & Guaranty Life
Form 10-Q
February 06, 2017

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

Form 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2016
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number: 001-36227

FIDELITY & GUARANTY LIFE
(Exact name of registrant as specified in its charter)

Delaware	46-3489149
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
Two Ruan Center 601 Locust Street, 14th Floor Des Moines, Iowa	50309
(Address of principal executive offices)	(Zip Code)

(800) 445-6758
(Registrant's telephone number, including area code)
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x or No ¨.

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

Large Accelerated Filer ¨	Accelerated Filer x
Non-accelerated Filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

There were 58,984,637 shares of the registrant's common stock outstanding as of February 2, 2017.

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
TABLE OF CONTENTS

Table of Contents

PART I: FINANCIAL INFORMATION
Item 1. Financial Statements
FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In millions, except share data)

	December 31, 2016 (Unaudited)	September 30, 2016
ASSETS		
Investments:		
Fixed maturity securities, available-for-sale, at fair value (amortized cost: December 31, 2016 - $19,173; September 30, 2016 - $18,521)	$ 19,437	$ 19,411
Equity securities, available-for-sale, at fair value (amortized cost: December 31, 2016 - $691; September 30, 2016 - $640)	696	683
Derivative investments	314	276
Commercial mortgage loans	582	595
Other invested assets	47	60
Total investments	21,076	21,025
Related party loans	71	71
Cash and cash equivalents	632	864
Accrued investment income	201	214
Reinsurance recoverable	3,444	3,464
Intangibles, net	1,228	1,026
Deferred tax assets	68	—
Other assets	232	371
Total assets	$ 26,952	$ 27,035
LIABILITIES AND SHAREHOLDERS' EQUITY		
Contractholder funds	$ 19,486	$ 19,251
Future policy benefits	3,453	3,467
Funds withheld for reinsurance liabilities	1,142	1,172
Liability for policy and contract claims	53	55
Debt	300	300
Revolving credit facility	100	100
Deferred tax liability	—	10
Other liabilities	666	746
Total liabilities	25,200	25,101
Commitments and contingencies ("Note 12")		
Shareholders' equity:		
Preferred stock ($.01 par value, 50,000,000 shares authorized, no shares issued at December 31, 2016 and September 30, 2016)	$ —	$ —
Common stock ($.01 par value, 500,000,000 shares authorized, 58,984,034 issued and outstanding at December 31, 2016; 58,956,127 shares issued and outstanding at September 30, 2016)	1	1
Additional paid-in capital	715	714
Retained earnings	896	792

Accumulated other comprehensive income	153	439
Treasury stock, at cost (565,723 shares at December 31, 2016; 537,613 shares at September 30, 2016)	(13)	(12)
Total shareholders' equity	1,752	1,934
Total liabilities and shareholders' equity	$ 26,952	$ 27,035

See accompanying notes to unaudited condensed consolidated financial statements.

3

Table of Contents

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except share data)

	Three months ended December 31, 2016	December 31, 2015
	(Unaudited)	
Revenues:		
Premiums	$11	$ 15
Net investment income	240	222
Net investment gains	51	63
Insurance and investment product fees and other	38	29
Total revenues	340	329
Benefits and expenses:		
Benefits and other changes in policy reserves	20	181
Acquisition and operating expenses, net of deferrals	28	28
Amortization of intangibles	123	41
Total benefits and expenses	171	250
Operating income	169	79
Interest expense	(6)	(6)
Income before income taxes	163	73
Income tax expense	(55)	(25)
Net income	$108	$ 48
Net income per common share:		
Basic	$1.85	$ 0.82
Diluted	$1.85	$ 0.82
Weighted average common shares used in computing net income per common share:		
Basic	58,280,532	58,219,260
Diluted	58,366,059	58,542,588
Cash dividend per common share	$0.065	$ 0.065
Supplemental disclosures:		
Total other-than-temporary impairments	$(1)	$ (10)
Portion of other-than-temporary impairments included in other comprehensive income	—	—
Net other-than-temporary impairments	(1)	(10)
(Losses) Gains on derivative and embedded derivatives	51	70
Other realized investment gains	1	3
Total net investment (losses) gains	$51	$ 63

See accompanying notes to unaudited condensed consolidated financial statements.

4

Table of Contents

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In millions)

	Three months ended	
	December 31, 2016	December 31, 2015
	(Unaudited)	
Net income	$ 108	$ 48
Other comprehensive (loss) income:		
Unrealized investment gains/(losses):		
Change in unrealized investment gains/losses before reclassification adjustment	(663)	(373)
Net reclassification adjustment for (gains) losses included in net income	(2)	7
Changes in unrealized investment gains/losses after reclassification adjustment	(665)	(366)
Adjustments to intangible assets	225	135
Changes in deferred income tax asset/liability	154	81
Net changes to derive comprehensive (loss) income for the period	(286)	(150)
Comprehensive (loss) income, net of tax	$ (178)	$ (102)

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
(Unaudited) (In millions)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total Shareholders' Equity
Balance, September 30, 2016	$ —	$ 1	$ 714	$ 792	$ 439	$ (12)	$ 1,934
Treasury shares purchased	—	—	—	—	—	(1)	(1)
Dividends	—	—	—	(4)	—	—	(4)
Net income	—	—	—	108	—	—	108
Unrealized investment losses, net	—	—	—	—	(286)	—	(286)
Stock compensation	—	—	1	—	—	—	1
Balance, December 31, 2016	$ —	$ 1	$ 715	$ 896	$ 153	$ (13)	$ 1,752

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

	Three months ended	
	December 31, 2016	December 31, 2015
	(Unaudited)	
Cash flows from operating activities:		
Net income	$108	$ 48
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock based compensation	1	4
Amortization	(6)	(15)
Deferred income taxes	76	23
Interest credited/index credit to contractholder account balances	(13)	136
Net recognized (gains) on investments and derivatives	(51)	(63)
Charges assessed to contractholders for mortality and administration	(32)	(24)
Deferred policy acquisition costs, net of related amortization	23	(39)
Changes in operating assets and liabilities:		
Reinsurance recoverable	(8)	(9)
Future policy benefits	(14)	5
Funds withheld from reinsurers	(26)	(16)
Collateral posted	40	66
Other assets and other liabilities	(26)	24
Net cash provided by operating activities	72	140
Cash flows from investing activities:		
Proceeds from available-for-sale investments sold, matured or repaid	733	896
Proceeds from derivatives instruments and other invested assets	71	89
Proceeds from commercial mortgage loans	13	2
Cost of available-for-sale investments acquired	(1,355)	(1,021)
Costs of derivatives instruments and other invested assets	(54)	(78)
Costs of commercial mortgage loans	—	(87)
Related party loans	—	(3)
Capital expenditures	(2)	(2)
Net cash (used in) investing activities	(594)	(204)
Cash flows from financing activities:		
Treasury stock	(1)	(1)
Common stock issued under employee plans	—	2
Dividends paid	(4)	(4)
Contractholder account deposits	698	569
Contractholder account withdrawals	(403)	(436)
Net cash provided by financing activities	290	130
Change in cash & cash equivalents	(232)	66
Cash & cash equivalents, beginning of period	864	502
Cash & cash equivalents, end of period	$632	$ 568
Supplemental disclosures of cash flow information		
Interest paid	$10	$ 10
Taxes paid	$—	$ 1
Deferred sales inducements	$—	$ 6

See accompanying notes to unaudited condensed consolidated financial statements.

FIDELITY & GUARANTY LIFE AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) Basis of Presentation

Fidelity & Guaranty Life ("FGL" and, collectively with its subsidiaries, the "Company") is a subsidiary of HRG Group, Inc. (formerly, Harbinger Group Inc. ("HRG")). The accompanying unaudited consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for the Securities and Exchange Commission ("SEC") Quarterly Report on Form 10-Q, including Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. Therefore, the information contained in the Notes to Consolidated Financial Statements included in Fidelity & Guaranty Life and Subsidiaries' Annual Report on Form 10-K, for the year ended September 30, 2016 ("2016 Form 10-K"), should be read in connection with the reading of these interim unaudited condensed consolidated financial statements. Dollar amounts in the accompanying sections are presented in millions, unless otherwise noted.

FGL markets products through its wholly-owned insurance subsidiaries, Fidelity & Guaranty Life Insurance Company ("FGL Insurance") and Fidelity & Guaranty Life Insurance Company of New York ("FGL NY Insurance"), which together is licensed in all fifty states and the District of Columbia.

On November 8, 2015, FGL entered into an Agreement and Plan of Merger (as amended "Merger Agreement" and the merger contemplated thereby, the "Merger"), by and among FGL, Anbang Insurance Group Co., Ltd., a joint-stock insurance company established in the People's Republic of China ("Anbang"), AB Infinity Holding, Inc., a Delaware corporation and a wholly-owned subsidiary of Anbang ("AB Infinity"), and AB Merger Sub, Inc., a Delaware corporation and a newly formed, wholly-owned subsidiary of AB Infinity ("Merger Sub"), which was amended on November 3, 2016, to extend the outside termination date for the completion of the Merger from November 7, 2016 to February 8, 2017. Accordingly, either party may terminate the merger agreement if the closing of the merger does not occur prior to February 8, 2017. As of the date of this report, the parties were in discussions regarding an extension of the outside termination date beyond February 8, 2017. The Company expects to make an announcement on or about February 9, 2017 regarding the outcome of their discussions.

Pursuant to the Merger Agreement, at the effective time of the Merger, each issued and outstanding share of FGL common stock will be canceled and converted automatically into the right to receive $26.80 in cash, without interest, other than any shares of common stock owned by FGL as treasury stock or otherwise or owned by Anbang, AB Infinity or Merger Sub (which will be canceled and no payment will be made with respect thereto), shares of common stock granted pursuant to FGL's employee equity award plan and those shares of common stock with respect to which appraisal rights under Delaware law are properly exercised and not withdrawn.

At the effective time of the Merger, each, vested and unvested, FGL option to purchase shares of common stock and restricted shares of common stock will become fully vested and automatically converted into the right to receive a cash payment in an amount pursuant to the Merger Agreement. In addition, at such time, each, vested and unvested, stock option and restricted stock unit relating to shares of Fidelity & Guaranty Life Holdings, Inc., a subsidiary of FGL ("FGLH") will become fully vested and automatically converted into the right to receive a cash payment in an amount pursuant to the Merger Agreement, and each dividend equivalent right held in respect of a share of FGLH stock (a "DER"), whether vested or unvested, will become fully vested and automatically converted into the right to receive a cash payment equal to the amount accrued with respect to such DER. All DER were vested as of March 31, 2016 and were paid out in April 2016.

The Merger is subject to closing conditions, including the receipt of regulatory approvals from the Iowa Insurance Division, New York Department of Financial Services, Vermont Department of Financial Regulation, China Insurance Regulatory Commission, and the Committee on Foreign Investment in the United States ("CFIUS"). In the event that the Merger Agreement is terminated, FGL may be required to pay a termination fee to Anbang and its subsidiaries of $51.

On November 8, 2015, FS Holdco II Ltd., a wholly-owned subsidiary of HRG Group, Inc. and direct holder of 47,000 thousand shares of FGL's common stock representing approximately 81% of the outstanding shares of FGL's common stock, delivered a written consent adopting, authorizing, accepting and approving in all respects the Merger Agreement and the transactions contemplated thereby, including the Merger. On November 25, 2015,

Table of Contents

FGL obtained the requisite approval for the Merger from the Vermont Department of Financial Regulation. On March 14, 2016, FGL received notification from CFIUS that it had concluded all action under Section 721 of the Defense Production Act of 1950, as amended, and determined that there are no unresolved national security concerns with respect to the merger. The parties are not required to file a notification of the Merger under the Hart-Scott Rodino Antitrust Improvements Act of 1976, as amended, due to an available exemption. The adoption of the Merger Agreement by FGL's shareholders required the affirmative vote or written consent of holders of at least a majority of the outstanding shares of FGL's common stock.

In the opinion of management, these statements include all normal recurring adjustments necessary for a fair presentation of the Company's results. Operating results for the three months ended December 31, 2016, are not necessarily indicative of the results that may be expected for the full year ending September 30, 2017. Amounts reclassified out of other comprehensive income are reflected in net investment gains in the unaudited Condensed Consolidated Statements of Operations.

(2) Significant Accounting Policies and Practices

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and all other entities in which FGL has a controlling financial interest. All intercompany accounts and transactions have been eliminated in consolidation.

We are involved in certain entities that are considered variable interest entities ("VIEs") as defined under GAAP. Our involvement with VIEs is primarily to invest in assets that allow us to gain exposure to a broadly diversified portfolio of asset classes. A VIE is an entity that does not have sufficient equity to finance its own activities without additional financial support or where investors lack certain characteristics of a controlling financial interest. We assess our relationships to determine if we have the ability to direct the activities, or otherwise exert control to evaluate if we are the primary beneficiary of the VIE. See "Note 4. Investments" to the Company's unaudited Condensed Consolidated Financial Statements for additional information on the Company's investments in unconsolidated VIEs.

Adoption of New Accounting Pronouncements

Share-Based Payments When a Performance Target is Achieved after the Requisite Service Period

In June 2014, the FASB issued new guidance on Stock Compensation (ASU 2014-12, Accounting for Share-Based Payments When the Term of an Award Provide that a Performance Target Could Be Achieved after the Requisite Service Period), effective for fiscal years beginning after December 15, 2015 and interim periods within those years. The new guidance requires performance targets that affect vesting and that could be achieved after the requisite service period to be treated as performance conditions. Such performance targets will not be included in the grant-date fair value calculation of the award, rather compensation cost will be recorded when it is probable the performance target will be reached and should represent the compensation cost attributable to period(s) for which the requisite service has already been rendered. The Company adopted this guidance effective October 1, 2016, as required. The adoption of ASU 2014-12 will not impact the Company's consolidated financial statements or related disclosures, as the Company has historically treated the performance targets for its share-based payment awards as a performance condition that affects vesting and has not reflected the targets in the grant-date fair value calculation of the awards.

Amendments to the Consolidation Analysis

In February 2015, the FASB issued amended consolidation guidance (ASU 2015-02, Amendments to the Consolidation Analysis), effective for fiscal years beginning after December 15, 2015. The amended guidance changes the consolidation analysis of reporting entities with variable interest entity ("VIE") relationships by i) modifying the criteria used to evaluate whether limited partnerships and similar legal entities are VIEs or voting interest entities and revising the primary beneficiary determination of a VIE, ii) eliminating the specialized consolidation model and guidance for limited partnerships thereby removing the presumption that a general partner should consolidate a limited partnership, iii) reducing the criteria in the variable interest model contained in Accounting Standards Codification Topic 810, Consolidation, that is used to evaluate whether the fees paid to a decision maker or service provider represents a variable interest, and iv) exempting reporting entities from consolidating money market funds that operate in accordance with Rule 2a-7 of the Investment Company Act of

9

Table of Contents

1940. The Company adopted ASU 2015-02 effective October 1, 2016, as required. The adoption of ASU 2015-02 will not impact the Company's consolidated financial statements or related disclosure as the Company determined that this new guidance does not change its conclusions regarding consolidation of its VIEs.

Presentation of Debt Issuance Costs

In April 2015, the FASB issued amended guidance (ASU 2015-03, Interest-Imputation of Interest (Subtopic 835-30), Simplifying the Presentation of Debt Issuance Costs), effective for fiscal years beginning after December 15, 2015 and interim periods within those years. The amended guidance requires debt issuance costs related to a recognized debt liability to be presented on the balance sheet as a direct deduction from the debt liability, similar to the presentation of debt discounts or premiums. The cost of issuing debt will no longer be recorded as a separate asset, except when incurred before the receipt of the funding from the associated debt liability. Instead, debt issuance costs will be presented on the balance sheet as a direct deduction from the carrying amount of the related debt liability, and the costs will be amortized to interest expense using the effective interest method. The Company adopted ASU 2015-03 effective October 1, 2016, as required. The Company retrospectively considered adjustments to adjust its historical balance sheets to present deferred debt issuance costs related to the Company's debt as a reduction of the debt liability. As the Company's debt issuance costs were fully amortized as of the period ended September 30, 2016, there is no impact to the current period financial statements.

Accounting for Fees Paid in Cloud Computing Arrangements

In April 2015, the FASB issued amended guidance (ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement), effective for fiscal years beginning after December 15, 2015 and interim periods within those years. Previous GAAP did not include explicit guidance regarding a customer's accounting for fees paid in a cloud computing arrangement, which may include software as a service, platform as a service, infrastructure as a service, and other similar hosting arrangements. The adopted guidance addresses whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If the cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The Company prospectively adopted ASU 2015-05 effective as of October 1, 2016, as required, for all new or materially modified cloud computing arrangements that contain a software license component.

Investments That Calculate Net Asset Value per Share

In May 2015, the FASB issued amended guidance (ASU 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)), effective for fiscal years beginning after December 15, 2015 and interim periods within those years. Previous GAAP required that investments for which fair value is measured at net asset value (or its equivalent) using the practical expedient in Topic 820 be categorized within the fair value hierarchy using criteria that differ from the criteria used to categorize other fair value measurements within the hierarchy. Previously, investments valued using the practical expedient were categorized within the fair value hierarchy on the basis of whether the investment is redeemable with the investee at net asset value on the measurement date, never redeemable with the investee at net asset value, or redeemable with the investee at net asset value at a future date. For investments that are redeemable with the investee at a future date, a reporting entity will take into account the length of time until those investments become redeemable to determine the classification within the fair value hierarchy. There is diversity in practice related to how certain investments measured at net asset value with redemption dates in the future (including periodic redemption dates) are categorized within the fair value hierarchy. Under the amendments in this Update, investments for which fair value will be measured at net asset value per share (or its equivalent) using the practical expedient should not be categorized in the fair value hierarchy. Removing those investments from the fair value hierarchy not only eliminates the diversity in practice resulting from the way in which investments measured at net asset value per share (or its equivalent) with future redemption dates are classified, but also ensures that all investments categorized in the fair value hierarchy are classified using a consistent approach. Investments that calculate net asset value per share (or its equivalent), but for which the practical expedient is not applied will continue to be included in the fair value hierarchy. The Company adopted ASU 2015-07 effective October 1, 2016, as required, and has updated the fair value disclosures to reflect the amended guidance. Refer to

"Note 6. Fair Value of Financial Instruments" for further details.

Table of Contents

Future Adoption of Accounting Pronouncements

Presentation of Changes in Restricted Cash on the Cash Flow Statement

In November 2016, the FASB issued amended guidance (ASU 2016-18, Statement of Cash Flows (Topic 230), Restricted Cash), effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. The ASU will require amounts generally described as changes in restricted cash and restricted cash equivalents to be included with cash and cash equivalents on the statement of cash flows. The amendments in this ASU may be early adopted during any period or interim period, however, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. The amendments should be applied using a retrospective transition method to each period presented. The Company will not early adopt this standard and is currently evaluating the impact of this new accounting guidance on its consolidated financial statements.

Technical Corrections and Improvements

In December 2016, the FASB issued new guidance on the Simplification of Topics Within Insurance and Debt Restructuring (ASU 2016-19, Technical Corrections and Improvements), effective upon issuance for most amendments in the Update. For several items requiring transition guidance, the ASU identifies adoption dates specific to those items. The amendments cover a wide range of topics in the Accounting Standards Codification ("ASC") and will correct differences between original guidance and the ASC, clarify guidance through updated wording or corrected references, and simplify guidance through minor editing. The amendments in this ASU that do not require transition guidance were effective upon issuance, however, those that require transition guidance may be early adopted. The Company adopted the amendments that do not require transition guidance upon issuance of ASU 2016-19 with no impact on its financial statements. The Company will not early adopt the guidance in this standard that require transition guidance and is currently evaluating the impact of this new accounting guidance on its consolidated financial statements.

(3) Significant Risks and Uncertainties

Federal Regulation

In April 2016, the Department of Labor (“DOL”) released its final “fiduciary” rule which could have a material impact on the Company, its products, distribution, and business model. The final rule treats persons who provide investment advice for a fee or other compensation with respect to assets of an employer plan or individual retirement account ("IRA") as fiduciaries of that plan or IRA. Significantly, the rule expands the definition of fiduciary to apply to persons, including insurance agents, who advise and sell products to IRA owners. As a practical matter, this means commissioned insurance agents selling the Company’s IRA products must qualify for a prohibited transaction exemption which requires the agent and financial institution to meet various conditions including that an annuity sale be in the “best interest” of the client without regard for the agent’s, financial institution’s or other party’s financial or other interests, and that any compensation paid to the agent and financial institution be reasonable. The final rule was effective June 2016 and generally applicable in April 2017. The rule has generated considerable controversy and is the subject of industry efforts to block implementation both in Congress and through court actions. The success or failure of these efforts cannot be predicted. Assuming the rule is not blocked, the precise impact of the rule on the financial services industry more generally, and the impact on the Company and its business in particular, is difficult to assess. We believe however it could have an adverse effect on sales of annuity products to IRA owners particularly in the independent agent distribution channel. A significant portion of our annuity sales are to IRAs. Compliance with the prohibited transaction exemptions would likely require additional supervision of agents, cause changes to compensation practices and product offerings, and increase litigation risk, all of which could adversely impact our business, results of operations and/or financial condition. Regardless of the outcome of the court and political challenges, FGL Insurance is prepared to execute on its implementation plans on the applicability date.

Use of Estimates and Assumptions

The preparation of the Company’s unaudited Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets

Table of Contents

and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions used.

Concentrations of Financial Instruments

As of December 31, 2016 and September 30, 2016, the Company's most significant investment in one industry, excluding United States ("U.S.") Government securities, was its investment securities in the banking industry with a fair value of $2,570 or 12% and $2,448 or 12%, respectively, of the invested assets portfolio, and an amortized cost of $2,552 and $2,352, respectively. As of December 31, 2016, the Company's holdings in this industry include investments in 106 different issuers with the top ten investments accounting for 32% of the total holdings in this industry. As of December 31, 2016 and September 30, 2016, the Company had no investments in issuers that exceeded 10% of shareholders' equity. The Company's largest concentration in any single issuer as of December 31, 2016 and September 30, 2016 was Wells Fargo & Company with a total fair value of $166 or 1% and $171 or 1% of the invested assets portfolio, respectively.

Concentrations of Financial and Capital Markets Risk

The Company is exposed to financial and capital markets risk, including changes in interest rates and credit spreads which can have an adverse effect on the Company's results of operations, financial condition and liquidity. The Company expects to continue to face challenges and uncertainties that could adversely affect its results of operations and financial condition. The Company attempts to mitigate the risk, including changes in interest rates by investing in less rate-sensitive investments, including senior tranches of collateralized loan obligations, non-agency residential mortgage-backed securities, and various types of asset backed securities.

The Company's exposure to such financial and capital markets risk relates primarily to the market price and cash flow variability associated with changes in interest rates. A rise in interest rates, in the absence of other countervailing changes, will decrease the net unrealized gain position of the Company's investment portfolio and, if long-term interest rates rise dramatically within a six to twelve month time period, certain of the Company's products may be exposed to disintermediation risk. Disintermediation risk refers to the risk that policyholders may surrender their contracts in a rising interest rate environment, requiring the Company to liquidate assets in an unrealized loss position. Management believes this risk is mitigated to some extent by surrender charge protection provided by the Company's products.

Concentration of Reinsurance Risk

The Company has a significant concentration of reinsurance with Wilton Reassurance Company ("Wilton Re") and Front Street Re (Cayman) Ltd. ("FSRCI"), an affiliate, that could have a material impact on the Company's financial position in the event that Wilton Re or FSRCI fail to perform their obligations under the various reinsurance treaties. Wilton Re is a wholly owned subsidiary of Canada Pension Plan Investment Board ("CPPIB"). CPPIB has an AAA issuer credit rating from Standard & Poor's Ratings Services ("S&P") as of December 31, 2016. As of December 31, 2016, the net amount recoverable from Wilton Re was $1,528 and the net amount recoverable from FSRCI was $1,087. The coinsurance agreement with FSRCI is on a funds withheld basis. The Company monitors both the financial condition of individual reinsurers and risk concentration arising from similar geographic regions, activities and economic characteristics of reinsurers to attempt to reduce the risk of default by such reinsurers.

Table of Contents

(4) Investments

The Company’s fixed maturity and equity securities investments have been designated as available-for-sale and are carried at fair value with unrealized gains and losses included in accumulated other comprehensive income (loss) (“AOCI”) net of associated adjustments for deferred acquisition costs (“DAC”), value of business acquired (“VOBA”), and deferred income taxes. The Company’s consolidated investments at December 31, 2016 and September 30, 2016 are summarized as follows:

	December 31, 2016				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Carrying Value
Available-for sale securities					
Asset-backed securities	$2,629	$ 17	$ (38)	$2,608	$2,608
Commercial mortgage-backed securities	852	7	(22)	837	837
Corporates	11,294	412	(227)	11,479	11,479
Equities	691	17	(12)	696	696
Hybrids	1,352	45	(64)	1,333	1,333
Municipals	1,553	113	(25)	1,641	1,641
Residential mortgage-backed securities	1,269	65	(25)	1,309	1,309
U.S. Government	224	6	—	230	230
Total available-for-sale securities	19,864	682	(413)	20,133	20,133
Derivative investments	218	104	(8)	314	314
Commercial mortgage loans	582	—	—	574	582
Other invested assets	47	—	—	43	47
Total investments	$20,711	$ 786	$ (421)	$21,064	$21,076

	September 30, 2016				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Carrying Value
Available-for-sale securities					
Asset-backed securities	$2,528	$ 16	$ (45)	$2,499	$2,499
Commercial mortgage-backed securities	850	23	(9)	864	864
Corporates	10,712	760	(132)	11,340	11,340
Equities	640	47	(4)	683	683
Hybrids	1,356	77	(47)	1,386	1,386
Municipals	1,515	206	(4)	1,717	1,717
Residential mortgage-backed securities	1,327	63	(28)	1,362	1,362
U.S. Government	233	10	—	243	243
Total available-for-sale securities	19,161	1,202	(269)	20,094	20,094
Derivative investments	221	78	(23)	276	276
Commercial mortgage loans	595	—	—	614	595
Other invested assets	60	—	—	58	60
Total investments	$20,037	$ 1,280	$ (292)	$21,042	$21,025

Included in AOCI were cumulative gross unrealized gains of $1 and gross unrealized losses of $3 related to the non-credit portion of other-than-temporary impairments ("OTTI") on non-agency residential mortgage-backed securities ("RMBS") at December 31, 2016 and gross unrealized gains of $1 and gross unrealized losses of $3 related to the non-credit portion of OTTI on RMBS at September 30, 2016.

Securities held on deposit with various state regulatory authorities had a fair value of $18,155 and $18,075 at December 31, 2016 and September 30, 2016, respectively. Under Iowa regulations, insurance companies are required to hold securities on deposit in an amount no less than the Company's legal reserve as prescribed by Iowa regulations.

Table of Contents

At December 31, 2016 and September 30, 2016, the company held investments that were non-income producing for a period greater than twelve months with fair values of $0 and $2, respectively.
In accordance with the Company's Federal Home Loan Bank of Atlanta ("FHLB") agreements, the investments supporting the funding agreement liabilities are pledged as collateral to secure the FHLB funding agreement liabilities. The collateral investments had a fair value of $622 and $649 at December 31, 2016 and September 30, 2016, respectively.
The amortized cost and fair value of fixed maturity available-for-sale securities by contractual maturities, as applicable, are shown below. Actual maturities may differ from contractual maturities because issuers may have the right to call or pre-pay obligations.

	December 31, 2016	
	Amortized Cost	Fair Value
Corporates, Non-structured Hybrids, Municipal and U.S. Government securities:		
Due in one year or less	$290	$294
Due after one year through five years	1,940	1,978
Due after five years through ten years	3,189	3,261
Due after ten years	8,256	8,433
Subtotal	13,675	13,966
Other securities which provide for periodic payments:		
Asset-backed securities	2,629	2,608
Commercial mortgage-backed securities	852	837
Structured hybrids	748	717
Residential mortgage-backed securities	1,269	1,309
Subtotal	5,498	5,471
Total fixed maturity available-for-sale securities	$19,173	$19,437

The Company's available-for-sale securities with unrealized losses are reviewed for potential OTTI. In evaluating whether a decline in value is other-than-temporary, the Company considers several factors including, but not limited to the following: (1) the extent and the duration of the decline; (2) the reasons for the decline in value (credit event, currency or interest-rate related, including general credit spread widening); and (3) the financial condition of and near-term prospects of the issuer. The Company also considers the ability and intent to hold the investment for a period of time to allow for a recovery of value.
The Company analyzes its ability to recover the amortized cost by comparing the net present value of cash flows expected to be collected with the amortized cost of the security. For mortgage-backed and asset-backed securities, cash flow estimates consider the payment terms of the underlying assets backing a particular security, including interest rate and prepayment assumptions, based on data from widely accepted third-party data sources or internal estimates. In addition to interest rate and prepayment assumptions, cash flow estimates also include other assumptions regarding the underlying collateral including default rates and recoveries, which vary based on the asset type and geographic location, as well as the vintage year of the security. For structured securities, the payment priority within the tranche structure is also considered. For all other fixed maturity securities, cash flow estimates are driven by assumptions regarding probability of default and estimates regarding timing and amount of recoveries associated with a default. If the net present value is less than the amortized cost of the investment, an OTTI is recognized.
Based on the results of our process for evaluating available-for-sale securities in unrealized loss positions for OTTI discussed above, the Company determined that the unrealized losses as of December 31, 2016 increased due to upward movement in the U.S. Treasury rates. Bond prices in most sectors moved lower based on these higher Treasury yields. Based on an assessment of all securities in the portfolio in unrealized loss positions, the Company determined that the unrealized losses on the securities presented in the table below were not other-than-temporarily impaired as of December 31, 2016.

14

Table of Contents

The fair value and gross unrealized losses of available-for-sale securities, aggregated by investment category and duration of fair value below amortized cost, were as follows:

	December 31, 2016					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available-for-sale securities						
Asset-backed securities	$439	$ (2)	$1,348	$ (36)	$1,787	$ (38)
Commercial mortgage-backed securities	327	(8)	188	(14)	515	(22)
Corporates	2,716	(88)	1,191	(139)	3,907	(227)
Equities	232	(9)	64	(3)	296	(12)
Hybrids	246	(15)	476	(49)	722	(64)
Municipals	440	(21)	36	(4)	476	(25)
Residential mortgage-backed securities	49	(1)	486	(24)	535	(25)
U.S. Government	51	—	—	—	51	—
Total available-for-sale securities	$4,500	$ (144)	$3,789	$ (269)	$8,289	$ (413)
Total number of available-for-sale securities in an unrealized loss position less than twelve months						620
Total number of available-for-sale securities in an unrealized loss position twelve months or longer						527
Total number of available-for-sale securities in an unrealized loss position						1,147

	September 30, 2016					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available-for-sale securities						
Asset-backed securities	$352	$ (4)	$1,368	$ (41)	$1,720	$ (45)
Commercial mortgage-backed securities	44	(1)	182	(8)	226	(9)
Corporates	413	(9)	1,031	(123)	1,444	(132)
Equities	51	(1)	75	(3)	126	(4)
Hybrids	41	(2)	412	(45)	453	(47)
Municipals	69	(2)	38	(2)	107	(4)
Residential mortgage-backed securities	70	(1)	544	(27)	614	(28)
Total available-for-sale securities	$1,040	$ (20)	$3,650	$ (249)	$4,690	$ (269)
Total number of available-for-sale securities in an unrealized loss position less than twelve months						193
Total number of available-for-sale securities in an unrealized loss position twelve months or longer						543
Total number of available-for-sale securities in an unrealized loss position						736

At December 31, 2016 and September 30, 2016, securities in an unrealized loss position were primarily concentrated in investment grade, corporate debt, asset-backed, and hybrid instruments.

At December 31, 2016 and September 30, 2016, securities with a fair value of $131 and $183, respectively, had an unrealized loss greater than 20% of amortized cost (excluding U.S. Government and U.S. Government sponsored agency securities), which represented less than 1% of the carrying value of all investments in both reporting periods.

Table of Contents

The following table provides a reconciliation of the beginning and ending balances of the credit loss portion of OTTI on fixed maturity available-for-sale securities held by the Company for the three months ended December 31, 2016 and 2015, for which a portion of the OTTI was recognized in AOCI:

	Three months ended	
	December 31, 2016	December 31, 2015
Beginning balance	$ 3	$ 3
Increases attributable to credit losses on securities:		
OTTI was previously recognized	—	—
OTTI was not previously recognized	—	—
Ending balance	$ 3	$ 3

The Company recognized $1 of credit impairment losses in operations during the three months ended December 31, 2016 and $0 of change of intent impairment losses in operations during the three months ended December 31, 2016, related to fixed maturity securities with an amortized cost of $115 and a fair value of $114 at December 31, 2016. During the three months ended December 31, 2015, the Company recognized $10 of credit impairment losses in operations related to fixed maturity securities and other invested assets with an amortized cost of $64 and a fair value of $54 at December 31, 2015.

Details underlying write-downs taken as a result of OTTI that were recognized in "Net income" and included in net realized gains on securities were as follows:

	Three months ended	
	December 31, 2016	December 31, 2015
OTTI Recognized in Net Income:		
Asset-backed securities	$ 1	$ 4
Corporates	—	6
Total	$ 1	$ 10

The portion of OTTI recognized in AOCI is disclosed in the unaudited Condensed Consolidated Statements of Comprehensive Income (Loss).

Table of Contents

Commercial Mortgage Loans

Commercial mortgage loans ("CMLs") represented approximately 3% of the Company's total investments as of December 31, 2016 and September 30, 2016. The Company primarily makes mortgage loans on income producing properties including hotels, industrial properties, retail buildings, multifamily properties and office buildings. The Company diversifies its CML portfolio by geographic region and property type to attempt to reduce concentration risk. Subsequent to origination, the Company continuously evaluates CMLs based on relevant current information to ensure properties are performing at a consistent and acceptable level to secure the related debt. The distribution of CMLs, gross of valuation allowances, by property type and geographic region is reflected in the following tables:

	December 31, 2016		September 30, 2016	
	Gross Carrying Value	% of Total	Gross Carrying Value	% of Total
Property Type:				
Funeral Home	$1	— %	$1	— %
Hotel	23	4 %	23	4 %
Industrial - General	46	8 %	58	10 %
Industrial - Warehouse	65	11 %	64	11 %
Multifamily	70	12 %	70	11 %
Office	159	27 %	160	27 %
Retail	219	38 %	220	37 %
Total commercial mortgage loans, gross of valuation allowance	$583	100 %	$596	100 %
Allowance for loan loss	(1)		(1)	
Total commercial mortgage loans	$582		$595	
U.S. Region:				
East North Central	$136	23 %	$137	23 %
East South Central	20	4 %	21	4 %
Middle Atlantic	86	15 %	97	16 %
Mountain	68			