

**AEGON GLOBAL INSTITUTIONAL MARKETS plc**  
**FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED**  
**31 DECEMBER 2008**

**REPORT OF THE DIRECTORS AND FINANCIAL STATEMENTS  
for the year ended 31 December 2008**

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**DIRECTORS AND OTHER INFORMATION**

**Directors**

Jacqueline D Griffin  
Nationality: American

Thomas Hartlage  
Nationality: American

C Michiel van Katwijk  
Nationality: Dutch

Redmond Murphy

J Walker Rainey  
Nationality: British

**Secretary**

Barry Knowles

**Registered Office**

AEGON Global Institutional Markets plc  
25-28 North Wall Quay  
Dublin 1  
Ireland

**Registered Number of Incorporation**

365437

**Solicitors**

A&L Goodbody  
25-28 North Wall Quay  
Dublin 1  
Ireland

**Bankers**

Allied Irish Banks plc (AIB)  
Bankcentre Branch  
Ballsbridge  
Dublin 4  
Ireland

Citibank N.A.  
388 Greenwich Street – 24<sup>th</sup> Floor  
New York, NY 10013  
United States

**Auditors**

Ernst & Young  
Registered Auditors  
Ernst & Young Building  
Harcourt Centre  
Harcourt Street  
Dublin 2  
Ireland

## **INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF AEGON GLOBAL INSTITUTIONAL MARKETS PLC**

We have audited the company financial statements of AEGON Global Institutional Markets plc for the year ended 31 December 2008, which comprise the Income Statement, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 24. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 193 of the Companies Act, 1990. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective responsibilities of directors and auditors**

The directors are responsible for the preparation of the financial statements in accordance with applicable Irish law and International Financial Reporting Standards (IFRS) as adopted by the European Union, as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Companies Acts, 1963 to 2006. We also report to you our opinion as to: whether proper books of account have been kept by the company; whether, at the balance sheet date, there exists a financial situation which may require the convening of an extraordinary general meeting of the company; and whether the information given in the Directors' Report is consistent with the financial statements.

In addition, we state whether we have obtained all the information and explanations necessary for the purposes of our audit and whether the financial statements are in agreement with the books of account.

We also report to you if, in our opinion, any information specified by law regarding directors' remuneration and directors' transactions is not disclosed and, where practicable, include such information in our report.

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatements within it.

## **INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF AEGON GLOBAL INSTITUTIONAL MARKETS PLC (continued)**

### **Basis of audit opinion**

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

### **Opinion**

In our opinion, the financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of affairs of the company as at 31 December 2008 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Acts, 1963 to 2006.

We have obtained all the information and explanations which we consider necessary for the purposes of our audit. In our opinion, proper books of account have been kept by the company. The financial statements are in agreement with the books of account.

In our opinion, the information given in the directors' report is consistent with the financial statements.

The balance sheet shows an excess of liabilities over assets and, in our opinion, on that basis there did exist at 31 December 2008 a financial situation which, under Section 40(1) of the Companies (Amendment) Act, 1983, may require the convening of an extraordinary general meeting of the company.

Ernst & Young  
Chartered Accountants and Registered Auditors  
Dublin

13 May 2009

**INCOME STATEMENT**  
for the year ended 31 December 2008

	Note	2008 US \$	2007 US \$
<b>Revenue:</b>			
Investment income	6	<u>133,167,743</u>	<u>186,322,801</u>
<b>Total revenues</b>		<u>133,167,743</u>	<u>186,322,801</u>
Gains and losses on investments	7	(109,518,720)	14,171,127
Other income		<u>78,110</u>	<u>66,037</u>
<b>Total income</b>		<u>23,727,133</u>	<u>200,559,965</u>
<b>Charges:</b>			
Investment expenses	23	(5,941,122)	(6,025,772)
Interest expense	8, 23	(98,469,536)	(176,171,364)
Impairment charges	11	(34,656,529)	(1,085,254)
Operating expenses	9, 10, 23	<u>(12,586,079)</u>	<u>(15,101,345)</u>
<b>Total charges</b>		<u>(151,653,266)</u>	<u>(198,383,735)</u>
<b>Income/(loss) before tax</b>		<u>(127,926,133)</u>	<u>2,176,230</u>
Tax (expense)/credit	12	<u>469,922</u>	<u>(508,545)</u>
<b>Net income/(loss)</b>		<u>(127,456,211)</u>	<u>1,667,685</u>
<b>Net income/(loss) attributable to equity holders of the company</b>		<u>(127,456,211)</u>	<u>1,667,685</u>

Approved by the Directors on behalf of the Board

Directors: **Thomas Hartlage**                      **Redmond Murphy**  
Date: 27 April 2009

**BALANCE SHEET**  
at 31 December 2008

	Note	2008 US \$	2007 US \$
<b>ASSETS</b>			
Mortgage loans	13	414,289,991	456,802,389
Bond available-for-sale investments	5	1,964,631,420	2,532,061,358
Investments at fair value through profit or loss	14	142,075,094	203,886,523
Derivatives	15	582,678,319	391,435,634
Deferred tax asset	12	92,430,707	21,871,261
Trade and other receivables	16	20,431,362	1,571,626
Accrued income on investments		76,641,533	78,992,027
Cash and cash equivalents	17	<u>294,737,547</u>	<u>483,484,071</u>
<b>TOTAL ASSETS</b>		<u><u>3,587,915,973</u></u>	<u><u>4,170,104,889</u></u>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity attributable to equity holders of the company:</b>			
Issued share capital	18	44,904	44,904
Contributed capital	19	164,217,444	49,217,624
Other reserves	20	(640,714,949)	(150,089,374)
Retained earnings		<u>(132,377,054)</u>	<u>(4,920,843)</u>
<b>Total equity</b>		<u>(608,829,655)</u>	<u>(105,747,689)</u>
<b>Liabilities:</b>			
Note liabilities	21	3,881,136,846	3,737,273,211
Derivatives	15	186,697,916	43,559,016
Mortgage loan escrow		2,158,733	5,278,642
Short-term borrowing	23	-	-
Trade and other payables	22	4,882,264	8,999,387
Derivatives collateral liability	15, 23	<u>121,869,869</u>	<u>480,742,322</u>
<b>Total liabilities</b>		<u>4,196,745,628</u>	<u>4,275,852,578</u>
<b>TOTAL EQUITY AND LIABILITIES</b>		<u><u>3,587,915,973</u></u>	<u><u>4,170,104,889</u></u>

Approved by the Directors on behalf of the Board

Directors: **Thomas Hartlage**                      **Redmond Murphy**  
Date: 27 April 2009

**STATEMENT OF CHANGES IN EQUITY**  
for the year ended 31 December 2008

	Issued share capital US \$	Contributed capital US \$	Other reserves US \$	Retained earnings US \$	Total equity US \$
<b>Balance at 1 January 2007</b>	<u>44,904</u>	<u>31,466,737</u>	<u>1,511,920</u>	<u>(6,588,528)</u>	<u>26,435,033</u>
Bond available-for sale investments change in unrealised gains/(losses), net of tax (see note 20)	<u>-</u>	<u>-</u>	<u>(151,601,294)</u>	<u>-</u>	<u>(151,601,294)</u>
<b>Net income/(expense) recognised directly in equity</b>	<u>-</u>	<u>-</u>	<u>(151,601,294)</u>	<u>-</u>	<u>(151,601,294)</u>
Loss for the period	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,667,685</u>	<u>1,667,685</u>
<b>Total recognised income/ (expense) for the year</b>	<u>-</u>	<u>-</u>	<u>(151,601,294)</u>	<u>1,667,685</u>	<u>(149,933,609)</u>
Capital contributions (see note 19)	<u>-</u>	<u>17,750,000</u>	<u>-</u>	<u>-</u>	<u>17,750,000</u>
Non-cash capital contributions	<u>-</u>	<u>887</u>	<u>-</u>	<u>-</u>	<u>887</u>
<b>Balance at 31 December 2007</b>	<u>44,904</u>	<u>49,217,624</u>	<u>(150,089,374)</u>	<u>(4,920,843)</u>	<u>(105,747,689)</u>
Bond available-for sale investments change in unrealised gains/(losses), net of tax (see note 20)	<u>-</u>	<u>-</u>	<u>(490,625,575)</u>	<u>-</u>	<u>(490,625,575)</u>
<b>Net income / (expense) recognised directly in equity</b>	<u>-</u>	<u>-</u>	<u>(490,625,575)</u>	<u>-</u>	<u>(490,625,575)</u>
Loss for the period	<u>-</u>	<u>-</u>	<u>-</u>	<u>(127,456,211)</u>	<u>(127,456,211)</u>
<b>Total recognised income/ (expense) for the year</b>	<u>-</u>	<u>-</u>	<u>(490,625,575)</u>	<u>(127,456,211)</u>	<u>(618,081,786)</u>
Capital contributions (see note 19)	<u>-</u>	<u>115,000,000</u>	<u>-</u>	<u>-</u>	<u>115,000,000</u>
Non-cash capital contributions	<u>-</u>	<u>(180)</u>	<u>-</u>	<u>-</u>	<u>(180)</u>
<b>Balance at 31 December 2008</b>	<u>44,904</u>	<u>164,217,444</u>	<u>(640,714,949)</u>	<u>(132,377,054)</u>	<u>(608,829,655)</u>

**CASH FLOW STATEMENT**  
for the year ended 31 December 2008

	Note	2008 US \$	2007 US \$
<b>Cash flows from operating activities:</b>			
Proceeds from issuance of notes	21	42,857,000	1,179,961,511
Interest received on investments		164,656,485	193,927,798
Interest paid on investments		(5,478,425)	(10,132,689)
Derivative interest paid or received		1,867,971	(94,460,857)
Proceeds from sale of investments		551,168,254	670,528,151
Purchase of investments		(523,798,212)	(1,763,683,921)
Collateral deposits	15	(358,872,453)	331,171,862
Payments to vendors and related party service providers		(5,916,458)	(11,621,190)
Interest paid on notes		(126,328,408)	(75,053,261)
Notes repurchased		(32,537,696)	
Fees paid		(10,094,399)	(8,741,134)
Income taxes paid		(156)	(2,052)
<b>Net cash flows from operating activities</b>		<u>(302,476,497)</u>	<u>411,894,218</u>
<b>Cash flows from financing activities:</b>			
Proceeds from capital contributions received	19	115,000,000	17,750,000
Proceeds from intercompany borrowing	23	291,500,000	803,900,000
Repayment of intercompany borrowing	23	(291,500,000)	(899,100,000)
Interest paid for intercompany borrowing	23	(1,270,027)	(3,604,892)
<b>Net cash flows from financing activities</b>		<u>113,729,973</u>	<u>(81,054,892)</u>
<b>Net increase or decrease in cash and cash equivalents</b>		(188,746,524)	330,839,326
Cash and cash equivalents at 1 January		<u>483,484,071</u>	<u>152,644,745</u>
<b>Cash and cash equivalents at 31 December</b>	17	<u><u>294,737,547</u></u>	<u><u>483,484,071</u></u>

**NOTES TO THE FINANCIAL STATEMENTS**

**31 December 2008**

**1. Approval of financial statements**

The financial statements of AEGON Global Institutional Markets plc (AGIM) for the year ended 31 December 2008 were authorised for issue in accordance with a resolution of the directors on 27 April 2009.

**2. Company information**

AGIM is incorporated and operating in Ireland as a public limited liability company for the purpose of issuing medium term notes and investing in a diversified portfolio of eligible assets with the proceeds of the issued notes. AEGON Financial Assurance Ireland Limited (AFA), another AEGON Ireland entity, provides a financial guarantee for the medium term notes issued by AGIM. AFA is an Irish limited liability non-life insurance company regulated by the Financial Regulator of Ireland. AEGON Ireland Services Limited (AIS) is an Irish limited liability company that provides support services for AGIM and AFA. AGIM, AFA and AIS are indirect, wholly owned, subsidiaries of AEGON N.V..

**3. Description of note programme and financial guarantees**

The AGIM Euro 3,000,000,000 Secured Medium Term Note Programme is listed on the Irish Stock Exchange. Notes have been issued since 2005. The notes are secured by a floating charge on a diversified asset pool maintained by AGIM for the benefit of the noteholders. These assets must be invested in accordance with the investment guidelines outlined in the note programme document and will be managed by two related parties who are subsidiaries of AEGON N.V. (AEGON USA Investment Management, LLC and AEGON USA Realty Advisors, Inc.) and any sub advisors they hire.

Under the note programme and related agreements, AGIM and AFA must maintain, at the date of any new note and financial guarantee issuance, a minimum capital threshold equal to or greater than 1 percent and 3 percent, respectively, of the book value of notes outstanding and notes proposed to be issued. Capital is defined as the aggregate amount of its issued share capital, contributed capital and retained earnings.

No notes may be issued by AGIM pursuant to the note programme and related agreements unless a related financial guarantee from AFA is also issued and certain conditions are met regarding AFA's credit rating. Each financial guarantee provides for AFA to unconditionally and irrevocably make timely payment of all amounts due and payable in respect of the notes covered by the financial guarantee that have been unpaid by AGIM to the notes Trustee. In return for providing this financial guarantee, AFA receives a negotiated fee that is accrued and paid quarterly in arrears. If the guarantee fee is not paid when due, interest will accrue on the amount due until payment is received.

If a guarantee payment has been made to the noteholders, and all noteholder obligations have been satisfied, AFA may request reimbursement from AGIM for amounts paid under the financial guarantee plus accrued interest. AFA will be paid the lesser of the amount owed or the amount in excess of AGIM's minimum capital threshold. If a default occurs under the note programme, AFA will have recourse to eligible investments and other assets of AGIM remaining after noteholder obligations have been satisfied.

**4. Accounting policies**

**(a) Basis of accounting**

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. The adoption of new or revised IFRS Standards and Interpretations are listed below.

The financial statements are prepared on the historical cost basis with the exception of certain financial instruments that are measured at fair value. All amounts in the notes are shown in US dollars (\$) unless otherwise stated.

**(b) Adoption of new or revised IFRS Accounting Standards and Interpretations**

New standards become effective on the date specified by IFRS but companies may be allowed to opt for an earlier adoption date. In 2008, AGIM has adopted the following new and revised Standards and Interpretations issued by the International Accounting Standards Board (the IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for accounting periods beginning on 1 January 2008 as adopted by the European Union. The

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(b) Adoption of new or revised IFRS Accounting Standards and Interpretations (Continued)

IFRS accounting standards and interpretations discussed below have been consistently applied for all of the years presented:

- IFRIC 14; IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction;
- IAS 39 (Revised) and IFRS 7 (Revised) Reclassification of Financial Assets

IFRIC 14 provides general guidance on how to assess the limit in IAS 19 Employee Benefits on the amount of the surplus that can be recognised as an asset in case of a surplus in the funding. It also explains how the pension asset or liability may be affected when there is a statutory or contractual minimum funding requirement. This interpretation had no impact on AGIM equity or net income.

The amendments to IAS 39 and IFRS 7 permit certain reclassifications of non-derivative financial assets out of the fair value through profit or loss category in certain circumstances. The amendments also permit an entity to transfer from the available-for-sale category to the loans and receivables category where certain requirements are met. These amendments were not applicable to AGIM's equity or net income.

The following interpretation and standards were issued before 1 January 2009 and will be applied in the coming years:

- IFRS 8 Operating Segments;
- IAS 23 (Revised) Borrowing Costs;
- IAS 1 (Revised) Presentation of Financial Statements;
- IFRS 2 (Revised) Share-based Payments;
- IAS 32 (Revised) and IAS 1 (Revised) Puttable Financial Instruments;
- Improvements to IFRS;
- IAS 39 (Revised) Eligible Hedged Items

AGIM intends to adopt IFRS 8 on the required adoption date of 1 January 2009. IFRS 8 replaces IAS 14 Segment Reporting and adopts a management approach to segment reporting. This standard has no impact on AGIM.

AGIM intends to adopt the amendments to IAS 23 on the required adoption date of 1 January 2009. The amendments to IAS 23 remove the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. The adoption of the amendment is not expected to impact AGIM's equity or net income.

AGIM intends to adopt the revisions to IAS 1 on the required adoption date of 1 January 2009. IAS 1 will require changes in equity to be presented separately for owners and non-owners. The changes in equity for non-owners will be presented in the new statement of comprehensive income. This revised standard is not expected to impact AGIM's equity or net income.

AGIM intends to adopt the revisions to IFRS 2 on the required adoption date of 1 January 2009. The amendments to IFRS 2 define the term vesting condition and give guidance on the accounting for non-vesting conditions. The adoption of the amendment is not expected to have a material impact on AGIM's equity or net income.

AGIM intends to adopt the amendments to IAS 32 and IAS 1 on the required adoption date of 1 January 2009. In accordance with the amendment to IAS 32, certain instruments normally classified as liabilities are classified as equity if they meet certain conditions. The revised standard is not expected to have a material impact on AGIM's equity or net income.

AGIM intends to adopt the May 2008 amendments to IFRS, which resulted from the IASB's annual improvements project. These amendments result in accounting changes for presentation, recognition or measurement purposes as well as terminology or editorial amendments related to a variety of individual standards. Most of the amendments are effective for annual periods beginning on or after 1 January 2009, with earlier adoption permitted. AGIM is currently evaluating the potential impact of these amendments on AGIM's equity and net income.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(b) Adoption of new or revised IFRS Accounting Standards and Interpretations (Continued)

AGIM intends to adopt the amendments to IAS 39 issued in July 2008, subject to European Union endorsement. These amendments are required to be adopted for annual periods beginning on or after 1 July 2009. These amendments clarify how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The adoption of the amendments is not expected to have a material impact on AGIM's equity or net income.

(c) Change in balance sheet presentation

The balance sheet presentation of AGIM assets and liabilities has been changed from a current / non-current distinction to a presentation based on liquidity under IAS 1. These changes have been applied retrospectively. The presentation based on liquidity is more relevant because AGIM does not supply services within a clearly identifiable operating cycle.

(d) Foreign currencies

Under IAS 21, the financial statements are expressed in US dollars (\$), which is both the presentation and functional currency. Transactions during the period denominated in foreign currencies have been translated primarily using average rates of exchange as approximations for transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated to US dollars at the rates of exchange ruling at the balance sheet date. The resulting gains or losses are recorded in the income statement. Non-monetary items carried at cost are translated using the exchange rate at the date of the transaction; items carried at fair value are translated at the exchange rate when fair value was determined.

(e) Segment reporting

Under IAS 14, AGIM has only one business segment and one geographical segment; therefore, segment reporting information is not required.

(f) Revenue recognition

Revenue arising from income on assets is recognised in the accounting period in which the revenues are earned.

(g) Investment income

Investment income is composed of interest income earned during the period. Interest income is recognised using the effective interest rate method.

(h) Taxation

Corporation tax represents the sum of the tax currently payable and deferred corporation tax.

The tax currently payable is based on taxable profit for the year. Taxable profit can differ from profit as reported in the income statement because it may exclude items of income or expense that are taxable or deductible in other years and it may exclude items that are never taxable or deductible. The liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profits will be available against which deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Unrecognised deferred tax assets, if any, are also reassessed at each balance

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(h) Taxation (Continued)

sheet date and are recognised when and if it becomes probable that the deferred tax asset will be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also reflected in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities, when the deferred taxes relate to the same taxable entity and the same taxation authority, and there is intent to settle current tax assets and liabilities on a net basis or to realise the asset and settle the liability simultaneously.

(i) Mortgage loans

Under IAS 39, mortgage loans are initially recognised at cost (excluding accrued interest) plus directly attributable transaction costs at the funding date. They are subsequently carried at amortised cost using the effective interest method less allowance for impairments.

(j) Bond available-for-sale investments

Under IAS 39, bond investments reported as available-for-sale are recognised on the trade date at cost (excluding accrued interest) plus directly attributable transaction costs. These investments are subsequently valued at fair value with the change in unrealised gains/losses recorded to equity in other reserves. When these investments are sold or impaired, the accumulated fair value adjustments are included in the income statement as net gains or net losses on investments. Bond investments classified as available-for-sale are investments that are not designated as held-to-maturity or at fair value through profit or loss.

(k) Derivatives

AGIM uses interest rate and cross-currency swaps to economically hedge exposure to interest rate and currency risks. An interest rate swap is an agreement between two parties to exchange, at specific dates, the difference between a fixed interest rate or a floating interest rate payment on a predetermined notional amount. Cross currency swap agreements are contracts to exchange two principal amounts of two currencies at the prevailing exchange rate at inception of the contract. During the life of the swap, the counterparties exchange fixed or floating rate interest payments in the swapped currencies and at maturity the principal amounts are swapped at a pre-determined rate of exchange. These swaps are recognised at cost at the trade date and subsequently valued at fair value. Swaps used to economically hedge the risk exposures associated with the change in fair value of a recognised asset or liability are designated as fair value hedges for accounting purposes. When a fair value hedge meets the conditions of hedge accounting treatment, any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and is recognised in the income statement. Hedge ineffectiveness resulting from this difference is reflected in net gain or loss on investments. If the swaps do not qualify for hedge accounting, any gains or losses for the year arising from changes in fair value are taken directly to net gain or loss on investments in the income statement.

Hedges that are no longer considered highly effective are derecognised. The derivative is prospectively accounted for as a freestanding derivative. The amount previously recognised as a remeasurement of the hedged item (fair value hedge) is released to the income statement in accordance with the accounting policies for the hedged item.

Swap interest is recorded in investment income for swaps hedging investments and in interest expense for swaps hedging note liabilities. Receivables/payables relating to accrued interest are netted because AGIM has the legal ability and intent to net settle these amounts.

When cash collateral is received or pledged, the cash is recognised or derecognised accordingly and the net balance at the reporting date is recorded as a receivable or a liability. AGIM has the legal ability and intent to net settle these amounts.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(l) Investments at fair value through profit or loss

AGIM has elected the option to carry its investment in shares of a hedge fund of funds at fair value through profit or loss. The investment is managed on a total return basis. Recognising the change in value in income is consistent with the risk management strategy. AGIM has investments in credit linked notes which contain embedded credit derivatives. In lieu of bifurcating the embedded derivative, AGIM has also designated these notes to be carried at fair value through profit or loss. These investments are recognised on the funding date at cost and are subsequently valued at fair value with the change in fair value recorded through profit or loss.

(m) Amortised cost

The amortised cost of a debt instrument is the amount at which it is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation of any difference between the initial amount and the maturity amount, and minus any reduction for impairment. The effective interest rate method is a method of calculating the amortised cost and of allocating the interest income or expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the debt instrument or, when appropriate, a shorter period to the net carrying amount of the instrument. When calculating the effective interest rate, all contractual terms are considered, with the exception of future credit losses. Fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts are included in the calculation.

(n) Fair value

The financial statements provide information on the fair value of all financial instruments, including those carried at amortised cost where the values are provided as comparative data in the notes to the financial statements.

The fair value of a financial instrument is the amount for which it could be exchanged or settled between knowledgeable, willing parties in an arm's length transaction. For quoted financial assets for which there is an active market, the fair value is the bid price at the balance sheet date. In the absence of an active market, fair value is estimated by using present value or other valuation techniques. Where discounting techniques are applied, the discount rate is based on current market rates applicable to financial instruments with similar characteristics. The valuation techniques that include non-market observable inputs can result in a different outcome than the actual transaction price at which the asset was acquired. Such differences are not recognised in the income statement immediately but are deferred. They are released over time to the income statement in line with the change in factors (including time) that market participants would consider in setting a price for the asset.

Interest accrued to date is not included in the fair value of the financial assets.

(o) Derecognition

A financial asset is derecognised when the contractual rights to the asset's cash flows expire, when the asset has been transferred along with substantially all the risks and rewards of ownership, or when the asset has been transferred without the transfer of substantially all the risks and rewards of ownership, provided the other party can sell or pledge the asset. A transfer of an asset generally involves the transfer of the contractual right to receive cash flows of the asset. Financial assets, in respect of which AGIM has neither transferred nor retained all the risks and rewards, are recognised to the extent of AGIM's continuing involvement. On derecognition, the difference between the disposal proceeds and the carrying amount is recognised in the income statement as a realised gain or loss. Any cumulative unrealised gain or loss previously recognised in Equity – other reserves is also recognised in the income statement.

Derecognition of the note liability is scheduled to occur at maturity.

(p) Impairment of assets

An asset is impaired if the amortised cost exceeds the amount that would be recovered through its use or sale. Asset values are routinely evaluated when there are indications that the asset may be impaired.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(p) Impairment of assets (Continued)

Available-for-sale investments are impaired to the asset's fair value and any net revaluation recognised in equity is reversed. Once impaired, the interest accretion on an available-for-sale asset is based on the rate of return that would be required by the market for similar rated investments at the date of impairment.

For debt instruments carried at amortised cost the impairment loss is calculated as the difference between the carrying and recoverable amount of the asset. The recoverable amount is determined by discounting the estimated probable future cash flows at the original effective interest rate of the asset. For floating rate assets, the current effective interest rate under the contract is applied.

Impairment losses can be reversed if in subsequent periods the amount of the impairment loss decreases and that decrease can be related objectively to an event occurring after the impairment was recognised.

(q) Cash and cash equivalents

Cash equivalents are short-term highly liquid investments that are readily convertible to known cash amounts, are subject to insignificant risks of changes in value and are held for the purpose of meeting short-term cash commitments.

(r) Short-term borrowings

Short-term borrowings with AEGON USA, a related party, are initially recognised at cost (which is fair value). Subsequently, these borrowings are valued at amortised cost. Interest amounts on the borrowings are expensed as incurred.

(s) Note liabilities

Note liabilities are recognised at trade date at cost (which is fair value net of transaction costs). They are subsequently accounted for at amortised cost with amortisation reflected in interest expense.

(t) Trade and other receivables

Trade and other receivables are initially recognised at fair value and are subsequently measured at amortised cost. Carrying value approximates fair value.

(u) Trade and other payables

Trade and other payables are initially recognised at fair value and are subsequently measured at amortised cost. Carrying value approximates fair value.

(v) Critical accounting estimates and judgements in applying accounting policies

Application of the accounting policies in the preparation of the financial statements requires management to apply judgements involving assumptions and estimates concerning future results or other developments, including the likelihood, timing or amount of future transactions or events. Actual results could differ materially from those estimates. Accounting policies that are critical to the financial statement presentation and that require complex estimates or significant judgements are described in the following sections.

IAS 39 Financial Instruments: Recognition and Measurement was amended late in 2008 permitting companies with a choice to reclassify certain financial assets between categories, the effect of which would be to hold assets at "deemed cost" (cost determined during the third or fourth quarter of 2008) and discontinue mark-to-market valuation. Moreover, the IASB published clarifications in the fourth quarter of 2008 of valuation techniques in illiquid or distressed markets including describing additional situations when mark-to-model valuations would be appropriate. AGIM has not reclassified assets held as available-for-sale (AFS) to loans or held-to-maturity assets. Also, AGIM transferred a very limited amount of assets valued based on market prices to mark-to-model valuations, driven by current market developments.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

- (v) Critical accounting estimates and judgements in applying accounting policies (Continued)

*Fair value of financial instruments determined using valuation techniques*

When available, AGIM uses quoted market prices in active markets to determine the fair value of investments and derivatives. In the absence of an active market, the fair value of investments in financial assets is estimated by using other market observable data such as external quotes and present value or other valuation techniques. An active market is one in which transactions are taking place regularly on an arm's length basis. Although not necessarily determinative, indicators that a market is inactive are lower transaction volumes, reduced transaction sizes and, in some cases, no observable trading activity for short periods. A fair value measurement assumes that an asset or liability is exchanged in an orderly transaction between market participants, and accordingly, fair value is not determined based upon a forced liquidation or distressed sale.

Valuation techniques are used when AGIM determines the market is inactive for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, that is, to arrive at the price at which an orderly transaction would occur between market participants at the measurement date. Therefore, unobservable inputs reflect AGIM's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). These inputs are developed based on the best information available.

AGIM employs an oversight structure over valuation of financial instruments that includes appropriate segregation of duties. Senior management, independent of the investing functions, is responsible for the oversight of control and valuation policies and for reporting the results of these policies. For fair values determined by reference to external quotation or evidenced pricing parameters, independent price determination or validation is utilised. Adjustments made to fair values as a result of the validation process are reported to senior management.

For derivatives where quoted market prices are not available, other valuation techniques are applied. The valuation techniques incorporate all factors that market participants would consider and are based on observable market data when available. All models are validated before they are used and calibrated to ensure that outputs reflect actual experience and comparable market prices. These derivatives may be valued using pricing models based on the net present value of estimated future cash flows, directly observed prices from exchange-traded derivatives, other over-the-counter trades, or external pricing services. Most valuations are derived from curves and volatility matrices, which are constructed for applicable indices and currencies using current market data from many industry standard sources. Option pricing is based on industry standard valuation models and current market levels, where applicable.

The fair values of investments held in non-quoted investment funds (hedge funds) are determined by management after taking into consideration information provided by the fund managers. AGIM reviews the valuations each month and performs analytical procedures and trending analyses to ensure the fair values are appropriate.

*Debt securities*

When available, AGIM uses quoted market prices in active markets to determine the fair value of its debt securities. These market quotes are obtained through index prices or pricing services.

The fair values of debt securities (including ABS–Housing and CMBS securities) are determined by management after taking into consideration several sources of data. AGIM's valuation policy dictates that publicly available prices are initially sought from several third party pricing services. In the event that pricing is not available from these services, those securities are submitted to brokers to obtain quotes. The majority of brokers' quotes are non-binding. As part of the pricing process AGIM assesses the appropriateness of each quote (i.e. as to whether the quote is based on observable market transactions or not) to determine the most appropriate estimate of fair value. Lastly, securities are priced using internal cash flow modelling techniques. These valuation methodologies commonly use the following inputs: reported trades, bids, offers, issuer spreads, benchmark yields, estimated prepayment speeds, and/or estimated cash flows. Only pricing services and brokers with a substantial presence in the market and with appropriate experience and expertise are used.

Third party pricing services will often determine prices using recently reported trades for identical or similar securities. The pricing service makes adjustments for the elapsed time from the trade date to the

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(v) Critical accounting estimates and judgements in applying accounting policies (Continued)

balance sheet date to take into account available market information. Lacking recently reported trades, third party pricing services and brokers will use modelling techniques to determine a security price where expected future cash flows are developed based on the performance of the underlying collateral and discounted using an estimated market rate. Also included within the modelling techniques for ABS-Housing and CMBS securities are estimates of the speed at which principal will be repaid over their remaining lives. These estimates are determined based on historical repayment speeds (adjusted for current markets) as well as the structural characteristics of each security.

Each month, AGIM performs an analysis of the inputs obtained from third party services and brokers to ensure that the inputs are reasonable and produce a reasonable estimate of fair value. AGIM's asset specialists and investment valuation specialists consider both qualitative and quantitative factors as part of this analysis. Several examples of analytical procedures performed include, but are not limited to, recent transactional activity for similar debt securities, review of pricing statistics and trends and consideration of recent relevant market events.

Credit ratings are an important consideration in the valuation of securities and are included in the internal process for determining AGIM's view of the risk associated with each security. However, AGIM does not rely solely on external credit ratings and there is an internal process, based on market observable inputs, for determining AGIM's view of the risks associated with each security.

AGIM's portfolio of private placement securities (held at fair value under the classification of available-for-sale) is valued using a matrix pricing methodology. The pricing matrix is obtained from a third party service provider and indicates current spreads for securities based on weighted average life, credit rating and industry sector. Each month, AGIM's asset specialists review the matrix to ensure the spreads are reasonable by comparing them to observed spreads for similar bonds traded in the market. Other inputs to the valuation include coupon rate, the current interest rate curve used for discounting and an illiquidity premium to account for the illiquid nature of these securities. The illiquidity premiums are determined based upon the pricing of recent transactions in the private placements market; comparing the value of the privately offered security to a similar public security. The impact of the illiquidity premium for private placement securities in 2008 and 2007 to the overall valuation is insignificant.

*Mortgages (held at amortised cost)*

For private loans, fixed interest mortgage and other loans originated by AGIM, the fair value used for disclosure purposes is estimated by discounting expected future cash flows using a current market rate applicable to financial instruments with similar yield, credit quality and maturity characteristics.

The fair value of floating interest rate mortgages, policy loans and private placements used for disclosure purposes is assumed to be approximated by their carrying amount adjusted for changes in credit risk, where appropriate, based on market observable credit spreads.

*Fair value measurement*

The fair values of the financial instruments carried at fair value were determined as follows:

31 December 2008 US \$	Published price quotations in an active market <sup>1</sup>	Valuation technique-based on market observable inputs <sup>2</sup>	Valuation technique-not based on market observable inputs <sup>3</sup>	Total
<b>Financial Assets</b>				
Bond available-for-sale investments	-	1,949,165,597	15,465,823	1,964,631,420
Investments at fair value through profit or loss	-	64,295,200	77,779,894	142,075,094
Derivatives	-	582,678,319	-	582,678,319
<b>Total Financial Assets</b>	-	<b>2,596,139,116</b>	<b>93,245,717</b>	<b>2,689,384,833</b>
<b>Financial Liabilities</b>				
Derivatives	-	186,697,916	-	186,697,916

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**
**4. Accounting policies (Continued)**

(v) Critical accounting estimates and judgements in applying accounting policies

31 December 2007 US \$	Published price quotations in an active market <sup>1</sup>	Valuation technique- based on market observable inputs <sup>2</sup>	Valuation technique-not based on market observable inputs <sup>3</sup>	Total
<b>Financial assets</b>				
Bond available-for-sale investments	884,017,772	1,613,928,921	34,114,665	2,532,061,358
Investments at fair value through profit or loss	-	91,586,691	112,299,832	203,886,523
Derivatives	-	391,435,634	-	391,435,634
<b>Total financial assets</b>	<b>884,017,772</b>	<b>2,096,951,246</b>	<b>146,414,497</b>	<b>3,127,383,515</b>
<b>Financial liabilities</b>				
Derivatives	-	43,559,016	-	43,559,016

<sup>1</sup> Included in this category are financial assets and liabilities that are measured by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. Main asset classes included in this category are financial assets for which the fair value is determined by management using various inputs, including pricing vendors or binding broker quotes and assets for which the fair value is determined by reference to indices.

<sup>2</sup> Included in this category are financial assets and liabilities that are measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions in the same or similar instrument or based on available market data. Main assets included in this category are financial assets for which pricing is determined by management based on various market observable inputs but may include insignificant assumptions which are not observable, such as the illiquidity premium assumption used in the valuation of private placements.

<sup>3</sup> Not based upon market observable input means that fair values are determined by management in whole or in part using a valuation technique (model) for which a significant input is not based on observable market data. A significant input is an input that is significant to the fair value measurement in its entirety. Main asset classes in this category are hedge funds.

Valuation techniques are used to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, that is, an exit price from the perspective of AGIM. Therefore, unobservable inputs reflect AGIM's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk).

The potential effect of using reasonably possible alternative assumptions for valuing financial instruments is not believed to have a significant impact on AGIM's net profit.

**Impairment of financial assets**

There are a number of significant risks and uncertainties inherent in the process of monitoring investments and determining if impairment exists. These risks and uncertainties include the risk that the assessment of an issuer's ability to meet all of its contractual obligations will change based on changes in the credit characteristics of that issuer and the risk that the economic outlook will be worse than expected or have more of an impact on the issuer than anticipated. Also, there is a risk that new information or changes in other facts and circumstances will cause a change in an investment decision. Any of these situations could result in a charge against the income statement in a future period to the extent of the impairment charge recorded.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

- (v) Critical accounting estimates and judgements in applying accounting policies (Continued)

*Debt securities*

AGIM regularly monitors industry sectors and individual debt securities for evidence of impairment. This evidence may include one or more of the following: 1) deteriorating market to book ratio, 2) increasing industry risk factors, 3) deteriorating financial condition of the issuer, 4) covenant violations, 5) high probability of bankruptcy of the issuer or 6) nationally recognised credit rating agency downgrades. Additionally, for asset-backed securities, cash flow trends and underlying levels of collateral are monitored. A security is impaired if there is objective evidence that a loss event has occurred after the initial recognition of the asset that has a negative impact on the estimated future cash flows. A specific security is considered to be impaired when it is determined that it is probable that not all amounts due (both principal and interest) will be collected as scheduled.

ABS-Housing securities and CMBS are monitored and reviewed on a monthly basis with detailed modelling completed on each portfolio quarterly. Model output is generated under a base and several stress-case scenarios. ABS-Housing and CMBS asset specialists utilise modelling software to perform a loan-by-loan, bottom-up approach to modelling. The ABS-Housing models incorporate market estimates on the property market, borrowing characteristics, propensity of a borrower to default or prepay and the overall security structure. The CMBS models incorporate market estimates on the property market, capital markets, property cash flows and loan structure. The results from the models are then closely analysed by the asset specialist to determine whether or not a principal or interest loss is expected to occur.

In addition, on a monthly basis, AGIM reviews all ABS-Housing securities and CMBS that have been in an unrealised loss position of greater than 12 months and those with a month to month market value decline of 5%. Additional reviews include a realised loss analysis and analysis of holdings with a price decline of 10% or more during the quarter. ABS-Housing securities and CMBS noted on exception reports are specifically addressed by research and credit analysts who evaluate the unrealised losses based upon current market conditions, changes in credit spreads specific to the asset class, and fundamentals related to the issuer. Impairments are recorded in instances where loss events have taken place that would affect future cash flows. The impairment analysis is therefore based on a combination of models and analysts' review of market events on individual securities.

As at the reporting date, AGIM performed stress testing on each security within its subprime mortgage portfolio. The stress testing revealed a significant reduction in the margin of safety for all fixed rate and senior floating rate mortgage products. Factors included in the analysis depend upon the type of collateral but for subprime mortgages they include delinquencies, prepayment assumptions, the percentage of borrowers with mortgage insurance, the percentage of borrowers in states more at risk for declining home values (Florida, California etc.) and credit enhancements. More detailed cash flow modelling was performed on issuances identified as being most at risk, such as issuances with a disproportionate number of borrowers from states experiencing significant declines in home values. Cash flows were modelled using the current collateral pool and capital structure to determine whether there has been an adverse change in cash flows (i.e. an event has occurred that would impact estimated future cash flows). Defaults were estimated by identifying the loans that are in various delinquency buckets and defaulting a certain percentage of them over the near-term and long-term. Recent payment history, a percentage of on-going delinquency rates and a constant repayment rate are also incorporated into the model. Once the entire pool is modelled, AGIM can determine whether the particular tranche or holding is at risk for payment interruption. Under these scenarios, the securities held in AGIM's subprime mortgage portfolio model full payment of principal and interest as of the reporting date.

*Recognition of deferred tax assets*

Deferred tax assets are established for the tax benefit related to deductible temporary differences, carry-forwards of unused tax losses and carry-forwards of unused tax credits when, in the judgement of management, it is more likely than not that AGIM will receive the tax benefits. Since there is no absolute assurance that these assets will ultimately be realised, management reviews AGIM's deferred tax positions periodically to determine if it is more likely than not that the assets will be realised. Periodic reviews include, among other things, the nature and amount of the tax income and expense items, the expected timing when certain assets will be used or liabilities will be required to be reported and the profitability of business expected to provide future earnings. Furthermore, management considers tax-planning strategies it can utilise to increase the likelihood that the tax assets will be realised. These strategies are also considered in the periodic reviews.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**4. Accounting policies (Continued)**

(w) Comparatives

Where necessary, comparatives have been reclassified and repositioned for consistency with current year disclosures.

**5. Management of financial risk and capital**

AGIM has an exposure to financial risk based on its note transactions. AGIM expects to earn a spread based on the difference between the investment return on the assets supporting the note liabilities and the interest credited and accrued to the noteholders. AGIM also earns investment returns on assets supporting its equity. The key financial risk is that proceeds from its financial assets are not sufficient to fund the note liability obligations. The most important components of this financial risk are credit risk, maturity mismatch risk, interest rate risk, hedge fund risk and liquidity risk. AGIM hedges essentially all of its foreign exchange risk so that all assets and liabilities are ultimately swapped to US dollars.

*Managing credit risk*

AGIM is exposed to credit risk on its bonds, mortgage loans, short term deposits and derivatives. Some issuers may default on their financial obligations for various reasons including bankruptcy, lack of liquidity, downturns in the economy or downturns in real estate values, operational failure or fraud.

AGIM manages its credit risk exposure by individual counterparty, sector and asset class. Management requires that the exposures in each of these are limited to ensure that excessive concentrations of credit risk are avoided and to ensure an appropriately diversified portfolio. To mitigate credit risk in derivative transactions, AGIM has executed a Credit Support Annex (the "Agreement") as part of the International Swaps and Derivatives Association (ISDA) Master Agreement with its derivative counterparty AEGON Derivatives N.V., a related party. The Agreement establishes a collateral protocol which features a master netting arrangement. The master netting arrangement provides for the netting of financial assets and liabilities arising from derivative transactions. Credit risk associated with these financial assets is eliminated only to the extent that financial liabilities exist to offset the exposure. The collateral supporting the derivative transactions ensures that AGIM is protected from the credit exposure that could otherwise arise as a result of market value changes on transactions in its favour. Transactions that occur subsequent to the balance sheet date can change the overall credit exposure in a short period.

AGIM monitors its credit risk exposures on an ongoing basis. AGIM records impairments (note 4(p)) and note 11) and establishes allowances for mortgage loan impairments (note 13) in the ordinary course of business. The ratings distribution of the AGIM investment portfolio is presented below.

Maximum credit risk exposure on AGIM assets (fair value):

	Gross exposure	
	2008 US \$	2007 US \$
Mortgage loans	362,822,223	445,679,358
Bonds	1,964,631,420	2,532,061,358
Derivative assets	582,678,319	391,435,634
Short-term deposits	172,060,567	2,383,400
Investments at fair value through profit or loss	142,075,094	203,886,523
Accrued income on investments	76,641,533	78,992,027
Totals	<u>3,300,909,156</u>	<u>3,654,438,300</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**5. Management of financial risk and capital (Continued)**

Credit risk concentrations by credit quality—bonds, including credit-linked notes:

	Carrying value	
	2008 US \$	2007 US \$
AAA	331,221,883	573,720,189
AA	262,190,629	336,815,196
A	510,544,759	484,545,163
BBB	489,525,709	702,430,503
BB	84,228,495	73,248,063
B	28,853,623	58,705,235
Sovereign exposure	46,520,181	55,570,577
Assets not externally rated	275,841,341	338,613,123
Totals	2,028,926,620	2,623,648,049

Credit risk concentrations—Bonds (carrying value):

	2008 US \$	2007 US \$
Asset backed securities (ABS)—Collateralised Bond Obligations (CBOs)	85,172,020	119,710,628
ABS—Housing related	71,891,904	212,750,442
ABS—Credit cards	124,453,929	225,950,846
ABS—Other	157,025,538	231,101,683
Collateralised mortgage backed securities	114,465,647	134,119,962
Collateralised mortgage obligations—non-agency	88,198,144	187,135,888
Financial—Banking	206,262,005	85,904,915
Financial—Brokerage	9,273,800	86,185,692
Financial—Finance Companies	74,245,984	100,130,929
Financial—Insurance	45,132,665	48,085,325
Financial—Real estate investment trusts	58,364,006	87,327,396
Industrial—Basic industry	40,477,162	68,186,272
Industrial—Capital goods	148,777,849	144,709,292
Industrial—Communications	173,688,898	143,756,873
Industrial—Consumer cyclical	92,881,691	141,107,741
Industrial—Consumer non-cyclical	119,181,415	115,588,611
Industrial—Energy	100,741,929	122,860,051
Industrial—Technology	50,906,582	59,527,598
Industrial—Transportation	60,915,815	62,010,690
Utility—Electric	59,129,148	68,554,158
Utility—Natural gas	36,925,108	31,785,789
Sovereign exposure	46,520,181	55,570,577
Totals	1,964,631,420	2,532,061,358

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**5. Management of financial risk and capital (Continued)**

Credit risk concentrations by credit quality—short-term deposits and mortgage loans:

	Carrying value	
	2008 US \$	2007 US \$
AA	-	-
A	172,060,567	2,383,400
BB	-	-
B	-	-
Assets not externally rated	414,289,991	456,802,389
	<hr/>	<hr/>
Totals	586,350,558	459,185,789
	<hr/>	<hr/>

Credit risk concentrations—Short-term deposits (carrying value):

	2008 US \$	2007 US \$
Financial—Other	<u>172,060,567</u>	<u>2,383,400</u>

Credit risk concentrations—Credit-linked notes (carrying value):

	2008 US \$	2007 US \$
Utility—Natural gas	31,491,200	52,535,771
Industrial—Environmental	<u>32,804,000</u>	<u>39,050,920</u>
Totals	<u>64,295,200</u>	<u>91,586,691</u>

Credit risk concentrations—Mortgage loans (carrying value):

	2008 US \$	2007 US \$
Apartment	72,217,133	72,506,200
Industrial	40,654,822	33,917,186
Office	134,738,503	223,126,652
Other commercial	6,618,803	6,837,868
Retail	<u>126,783,043</u>	<u>109,370,580</u>
Subtotal	<u>381,012,304</u>	<u>445,758,486</u>
Origination fees	479,183	499,407
Allowance for impairments	(63,292)	(92,760)
Fair value hedge adjustments	<u>32,861,796</u>	<u>10,637,256</u>
Total	<u>414,289,991</u>	<u>456,802,389</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**5. Management of financial risk and capital (Continued)**

*Alt-A Mortgage*

Alt-A loans are made to borrowers whose qualifying mortgage characteristics do not meet the standard underwriting criteria established by the GSEs (Government-Sponsored Enterprises). The typical Alt-A borrower has a credit score high enough to obtain an "A" standing, which is especially important since the score must compensate for the lack of other necessary documentation related to borrower income and/or assets.

The company's investments in Alt-A mortgages are in the form of mortgage backed securities. The Company's Alt-A investments are primarily backed by loans with fixed interest rates for the entire term of the loan. Additionally, virtually all of the Company's Alt-A positions are AAA rated, and a significant portion of those are invested in super-senior tranches. Mortgage-backed securities classified as super-senior are those that substantially exceed the subordination requirements of AAA-rated securities. The Company's Alt-A portfolio is backed by loans with loan to values (LTVs) greater than 70%, average FICO scores between 660 and 720 at issue, and greater than 50% of the loans in the pool contained limited documentation to support the borrowers' financial position at issue.

*Negative Amortisation Mortgage*

Negative amortisation mortgages (also known as option ARMs) are loans whereby the payment made by the borrower is less than the accrued interest due and the difference is added to the loan balance. When the accrued balance of the loan reaches the negative amortisation limit (typically 110% to 125% of the original loan amount), the loan recalibrates to a fully amortising level and a new minimum payment amount is determined. The home-owner's new minimum payment amount can be dramatically higher than the original minimum payment amount. The timing of when these loans reach their negative amortisation cap will vary, and is a function of the accrual rate on each loan, the minimum payment rate on each loan and the negative amortisation limit itself. Typically, these loans are estimated to reach their negative amortisation limit between 3 and 5 years from the date of origination. The Company's exposure to negative amortisation mortgages is primarily AAA rated, with virtually all of these positions being super-senior AAA rated securities.

The table below provides the fair value of the Alt-A and Residential Mortgage Backed Securities (RMBS) Negative Amortisation portfolio summarised by the credit quality of the underlying loans backing the securities and the vintage year at 31 December.

Estimated Fair Value by Vintage and Rating – Alt-A & Negative Amortisation RMBS

	2004 & Prior US \$	2005 US \$	2006 US \$	2007 US \$	2008 US \$	Total US \$
AAA	1,970,074	3,793,127	27,560,756	5,581,492	-	38,905,449
AA	-	-	449,722	-	-	449,722
A	-	-	-	-	-	-
BBB	-	-	-	-	-	-
<BBB	-	-	80,773	-	-	80,773
Total	<u>1,970,074</u>	<u>3,793,127</u>	<u>28,091,251</u>	<u>5,581,492</u>	<u>-</u>	<u>39,435,944</u>

*Commercial Mortgage Backed Securities*

Commercial mortgage-backed securities (CMBS) are securitisations of underlying pools of mortgages on commercial real estate. The underlying mortgages have varying risk characteristics and are pooled together and sold in different rated tranches. The Company's CMBS includes conduit, large loan, single borrower, and commercial real estate collateral debt obligations (CRE CDOs).

The following table summarises the fair value of the Company's CMBS portfolio by rating and vintage at 31 December:

NOTES TO THE FINANCIAL STATEMENTS  
31 December 2008 (Continued)

5. Management of financial risk and capital (Continued)

Estimated Fair Value by Vintage and Rating – CMBS

	2004 & Prior US \$	2005 US \$	2006 US \$	2007 US \$	2008 US \$	Total US \$
AAA – Senior <sup>(a)</sup>	24,917,266	-	8,865,895	10,040,700	-	43,823,861
AAA – Mezzanine	-	9,031,080	5,414,385	-	-	14,445,465
AAA – Junior	-	-	5,549,025	6,045,800	-	11,954,825
AA	968,446	-	12,120,260	7,812,310	-	20,921,016
A	-	-	-	6,607,480	-	6,607,480
BBB	-	-	4,790,280	5,999,100	-	10,789,380
<BBB	-	-	5,923,620	-	-	5,923,620
Total	<u>25,905,712</u>	<u>9,031,080</u>	<u>42,663,465</u>	<u>36,865,390</u>	<u>-</u>	<u>114,465,647</u>

<sup>(a)</sup> All 2004 and prior AAAs are classified as AAA – Senior. This was prior to the market convention of Credit-enhanced tiering within AAAs, which started in 2005.

Subprime Mortgage

The Company does not currently invest in or originate whole loan residential mortgages. The Company categorises asset backed securities issued by a securitisation trust as having subprime mortgage exposure when the average credit score at issue of the underlying mortgage borrowers in a securitisation trust is below 660. The Company also categorises asset backed securities issued by a securitisation trust with second lien mortgages as subprime mortgage exposure, even though a significant percentage of second lien mortgage borrowers may not necessarily have credit scores below 660 at issue.

The following table provides the fair values of the AFS subprime mortgage exposure by rating and vintage:

Estimated Fair Value by Vintage and Rating – Subprime Mortgage Securities

Subprime Mortgages – Fixed Rate	2004 & Prior US \$	2005 US \$	2006 US \$	2007 US \$	2008 US \$	Total US \$
AAA	-	-	-	-	-	-
AA	-	2,316,382	18,353,022	-	-	20,669,404
A	-	-	-	-	-	-
BBB	-	-	-	-	-	-
<BBB	-	-	-	-	-	-
Total	<u>-</u>	<u>2,316,382</u>	<u>18,353,022</u>	<u>-</u>	<u>-</u>	<u>20,669,404</u>
Subprime Mortgages – Floating Rate	2004 & Prior US \$	2005 US \$	2006 US \$	2007 US \$	2008 US \$	Total US \$
AAA	-	2,072,561	15,596,000	-	-	17,668,561
AA	-	-	18,641,040	-	-	18,641,040
A	1,717,672	-	-	-	-	1,717,672
BBB	431,566	-	4,927,955	652,285	-	6,011,806
<BBB	-	-	-	1,793,850	-	1,793,850
Total	<u>2,149,238</u>	<u>2,072,561</u>	<u>39,164,995</u>	<u>2,446,135</u>	<u>-</u>	<u>45,832,929</u>
Second Lien Mortgages <sup>(a)</sup>	2004 & Prior US \$	2005 US \$	2006 US \$	2007 US \$	2008 US \$	Total US \$
AAA	-	-	-	3,837,181	-	3,837,181
AA	-	-	-	-	-	-
A	-	1,552,390	-	-	-	1,552,390
BBB	-	-	-	-	-	-
<BBB	-	-	-	-	-	-
Total	<u>-</u>	<u>1,552,390</u>	<u>-</u>	<u>3,837,181</u>	<u>-</u>	<u>5,389,571</u>
Grand Total	<u>2,149,238</u>	<u>5,941,333</u>	<u>57,518,017</u>	<u>6,283,316</u>	<u>-</u>	<u>71,891,904</u>

<sup>(a)</sup> Second lien collateral primarily composed of loans to prime and Alt-A borrowers.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**5. Management of financial risk and capital (Continued)**

*Managing maturity and mismatch risk*

Maturity mismatch risk for AGIM arises because the maturities of assets and liabilities are not perfectly matched. As a result, if the assets are longer than the liabilities, assets may need to be liquidated at a loss at the maturity of the liabilities if the liabilities cannot be extended or new liabilities cannot be issued at that time. Conversely, if the assets are shorter than the liabilities, the proceeds from the asset maturities may have to be reinvested at a lower investment spread. Management requires that the ongoing maturity mismatch be limited to avoid an excessive disparity between the maturity profile of the assets and liabilities.

On an ongoing basis, the weighted average life of the investment portfolio is expected to exceed that of the liability portfolio. This mismatch is monitored and managed to a target mismatch of 2 years or less. At 31 December 2008, the weighted average life of the investment portfolio was 3.57 years (2007: 4.0 years) and the weighted average life of the liability portfolio was 2 years (2007: 3.1 years). AGIM surplus assets are not included in the mismatch analysis but would be available to cover losses.

The amount of Bond available-for-sale investments that is expected to be recovered or settled after more than twelve months after the balance sheet date is US \$1,890,519,859 at 31 December 2008 and US \$2,514,298,465 at 31 December 2007.

*Managing interest rate risk*

All financial liabilities and most financial assets are either naturally floating rate or are swapped to a floating rate basis, using interest rate swaps. These interest rate swaps generally provide for the exchange of the difference between a fixed rate and a floating rate based upon an index. The floating rate index for the assets and liabilities may differ and create some cash flow risk. However, to constrain the open interest rate risk, management requires that the exposure of AGIM to interest rate risk is significantly limited.

Below is a summary of financial asset and liability carrying values (net of swaps) and yields. The indicated maturity periods are based on contractual maturities or, if earlier, the repricing dates for floating rate instruments.

31 December 2008

Carrying Value (US \$)

	<1 yr	1<2 yrs	2<3 yrs	3<4 yrs	4<5 yrs	>5 yrs
Mortgage loans	414,289,991	-	-	-	-	-
Bonds	1,880,543,725	15,130,503	13,858,375	10,980,650	25,184,780	18,933,387
Short-term deposits	172,060,567	-	-	-	-	-
Credit-linked notes	64,295,200	-	-	-	-	-
Note liabilities	3,881,136,846	-	-	-	-	-

Yields

	<1 yr	1<2 yrs	2<3 yrs	3<4 yrs	4<5 yrs	>5 yrs
Mortgage loans	2.89%	-	-	-	-	-
Bonds	4.76%	6.21%	6.84%	7.21%	7.23%	6.80%
Short-term deposits	-	-	-	-	-	-
Credit-linked notes	3.22%	-	-	-	-	-
Note liabilities	1.24%	-	-	-	-	-

31 December 2007

Carrying Value (US \$)

	<1 yr	1<2 yrs	2<3 yrs	3<4 yrs	4<5 yrs	>5 yrs
Mortgage loans	456,802,389	-	-	-	-	-
Bonds	2,398,123,548	18,211,517	24,774,638	15,702,500	31,903,205	43,345,950
Short-term deposits	2,383,400	-	-	-	-	-
Credit-linked notes	91,586,691	-	-	-	-	-
Note liabilities	3,737,273,211	-	-	-	-	-

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**
**5. Management of financial risk and capital (Continued)**
**Yields**

	<1 yr	1<2 yrs	2<3 yrs	3<4 yrs	4<5 yrs	>5 yrs
Mortgage loans	6.39%	-	-	-	-	-
Bonds	5.71%	7.80%	8.17%	7.36%	7.72%	6.89%
Short-term deposits	4.50%	-	-	-	-	-
Credit-linked notes	5.71%	-	-	-	-	-
Note liabilities	5.15%	-	-	-	-	-

AGIM monitors interest rate risk by calculating the mean duration of the note liabilities and the related assets. Mean duration, an indicator of the sensitivity of a financial instrument to changes in interest rates, is determined by shocking the zero swap curve upwards and downwards at a number of points along the curve. The asset / liability duration mismatch is monitored and managed to a target mismatch between -0.5 and +0.5 years. This range was extended during the year from 0 to 0.5 years to reflect the impact of stressed market conditions. The mismatch was within the specified range at 31 December 2008 and at 31 December 2007. AGIM surplus assets are not included in this duration analysis but would be available to cover losses.

*Managing hedge fund risk*

AGIM has an exposure to hedge fund risk arising from its investment in Prisma Spectrum Fund Ltd. The Prisma Spectrum fund is a "fund of funds" hedge fund investment with underlying investments made by the Fund manager in a range of individual hedge funds. The individual underlying hedge funds operate across a range of strategies. These strategies provide exposure to a range of risks including equity, interest rate, currency and credit risk. Risk is mitigated by the fact that the overall "fund of funds" is designed to be neutral to equity, interest rate, and credit risk.

*Managing liquidity risk*

AGIM monitors exposure to liquidity risk that arises from timing of certain investment maturities. The risk is controlled through a small allocation to more illiquid asset classes and through the participation of AGIM in the internal AEGON USA intercompany borrowing programme which facilitates short-term borrowing from AEGON USA entities.

*Managing currency risk*

AGIM uses cross currency swaps to hedge currency risk by swapping non-US dollar denominated assets and liabilities to US dollars. As of 31 December 2008 and 31 December 2007, the only foreign currency denominated financial instruments are the note liabilities and the cross currency swaps which convert the liabilities to US dollars. See the note liabilities and hedge activity notes (note 21 and note 15, respectively) for more details.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**5. Management of financial risk and capital (Continued)**

*Sensitivity analysis*

The sensitivity analysis in the table below shows an estimate of the effects of interest rate movements, changes in equity prices and changes in currencies on net income and equity.

	Estimated impact on net income		Estimated impact on equity	
	2008	2007	2008	2007
Financial risks:				
Parallel movement of yield curve:				
-Shift up 100 basis points	(2,785,738)	(4,556,140)	8,241,584	(6,979,635)
-Shift down 100 basis points	2,785,738	4,556,140	(8,142,956)	6,732,140
Change in equity prices:				
Equity increase 10%	6,805,741	9,826,235	6,805,741	9,826,235
Equity decrease 10%	(6,805,741)	(9,826,235)	(6,805,741)	(9,826,235)
Immediate change in:				
Non US dollars relative to US dollars				
increase 15%	(102,520)	(320,162)	(102,520)	(320,162)
Non US dollars relative to US dollars				
decrease 15%	102,520	320,162	102,520	320,162

*Managing capital*

The primary objective of AGIM's capital management is to maintain the appropriate capital level to support the AGIM Secured Medium Term Note Programme and to maintain strong credit ratings for these notes.

AGIM manages its capital structure to address changes that occur from changing economic conditions. To maintain or adjust the capital structure, AGIM may provide dividend payments to shareholders, return capital to shareholders, issue new shares, or receive capital contributions. AGIM did not provide any dividend payments, return capital to shareholders or issue new shares during the years ended 31 December 2008 or 31 December 2007.

AGIM maintains, at the time of issuance of any new note, the appropriate minimum level of capital required under the AGIM/AFA Secured Medium Term Note Programme as described in Note 3. Appropriate capital contributions are received, if necessary, before each note issuance.

**6. Investment income**

	2008	2007
	US \$	US \$
Interest on financial assets designated at fair value through profit or loss:		
Interest from credit-linked notes designated at fair value through profit or loss	3,373,153	5,517,493
Interest on other financial assets:		
Interest from mortgage loans	21,139,050	25,923,453
Interest from bond available-for-sale investments	123,397,083	150,534,370
Interest from derivatives hedging investments	(16,247,961)	2,699,503
Interest from short-term deposits	1,504,261	1,647,792
Other interest income	2,157	190
Subtotal	<u>129,794,590</u>	<u>180,805,308</u>
Total	<u>133,167,743</u>	<u>186,322,801</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**7. Gains/(losses) on investments**

	2008 US \$	2007 US \$
Realised gains/(losses) from the sale of available-for-sale investments	(88,541,097)	3,622,763
Gains/(losses) on investments designated at fair value through profit or loss	(24,647,933)	12,306,884
Hedge ineffectiveness	3,640,842	(1,758,955)
Allowance for mortgage impairments	29,468	435
	<u>(109,518,720)</u>	<u>14,171,127</u>

	2008 US \$	2007 US \$
Gains/(losses) on fair value hedging instruments	96,818,355	(55,350,439)
Gains/(losses) on fair value hedged instrument attributable to hedged risk	(93,177,513)	53,591,484
	<u>3,640,842</u>	<u>(1,758,955)</u>
Total hedge ineffectiveness		

**8. Interest expense**

	2008 US \$	2007 US \$
Interest on note liabilities	84,725,098	428,110,043
Interest on derivatives hedging note liabilities	13,290,217	(254,151,246)
Interest on cash collateral	-	7,152
Interest on intercompany borrowing	420,039	2,014,259
Interest on mortgage escrow accounts	34,182	191,156
	<u>98,469,536</u>	<u>176,171,364</u>
Total		

**9. Foreign currency transaction gains**

The following are foreign currency exchange differences recognised in operating expense in the income statement.

	2008 US \$	2007 US \$
Foreign currency transaction gains	<u>112,672</u>	<u>40,458</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**10. Operating expenses**

	2008 US \$	2007 US \$
Key management (directors):		
–Directors fees	23,925	19,303
–Salaries and benefits	<u>(13,829)</u>	<u>(4,473)</u>
Subtotal	<u>10,096</u>	<u>14,830</u>
Key management are deemed to be the directors only.		
Other staff:		
Short-term employee benefits:		
Salaries and benefits	(4,012)	110,757
Social welfare	-	(234,357)
Post-employment benefits (pension)	<u>-</u>	<u>7,868</u>
Subtotal	<u>(4,012)</u>	<u>(115,732)</u>
Audit fees	39,347	42,086
Guarantee fee expense	10,126,959	9,693,442
Other operating expenses	<u>2,413,689</u>	<u>5,466,719</u>
Total operating expenses	<u>12,586,079</u>	<u>15,101,345</u>

The average number of persons employed by AGIM for the year were as follows:

	2008	2007
Sales	-	-
Administration	<u>-</u>	<u>-</u>

**11. Impairment charges and past due assets**

	2008 US \$	2007 US \$
Impairment charges on bond available-for-sale investments	<u>34,656,529</u>	<u>1,085,254</u>

The 2008 impairment charges were related to the bankruptcy filings of Lehman Brothers (\$29,205,397), Nortel Networks (\$3,923,061) and Washington Mutual (\$1,528,071).

The 2007 impairment charge was incurred due to the decrease in the investment's value by over 20% related to the investment's exposure to the subprime mortgage market. The investment was sold in 2007.

AGIM had \$1,250,000 (Nortel Networks) of impaired assets at 31 December 2008 and none at 31 December 2007.

**12. Tax**

The major components of corporation tax for the years ended 31 December 2008 and 2007 are:

**Tax (expense)/credit in the income statement**

	2008 US \$	2007 US \$
Current tax (expense)	(156)	(2,052)
Deferred (expense) or credit	<u>470,078</u>	<u>(506,493)</u>
Tax (expense) or credit	<u>469,922</u>	<u>(508,545)</u>

Domestic corporation tax is calculated at 12.5% of the estimated assessable profit for the year.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**12. Tax (Continued)**

A reconciliation between tax expense and accounting profit multiplied by the applicable tax rate of 12.5% for the years ended 31 December 2008 and 2007 follows:

	2008 US \$	2007 US \$
Income/(loss) before tax	(127,926,133)	2,176,230
Tax (expense)/credit at Ireland's corporate tax rate (12.5%)	15,990,767	(272,028)
Tax effects of:		
Deferred tax determined to be unrecoverable	(15,522,934)	-
Expenses not deductible for tax purposes	2,066	142
Prior year tax benefit utilised by affiliate	-	(234,607)
Foreign exchange differences	23	(2,052)
Tax (expense)/credit (effective tax rate 2008: 0.4%, 2007: 23.4%)	<u>469,922</u>	<u>(508,545)</u>

**Tax credit/(expense) in equity**

*Deferred tax:*

Revaluation of bond available-for-sale investments	<u>70,089,368</u>	<u>21,657,328</u>
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**Deferred taxes**

Deferred taxes at 31 December relate to the following:

	Balance sheet		Income statement	
	2008 US \$	2007 US \$	2008 US \$	2007 US \$
<i>Deferred tax asset:</i>				
Losses available for offset against future taxable income	900,000	429,922	470,078	(506,493)
Revaluation of bond available-for-sale investments to fair value	91,530,707	21,441,339	-	-
Deferred tax asset	<u>92,430,707</u>	<u>21,871,261</u>	<u>470,078</u>	<u>(506,493)</u>

At 31 December 2008, AGIM has unused tax losses of US \$131,078,256 (2007: US \$3,408,102) available for offset against future profits. A deferred tax asset has been recognised in respect of US \$900,000 (2007: US \$429,922). The remaining tax losses may be carried forward indefinitely. AGIM believes that it is improbable that sufficient taxable profit will be available to allow the benefit of the entire deferred tax asset to be utilised; therefore, the deferred tax asset has been recognised at an amount AGIM believes it will be able to recover.

**13. Mortgage loans**

	2008 US \$ Carrying Value	2007 US \$ Carrying Value
Mortgage loans	414,353,283	456,895,149
Allowance for impairments	<u>(63,292)</u>	<u>(92,760)</u>
Total mortgage loans	<u>414,289,991</u>	<u>456,802,389</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**
**13. Mortgage loans (Continued)**

Allowance for impairments:

	2008 US \$	2007 US \$
Movements during the year:		
At 1 January	(92,760)	(93,195)
Additions	-	-
Deductions	<u>29,468</u>	<u>435</u>
At 31 December	<u><u>(63,292)</u></u>	<u><u>(92,760)</u></u>

The fair value of mortgage loans was US \$362,822,223 at 31 December 2008 and US \$445,679,358 at 31 December 2007. The fair value is estimated using discounted cash flow analysis, applying interest rates currently being offered for similar loans to borrowers with similar credit ratings.

The amount of mortgage loans that is expected to be recovered or settled after more than twelve months after the balance sheet date is US \$381,477,885 at 31 December 2008 and US \$403,937,251 at 31 December 2007.

**14. Investments at fair value through profit or loss**

	2008 US \$	2007 US \$
Assets:		
Shares	77,779,894	112,299,832
Credit-linked notes	<u>64,295,200</u>	<u>91,586,691</u>
Total	<u><u>142,075,094</u></u>	<u><u>203,886,523</u></u>

The amount of investments at fair value through profit or loss that is expected to be recovered or settled after more than twelve months after the balance sheet date is US \$110,583,894 at 31 December 2008 and US \$91,586,691 at 31 December 2007.

**15. Derivative hedging activities**

Derivative financial instruments are used to hedge interest and currency exposures for investments and note liabilities and all of these instruments are designated as fair value hedges. Interest rate swaps are used to convert certain fixed rate investments and note liabilities to a floating rate basis (generally to six month US LIBOR or shorter) or to convert exposure from one floating rate basis to another. These agreements involve the payment or receipt of fixed rate interest amounts in exchange for floating interest amounts over the life of the agreement without the exchange of the underlying principal amounts. Cross currency swaps are used to convert certain foreign currency fixed and floating rate assets and liabilities to US dollar floating rate assets and liabilities. A cross currency swap is an agreement between two parties to exchange two principal amounts of two currencies at the prevailing exchange rate at inception of the contract. During the life of the swap, the counterparties exchange fixed or floating rate interest payments in the swapped currencies. At maturity, the principal amounts are again swapped at a predetermined rate of exchange.

All of these swaps were executed with a related party, AEGON Derivatives N.V., who entered into mirror swaps with third party counterparties.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**15. Derivative hedging activities (Continued)**

The fair value of swaps outstanding at 31 December 2008 and 31 December 2007 are as follows:

	Asset 2008 US \$	Liability 2008 US \$	Asset 2007 US \$	Liability 2007 US \$
Swaps hedging investments:				
Designated as fair value hedges	5,405	138,089,279	707,859	43,559,016
Swaps hedging note liabilities:				
Designated as fair value hedges	<u>582,672,914</u>	<u>48,608,637</u>	<u>390,727,775</u>	<u>-</u>
Total	<u>582,678,319</u>	<u>186,697,916</u>	<u>391,435,634</u>	<u>43,559,016</u>

All swap fair values were obtained through market quotes or through discounting cash flows using market based inputs.

The maturities of the contractual undiscounted cash flows of swaps hedging note liabilities at 31 December 2008 and 31 December 2007 are as follows:

	2008 US \$	2007 US \$
0<1 years	489,962,958	355,871,399
1<3 years	2,229,299,640	2,164,881,389
3<5 years	1,096,571,470	1,904,994,816
5<10 years	44,911,075	65,091,696
>10 years	<u>4,357,161</u>	<u>6,219,968</u>
	<u>3,865,102,304</u>	<u>4,497,059,268</u>

Gains/(losses) relating to the ineffective portion of designated fair value hedges netted to US \$3,640,842 and US \$(1,758,955) as of 2008 and 2007, respectively. No portion of derivatives was excluded when assessing hedge effectiveness.

*Collateral*

AGIM is permitted to utilise cash collateral received without restriction. The liability to return cash collateral is reflected in the Derivatives collateral liability line. AGIM pays interest on the cash collateral at the Euro Overnight Index Average rate. The maturity of the contractual undiscounted cash flows for the Derivative collateral liability is on demand for \$121,869,869 at 31 December 2008 and \$480,742,322 at 31 December 2007.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**
**16. Trade and other receivables**

	2008 US \$	2007 US \$
Due from broker	19,285,300	1,402,837
Receivable from related parties	1,146,062	118,165
Value added tax receivable	-	50,624
	<u>20,431,362</u>	<u>1,571,626</u>
Total trade and other receivables	<u>20,431,362</u>	<u>1,571,626</u>

**17. Cash and cash equivalents**

	2008 US \$	2007 US \$
Cash at bank and in hand	807,111	358,349
Derivatives cash collateral	121,869,869	480,742,322
Short-term deposits	172,060,567	2,383,400
	<u>294,737,547</u>	<u>483,484,071</u>
Total cash and cash equivalents	<u>294,737,547</u>	<u>483,484,071</u>

**18. Share capital**

	2008 US \$	2007 US \$
Allotted, called up and fully paid:		
40,000 ordinary shares of 1 euro each (US \$1.1226)	<u>44,904</u>	<u>44,904</u>

10,000,000 ordinary shares have been authorised of 1 euro each.

AEGON Ireland Holding B.V. has beneficial ownership of all shares issued, including rights to vote, receive dividends and receive repayments of capital on all shares.

**19. Contributed capital**

	2008 US \$	2007 US \$
Balance at beginning of period	49,217,624	31,466,737
Cash contributions during the period	115,000,000	17,750,000
Non-cash contributions during the period	(180)	887
	<u>164,217,444</u>	<u>49,217,624</u>
Balance at end of period	<u>164,217,444</u>	<u>49,217,624</u>

All cash capital contributions were made by AEGON N.V., the ultimate parent, and were not given in return for any rights such as voting rights, a share in the profits nor a share in the surplus assets of AGIM on liquidation.

**20. Equity – other reserves**

	2008 US \$	2007 US \$
Balance at beginning of period	(150,089,374)	1,511,920
Bond available-for-sale investments change in unrealised gains/(losses), net of tax	<u>(490,625,575)</u>	<u>(151,601,294)</u>
Balance at end of period	<u>(640,714,949)</u>	<u>(150,089,374)</u>

The other reserves component of Equity includes unrealised gains/(losses) for bond available-for-sale investments. If the investments are sold before they mature, any outstanding unrealised gains/(losses) will be recognised in net gain or loss on investments in the income statement.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**21. Note liabilities**

The following note liabilities are outstanding as of 31 December 2008:

Par Value US \$	Par Value Currency	Currency
1,488,500,000	1,200,000,000	Euro
1,440,994,958	1,803,650,000	Swiss Franc
259,410,000	145,000,000	British Pound
59,146,600	7,000,000,000	Japanese Yen
42,857,000	750,000,000	Czech Koruna
<u>3,290,908,558</u>		

The following note liabilities were outstanding as of 31 December 2007:

Par Value US \$	Par Value Currency	Currency
1,488,500,000	1,200,000,000	Euro
1,476,587,123	1,850,000,000	Swiss Franc
259,410,000	145,000,000	British Pound
59,146,600	7,000,000,000	Japanese Yen
<u>3,283,643,723</u>		

The note liabilities may be issued at proceeds that are different than par. They will be amortised to par over their life with amortisation reflected in interest expense. There are no scheduled note principal repayments planned during the term of the note. The note principal is scheduled to be repaid at maturity.

The portion of note liabilities that is expected to be recovered or settled within one year includes accrued interest and is US \$438,834,256 at 31 December 2008 and US \$61,291,086 at 31 December 2007. The note liability balances that are expected to be recovered or settled after more than twelve months after the balance sheet date are US \$3,442,302,590 at 31 December 2008 and US \$3,675,982,125 at 31 December 2007.

	2008 US \$	2007 US \$
Movements during the year:		
At 1 January	3,737,273,211	2,215,757,996
Notes issued	42,857,000	1,179,961,511
Interest expense accrued	126,269,311	121,060,051
Interest payments	(126,269,311)	(74,980,649)
Note Repurchase	(32,537,696)	
Fair value hedge adjustment	175,147,640	(11,503,078)
Net exchange differences	<u>(41,603,309)</u>	<u>306,977,380</u>
At 31 December	<u>3,881,136,846</u>	<u>3,737,273,211</u>

The fair value of the note liabilities is computed by translating the expected future foreign cash flows to US dollars using the relevant currency forward rates and then discounting the cash flows using the relevant US LIBOR interest rate curve with an appropriate spread reflecting non-performance risk and any other risk considered by market participants. The fair value of the note liabilities at 31 December 2008 was US \$3,111,501,878 and at 31 December 2007 was US \$3,653,288,058.

**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**21. Note liabilities (Continued)**

Maturities of note liabilities:

Carrying value	2008 US \$	2007 US \$
0<1 years	382,832,553	-
1<2 years	1,469,835,595	399,721,766
2<3 years	807,804,488	1,424,261,830
3<4 years	1,220,664,210	746,187,452
4<5 years	-	1,167,102,163
	<u>3,881,136,846</u>	<u>3,737,273,211</u>

Contractual undiscounted cash flows	2008 US \$	2007 US \$
0<1 years	488,638,865	128,166,741
1<2 years	1,532,131,309	523,124,659
2<3 years	846,023,920	1,546,519,183
3<4 years	1,158,827,058	831,254,000
4<5 years	-	1,185,046,207
	<u>4,025,621,152</u>	<u>4,214,110,790</u>

**22. Trade and other payables**

	2008 US \$	2007 US \$
Accrued expenses	1,342,405	1,458,190
Due to broker and investment payables	231,361	208,199
Payables to related parties	<u>3,308,498</u>	<u>7,332,998</u>
Total trade and other payables	<u>4,882,264</u>	<u>8,999,387</u>

**23. Related party disclosures**

*Parent*

AGIM's immediate parent and immediate controlling party is AEGON Ireland Holding B.V., a company incorporated in The Netherlands. AGIM's ultimate parent and ultimate controlling party is AEGON N.V., a company incorporated in The Netherlands.

The smallest and largest group into which the results of AGIM are consolidated is that headed by AEGON N.V.. Copies of its group financial statements are available from the Company Secretary, AEGONplein 50, P.O. Box 202, 2501 CE The Hague, The Netherlands.

*Other related parties*

AGIM has entered into financial guarantee contracts with AEGON Financial Assurance Ireland limited (AFA), a related party, related to the notes issued by AGIM (see notes 3, 5 and 21).

AGIM has entered into both asset and liability interest rate and cross currency swaps with AEGON Derivatives N.V., a related party (see note 15). AGIM entered into an International Swaps and Derivatives Association, Inc. (ISDA) Master Agreement and Credit Support Annex with AEGON Derivatives N.V..



**NOTES TO THE FINANCIAL STATEMENTS**  
**31 December 2008 (Continued)**

**23. Related party disclosures (Continued)**

Expense amounts with related parties:

AEGON Derivatives N.V.	-	7,152
AEGON USA, Inc.	420,039	2,014,259
AEGON USA Realty Advisors, Inc.	1,026,417	1,195,353
AEGON Institutional Markets, Inc.	(17,841)	2,752,173
AEGON Ireland Services Limited	2,187,687	1,543,237
AEGON USA Investment Management, LLC	4,540,264	4,428,551
Prisma Capital Partners	185,709	235,915
AEGON Scottish Equitable International plc	-	2,921
AEGON Financial Assurance Ireland Limited	10,126,959	9,693,442

Accounts receivable from related parties:

AEGON Financial Assurance Ireland Limited	-	118,165
AEGON USA Investment Management, LLC	1,146,062	-
	2008	2007
	US \$	US \$

Accounts payable to related parties:

AEGON Institutional Markets, Inc.	2,316	376,735
AEGON Ireland Services Limited	519,692	391,027
AEGON USA, Inc.	238,785	4,067,753
AEGON Scottish Equitable International plc	-	-
AEGON Financial Assurance Ireland Limited	2,550,021	2,399,295
AEGON Derivatives N.V.	121,869,869	480,742,322

**24. Subsequent Events**

On 30 January 2009 AGIM allotted one Ordinary Share of EUR 1 to AEGON Ireland Holdings B.V. for a subscription price of US\$40,000,000.

On 17 February 2009, AGIM gave notice that it will not issue any additional Notes under the Programme. This notice was the result of a decision by the Board acting upon the announcement by AEGON NV that it was planning to reduce spread based balances in the AEGON Institutional Markets Division..

On 31 March 2009, AGIM entered into a Facility Agreement with AEGON N.V. whereby AEGON N.V. undertakes to provide a liquidity facility of USD 500 million subject to specified terms and conditions.

On 31 March 2009, Standard & Poor's Ratings Services announced that it had lowered its long- and short-term counterparty credit ratings on AEGON N.V. to 'A-/A-2' from 'A+/A-1' and AEGON Schadeverzekering N.V. to 'AA-' from 'AA', and at the same time lowered its financial strength rating on AFA to 'AA-' from 'AA' and its rating on the notes issued under the Programme to 'AA-' from 'AA'.