

STATEMENT OF ADDITIONAL INFORMATION

May 1, 2009

FLEXIBLE PAYMENT VARIABLE ANNUITY

An individual flexible payment Variable Annuity Contract (the "Contract") for:

Individual Retirement Annuities ("IRAs")	457 Deferred Compensation Plan Annuities
Roth IRAs	Tax Deferred Annuities
Simple IRAs	Non-Transferable Annuities
Simplified Employee Pension Plan IRAs	Nontax-Qualified Annuities

**Issued by The Northwestern Mutual Life Insurance Company
and
NML Variable Annuity Account B**

This Statement of Additional Information ("SAI") is not a prospectus, but supplements and should be read in conjunction with the prospectus for the Contract identified above and dated the same date as this SAI. A copy of the prospectus may be obtained by writing The Northwestern Mutual Life Insurance Company, Investment Products and Services Department, Room W07SW, 720 East Wisconsin Avenue, Milwaukee, Wisconsin 53202, calling telephone number 1-888-455-2232, or visiting the website www.nmfn.com.

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DISTRIBUTION OF THE CONTRACTS

The Contracts are offered on a continuous basis exclusively through individuals who, in addition to being life insurance agents of Northwestern Mutual, are registered representatives of Northwestern Mutual Investment Services, LLC (“NMIS”). NMIS is our wholly-owned company. The principal business address of NMIS is 720 East Wisconsin Avenue, Milwaukee, Wisconsin 53202.

NMIS is the principal underwriter of the Contracts for purposes of the federal securities laws. We paid the following amounts to NMIS with respect to sales of the Contracts, including commissions on sales of variable annuity contracts to corporate pension plans, during each of the last three years representing commission payments NMIS made to our agents and related benefits. None of these amounts was retained by NMIS and no amounts were paid to other underwriters or broker-dealers. We also paid additional amounts to NMIS in reimbursement for other expenses related to the distribution of variable annuity contracts.

<u>Year</u>	<u>Amount</u>
2008	\$42,432,422
2007	\$48,954,470
2006	\$41,642,588

NMIS also provides certain services related to the administration of certain payment plans under the Policies. In exchange for these services, NMIS receives compensation to cover the actual costs incurred by NMIS in performing these services under an administrative services contract with us.

DETERMINATION OF ANNUITY PAYMENTS

The following discussion of the method for determining the amount of monthly annuity payments under a variable payment plan is intended to be read in conjunction with these sections of the prospectus for the Contracts: “Variable Payment Plans,” including “Description of Payment Plans,” “Amount of Annuity Payments,” and “Assumed Investment Rate”; “Dividends”; “Net Investment Factor”; and “Deductions.”

Amount of Annuity Payments The amount of the first annuity payment under a variable Payment Plan will be determined on the basis of the particular Payment Plan selected, the annuity payment rate and, for plans involving life contingencies, the Annuitant's adjusted age and sex. The amount of the first payment is the sum of the payments from each Division of the Account determined by applying the appropriate annuity payment rate to the product of the number of Accumulation Units in the Division on the effective date of the Payment Plan and the Accumulation Unit value for the Division on that date. Annuity rates currently in use are based on the 1983 a Table with Projection Scale G and age adjustment.

Variable annuity payments after the first will vary from month to month and will depend upon the number and value of Annuity Units credited to the Annuitant. After the effective date of a Payment Plan a Contract will not share in the divisible surplus of Northwestern Mutual. The number of Annuity Units in each Division is determined by dividing the amount of the first annuity payment from the Division by the value of an Annuity Unit on the effective date of the Payment Plan. The number of Annuity Units thus credited to the Annuitant in each Division remains constant throughout the annuity period. However, the value of Annuity Units in each Division will fluctuate with the investment experience of the Division.

The amount of each variable annuity payment after the first is the sum of payments from each Division determined by multiplying this fixed number of Annuity Units each month by the value of an Annuity Unit for the Division on (a) the fifth valuation date prior to the payment due date if the payment due date is a valuation date, or (b) the sixth valuation date prior to the payment due date if the payment due date is not a valuation date. To illustrate, if a payment due date falls on a Friday, Saturday or Sunday, the amount of the payment will normally be based upon the Annuity Unit value calculated on the preceding Friday. The preceding Friday would be the fifth valuation date prior to the Friday due date, and the sixth valuation date prior to the Saturday or Sunday due dates.

Annuity Unit Value The value of an Annuity Unit for each Division was established at \$1.00 as of the date operations began for that Division. The value of an Annuity Unit on any later date varies to reflect the investment experience of the Division, the Assumed Investment Rate on which the annuity rate tables are based, and the deduction for mortality rate and expense risks assumed by Northwestern Mutual.

The Annuity Unit value for each Division on any valuation date is determined by multiplying the Annuity Unit value on the immediately preceding valuation date by two factors: (a) the net investment factor for the current period for the Division; and (b) an adjustment factor to neutralize the Assumed Investment Rate used in calculating the annuity rate tables.

Illustrations of Variable Annuity Payments To illustrate the manner in which variable annuity payments are determined consider this example. Item (4) in the example shows the applicable monthly payment rate for a male, adjusted age 65, who has elected a life annuity Payment Plan with a certain period of 10 years with an Assumed Investment Rate of 3-1/2% (Plan 2, as described in the prospectus). The example is for a Contract with sex-distinct rates.

(1)	Assumed number of Accumulation Units in Balanced Division on maturity date.....	25,000
(2)	Assumed Value of an Accumulation Unit in Balanced Division at maturity	\$2.000000
(3)	Cash Value of Contract at maturity, (1) X (2)	\$50,000
(4)	Assumed applicable monthly payment rate per \$1,000 from annuity rate table	\$5.35
(5)	Amount of first payment from Balanced Division, (3) X (4) divided by \$1,000	\$267.50
(6)	Assumed Value of Annuity Unit in Balanced Division at maturity	\$1.500000
(7)	Number of Annuity Units credited in Balanced Division, (5) divided by (6).....	178.33

The \$50,000 value at maturity provides a first payment from the Balanced Division of \$267.50, and payments thereafter of the varying dollar value of 178.33 Annuity Units. The amount of subsequent payments from the Balanced Division is determined by multiplying 178.33 units by the value of an Annuity Unit in the Balanced Division on the applicable valuation date. For example, if that unit value is \$1.501000, the monthly payment from the Division will be 178.33 multiplied by \$1.501000, or \$267.68.

However, the value of the Annuity Unit depends entirely on the investment performance of the Division. Thus in the example above, if the net investment rate for the following month was less than the Assumed Investment Rate of 3-1/2%, the Annuity Unit would decline in value. If the Annuity Unit value declined to \$1.499000 the succeeding monthly payment would then be 178.33 X \$1.499000, or \$267.32.

For the sake of simplicity the foregoing example assumes that all of the Annuity Units are in the Balanced Division. If there are Annuity Units in two or more Divisions, the annuity payment from each Division is calculated separately, in the manner illustrated, and the total monthly payment is the sum of the payments from the Divisions.

VALUATION OF ASSETS OF THE ACCOUNT

The value of Portfolio or Fund shares held in each Division of the Account at the time of each valuation is the redemption value of such shares at such time. If the right to redeem shares of a Portfolio

or Fund has been suspended, or payment of redemption value has been postponed, for the sole purpose of computing annuity payments the shares held in the Account (and Annuity Units) may be valued at fair value as determined in good faith by the Board of Trustees of Northwestern Mutual.

TRANSFERABILITY RESTRICTIONS

Ownership of a Contract purchased as a tax-deferred annuity pursuant to Section 403(b) of the Internal Revenue Code of 1954, as amended (the “Code”) cannot be changed and the Contract cannot be sold, assigned or pledged as collateral for a loan, or for any other purpose, to any person other than Northwestern Mutual. Similar restrictions are applicable to Contracts purchased in exchange transactions by persons who have received fixed dollar policies as distributions of termination benefits from tax-qualified corporate or HR-10 plans or trusts. Ownership of a Contract purchased as an individual retirement annuity pursuant to Section 408(b) of the Code cannot be transferred except in limited circumstances involving divorce.

EXPERTS

The financial statements of the Account, and the related notes and report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, included in this Statement of Additional Information and the financial statements of Northwestern Mutual, and the related notes and report of PricewaterhouseCoopers LLP included in this Statement of Additional Information are so included in reliance on the reports of PricewaterhouseCoopers LLP, given on the authority of said firm as experts in auditing and accounting. PricewaterhouseCoopers LLP provides audit services for the Account. The address of PricewaterhouseCoopers LLP is 100 East Wisconsin Avenue, Suite 1800, Milwaukee, Wisconsin 53202.

**Annual Report December 31, 2008
NML Variable Annuity Account B
Financial Statements**

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Growth Stock Division	Focused Appreciation Division (a)	Large Cap Core Stock Division	Large Cap Blend Division (a)	Index 500 Stock Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$197,933	\$104,953	\$159,814	\$14,744	\$635,497
Fidelity Variable Insurance Products	—	—	—	—	—
Neuberger Berman Advisers Management Trust	—	—	—	—	—
Russell Investment Funds	—	—	—	—	—
Due from Northwestern Mutual Life Insurance Company	28	7	39	1	75
Total Assets	197,961	104,960	159,853	14,745	635,572
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	24	1	4	21	41
Due to Participants	454	26	432	—	915
Total Liabilities	478	27	436	21	956
Total Net Assets	\$197,483	\$104,933	\$159,417	\$14,724	\$634,616
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$589	\$391	\$445	\$10	\$14,056
Annuity Reserves	1	—	34	—	290
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	50,443	19,216	45,268	2,254	218,130
Annuity Reserves	569	107	747	2	2,573
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	22,847	5,257	16,957	591	53,692
Annuity Reserves	235	67	350	—	945
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	59,472	14,363	50,305	1,545	162,816
Annuity Reserves	205	212	379	11	849
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	22,776	30,598	16,703	5,349	64,267
Annuity Reserves	183	165	196	121	422
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	5,120	3,094	3,524	224	13,711
Class B Accumulation Units (9)	33,460	30,944	23,959	4,591	99,562
Annuity Reserves	160	141	114	23	328
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	1,423	378	436	3	2,975
Annuity Reserves	—	—	—	—	—
Total Net Assets	\$197,483	\$104,933	\$159,417	\$14,724	\$634,616
(1) Investments, at cost	\$276,382	\$154,171	\$237,838	\$22,514	\$851,134
(2) Shares Outstanding	140,179	87,754	182,228	27,052	326,566
(3) Accumulation Unit Value Units Outstanding	\$1.918211 307	\$1.284107 304	\$1.624552 274	\$0.551598 18	\$3.450407 4,074
(4) Accumulation Unit Value Units Outstanding	\$1.782457 28,300	\$1.248176 15,395	\$1.509570 29,987	\$0.546962 4,120	\$3.152106 69,201
(5) Accumulation Unit Value Units Outstanding	\$1.850502 12,347	\$1.309615 4,015	\$1.566681 10,824	\$0.554826 1,066	\$2.163516 24,817
(6) Accumulation Unit Value Units Outstanding	\$1.782457 33,365	\$1.248176 11,507	\$1.509570 33,324	\$0.546962 2,825	\$3.152106 51,653
(7) Accumulation Unit Value Units Outstanding	\$0.598090 38,080	\$1.302296 23,496	\$0.612094 27,288	\$0.553912 9,656	\$0.670905 95,792
(8) Accumulation Unit Value Units Outstanding	\$0.598090 8,560	\$1.302296 2,376	\$0.612094 5,757	\$0.553912 404	\$0.670905 20,437
(9) Accumulation Unit Value Units Outstanding	\$1.782457 18,772	\$1.248176 24,791	\$1.509570 15,871	\$0.546962 8,394	\$3.152106 31,586
(10) Accumulation Unit Value Units Outstanding	\$0.617447 2,305	\$1.313419 288	\$0.657733 663	\$0.555297 5	\$0.698694 4,258

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Large Company Value Division (a)	Domestic Equity Division (a)	Equity Income Division (a)	Mid Cap Growth Stock Division	Index 400 Stock Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$12,151	\$179,177	\$96,908	\$375,474	\$165,471
Fidelity Variable Insurance Products	—	—	—	—	—
Neuberger Berman Advisers Management Trust	—	—	—	—	—
Russell Investment Funds	—	—	—	—	—
Due from Northwestern Mutual Life Insurance Company	5	15	10	29	13
Total Assets	12,156	179,192	96,918	375,503	165,484
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	2	23	260	18	3
Due to Participants	8	387	37	744	157
Total Liabilities	10	410	297	762	160
Total Net Assets	\$12,146	\$178,782	\$96,621	\$374,741	\$165,324
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$18	\$249	\$163	\$1,306	\$443
Annuity Reserves	—	—	—	78	9
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	1,941	32,430	20,470	177,962	37,774
Annuity Reserves	3	275	206	1,448	332
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	384	11,282	4,155	29,780	11,416
Annuity Reserves	—	268	119	218	273
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	1,121	22,564	11,246	101,463	32,060
Annuity Reserves	—	228	224	446	156
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	3,852	53,162	26,364	19,457	27,484
Annuity Reserves	98	1,255	1,336	158	416
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	717	4,624	2,636	6,821	6,788
Class B Accumulation Units (9)	3,045	47,148	25,749	34,603	45,787
Annuity Reserves	22	203	236	208	256
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	945	5,094	3,717	793	2,130
Annuity Reserves	—	—	—	—	—
Total Net Assets	\$12,146	\$178,782	\$96,621	\$374,741	\$165,324
(1) Investments, at cost	\$17,432	\$314,737	\$156,336	\$722,145	\$246,346
(2) Shares Outstanding	21,430	283,957	111,645	195,763	183,044
(3) Accumulation Unit Value Units Outstanding	\$0.582824 31	\$0.830435 300	\$1.122817 144	\$4.064928 321	\$1.394193 318
(4) Accumulation Unit Value Units Outstanding	\$0.577921 3,358	\$0.800161 40,529	\$1.091416 18,755	\$3.713247 47,926	\$1.328286 28,439
(5) Accumulation Unit Value Units Outstanding	\$0.586235 656	\$0.852113 13,240	\$1.145119 3,629	\$1.965508 15,151	\$1.441782 7,918
(6) Accumulation Unit Value Units Outstanding	\$0.577921 1,940	\$0.800161 28,199	\$1.091416 10,304	\$3.713247 27,325	\$1.328286 24,136
(7) Accumulation Unit Value Units Outstanding	\$0.585260 6,582	\$0.845901 62,847	\$1.138754 23,152	\$0.624751 31,143	\$1.127625 24,373
(8) Accumulation Unit Value Units Outstanding	\$0.585260 1,226	\$0.845901 5,466	\$1.138754 2,315	\$0.624751 10,918	\$1.127625 6,019
(9) Accumulation Unit Value Units Outstanding	\$0.577921 5,269	\$0.800161 58,923	\$1.091416 23,592	\$3.713247 9,319	\$1.328286 34,471
(10) Accumulation Unit Value Units Outstanding	\$0.586742 1,610	\$0.855358 5,955	\$1.148461 3,237	\$0.643955 1,232	\$1.174655 1,813

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Mid Cap Value Division (a)	Small Cap Growth Stock Division	Index 600 Stock Division	Small Cap Value Division (a)	International Growth Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$45,938	\$139,425	\$7,580	\$135,841	\$126,530
Fidelity Variable Insurance Products	—	—	—	—	—
Neuberger Berman Advisers Management Trust	—	—	—	—	—
Russell Investment Funds	—	—	—	—	—
Due from Northwestern Mutual Life Insurance Company	10	14	32	12	14
Total Assets	45,948	139,439	7,612	135,853	126,544
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	59	18	1	24	176
Due to Participants	21	243	—	241	68
Total Liabilities	80	261	1	265	244
Total Net Assets	\$45,868	\$139,178	\$7,611	\$135,588	\$126,300
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$159	\$244	\$4	\$361	\$283
Annuity Reserves	—	—	—	—	—
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	9,158	29,320	1,162	28,196	23,639
Annuity Reserves	79	250	63	157	174
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	2,464	10,345	470	7,886	6,620
Annuity Reserves	4	166	2	118	111
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	6,318	26,705	652	19,305	17,072
Annuity Reserves	20	223	—	76	143
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	11,903	27,871	3,016	32,789	32,456
Annuity Reserves	109	283	16	525	973
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	1,032	5,135	132	4,420	4,544
Class B Accumulation Units (9)	13,008	37,639	1,870	39,802	37,789
Annuity Reserves	56	176	10	152	180
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	1,558	821	214	1,801	2,316
Annuity Reserves	—	—	—	—	—
Total Net Assets	\$45,868	\$139,178	\$7,611	\$135,588	\$126,300
(1) Investments, at cost	\$81,389	\$257,393	\$9,793	\$190,462	\$223,243
(2) Shares Outstanding	56,366	128,266	11,937	119,578	147,643
(3) Accumulation Unit Value	\$1.185376	\$1.671791	\$0.638371	\$1.362805	\$1.103010
Units Outstanding	134	146	6	265	256
(4) Accumulation Unit Value	\$1.152226	\$1.592747	\$0.633010	\$1.313119	\$1.062818
Units Outstanding	7,949	18,409	1,836	21,473	22,242
(5) Accumulation Unit Value	\$1.208947	\$1.728904	\$0.642108	\$1.398335	\$1.131785
Units Outstanding	2,038	5,983	731	5,640	5,849
(6) Accumulation Unit Value	\$1.152226	\$1.592747	\$0.633010	\$1.313119	\$1.062818
Units Outstanding	5,483	16,766	1,031	14,701	16,063
(7) Accumulation Unit Value	\$1.202201	\$0.786331	\$0.641044	\$1.388120	\$1.123539
Units Outstanding	9,901	35,444	4,705	23,621	28,887
(8) Accumulation Unit Value	\$1.202201	\$0.786331	\$0.641044	\$1.388120	\$1.123539
Units Outstanding	858	6,531	206	3,184	4,045
(9) Accumulation Unit Value	\$1.152226	\$1.592747	\$0.633010	\$1.313119	\$1.062818
Units Outstanding	11,290	23,632	2,954	30,311	35,555
(10) Accumulation Unit Value	\$1.212458	\$0.774891	\$0.642663	\$1.403637	\$1.136109
Units Outstanding	1,285	1,059	333	1,283	2,039

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Research International Core Division (a)	International Equity Division (a)	Emerging Markets Equity Division (a)	Money Market Division	Short-Term Bond Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$11,102	\$580,466	\$21,742	\$417,547	\$14,551
Fidelity Variable Insurance Products	—	—	—	—	—
Neuberger Berman Advisers Management Trust	—	—	—	—	—
Russell Investment Funds	—	—	—	—	—
Due from Northwestern Mutual Life Insurance Company	1	45	—	137	19
Total Assets	11,103	580,511	21,742	417,684	14,570
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	7	33	14	14	3
Due to Participants	22	1,202	14	998	—
Total Liabilities	29	1,235	28	1,012	3
Total Net Assets	\$11,074	\$579,276	\$21,714	\$416,672	\$14,567
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$29	\$2,199	\$39	\$1,597	\$2
Annuity Reserves	—	381	—	15	—
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	1,769	190,059	4,299	131,876	2,367
Annuity Reserves	37	1,653	37	505	—
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	401	42,889	932	33,988	605
Annuity Reserves	—	509	1	85	12
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	1,240	113,074	2,449	64,744	1,851
Annuity Reserves	—	604	11	222	—
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	3,503	98,893	5,936	72,570	3,461
Annuity Reserves	11	1,553	45	236	7
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	181	12,951	380	16,052	283
Class B Accumulation Units (9)	2,768	107,569	5,970	89,934	4,220
Annuity Reserves	6	500	8	339	173
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	1,129	6,442	1,607	4,509	1,586
Annuity Reserves	—	—	—	—	—
Total Net Assets	\$11,074	\$579,276	\$21,714	\$416,672	\$14,567
(1) Investments, at cost	\$17,373	\$732,866	\$41,549	\$417,547	\$14,971
(2) Shares Outstanding	19,142	439,082	40,639	417,547	14,727
(3) Accumulation Unit Value Units Outstanding	\$0.598615 48	\$2.541401 865	\$0.551511 71	\$3.484273 458	\$1.045715 2
(4) Accumulation Unit Value Units Outstanding	\$0.593588 2,980	\$2.349745 80,885	\$0.546886 7,860	\$3.043975 43,323	\$1.036955 2,282
(5) Accumulation Unit Value Units Outstanding	\$0.602115 666	\$2.168093 19,782	\$0.554746 1,680	\$1.636123 20,774	\$1.051836 576
(6) Accumulation Unit Value Units Outstanding	\$0.593588 2,088	\$2.349745 48,122	\$0.546886 4,478	\$3.043975 21,270	\$1.036955 1,785
(7) Accumulation Unit Value Units Outstanding	\$0.601121 5,827	\$1.103430 89,623	\$0.553822 10,719	\$1.271472 57,076	\$1.050082 3,296
(8) Accumulation Unit Value Units Outstanding	\$0.601121 301	\$1.103430 11,737	\$0.553822 686	\$1.271472 12,624	\$1.050082 269
(9) Accumulation Unit Value Units Outstanding	\$0.593588 4,663	\$2.349745 45,779	\$0.546886 10,917	\$3.043975 29,545	\$1.036955 4,070
(10) Accumulation Unit Value Units Outstanding	\$0.602638 1,873	\$1.095512 5,880	\$0.555222 2,894	\$1.270343 3,549	\$1.052716 1,507

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Select Bond Division	Long-Term U.S. Government Bond Division (a)	Inflation Protection Division (a)	High Yield Bond Division	Multi-Sector Bond Division (a)
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$844,453	\$52,265	\$38,545	\$147,475	\$41,572
Fidelity Variable Insurance Products	—	—	—	—	—
Neuberger Berman Advisers Management Trust	—	—	—	—	—
Russell Investment Funds	—	—	—	—	—
Due from Northwestern Mutual Life Insurance Company	63	7	10	20	4
Total Assets	844,516	52,272	38,555	147,495	41,576
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	142	8	69	55	154
Due to Participants	1,841	—	118	276	10
Total Liabilities	1,983	8	187	331	164
Total Net Assets	\$842,533	\$52,264	\$38,368	\$147,164	\$41,412
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$5,749	\$40	\$74	\$272	\$32
Annuity Reserves	306	—	—	7	—
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	183,076	11,461	6,162	30,025	4,914
Annuity Reserves	2,200	—	39	438	—
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	50,992	1,510	1,871	13,410	1,466
Annuity Reserves	1,548	—	—	365	12
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	116,378	7,748	4,823	31,004	3,271
Annuity Reserves	982	—	—	186	19
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	212,997	10,989	9,435	30,632	14,116
Annuity Reserves	2,740	195	144	241	185
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	25,632	2,400	1,297	3,806	720
Class B Accumulation Units (9)	206,175	16,767	8,414	32,454	11,949
Annuity Reserves	2,362	252	80	278	12
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	31,396	902	6,029	4,046	4,716
Annuity Reserves	—	—	—	—	—
Total Net Assets	\$842,533	\$52,264	\$38,368	\$147,164	\$41,412
(1) Investments, at cost	\$842,061	\$46,565	\$41,061	\$199,203	\$47,221
(2) Shares Outstanding	699,051	42,805	38,974	288,600	48,851
(3) Accumulation Unit Value	\$12.561982	\$1.282537	\$1.040339	\$1.854701	\$0.929693
Units Outstanding	458	31	71	147	35
(4) Accumulation Unit Value	\$10.972665	\$1.271820	\$1.031635	\$1.723455	\$0.921898
Units Outstanding	16,685	9,012	5,973	17,421	5,330
(5) Accumulation Unit Value	\$2.253325	\$1.290041	\$1.046430	\$1.815250	\$0.935121
Units Outstanding	22,630	1,170	1,788	7,388	1,568
(6) Accumulation Unit Value	\$10.972665	\$1.271820	\$1.031635	\$1.723455	\$0.921898
Units Outstanding	10,606	6,092	4,675	17,990	3,548
(7) Accumulation Unit Value	\$1.650650	\$1.287905	\$1.044699	\$1.231169	\$0.933576
Units Outstanding	129,038	8,532	9,031	24,880	15,120
(8) Accumulation Unit Value	\$1.650650	\$1.287905	\$1.044699	\$1.231169	\$0.933576
Units Outstanding	15,528	1,863	1,242	3,091	771
(9) Accumulation Unit Value	\$10.972665	\$1.271820	\$1.031635	\$1.723455	\$0.921898
Units Outstanding	18,790	13,184	8,156	18,831	12,961
(10) Accumulation Unit Value	\$1.654323	\$1.291153	\$1.047325	\$1.246182	\$0.935931
Units Outstanding	18,978	699	5,756	3,247	5,039

(a) Division was renamed effective April 30, 2008. See Note 1.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Balanced Division	Asset Allocation Division	Fidelity VIP Mid Cap Division	Fidelity VIP Contrafund Division	Neuberger Berman AMT Socially Responsive Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$1,607,791	\$164,197	\$-	\$-	\$-
Fidelity Variable Insurance Products	-	-	142,657	45,991	-
Neuberger Berman Advisers Management Trust	-	-	-	-	4,881
Russell Investment Funds	-	-	-	-	-
Due from Northwestern Mutual Life Insurance Company	323	14	17	3	1
Total Assets	1,608,114	164,211	142,674	45,994	4,882
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	339	545	6	6	-
Due to Participants	5,792	405	77	17	-
Total Liabilities	6,131	950	83	23	-
Total Net Assets	\$1,601,983	\$163,261	\$142,591	\$45,971	\$4,882
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$17,469	\$436	\$269	\$37	\$12
Annuity Reserves	927	7	-	-	-
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	942,803	37,593	26,002	6,255	582
Annuity Reserves	20,072	1,375	107	9	7
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	74,508	8,157	6,878	1,798	306
Annuity Reserves	2,836	628	49	22	-
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	229,611	22,759	17,990	5,224	735
Annuity Reserves	4,365	475	244	24	1
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	103,770	32,956	41,388	15,030	1,482
Annuity Reserves	8,120	1,439	222	73	6
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	38,727	6,035	3,549	631	75
Class B Accumulation Units (9)	153,998	49,883	42,835	12,302	1,450
Annuity Reserves	4,146	840	197	7	2
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	631	527	2,861	4,559	224
Annuity Reserves	-	151	-	-	-
Total Net Assets	\$1,601,983	\$163,261	\$142,591	\$45,971	\$4,882
(1) Investments, at cost	\$2,329,013	\$233,317	\$243,675	\$78,057	\$7,872
(2) Shares Outstanding	1,460,300	211,868	7,873	3,038	520
(3) Accumulation Unit Value	\$8.162059	\$0.991527	\$1.552966	\$0.632696	\$0.609253
Units Outstanding	2,140	440	174	58	19
(4) Accumulation Unit Value	\$7.131449	\$0.955398	\$1.509505	\$0.627398	\$0.604143
Units Outstanding	132,204	39,348	17,225	9,969	963
(5) Accumulation Unit Value	\$2.181253	\$1.017397	\$1.583809	\$0.636396	\$0.612825
Units Outstanding	34,158	8,017	4,343	2,825	499
(6) Accumulation Unit Value	\$7.131449	\$0.955398	\$1.509505	\$0.627398	\$0.604143
Units Outstanding	32,197	23,822	11,918	8,326	1,216
(7) Accumulation Unit Value	\$1.00063	\$1.009999	\$1.574980	\$0.635349	\$0.611798
Units Outstanding	103,763	32,630	26,278	23,657	2,423
(8) Accumulation Unit Value	\$1.00063	\$1.009999	\$1.574980	\$0.635349	\$0.611798
Units Outstanding	38,725	5,975	2,253	993	123
(9) Accumulation Unit Value	\$7.131449	\$0.955398	\$1.509505	\$0.627398	\$0.604143
Units Outstanding	21,594	52,211	28,377	19,609	2,401
(10) Accumulation Unit Value	\$1.019693	\$1.021282	\$1.588398	\$0.636958	\$0.613346
Units Outstanding	619	516	1,801	7,157	365

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Russell Multi-Style Equity Division	Russell Aggressive Equity Division	Russell Non-U.S. Division	Russell Real Estate Securities Division	Russell Core Bond Division
Assets:					
Investments, at value (1) (2)					
Northwestern Mutual Series Fund, Inc.	\$-	\$-	\$-	\$-	\$-
Fidelity Variable Insurance Products	-	-	-	-	-
Neuberger Berman Advisers Management Trust	-	-	-	-	-
Russell Investment Funds	121,860	50,615	119,593	191,912	187,958
Due from Northwestern Mutual Life Insurance Company	14	4	13	71	173
Total Assets	121,874	50,619	119,606	191,983	188,131
Liabilities:					
Due to Northwestern Mutual Life Insurance Company	147	10	170	25	4
Due to Participants	292	161	68	173	296
Total Liabilities	439	171	238	198	300
Total Net Assets	\$121,435	\$50,448	\$119,368	\$191,785	\$187,831
Net Assets:					
Variable Annuity Contracts Issued:					
Prior to December 17, 1981					
Accumulation Units (3)	\$360	\$218	\$265	\$454	\$300
Annuity Reserves	-	-	-	2	-
After December 16, 1981 and Prior to March 31, 1995					
Accumulation Units (4)	15,567	9,531	18,859	33,914	23,558
Annuity Reserves	185	64	160	318	291
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version					
Accumulation Units (5)	9,891	4,610	8,519	11,243	10,163
Annuity Reserves	76	28	37	280	184
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version					
Accumulation Units (6)	15,639	7,621	15,273	26,407	18,596
Annuity Reserves	117	29	117	260	221
On or After March 31, 2000 – Front Load Version					
Accumulation Units (7)	35,991	12,120	34,480	50,628	61,921
Annuity Reserves	331	180	309	413	1,230
On or After March 31, 2000 – Back Load Version					
Class A Accumulation Units (8)	3,651	1,460	3,279	5,866	5,799
Class B Accumulation Units (9)	33,636	13,347	32,725	56,333	57,285
Annuity Reserves	554	264	424	442	1,494
On or After October 16, 2006 – Fee Based Version					
Accumulation Units (10)	5,401	970	4,908	5,219	6,747
Annuity Reserves	36	6	13	6	42
Total Net Assets	\$121,435	\$50,448	\$119,368	\$191,785	\$187,831
(1) Investments, at cost	\$174,091	\$95,433	\$196,851	\$347,447	\$204,775
(2) Shares Outstanding	13,406	6,896	15,882	20,287	20,081
(3) Accumulation Unit Value Units Outstanding	\$0.649525 553	\$0.975105 223	\$0.965924 274	\$1.858618 244	\$1.441509 208
(4) Accumulation Unit Value Units Outstanding	\$0.618811 25,157	\$0.928999 10,259	\$0.920266 20,493	\$1.770725 19,153	\$1.373433 17,152
(5) Accumulation Unit Value Units Outstanding	\$0.671704 14,726	\$1.008404 4,572	\$0.998879 8,528	\$1.922046 5,849	\$1.490712 6,818
(6) Accumulation Unit Value Units Outstanding	\$0.618811 25,272	\$0.928999 8,203	\$0.920266 16,596	\$1.770725 14,913	\$1.373433 13,540
(7) Accumulation Unit Value Units Outstanding	\$0.625460 57,543	\$0.850538 14,250	\$0.791402 43,569	\$2.018711 25,080	\$1.467276 42,201
(8) Accumulation Unit Value Units Outstanding	\$0.625460 5,838	\$0.850538 1,717	\$0.791402 4,143	\$2.018711 2,906	\$1.467276 3,952
(9) Accumulation Unit Value Units Outstanding	\$0.618811 54,356	\$0.928999 14,367	\$0.920266 35,561	\$1.770725 31,813	\$1.373433 41,709
(10) Accumulation Unit Value Units Outstanding	\$0.658748 8,199	\$0.887231 1,094	\$0.843523 5,819	\$1.869424 2,792	\$1.463384 4,611

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Assets and Liabilities
December 31, 2008
(in thousands, except accumulation unit values)

	Russell LifePoints Moderate Strategy Division	Russell LifePoints Balanced Strategy Division	Russell LifePoints Growth Strategy Division	Russell LifePoints Equity Growth Strategy Division
Assets:				
Investments, at value (1) (2)				
Northwestern Mutual Series Fund, Inc.	\$-	\$-	\$-	\$-
Fidelity Variable Insurance Products	-	-	-	-
Neuberger Berman Advisers Management Trust	-	-	-	-
Russell Investment Funds	18,945	58,804	34,354	12,442
Due from Northwestern Mutual Life Insurance Company	10	-	1	2
Total Assets	18,955	58,804	34,355	12,444
Liabilities:				
Due to Northwestern Mutual Life Insurance Company	7	335	41	-
Due to Participants	10	-	-	-
Total Liabilities	17	335	41	-
Total Net Assets	\$18,938	\$58,469	\$34,314	\$12,444

Net Assets:				
Variable Annuity Contracts Issued:				
Prior to December 17, 1981				
Accumulation Units (3)	\$-	\$221	\$-	\$1
Annuity Reserves	-	-	-	-
After December 16, 1981 and Prior to March 31, 1995				
Accumulation Units (4)	3,128	7,890	3,682	2,817
Annuity Reserves	197	89	-	-
On or After March 31, 1995 and Prior to March 31, 2000 – Front Load Version				
Accumulation Units (5)	776	1,823	782	1,084
Annuity Reserves	-	-	-	-
On or After March 31, 1995 and Prior to March 31, 2000 – Back Load Version				
Accumulation Units (6)	2,059	4,866	3,639	960
Annuity Reserves	14	50	-	-
On or After March 31, 2000 – Front Load Version				
Accumulation Units (7)	6,442	24,143	13,885	4,441
Annuity Reserves	432	88	554	167
On or After March 31, 2000 – Back Load Version				
Class A Accumulation Units (8)	355	725	321	13
Class B Accumulation Units (9)	5,505	18,206	11,451	2,961
Annuity Reserves	30	301	-	-
On or After October 16, 2006 – Fee Based Version				
Accumulation Units (10)	-	67	-	-
Annuity Reserves	-	-	-	-
Total Net Assets	\$18,938	\$58,469	\$34,314	\$12,444

(1) Investments, at cost	\$22,733	\$78,084	\$50,760	\$19,559
(2) Shares Outstanding	2,457	8,597	5,586	2,279
(3) Accumulation Unit Value	\$0.818186	\$0.737777	\$0.662577	\$0.592413
Units Outstanding	-	300	-	2
(4) Accumulation Unit Value	\$0.811324	\$0.731582	\$0.657020	\$0.587444
Units Outstanding	3,856	10,785	5,603	4,795
(5) Accumulation Unit Value	\$0.822977	\$0.742083	\$0.666470	\$0.595885
Units Outstanding	942	2,456	1,174	1,819
(6) Accumulation Unit Value	\$0.811324	\$0.731582	\$0.657020	\$0.587444
Units Outstanding	2,537	6,652	5,538	1,634
(7) Accumulation Unit Value	\$0.821607	\$0.740864	\$0.665350	\$0.594901
Units Outstanding	7,841	32,587	20,869	7,464
(8) Accumulation Unit Value	\$0.821607	\$0.740864	\$0.665350	\$0.594901
Units Outstanding	432	978	483	23
(9) Accumulation Unit Value	\$0.811324	\$0.731582	\$0.657020	\$0.587444
Units Outstanding	6,786	24,886	17,429	5,040
(10) Accumulation Unit Value	\$0.823673	\$0.742732	\$0.667030	\$0.596398
Units Outstanding	-	90	-	-

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Operations
For the Year Ended December 31, 2008
(in thousands)

	Growth Stock Division	Focused Appreciation Division (a)	Large Cap Core Stock Division	Large Cap Blend Division (a)	Index 500 Stock Division
Income:					
Dividend income	\$2,955	\$495	\$3,647	\$197	\$19,549
Expenses:					
Mortality and expense risk charges	2,970	1,389	2,436	136	9,453
Net investment income (loss)	(15)	(894)	1,211	61	10,096
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	691	1,142	(4,958)	(1,034)	12,585
Realized gain distributions	18,364	3,836	–	–	27,642
Realized gains (losses)	19,055	4,978	(4,958)	(1,034)	40,227
Change in unrealized appreciation/ depreciation of investments during the period	(153,148)	(74,492)	(104,820)	(6,893)	(443,621)
Net increase (decrease) in net assets resulting from operations	<u>\$(134,108)</u>	<u>\$(70,408)</u>	<u>\$(108,567)</u>	<u>\$(7,866)</u>	<u>\$(393,298)</u>
	Large Company Value Division (a)	Domestic Equity Division (a)	Equity Income Division (a)	Mid Cap Growth Stock Division	Index 400 Stock Division
Income:					
Dividend income	\$292	\$6,804	\$31	\$1,613	\$3,588
Expenses:					
Mortality and expense risk charges	98	2,192	1,150	6,230	2,415
Net investment income (loss)	194	4,612	(1,119)	(4,617)	1,173
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(1,185)	(67)	(2,163)	(30,288)	5,032
Realized gain distributions	33	19,919	2,856	72,786	24,329
Realized gains (losses)	(1,152)	19,852	693	42,498	29,361
Change in unrealized appreciation/ depreciation of investments during the period	(4,803)	(137,702)	(52,491)	(308,007)	(129,812)
Net increase (decrease) in net assets resulting from operations	<u>\$(5,761)</u>	<u>\$(113,238)</u>	<u>\$(52,917)</u>	<u>\$(270,126)</u>	<u>\$(99,278)</u>

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Operations
For the Year Ended December 31, 2008
(in thousands)

	Mid Cap Value Division (a)	Small Cap Growth Stock Division	Index 600 Stock Division	Small Cap Value Division (a)	International Growth Division
Income:					
Dividend income	\$-	\$343	\$-	\$607	\$2,704
Expenses:					
Mortality and expense risk charges	594	2,010	60	1,726	1,773
Net investment income (loss)	(594)	(1,667)	(60)	(1,119)	931
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(2,559)	(2,625)	(964)	5,293	1,471
Realized gain distributions	1,321	38,629	70	14,790	21,165
Realized gains (losses)	(1,238)	36,004	(894)	20,083	22,636
Change in unrealized appreciation/ depreciation of investments during the period	(22,823)	(147,804)	(1,839)	(74,459)	(131,566)
Net increase (decrease) in net assets resulting from operations	\$(24,655)	\$(113,467)	\$(2,793)	\$(55,495)	\$(107,999)
	Research International Core Division (a)	International Equity Division (a)	Emerging Markets Equity Division (a)	Money Market Division	Short-Term Bond Division
Income:					
Dividend income	\$204	\$21,797	\$761	\$9,481	\$564
Expenses:					
Mortality and expense risk charges	105	8,640	281	3,608	95
Net investment income (loss)	99	13,157	480	5,873	469
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(482)	25,892	(1,669)	-	3
Realized gain distributions	107	80,444	160	77	-
Realized gains (losses)	(375)	106,336	(1,509)	77	3
Change in unrealized appreciation/ depreciation of investments during the period	(6,297)	(584,610)	(21,579)	-	(347)
Net increase (decrease) in net assets resulting from operations	\$(6,573)	\$(465,117)	\$(22,608)	\$5,950	\$125

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Operations
For the Year Ended December 31, 2008
(in thousands)

	Select Bond Division	Long-Term U.S. Government Bond Division (a)	Inflation Protection Division (a)	High Yield Bond Division	Multi-Sector Bond Division (a)
Income:					
Dividend income	\$41,864	\$826	\$1,324	\$14,805	\$2,731
Expenses:					
Mortality and expense risk charges	8,489	262	232	1,790	300
Net investment income (loss)	33,375	564	1,092	13,015	2,431
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(1,016)	295	(28)	(6,538)	(553)
Realized gain distributions	-	497	47	-	197
Realized gains (losses)	(1,016)	792	19	(6,538)	(356)
Change in unrealized appreciation/ depreciation of investments during the period	(14,375)	5,498	(2,652)	(50,125)	(5,534)
Net increase (decrease) in net assets resulting from operations	\$17,984	\$6,854	\$(1,541)	\$(43,648)	\$(3,459)
	Balanced Division	Asset Allocation Division	Fidelity VIP Mid Cap Division	Fidelity VIP Contrafund Division	Neuberger Berman AMT Socially Responsive Division
Income:					
Dividend income	\$25,935	\$6,253	\$465	\$518	\$139
Expenses:					
Mortality and expense risk charges	22,872	2,178	1,834	411	45
Net investment income (loss)	3,063	4,075	(1,369)	107	94
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(29,156)	2,582	(3,194)	(2,583)	(309)
Realized gain distributions	559,590	17,460	30,655	974	475
Realized gains (losses)	530,434	20,042	27,461	(1,609)	166
Change in unrealized appreciation/ depreciation of investments during the period	(1,058,413)	(100,425)	(118,274)	(25,260)	(2,945)
Net increase (decrease) in net assets resulting from operations	\$(524,916)	\$(76,308)	\$(92,182)	\$(26,762)	\$(2,685)

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Operations
For the Year Ended December 31, 2008
(in thousands)

	Russell Multi-Style Equity Division	Russell Aggressive Equity Division	Russell Non-U.S. Division	Russell Real Estate Securities Division	Russell Core Bond Division
Income:					
Dividend income	\$2,464	\$632	\$-	\$5,217	\$8,438
Expenses:					
Mortality and expense risk charges	1,529	703	1,537	2,620	1,886
Net investment income (loss)	935	(71)	(1,537)	2,597	6,552
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	976	(2,777)	3,583	1,236	(3,867)
Realized gain distributions	1,713	18	1,609	-	4,178
Realized gains (losses)	2,689	(2,759)	5,192	1,236	311
Change in unrealized appreciation/ depreciation of investments during the period	(87,876)	(36,402)	(92,865)	(113,064)	(17,100)
Net increase (decrease) in net assets resulting from operations	<u>\$(84,252)</u>	<u>\$(39,232)</u>	<u>\$(89,210)</u>	<u>\$(109,231)</u>	<u>\$(10,237)</u>
	Russell LifePoints Moderate Strategy Division	Russell LifePoints Balanced Strategy Division	Russell LifePoints Growth Strategy Division	Russell LifePoints Equity Growth Strategy Division	
Income:					
Dividend income	\$474	\$1,437	\$635	\$88	
Expenses:					
Mortality and expense risk charges	159	494	316	120	
Net investment income (loss)	315	943	319	(32)	
Realized gain (loss) on investments:					
Realized gain (loss) on sale of fund shares	(920)	(2,126)	(1,049)	(941)	
Realized gain distributions	154	1,104	1,087	740	
Realized gains (losses)	(766)	(1,022)	38	(201)	
Change in unrealized appreciation/ depreciation of investments during the period	(3,753)	(18,881)	(15,969)	(6,637)	
Net increase (decrease) in net assets resulting from operations	<u>\$(4,204)</u>	<u>\$(18,960)</u>	<u>\$(15,612)</u>	<u>\$(6,870)</u>	

(a) Division was renamed effective April 30, 2008. See Note 1.

The Accompanying Notes are an Integral Part of the Financial Statements.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Growth Stock Division		Focused Appreciation Division (a)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$ (15)	\$ (600)	\$ (894)	\$ (999)
Net realized gains (losses)	19,055	9,111	4,978	3,458
Net change in unrealized appreciation/depreciation	(153,148)	20,000	(74,492)	23,101
Net increase (decrease) in net assets resulting from operations	(134,108)	28,511	(70,408)	25,560
Contract Transactions:				
Contract owners' net payments	14,708	21,306	23,143	21,998
Annuity payments	(247)	(315)	(109)	(82)
Surrenders and other (net)	(23,137)	(29,265)	(9,561)	(6,112)
Transfers from other divisions or sponsor	162,846	197,425	217,535	180,151
Transfers to other divisions or sponsor	(180,648)	(224,226)	(196,419)	(165,019)
Net increase (decrease) in net assets resulting from contract transactions	(26,478)	(35,075)	34,589	30,936
Net increase (decrease) in net assets	(160,586)	(6,564)	(35,819)	56,496
Net Assets:				
Beginning of period	358,069	364,633	140,752	84,256
End of period	\$197,483	\$358,069	\$104,933	\$140,752
Units issued during the period	124,142	125,467	130,570	108,928
Units redeemed during the period	(134,438)	(139,345)	(113,890)	(92,611)
Net units issued (redeemed) during the period	(10,296)	(13,878)	16,680	16,317
	Large Cap Core Stock Division		Large Cap Blend Division (a) (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$1,211	\$195	\$61	\$23
Net realized gains (losses)	(4,958)	357	(1,034)	46
Net change in unrealized appreciation/depreciation	(104,820)	21,543	(6,893)	(878)
Net increase (decrease) in net assets resulting from operations	(108,567)	22,095	(7,866)	(809)
Contract Transactions:				
Contract owners' net payments	12,243	19,472	6,238	5,204
Annuity payments	(340)	(430)	(9)	(1)
Surrenders and other (net)	(20,719)	(24,193)	(918)	(145)
Transfers from other divisions or sponsor	127,015	144,536	32,901	13,045
Transfers to other divisions or sponsor	(138,088)	(156,543)	(26,687)	(6,229)
Net increase (decrease) in net assets resulting from contract transactions	(19,889)	(17,158)	11,525	11,874
Net increase (decrease) in net assets	(128,456)	4,937	3,659	11,065
Net Assets:				
Beginning of period	287,873	282,936	11,065	—
End of period	\$159,417	\$287,873	\$14,724	\$11,065
Units issued during the period	102,439	98,623	53,546	19,022
Units redeemed during the period	(112,042)	(103,629)	(38,944)	(7,136)
Net units issued (redeemed) during the period	(9,603)	(5,006)	14,602	11,886

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Index 500 Stock Division		Large Company Value Division (a) (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$10,096	\$5,883	\$194	\$76
Net realized gains (losses)	40,227	77,500	(1,152)	(41)
Net change in unrealized appreciation/depreciation	(443,621)	(35,901)	(4,803)	(479)
Net increase (decrease) in net assets resulting from operations	(393,298)	47,482	(5,761)	(444)
Contract Transactions:				
Contract owners' net payments	53,448	75,993	5,209	2,608
Annuity payments	(1,023)	(1,378)	(8)	(1)
Surrenders and other (net)	(68,805)	(92,070)	(796)	(289)
Transfers from other divisions or sponsor	415,967	445,477	22,508	9,060
Transfers to other divisions or sponsor	(459,496)	(490,417)	(17,313)	(2,627)
Net increase (decrease) in net assets resulting from contract transactions	(59,909)	(62,395)	9,600	8,751
Net increase (decrease) in net assets	(453,207)	(14,913)	3,839	8,307
Net Assets:				
Beginning of period	1,087,823	1,102,736	8,307	–
End of period	\$634,616	\$1,087,823	\$12,146	\$8,307
Units issued during the period	258,703	227,014	37,860	12,218
Units redeemed during the period	(264,508)	(229,816)	(26,016)	(3,390)
Net units issued (redeemed) during the period	(5,805)	(2,802)	11,844	8,828
Domestic Equity Division (a)				
	Year Ended December 31, 2008	Year Ended December 31, 2007	Equity Income Division (a)	
			Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$4,612	\$1,409	\$(1,119)	\$1,530
Net realized gains (losses)	19,852	20,657	693	17,324
Net change in unrealized appreciation/depreciation	(137,702)	(44,250)	(52,491)	(17,024)
Net increase (decrease) in net assets resulting from operations	(113,238)	(22,184)	(52,917)	1,830
Contract Transactions:				
Contract owners' net payments	24,566	47,676	16,659	24,002
Annuity payments	(237)	(321)	(238)	(268)
Surrenders and other (net)	(16,693)	(17,808)	(8,451)	(9,785)
Transfers from other divisions or sponsor	359,078	415,124	155,776	170,151
Transfers to other divisions or sponsor	(355,409)	(402,842)	(152,284)	(149,357)
Net increase (decrease) in net assets resulting from contract transactions	11,305	41,829	11,462	34,743
Net increase (decrease) in net assets	(101,933)	19,645	(41,455)	36,573
Net Assets:				
Beginning of period	280,715	261,070	138,076	101,503
End of period	\$178,782	\$280,715	\$96,621	\$138,076
Units issued during the period	356,631	317,792	121,063	111,402
Units redeemed during the period	(347,395)	(289,333)	(113,117)	(92,181)
Net units issued (redeemed) during the period	9,236	28,459	7,946	19,221

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Mid Cap Growth Stock Division (c)		Index 400 Stock Division	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$(4,617)	\$(2,616)	\$1,173	\$587
Net realized gains (losses)	42,498	41,438	29,361	28,084
Net change in unrealized appreciation/depreciation	(308,007)	81,635	(129,812)	(9,555)
Net increase (decrease) in net assets resulting from operations	(270,126)	120,457	(99,278)	19,116
Contract Transactions:				
Contract owners' net payments	21,663	27,444	14,547	25,301
Annuity payments	(475)	(585)	(264)	(347)
Surrenders and other (net)	(41,700)	(57,452)	(17,478)	(19,124)
Transfers from other divisions or sponsor	152,075	189,239	192,657	237,754
Transfers to other divisions or sponsor	(186,366)	(238,737)	(210,520)	(254,430)
Net increase (decrease) in net assets resulting from contract transactions	(54,803)	(80,091)	(21,058)	(10,846)
Net increase (decrease) in net assets	(324,929)	40,366	(120,336)	8,270
Net Assets:				
Beginning of period	699,670	659,304	285,660	277,390
End of period	\$374,741	\$699,670	\$165,324	\$285,660
Units issued during the period	84,214	92,574	122,805	130,846
Units redeemed during the period	(95,756)	(106,642)	(133,462)	(135,458)
Net units issued (redeemed) during the period	(11,542)	(14,068)	(10,657)	(4,612)
	Mid Cap Value Division (a)		Small Cap Growth Stock Division	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$(594)	\$(118)	\$(1,667)	\$(2,486)
Net realized gains (losses)	(1,238)	13,066	36,004	31,631
Net change in unrealized appreciation/depreciation	(22,823)	(14,702)	(147,804)	(8,415)
Net increase (decrease) in net assets resulting from operations	(24,655)	(1,754)	(113,467)	20,730
Contract Transactions:				
Contract owners' net payments	7,163	13,003	14,772	23,512
Annuity payments	(31)	(33)	(172)	(222)
Surrenders and other (net)	(4,773)	(4,092)	(15,366)	(18,744)
Transfers from other divisions or sponsor	85,999	122,093	185,691	222,909
Transfers to other divisions or sponsor	(87,474)	(112,047)	(192,241)	(244,678)
Net increase (decrease) in net assets resulting from contract transactions	884	18,924	(7,316)	(17,223)
Net increase (decrease) in net assets	(23,771)	17,170	(120,783)	3,507
Net Assets:				
Beginning of period	69,639	52,469	259,961	256,454
End of period	\$45,868	\$69,639	\$139,178	\$259,961
Units issued during the period	59,959	69,843	126,496	119,778
Units redeemed during the period	(59,084)	(60,121)	(127,447)	(125,440)
Net units issued (redeemed) during the period	875	9,722	(951)	(5,662)

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

(c) Division was renamed effective April 30, 2007. See Note 1.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Index 600 Stock Division (b)		Small Cap Value Division (a)	
	Year Ended December 31, 2008	Period Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$ (60)	\$ (22)	\$ (1,119)	\$ (1,161)
Net realized gains (losses)	(894)	8	20,083	19,373
Net change in unrealized appreciation/depreciation	(1,839)	(374)	(74,459)	(22,520)
Net increase (decrease) in net assets resulting from operations	(2,793)	(388)	(55,495)	(4,308)
Contract Transactions:				
Contract owners' net payments	1,994	1,473	19,451	29,360
Annuity payments	(9)	(3)	(110)	(128)
Surrenders and other (net)	(299)	(74)	(12,082)	(12,909)
Transfers from other divisions or sponsor	13,549	6,098	203,664	215,563
Transfers to other divisions or sponsor	(9,859)	(2,078)	(212,134)	(217,283)
Net increase (decrease) in net assets resulting from contract transactions	5,376	5,416	(1,211)	14,603
Net increase (decrease) in net assets	2,583	5,028	(56,706)	10,295
Net Assets:				
Beginning of period	5,028	–	192,294	181,999
End of period	\$7,611	\$5,028	\$135,588	\$192,294
Units issued during the period	19,898	7,673	132,129	125,509
Units redeemed during the period	(13,348)	(2,421)	(133,160)	(118,302)
Net units issued (redeemed) during the period	6,550	5,252	(1,031)	7,207
International Growth Division				
	Year Ended December 31, 2008	Year Ended December 31, 2007	Research International Core Division (a) (b)	
			Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$931	\$ (336)	\$99	\$43
Net realized gains (losses)	22,636	27,087	(375)	110
Net change in unrealized appreciation/depreciation	(131,566)	(5,171)	(6,297)	25
Net increase (decrease) in net assets resulting from operations	(107,999)	21,580	(6,573)	178
Contract Transactions:				
Contract owners' net payments	20,518	30,783	3,668	2,499
Annuity payments	(190)	(252)	(11)	(3)
Surrenders and other (net)	(12,391)	(12,557)	(484)	(128)
Transfers from other divisions or sponsor	236,132	281,949	19,929	10,893
Transfers to other divisions or sponsor	(237,494)	(275,256)	(14,902)	(3,992)
Net increase (decrease) in net assets resulting from contract transactions	6,575	24,667	8,200	9,269
Net increase (decrease) in net assets	(101,424)	46,247	1,627	9,447
Net Assets:				
Beginning of period	227,724	181,477	9,447	–
End of period	\$126,300	\$227,724	\$11,074	\$9,447
Units issued during the period	166,264	160,849	29,097	13,748
Units redeemed during the period	(161,701)	(148,338)	(19,583)	(4,816)
Net units issued (redeemed) during the period	4,563	12,511	9,514	8,932

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	International Equity Division (a)		Emerging Markets Equity Division (a) (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$13,157	\$7,893	\$480	\$(3)
Net realized gains (losses)	106,336	46,893	(1,509)	193
Net change in unrealized appreciation/depreciation	(584,610)	93,717	(21,579)	1,771
Net increase (decrease) in net assets resulting from operations	(465,117)	148,503	(22,608)	1,961
Contract Transactions:				
Contract owners' net payments	71,571	95,528	8,000	4,181
Annuity payments	(792)	(975)	(18)	(5)
Surrenders and other (net)	(63,108)	(70,193)	(1,562)	(149)
Transfers from other divisions or sponsor	649,432	728,526	53,629	28,165
Transfers to other divisions or sponsor	(669,589)	(714,314)	(40,934)	(8,946)
Net increase (decrease) in net assets resulting from contract transactions	(12,486)	38,572	19,115	23,246
Net increase (decrease) in net assets	(477,603)	187,075	(3,493)	25,207
Net Assets:				
Beginning of period	1,056,879	869,804	25,207	–
End of period	\$579,276	\$1,056,879	\$21,714	\$25,207
Units issued during the period	322,098	291,767	67,675	29,062
Units redeemed during the period	(316,863)	(273,404)	(48,610)	(8,822)
Net units issued (redeemed) during the period	5,235	18,363	19,065	20,240
	Money Market Division		Short-Term Bond Division (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$5,873	\$10,867	\$469	\$152
Net realized gains (losses)	77	–	3	8
Net change in unrealized appreciation/depreciation	–	–	(347)	(73)
Net increase (decrease) in net assets resulting from operations	5,950	10,867	125	87
Contract Transactions:				
Contract owners' net payments	96,507	96,926	3,609	1,248
Annuity payments	(245)	(183)	(14)	–
Surrenders and other (net)	(77,558)	(51,545)	(1,203)	(53)
Transfers from other divisions or sponsor	360,330	353,960	24,163	6,117
Transfers to other divisions or sponsor	(261,846)	(353,263)	(17,885)	(1,627)
Net increase (decrease) in net assets resulting from contract transactions	117,188	45,895	8,670	5,685
Net increase (decrease) in net assets	123,138	56,762	8,795	5,772
Net Assets:				
Beginning of period	293,534	236,772	5,772	–
End of period	\$416,672	\$293,534	\$14,567	\$5,772
Units issued during the period	235,826	282,393	26,786	7,776
Units redeemed during the period	(180,962)	(257,135)	(18,614)	(2,161)
Net units issued (redeemed) during the period	54,864	25,258	8,172	5,615

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Select Bond Division		Long-Term U.S. Government Bond Division (a) (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$33,375	\$25,167	\$564	\$163
Net realized gains (losses)	(1,016)	146	792	86
Net change in unrealized appreciation/depreciation	(14,375)	18,853	5,498	201
Net increase (decrease) in net assets resulting from operations	17,984	44,166	6,854	450
Contract Transactions:				
Contract owners' net payments	89,251	122,438	9,145	2,475
Annuity payments	(1,114)	(1,045)	(14)	–
Surrenders and other (net)	(73,294)	(61,722)	(2,000)	(115)
Transfers from other divisions or sponsor	1,104,323	1,064,375	76,479	8,973
Transfers to other divisions or sponsor	(1,191,919)	(1,015,092)	(46,280)	(3,703)
Net increase (decrease) in net assets resulting from contract transactions	(72,753)	108,954	37,330	7,630
Net increase (decrease) in net assets	(54,769)	153,120	44,184	8,080
Net Assets:				
Beginning of period	897,302	744,182	8,080	–
End of period	\$842,533	\$897,302	\$52,264	\$8,080
Units issued during the period	391,350	404,325	79,036	11,799
Units redeemed during the period	(412,123)	(363,463)	(46,001)	(4,251)
Net units issued (redeemed) during the period	(20,773)	40,862	33,035	7,548
	Inflation Protection Division (a) (b)		High Yield Bond Division	
	Year Ended December 31, 2008	Period Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$1,092	\$229	\$13,015	\$10,691
Net realized gains (losses)	19	29	(6,538)	(2,932)
Net change in unrealized appreciation/depreciation	(2,652)	137	(50,125)	(5,205)
Net increase (decrease) in net assets resulting from operations	(1,541)	395	(43,648)	2,554
Contract Transactions:				
Contract owners' net payments	8,028	2,113	14,680	24,445
Annuity payments	(22)	–	(277)	(282)
Surrenders and other (net)	(2,146)	(81)	(14,645)	(14,641)
Transfers from other divisions or sponsor	60,876	9,530	191,420	216,221
Transfers to other divisions or sponsor	(36,654)	(2,130)	(206,766)	(216,976)
Net increase (decrease) in net assets resulting from contract transactions	30,082	9,432	(15,588)	8,767
Net increase (decrease) in net assets	28,541	9,827	(59,236)	11,321
Net Assets:				
Beginning of period	9,827	–	206,400	195,079
End of period	\$38,368	\$9,827	\$147,164	\$206,400
Units issued during the period	65,661	11,751	117,909	126,995
Units redeemed during the period	(38,218)	(2,502)	(125,849)	(121,990)
Net units issued (redeemed) during the period	27,443	9,249	(7,940)	5,005

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Multi-Sector Bond Division (a) (b)		Balanced Division	
	Year Ended December 31, 2008	Period Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$2,431	\$546	\$3,063	\$45,049
Net realized gains (losses)	(356)	(1)	530,434	86,081
Net change in unrealized appreciation/depreciation	(5,534)	(114)	(1,058,413)	(16,167)
Net increase (decrease) in net assets resulting from operations	(3,459)	431	(524,916)	114,963
Contract Transactions:				
Contract owners' net payments	14,949	6,844	83,312	107,776
Annuity payments	(13)	(1)	(5,867)	(7,015)
Surrenders and other (net)	(2,740)	(239)	(174,091)	(199,693)
Transfers from other divisions or sponsor	65,045	22,112	288,157	323,790
Transfers to other divisions or sponsor	(54,699)	(6,818)	(392,814)	(391,952)
Net increase (decrease) in net assets resulting from contract transactions	22,542	21,898	(201,303)	(167,094)
Net increase (decrease) in net assets	19,083	22,329	(726,219)	(52,131)
Net Assets:				
Beginning of period	22,329	—	2,328,202	2,380,333
End of period	\$41,412	\$22,329	\$1,601,983	\$2,328,202
Units issued during the period	84,136	30,045	133,488	136,555
Units redeemed during the period	(61,962)	(7,847)	(166,578)	(156,706)
Net units issued (redeemed) during the period	22,174	22,198	(33,090)	(20,151)
Asset Allocation Division				
	Year Ended December 31, 2008	Year Ended December 31, 2007	Fidelity VIP Mid Cap Division	
			Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$4,075	\$2,972	\$(1,369)	\$(949)
Net realized gains (losses)	20,042	19,450	27,461	19,251
Net change in unrealized appreciation/depreciation	(100,425)	(3,406)	(118,274)	5,249
Net increase (decrease) in net assets resulting from operations	(76,308)	19,016	(92,182)	23,551
Contract Transactions:				
Contract owners' net payments	19,849	21,842	28,305	37,278
Annuity payments	(626)	(636)	(117)	(163)
Surrenders and other (net)	(17,034)	(17,843)	(12,599)	(12,489)
Transfers from other divisions or sponsor	126,000	131,677	235,810	238,995
Transfers to other divisions or sponsor	(136,568)	(139,076)	(233,771)	(228,922)
Net increase (decrease) in net assets resulting from contract transactions	(8,379)	(4,036)	17,628	34,699
Net increase (decrease) in net assets	(84,687)	14,980	(74,554)	58,250
Net Assets:				
Beginning of period	247,948	232,968	217,145	158,895
End of period	\$163,261	\$247,948	\$142,591	\$217,145
Units issued during the period	120,679	113,888	127,206	114,326
Units redeemed during the period	(129,427)	(116,552)	(118,850)	(100,439)
Net units issued (redeemed) during the period	(8,748)	(2,664)	8,356	13,887

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Fidelity VIP Contrafund Division (b)		Neuberger Berman AMT Socially Responsive Division (b)	
	Year Ended December 31, 2008	Period Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$107	\$141	\$94	\$(10)
Net realized gains (losses)	(1,609)	7,833	166	14
Net change in unrealized appreciation/depreciation	(25,260)	(6,804)	(2,945)	(45)
Net increase (decrease) in net assets resulting from operations	(26,762)	1,170	(2,685)	(41)
Contract Transactions:				
Contract owners' net payments	17,286	8,173	1,887	1,268
Annuity payments	(11)	(1)	(2)	—
Surrenders and other (net)	(2,838)	(301)	(211)	(51)
Transfers from other divisions or sponsor	83,448	34,726	8,470	3,991
Transfers to other divisions or sponsor	(59,867)	(9,052)	(6,370)	(1,374)
Net increase (decrease) in net assets resulting from contract transactions	38,018	33,545	3,774	3,834
Net increase (decrease) in net assets	11,256	34,715	1,089	3,793
Net Assets:				
Beginning of period	34,715	—	3,793	—
End of period	\$45,971	\$34,715	\$4,882	\$3,793
Units issued during the period	120,407	40,633	12,559	5,197
Units redeemed during the period	(78,920)	(9,526)	(8,278)	(1,469)
Net units issued (redeemed) during the period	41,487	31,107	4,281	3,728
	Russell Multi-Style Equity Division		Russell Aggressive Equity Division	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$935	\$159	\$(71)	\$(581)
Net realized gains (losses)	2,689	12,062	(2,759)	14,415
Net change in unrealized appreciation/depreciation	(87,876)	5,712	(36,402)	(11,445)
Net increase (decrease) in net assets resulting from operations	(84,252)	17,933	(39,232)	2,389
Contract Transactions:				
Contract owners' net payments	12,962	28,130	5,444	11,216
Annuity payments	(269)	(229)	(93)	(100)
Surrenders and other (net)	(12,390)	(13,623)	(5,695)	(7,549)
Transfers from other divisions or sponsor	274,625	309,851	98,627	118,938
Transfers to other divisions or sponsor	(277,569)	(316,017)	(102,251)	(124,538)
Net increase (decrease) in net assets resulting from contract transactions	(2,641)	8,112	(3,968)	(2,033)
Net increase (decrease) in net assets	(86,893)	26,045	(43,200)	356
Net Assets:				
Beginning of period	208,328	182,283	93,648	93,292
End of period	\$121,435	\$208,328	\$50,448	\$93,648
Units issued during the period	333,503	329,951	82,411	81,139
Units redeemed during the period	(335,575)	(321,404)	(85,033)	(82,194)
Net units issued (redeemed) during the period	(2,072)	8,547	(2,622)	(1,055)

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Russell Non-U.S. Division		Russell Real Estate Securities Division	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Year Ended December 31, 2007
Operations:				
Net investment income (loss)	\$(1,537)	\$3,396	\$2,597	\$4,668
Net realized gains (losses)	5,192	47,280	1,236	70,510
Net change in unrealized appreciation/depreciation	(92,865)	(33,206)	(113,064)	(138,229)
Net increase (decrease) in net assets resulting from operations	(89,210)	17,470	(109,231)	(63,051)
Contract Transactions:				
Contract owners' net payments	14,711	29,970	28,406	49,098
Annuity payments	(218)	(219)	(276)	(394)
Surrenders and other (net)	(12,022)	(12,841)	(20,205)	(23,560)
Transfers from other divisions or sponsor	260,287	296,501	357,141	413,790
Transfers to other divisions or sponsor	(264,430)	(303,320)	(364,965)	(456,334)
Net increase (decrease) in net assets resulting from contract transactions	(1,672)	10,091	101	(17,400)
Net increase (decrease) in net assets	(90,882)	27,561	(109,130)	(80,451)
Net Assets:				
Beginning of period	210,250	182,689	300,915	381,366
End of period	\$119,368	\$210,250	\$191,785	\$300,915
Units issued during the period	231,979	223,259	146,849	136,823
Units redeemed during the period	(231,863)	(215,687)	(145,526)	(142,715)
Net units issued (redeemed) during the period	116	7,572	1,323	(5,892)
	Russell Core Bond Division		Russell LifePoints Moderate Strategy Division (b)	
	Year Ended December 31, 2008	Year Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$6,552	\$9,016	\$315	\$171
Net realized gains (losses)	311	(391)	(766)	(3)
Net change in unrealized appreciation/depreciation	(17,100)	4,058	(3,753)	(35)
Net increase (decrease) in net assets resulting from operations	(10,237)	12,683	(4,204)	133
Contract Transactions:				
Contract owners' net payments	22,878	34,127	6,387	3,482
Annuity payments	(430)	(287)	(36)	(1)
Surrenders and other (net)	(18,563)	(13,071)	(993)	(546)
Transfers from other divisions or sponsor	388,340	404,423	34,139	6,812
Transfers to other divisions or sponsor	(416,145)	(394,903)	(24,461)	(1,774)
Net increase (decrease) in net assets resulting from contract transactions	(23,920)	30,289	15,036	7,973
Net increase (decrease) in net assets	(34,157)	42,972	10,832	8,106
Net Assets:				
Beginning of period	221,988	179,016	8,106	—
End of period	\$187,831	\$221,988	\$18,938	\$8,106
Units issued during the period	286,510	309,738	42,463	10,359
Units redeemed during the period	(303,978)	(288,707)	(27,915)	(2,513)
Net units issued (redeemed) during the period	(17,468)	21,031	14,548	7,846

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Statements of Changes in Net Assets
(in thousands)

	Russell LifePoints Balanced Strategy Division (b)		Russell LifePoints Growth Strategy Division (b)	
	Year Ended December 31, 2008	Period Ended December 31, 2007	Year Ended December 31, 2008	Period Ended December 31, 2007
Operations:				
Net investment income (loss)	\$943	\$781	\$319	\$571
Net realized gains (losses)	(1,022)	29	38	28
Net change in unrealized appreciation/depreciation	(18,881)	(398)	(15,969)	(438)
Net increase (decrease) in net assets resulting from operations	(18,960)	412	(15,612)	161
Contract Transactions:				
Contract owners' net payments	26,987	18,850	16,267	11,312
Annuity payments	(55)	(15)	(132)	(57)
Surrenders and other (net)	(3,320)	(251)	(991)	572
Transfers from other divisions or sponsor	52,956	21,446	31,665	21,904
Transfers to other divisions or sponsor	(34,140)	(5,441)	(24,343)	(6,432)
Net increase (decrease) in net assets resulting from contract transactions	42,428	34,589	22,466	27,299
Net increase (decrease) in net assets	23,468	35,001	6,854	27,460
Net Assets:				
Beginning of period	35,001	—	27,460	—
End of period	\$58,469	\$35,001	\$34,314	\$27,460
Units issued during the period	93,054	40,350	55,444	33,448
Units redeemed during the period	(48,299)	(6,371)	(30,472)	(7,324)
Net units issued (redeemed) during the period	44,755	33,979	24,972	26,124
Russell LifePoints Equity Growth Strategy Division (b)				
	Year Ended December 31, 2008	Period Ended December 31, 2007		
Operations:				
Net investment income (loss)	\$(32)	\$297		
Net realized gains (losses)	(201)	(15)		
Net change in unrealized appreciation/depreciation	(6,637)	(479)		
Net increase (decrease) in net assets resulting from operations	(6,870)	(197)		
Contract Transactions:				
Contract owners' net payments	6,047	1,997		
Annuity payments	(11)	—		
Surrenders and other (net)	(1,250)	(24)		
Transfers from other divisions or sponsor	9,614	11,586		
Transfers to other divisions or sponsor	(7,111)	(1,337)		
Net increase (decrease) in net assets resulting from contract transactions	7,289	12,222		
Net increase (decrease) in net assets	419	12,025		
Net Assets:				
Beginning of period	12,025	—		
End of period	\$12,444	\$12,025		
Units issued during the period	19,586	13,355		
Units redeemed during the period	(10,757)	(1,407)		
Net units issued (redeemed) during the period	8,829	11,948		

(a) Division was renamed effective April 30, 2008. See Note 1.

(b) Division commenced operations on April 30, 2007.

NML Variable Annuity Account B
Notes to Financial Statements
December 31, 2008

1. Organization

NML Variable Annuity Account B (the "Account") is registered as a unit investment trust under the Investment Company Act of 1940 and is a segregated asset account of The Northwestern Mutual Life Insurance Company ("Northwestern Mutual") used to fund variable annuity contracts ("contracts") for tax-deferred annuities, individual retirement annuities and non-qualified plans. Three versions of the contract are currently offered: Front-Load contracts with a sales charge up to 4.5% of purchase payments; Back-Load contracts with a withdrawal charge up to 6%; and Fee Based contracts with no sales or withdrawal charges.

All assets of each Division of the Account are invested in shares of the corresponding Portfolio of Northwestern Mutual Series Fund, Inc., Fidelity Variable Insurance Products, Neuberger Berman Advisers Management Trust and the Russell Investment Funds (collectively known as "the Funds"). The Funds are open-end investment companies registered under the Investment Company Act of 1940.

Effective April 30, 2008, the following Divisions of the Account were renamed:

<u>Old Name</u>	<u>New Name</u>
Janus Capital Appreciation Division	Focused Appreciation Division
Capital Guardian Large Cap Blend Division	Large Cap Blend Division
American Century Large Company Value Division	Large Company Value Division
Capital Guardian Domestic Equity Division	Domestic Equity Division
T. Rowe Price Equity Income Division	Equity Income Division
AllianceBernstein Mid Cap Value Division	Mid Cap Value Division
T. Rowe Price Small Cap Value Division	Small Cap Value Division
MFS Research International Core Division	Research International Core Division
Franklin Templeton International Equity Division	International Equity Division
MFS Emerging Markets Equity Division	Emerging Markets Equity Division
PIMCO Long-Term U.S. Government Bond Division	Long-Term U.S. Government Bond Division
American Century Inflation Protection Division	Inflation Protection Division
PIMCO Multi-Sector Bond Division	Multi-Sector Bond Division

Effective April 30, 2007, the Aggressive Growth Stock Division was renamed to the Mid Cap Growth Stock Division.

2. Significant Accounting Policies

A. *Use of Estimates* – The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

B. *Investment Valuation* – The shares are valued at the Funds' offering and redemption prices per share. In September 2006, the Financial Accounting Standards Board issued Standard No. 157, "Fair Value Measurements" ("FAS 157") effective for fiscal years beginning after November 15, 2007. FAS 157 redefines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value and requires additional disclosure about the use of fair value measurements in an effort to make the measurement of fair value more consistent and comparable. The Account adopted FAS 157 effective January 1, 2008. As of December 31, 2008, all of the Account's investments are identified as Level 1 securities for valuation purposes

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under FAS 157. Level 1 securities are valued at fair value as determined by quoted prices in active markets for identical securities.

- C. *Investment Income, Securities Transactions and Contract Dividends* – Transactions in the Funds' shares are accounted for on the trade date. The basis for determining cost on sale of the Funds' shares is identified cost. Dividend income and distributions of net realized gains from the Funds are recorded on the ex-date of the dividends. Dividends and distributions received are reinvested in additional shares of the respective portfolios of the Funds. Certain contracts are eligible to receive dividends from Northwestern Mutual. The dividends are reinvested in the Account and have been reflected in Contract owners' net payments in the accompanying financial statements.
- D. *Due to Participants* – Upon notification of death of the contract owner or maturity of a contract, a liability is recorded and is included in due to participants in the accompanying financial statements. This liability is identified as Level 2 for valuation purposes under FAS 157. Level 2 liabilities are valued at fair value based on significant observable inputs other than quoted prices in active markets for identical liabilities.
- E. *Annuity Reserves* – Annuity reserves are based on published annuity tables with age adjustment and interest based on actual investment experience or assumed investment rates of 3.5% or 5%.
- F. *Taxes* – Northwestern Mutual is taxed as a "life insurance company" under the Internal Revenue Code and the operations of the Account form a part of and are taxed with those of Northwestern Mutual. Under current law, no federal income taxes are payable with respect to the Account. Accordingly, no provision for any such liability has been made.

3. Purchases and Sales of Investments

Purchases and sales of the Funds' shares for the year ended December 31, 2008 were as follows: (*in thousands*)

<u>Division</u>	<u>Purchases</u>	<u>Sales</u>
Growth Stock	\$37,287	\$45,481
Focused Appreciation	49,040	11,750
Large Cap Core Stock	17,435	36,343
Large Cap Blend	13,073	1,468
Index 500 Stock	104,761	127,549
Large Company Value	11,429	1,598
Domestic Equity	54,995	19,009
Equity Income	23,305	10,010
Mid Cap Growth Stock	98,226	84,875
Index 400 Stock	43,886	39,494
Mid Cap Value	9,094	7,509
Small Cap Growth Stock	55,010	25,421
Index 600 Stock	5,772	416
Small Cap Value	36,186	23,748
International Growth	45,817	17,057
Research International Core	9,211	778
International Equity	179,538	98,677
Emerging Markets Equity	22,107	2,315
Money Market	210,038	86,070
Short-Term Bond	10,663	1,537
Select Bond	140,804	179,173
Long-Term U.S. Government Bond	41,694	3,297
Inflation Protection	34,101	2,703
High Yield Bond	30,709	33,399

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<u>Division</u>	<u>Purchases</u>	<u>Sales</u>
Multi-Sector Bond	\$29,024	\$3,696
Balanced	680,626	319,438
Asset Allocation	46,551	33,428
Fidelity VIP Mid Cap	62,188	15,309
Fidelity VIP Contrafund	43,065	3,959
Neuberger Berman AMT Socially Responsive	4,626	294
Russell Multi-Style Equity	18,161	17,903
Russell Aggressive Equity	6,603	10,510
Russell Non-U.S.	17,615	19,239
Russell Real Estate Securities	35,678	33,525
Russell Core Bond	38,172	51,563
Russell LifePoints Moderate Strategy	16,992	1,482
Russell LifePoints Balanced Strategy	51,764	6,900
Russell LifePoints Growth Strategy	26,131	1,859
Russell LifePoints Equity Growth Strategy	9,973	1,977

4. Expenses and Related Party Transactions

A deduction for mortality and expense risks is determined daily and paid to Northwestern Mutual as compensation for assuming the risk that annuity payments will continue for longer periods than anticipated because the annuitants as a group live longer than expected, and the risk that the charges made by Northwestern Mutual may be insufficient to cover the actual costs incurred in connection with the contracts.

For contracts issued prior to December 17, 1981, the deduction is at an annual rate of 0.75% of the net assets of each Division attributable to these contracts. For these contracts, the rate may be increased or decreased by the Board of Trustees of Northwestern Mutual not to exceed a 1% annual rate.

For contracts issued after December 16, 1981 and prior to March 31, 1995, the deduction is at an annual rate of 1.25% of the net assets of each Division attributable to these contracts.

For contracts issued on or after March 31, 1995 and prior to March 31, 2000, for the Front-Load version and the Back-Load version, the deduction for mortality and expense risks is determined daily at annual rates of 0.40% and 1.25%, respectively, of the net assets of each Division attributable to these contracts and is paid to Northwestern Mutual. For these contracts, the rates may be increased or decreased by the Board of Trustees of Northwestern Mutual not to exceed a maximum annual rate of 0.75% and 1.50%, respectively.

For contracts issued on or after March 31, 2000, for the Front-Load version and the Back-Load version, the deduction for mortality and expense risks is determined daily at annual rates of 0.50% and 1.25%, respectively, of the net assets of each Division attributable to these contracts and is paid to Northwestern Mutual. Under the terms of the back-load version of the contract, the net assets may be subject to the deduction for the front-load version of the contract after the withdrawal charge period. Rates may be increased or decreased by the Board of Trustees of Northwestern Mutual not to exceed a maximum annual rate of 0.75% and 1.50% for the Front-Load version and the Back-Load version, respectively. For Front-Load and Back-Load version contracts purchased before April 30, 2008, the current mortality and expense risk charges will not be increased before May 1, 2012.

For Fee Based contracts issued on or after December 31, 2000, the deduction for mortality and expense risks is determined daily at an annual rate of 0.35% of the net assets of each Division attributable to these contracts and is paid to Northwestern Mutual. For these contracts, the rate may be increased by the Board of Trustees of Northwestern Mutual not to exceed a maximum annual

NML Variable Annuity Account B
Notes to Financial Statements
December 31, 2008

rate of 0.75%. For Fee Based contracts purchased before April 30, 2007, the current mortality and expense risk charges will not be increased before May 1, 2011.

5. Financial Highlights
(For a unit outstanding during the period)

Division	As of the respective period end date:			For the respective period ended:		
	Units Outstanding	Unit Value, Lowest to Highest	Net Assets (000's)	Dividend Income as a % of Average Net Assets	Expense Ratio, Lowest to Highest	Total Return, Lowest to Highest (2)
Growth Stock						
Year Ended 12/31/08	142,036	\$0.598090 to \$1.918211	\$197,483	1.05%	0.35% to 1.25%	(39.62)% to (39.07)%
Year Ended 12/31/07	152,332	\$0.983146 to \$3.161031	\$358,069	0.89%	0.35% to 1.25%	7.83% to 8.81%
Year Ended 12/31/06	166,209	\$0.904890 to \$2.916699	\$364,633	0.76%	0.35% to 1.25%	8.21% to 9.19%
Year Ended 12/31/05	170,577	\$0.829993 to \$2.681914	\$360,468	1.05%	0.35% to 1.25%	6.38% to 7.34%
Year Ended 12/31/04	176,713	\$0.774425 to \$2.508557	\$362,855	0.69%	0.35% to 1.25%	5.34% to 6.30%
Focused Appreciation						
Year Ended 12/31/08	82,172	\$1.248176 to \$1.313419	\$104,933	0.35%	0.35% to 1.25%	(40.76)% to (40.22)%
Year Ended 12/31/07	65,492	\$2.106906 to \$2.197094	\$140,752	0.04%	0.35% to 1.25%	25.26% to 26.39%
Year Ended 12/31/06	49,176	\$1.682068 to \$1.738315	\$84,256	0.44%	0.35% to 1.25%	3.58% to 4.52%
Year Ended 12/31/05	32,378	\$1.623859 to \$1.663190	\$53,274	0.20%	0.35% to 1.25%	15.55% to 16.59%
Year Ended 12/31/04	8,535	\$1.405312 to \$1.426538	\$12,060	0.15%	0.35% to 1.25%	18.19% to 19.25%
Large Cap Core Stock						
Year Ended 12/31/08	123,988	\$0.612094 to \$1.624552	\$159,417	1.61%	0.35% to 1.25%	(39.50)% to (38.96)%
Year Ended 12/31/07	133,591	\$1.004227 to \$2.671949	\$287,873	1.14%	0.35% to 1.25%	7.76% to 8.74%
Year Ended 12/31/06	138,596	\$0.924940 to \$2.467131	\$282,936	1.08%	0.35% to 1.25%	10.12% to 11.11%
Year Ended 12/31/05	140,199	\$0.833720 to \$2.229337	\$268,827	1.30%	0.35% to 1.25%	7.12% to 8.08%
Year Ended 12/31/04	144,588	\$0.772557 to \$2.070897	\$265,200	0.95%	0.35% to 1.25%	6.82% to 7.78%
Large Cap Blend (1)						
Year Ended 12/31/08	26,488	\$0.546962 to \$0.555297	\$14,724	1.32%	0.35% to 1.25%	(40.99)% to (40.46)%
Year Ended 12/31/07	11,886	\$0.926940 to \$0.932619	\$11,065	0.93%	0.35% to 1.25%	(7.30)% to (6.74)%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Index 500 Stock						
Year Ended 12/31/08	301,818	\$0.670905 to \$3.450407	\$634,616	2.25%	0.35% to 1.25%	(37.73)% to (37.16)%
Year Ended 12/31/07	307,623	\$1.069283 to \$5.512984	\$1,087,823	1.62%	0.35% to 1.25%	4.11% to 5.06%
Year Ended 12/31/06	310,424	\$1.019334 to \$5.268640	\$1,102,736	1.60%	0.35% to 1.25%	14.19% to 15.22%
Year Ended 12/31/05	317,806	\$0.886007 to \$4.590845	\$1,034,273	1.75%	0.35% to 1.25%	3.43% to 4.36%
Year Ended 12/31/04	321,263	\$0.850261 to \$4.416556	\$1,063,411	1.34%	0.35% to 1.25%	9.32% to 10.31%
Large Company Value (1)						
Year Ended 12/31/08	20,672	\$0.577921 to \$0.586742	\$12,146	2.44%	0.35% to 1.25%	(38.02)% to (37.45)%
Year Ended 12/31/07	8,828	\$0.932366 to \$0.938079	\$8,307	2.11%	0.35% to 1.25%	(6.75)% to (6.19)%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Domestic Equity						
Year Ended 12/31/08	215,459	\$0.800161 to \$0.855358	\$178,782	2.91%	0.35% to 1.25%	(39.26)% to (38.71)%
Year Ended 12/31/07	206,223	\$1.317376 to \$1.395608	\$280,715	1.43%	0.35% to 1.25%	(7.50)% to (6.66)%
Year Ended 12/31/06	177,765	\$1.424141 to \$1.495151	\$261,070	0.00%	0.35% to 1.25%	15.12% to 16.16%
Year Ended 12/31/05	134,350	\$1.237056 to \$1.287166	\$169,447	1.91%	0.35% to 1.25%	6.71% to 7.67%
Year Ended 12/31/04	93,992	\$1.159280 to \$1.195493	\$110,874	1.61%	0.35% to 1.25%	15.40% to 16.44%
Equity Income						
Year Ended 12/31/08	85,128	\$1.091416 to \$1.148461	\$96,621	0.03%	0.35% to 1.25%	(36.61)% to (36.03)%
Year Ended 12/31/07	77,182	\$1.721722 to \$1.795424	\$138,076	2.14%	0.35% to 1.25%	1.97% to 2.89%
Year Ended 12/31/06	57,961	\$1.688469 to \$1.744928	\$101,503	1.83%	0.35% to 1.25%	17.68% to 18.74%
Year Ended 12/31/05	41,726	\$1.434821 to \$1.469591	\$61,034	1.83%	0.35% to 1.25%	2.90% to 3.82%
Year Ended 12/31/04	23,505	\$1.394433 to \$1.415494	\$33,324	1.92%	0.35% to 1.25%	13.73% to 14.76%

(1) Division commenced operations on April 30, 2007.

(2) Total return includes deductions for management and other expenses; it excludes deduction for sales loads and other charges. Returns are not annualized for periods less than one year.

NML Variable Annuity Account B
Notes to Financial Statements
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Division	As of the respective period end date:			For the respective period ended:		
	Units Outstanding	Unit Value, Lowest to Highest	Net Assets ('000's)	Dividend Income as a % of Average Net Assets	Expense Ratio, Lowest to Highest	Total Return, Lowest to Highest (2)
Mid Cap Growth Stock						
Year Ended 12/31/08	143,335	\$0.624751 to \$4.064928	\$374,741	0.30%	0.35% to 1.25%	(40.83)% to (40.29)%
Year Ended 12/31/07	154,877	\$1.047939 to \$6.835316	\$699,670	0.75%	0.35% to 1.25%	19.19% to 20.27%
Year Ended 12/31/06	168,944	\$0.872601 to \$5.705905	\$659,304	0.13%	0.35% to 1.25%	3.11% to 4.04%
Year Ended 12/31/05	185,752	\$0.839995 to \$5.506309	\$720,485	0.05%	0.35% to 1.25%	4.82% to 5.77%
Year Ended 12/31/04	196,196	\$0.795400 to \$5.226856	\$753,933	0.00%	0.35% to 1.25%	12.80% to 13.82%
Index 400 Stock						
Year Ended 12/31/08	127,487	\$1.127625 to \$1.441782	\$165,324	1.54%	0.35% to 1.25%	(37.07)% to (36.50)%
Year Ended 12/31/07	138,144	\$1.778444 to \$2.271681	\$285,660	1.23%	0.35% to 1.25%	6.58% to 7.55%
Year Ended 12/31/06	142,755	\$1.656125 to \$2.113326	\$277,390	1.07%	0.35% to 1.25%	8.68% to 9.66%
Year Ended 12/31/05	144,810	\$1.512499 to \$1.928160	\$259,212	0.77%	0.35% to 1.25%	10.98% to 11.98%
Year Ended 12/31/04	142,795	\$1.352705 to \$1.722759	\$230,656	0.67%	0.35% to 1.25%	14.82% to 15.86%
Mid Cap Value						
Year Ended 12/31/08	38,938	\$1.152226 to \$1.212458	\$45,868	0.00%	0.35% to 1.25%	(35.88)% to (35.30)%
Year Ended 12/31/07	38,063	\$1.796945 to \$1.873865	\$69,639	0.81%	0.35% to 1.25%	(1.41)% to (0.51)%
Year Ended 12/31/06	28,340	\$1.822606 to \$1.883538	\$52,469	1.28%	0.35% to 1.25%	13.08% to 14.09%
Year Ended 12/31/05	21,558	\$1.611849 to \$1.650893	\$35,219	0.65%	0.35% to 1.25%	4.15% to 5.09%
Year Ended 12/31/04	13,191	\$1.547558 to \$1.570931	\$20,658	1.16%	0.35% to 1.25%	17.19% to 18.25%
Small Cap Growth Stock						
Year Ended 12/31/08	107,970	\$0.774891 to \$1.728904	\$139,178	0.17%	0.35% to 1.25%	(44.57)% to (44.07)%
Year Ended 12/31/07	108,921	\$1.385379 to \$3.092578	\$259,961	0.08%	0.35% to 1.25%	8.18% to 9.16%
Year Ended 12/31/06	114,581	\$1.269179 to \$2.834618	\$256,454	0.00%	0.35% to 1.25%	5.36% to 6.31%
Year Ended 12/31/05	112,059	\$1.193857 to \$2.667734	\$243,675	0.00%	0.35% to 1.25%	9.81% to 10.79%
Year Ended 12/31/04	107,008	\$1.077557 to \$2.409091	\$217,489	0.00%	0.35% to 1.25%	17.32% to 18.38%
Index 600 Stock (1)						
Year Ended 12/31/08	11,802	\$0.633010 to \$0.642663	\$7,611	0.00%	0.35% to 1.25%	(32.16)% to (31.55)%
Year Ended 12/31/07	5,252	\$0.933101 to \$0.938826	\$5,028	0.00%	0.35% to 1.25%	(6.68)% to (6.11)%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Small Cap Value						
Year Ended 12/31/08	100,478	\$1.313119 to \$1.403637	\$135,588	0.35%	0.35% to 1.25%	(29.03)% to (28.39)%
Year Ended 12/31/07	101,509	\$1.850222 to \$1.959983	\$192,294	0.42%	0.35% to 1.25%	(2.07)% to (1.18)%
Year Ended 12/31/06	94,302	\$1.889257 to \$1.983334	\$181,999	0.23%	0.35% to 1.25%	15.11% to 16.15%
Year Ended 12/31/05	80,906	\$1.641244 to \$1.707618	\$135,156	0.31%	0.35% to 1.25%	5.89% to 6.84%
Year Ended 12/31/04	69,029	\$1.549988 to \$1.598319	\$108,671	0.21%	0.35% to 1.25%	23.02% to 24.13%
International Growth						
Year Ended 12/31/08	114,936	\$1.062818 to \$1.136109	\$126,300	1.50%	0.35% to 1.25%	(46.86)% to (46.38)%
Year Ended 12/31/07	110,373	\$1.999925 to \$2.118626	\$227,724	0.81%	0.35% to 1.25%	11.22% to 12.22%
Year Ended 12/31/06	97,860	\$1.798235 to \$1.887847	\$181,477	0.20%	0.35% to 1.25%	19.97% to 21.05%
Year Ended 12/31/05	72,763	\$1.498861 to \$1.559523	\$111,164	1.24%	0.35% to 1.25%	16.54% to 17.59%
Year Ended 12/31/04	44,100	\$1.286123 to \$1.326256	\$57,621	0.78%	0.35% to 1.25%	20.08% to 21.17%
Research International Core (1)						
Year Ended 12/31/08	18,446	\$0.593588 to \$0.602638	\$11,074	1.70%	0.35% to 1.25%	(43.25)% to (42.74)%
Year Ended 12/31/07	8,932	\$1.046028 to \$1.052433	\$9,447	1.34%	0.35% to 1.25%	4.61% to 5.25%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
International Equity						
Year Ended 12/31/08	302,673	\$1.095512 to \$2.541401	\$579,276	2.67%	0.35% to 1.25%	(44.48)% to (43.98)%
Year Ended 12/31/07	297,438	\$1.955614 to \$4.554870	\$1,056,879	1.84%	0.35% to 1.25%	16.59% to 17.65%
Year Ended 12/31/06	279,075	\$1.662262 to \$3.887138	\$869,804	1.70%	0.35% to 1.25%	29.28% to 30.44%
Year Ended 12/31/05	255,999	\$1.274348 to \$2.991857	\$634,347	1.75%	0.35% to 1.25%	10.14% to 11.13%
Year Ended 12/31/04	236,402	\$1.146710 to \$2.702895	\$550,495	1.71%	0.35% to 1.25%	17.85% to 18.91%
Emerging Markets Equity (1)						
Year Ended 12/31/08	39,305	\$0.546886 to \$0.555222	\$21,714	2.54%	0.35% to 1.25%	(55.78)% to (55.38)%
Year Ended 12/31/07	20,240	\$1.236747 to \$1.244312	\$25,207	0.52%	0.35% to 1.25%	23.69% to 24.43%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a

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Division	As of the respective period end date:			For the respective period ended:			
	Units Outstanding	Unit Value, Lowest to Highest	Net Assets (000's)	Dividend Income as a % of Average Net Assets	Expense Ratio, Lowest to Highest	Total Return, Lowest to Highest (2)	
Money Market							
Year Ended 12/31/08	188,619	\$1.270343 to \$3.484273	\$416,672	2.62%	0.35% to 1.25%	1.48% to	2.40%
Year Ended 12/31/07	133,755	\$1.240571 to \$3.416215	\$293,534	5.13%	0.35% to 1.25%	3.97% to	4.91%
Year Ended 12/31/06	108,497	\$1.182475 to \$3.269294	\$236,772	4.74%	0.35% to 1.25%	3.56% to	4.49%
Year Ended 12/31/05	92,906	\$1.131639 to \$3.141208	\$201,838	2.95%	0.35% to 1.25%	1.71% to	2.63%
Year Ended 12/31/04	95,405	\$1.102690 to \$3.073012	\$206,436	1.43%	0.35% to 1.25%	0.17% to	1.08%
Short-Term Bond (1)							
Year Ended 12/31/08	13,787	\$1.036955 to \$1.052716	\$14,567	4.97%	0.35% to 1.25%	1.44% to	2.35%
Year Ended 12/31/07	5,615	\$1.022274 to \$1.028506	\$5,772	5.37%	0.35% to 1.25%	2.24% to	2.85%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Select Bond							
Year Ended 12/31/08	232,713	\$1.650650 to \$12.561982	\$842,533	4.67%	0.35% to 1.25%	1.97% to	2.89%
Year Ended 12/31/07	253,486	\$1.606628 to \$12.257484	\$897,302	3.99%	0.35% to 1.25%	5.07% to	6.02%
Year Ended 12/31/06	212,625	\$1.516531 to \$11.608006	\$744,182	3.66%	0.35% to 1.25%	2.46% to	3.38%
Year Ended 12/31/05	168,714	\$1.466954 to \$11.273136	\$622,741	3.42%	0.35% to 1.25%	0.95% to	1.86%
Year Ended 12/31/04	125,912	\$1.440153 to \$11.111137	\$516,249	4.04%	0.35% to 1.25%	3.44% to	4.38%
Long-Term U.S Government Bond (1)							
Year Ended 12/31/08	40,583	\$1.271820 to \$1.291153	\$52,264	2.95%	0.35% to 1.25%	19.26% to	20.34%
Year Ended 12/31/07	7,548	\$1.066436 to \$1.072953	\$8,080	4.30%	0.35% to 1.25%	6.65% to	7.30%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Inflation Protection Bond (1)							
Year Ended 12/31/08	36,692	\$1.031635 to \$1.047325	\$38,368	4.82%	0.35% to 1.25%	(2.61)% to	(1.73)%
Year Ended 12/31/07	9,249	\$1.059280 to \$1.065745	\$9,827	5.15%	0.35% to 1.25%	5.94% to	6.58%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a	n/a
High Yield Bond							
Year Ended 12/31/08	92,995	\$1.231169 to \$1.854701	\$147,164	8.13%	0.35% to 1.25%	(22.33)% to	(21.62)%
Year Ended 12/31/07	100,935	\$1.573219 to \$2.375895	\$206,400	6.16%	0.35% to 1.25%	1.10% to	2.02%
Year Ended 12/31/06	95,929	\$1.544440 to \$2.338260	\$195,079	6.57%	0.35% to 1.25%	8.42% to	9.39%
Year Ended 12/31/05	89,781	\$1.413965 to \$2.146008	\$170,738	6.58%	0.35% to 1.25%	0.14% to	1.03%
Year Ended 12/31/04	81,452	\$1.401540 to \$2.132449	\$157,870	6.88%	0.35% to 1.25%	11.36% to	12.37%
Multi-Sector Bond (1)							
Year Ended 12/31/08	44,372	\$0.921898 to \$0.935931	\$41,412	7.35%	0.35% to 1.25%	(8.02)% to	(7.19)%
Year Ended 12/31/07	22,198	\$1.002320 to \$1.008445	\$22,329	5.17%	0.35% to 1.25%	0.24% to	0.85%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Balanced							
Year Ended 12/31/08	365,400	\$1.000063 to \$8.162059	\$1,601,983	1.30%	0.35% to 1.25%	(23.69)% to	(23.00)%
Year Ended 12/31/07	398,490	\$1.300669 to \$10.641985	\$2,328,202	3.04%	0.35% to 1.25%	4.83% to	5.78%
Year Ended 12/31/06	418,640	\$1.231506 to \$10.101237	\$2,380,333	2.86%	0.35% to 1.25%	9.05% to	10.03%
Year Ended 12/31/05	442,202	\$1.120868 to \$9.216522	\$2,360,699	2.66%	0.35% to 1.25%	2.31% to	3.23%
Year Ended 12/31/04	440,624	\$1.087384 to \$8.963381	\$2,424,304	2.54%	0.35% to 1.25%	6.55% to	7.52%
Asset Allocation							
Year Ended 12/31/08	162,959	\$0.955398 to \$1.021282	\$163,261	2.94%	0.35% to 1.25%	(31.00)% to	(30.37)%
Year Ended 12/31/07	171,707	\$1.384559 to \$1.466752	\$247,948	2.25%	0.35% to 1.25%	8.03% to	9.01%
Year Ended 12/31/06	174,372	\$1.281584 to \$1.345472	\$232,968	1.82%	0.35% to 1.25%	8.56% to	9.53%
Year Ended 12/31/05	164,774	\$1.180583 to \$1.228390	\$201,054	1.41%	0.35% to 1.25%	5.67% to	6.62%
Year Ended 12/31/04	140,560	\$1.117219 to \$1.152100	\$161,896	0.00%	0.35% to 1.25%	8.65% to	9.63%
Fidelity VIP Mid Cap							
Year Ended 12/31/08	92,369	\$1.509505 to \$1.588398	\$142,591	0.25%	0.35% to 1.25%	(40.36)% to	(39.82)%
Year Ended 12/31/07	84,013	\$2.530987 to \$2.639341	\$217,145	0.48%	0.35% to 1.25%	13.90% to	14.93%
Year Ended 12/31/06	70,124	\$2.222115 to \$2.296424	\$158,895	0.15%	0.35% to 1.25%	11.01% to	12.01%
Year Ended 12/31/05	46,885	\$2.001683 to \$2.050180	\$95,468	0.00%	0.35% to 1.25%	16.56% to	17.60%
Year Ended 12/31/04	23,113	\$1.717354 to \$1.743292	\$40,054	0.00%	0.35% to 1.25%	23.11% to	24.22%

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Fidelity VIP Contrafund (1)						
Year Ended 12/31/08	72,594	\$0.627398 to \$0.636958	\$45,971	1.08%	0.35% to 1.25%	(43.40)% to (42.89)%
Year Ended 12/31/07	31,107	\$1.108565 to \$1.115338	\$34,715	1.30%	0.35% to 1.25%	10.87% to 11.54%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Neuberger Berman AMT Socially Responsive (1)						
Year Ended 12/31/08	8,009	\$0.604143 to \$0.613346	\$4,882	2.73%	0.35% to 1.25%	(40.20)% to (39.66)%
Year Ended 12/31/07	3,728	\$1.010221 to \$1.016402	\$3,793	0.11%	0.35% to 1.25%	1.03% to 1.64%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Russell Multi-Style Equity						
Year Ended 12/31/08	191,644	\$0.618811 to \$0.671704	\$121,435	1.46%	0.35% to 1.25%	(41.31)% to (40.77)%
Year Ended 12/31/07	193,716	\$1.054304 to \$1.134719	\$208,328	0.97%	0.35% to 1.25%	8.98% to 9.97%
Year Ended 12/31/06	185,171	\$0.963199 to \$1.032365	\$182,283	0.93%	0.35% to 1.25%	11.35% to 12.35%
Year Ended 12/31/05	160,461	\$0.858577 to \$0.919329	\$141,151	1.05%	0.35% to 1.25%	5.94% to 6.90%
Year Ended 12/31/04	141,072	\$0.804386 to \$0.860463	\$117,097	0.73%	0.35% to 1.25%	8.44% to 9.42%
Russell Aggressive Equity						
Year Ended 12/31/08	54,685	\$0.850538 to \$1.008404	\$50,448	0.86%	0.35% to 1.25%	(43.63)% to (43.12)%
Year Ended 12/31/07	57,307	\$1.497529 to \$1.773725	\$93,648	0.37%	0.35% to 1.25%	2.13% to 3.06%
Year Ended 12/31/06	58,363	\$1.455332 to \$1.722029	\$93,292	0.19%	0.35% to 1.25%	13.37% to 14.39%
Year Ended 12/31/05	53,263	\$1.274157 to \$1.506167	\$75,049	0.18%	0.35% to 1.25%	5.04% to 5.99%
Year Ended 12/31/04	51,192	\$1.203942 to \$1.421771	\$68,855	0.17%	0.35% to 1.25%	13.30% to 14.33%
Russell Non-U.S.						
Year Ended 12/31/08	134,983	\$0.791402 to \$0.998879	\$119,368	0.00%	0.35% to 1.25%	(43.13)% to (42.61)%
Year Ended 12/31/07	134,867	\$1.381147 to \$1.741498	\$210,250	2.56%	0.35% to 1.25%	8.74% to 9.73%
Year Ended 12/31/06	127,295	\$1.260557 to \$1.587886	\$182,689	2.63%	0.35% to 1.25%	22.11% to 23.21%
Year Ended 12/31/05	99,849	\$1.024633 to \$1.289430	\$117,602	1.59%	0.35% to 1.25%	12.28% to 13.29%
Year Ended 12/31/04	79,941	\$0.905783 to \$1.138748	\$84,397	2.11%	0.35% to 1.25%	16.83% to 17.89%
Russell Real Estate Securities						
Year Ended 12/31/08	102,750	\$1.770725 to \$2.018711	\$191,785	1.92%	0.35% to 1.25%	(37.48)% to (36.91)%
Year Ended 12/31/07	101,427	\$2.832067 to \$3.204435	\$300,915	2.29%	0.35% to 1.25%	(16.91)% to (16.15)%
Year Ended 12/31/06	107,317	\$3.408298 to \$3.827505	\$381,366	1.96%	0.35% to 1.25%	34.16% to 35.36%
Year Ended 12/31/05	95,902	\$2.540501 to \$2.831791	\$252,942	2.13%	0.35% to 1.25%	11.56% to 12.56%
Year Ended 12/31/04	83,376	\$2.277262 to \$2.519496	\$196,014	2.31%	0.35% to 1.25%	33.20% to 34.40%
Russell Core Bond						
Year Ended 12/31/08	130,191	\$1.373433 to \$1.490712	\$187,831	4.00%	0.35% to 1.25%	(4.76)% to (3.90)%
Year Ended 12/31/07	147,659	\$1.442151 to \$1.552068	\$221,988	5.30%	0.35% to 1.25%	5.91% to 6.86%
Year Ended 12/31/06	126,626	\$1.361728 to \$1.453107	\$179,016	4.58%	0.35% to 1.25%	2.44% to 3.36%
Year Ended 12/31/05	97,984	\$1.329349 to \$1.406633	\$134,224	3.65%	0.35% to 1.25%	0.75% to 1.66%
Year Ended 12/31/04	71,697	\$1.319453 to \$1.384409	\$97,182	2.44%	0.35% to 1.25%	3.36% to 4.30%
Russell LifePoints Moderate Strategy (1)						
Year Ended 12/31/08	22,394	\$0.811324 to \$0.823673	\$18,938	2.67%	0.35% to 1.25%	(20.97)% to (20.25)%
Year Ended 12/31/07	7,846	\$1.026594 to \$1.032870	\$8,106	4.90%	0.35% to 1.25%	2.67% to 3.29%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Russell LifePoints Balanced Strategy (1)						
Year Ended 12/31/08	78,734	\$0.731582 to \$0.742732	\$58,469	2.56%	0.35% to 1.25%	(28.18)% to (27.53)%
Year Ended 12/31/07	33,979	\$1.018600 to \$1.024838	\$35,001	4.66%	0.35% to 1.25%	1.87% to 2.49%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a
Russell LifePoints Growth Strategy (1)						
Year Ended 12/31/08	51,096	\$0.657020 to \$0.667030	\$34,314	1.78%	0.35% to 1.25%	(35.12)% to (34.53)%
Year Ended 12/31/07	26,124	\$1.012636 to \$1.018835	\$27,460	4.38%	0.35% to 1.25%	1.27% to 1.89%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a

(1) Division commenced operations on April 30, 2007.

(2) Total return includes deductions for management and other expenses; it excludes deduction for sales loads and other charges. Returns are not annualized for periods less than one year.

NML Variable Annuity Account B
Notes to Financial Statements
December 31, 2008

Division	As of the respective period end date:			For the respective period ended:		
	Units Outstanding	Unit Value, Lowest to Highest	Net Assets (000's)	Dividend Income as a % of Average Net Assets	Expense Ratio, Lowest to Highest	Total Return, Lowest to Highest (2)
Russell LifePoints Equity Growth Strategy (1)						
Year Ended 12/31/08	20,777	\$0.587444 to \$0.596398	\$12,444	0.63%	0.35% to 1.25%	(41.49)% to (40.96)%
Year Ended 12/31/07	11,948	\$1.003947 to \$1.010091	\$12,025	5.12%	0.35% to 1.25%	0.41% to 1.01%
Year Ended 12/31/06	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/05	n/a	n/a	n/a	n/a	n/a	n/a
Year Ended 12/31/04	n/a	n/a	n/a	n/a	n/a	n/a

(1) Division commenced operations on April 30, 2007.

(2) Total return includes deductions for management and other expenses; it excludes deduction for sales loads and other charges. Returns are not annualized for periods less than one year.

Report of Independent Registered Public Accounting Firm

To The Northwestern Mutual Life Insurance Company and
Contract Owners of NML Variable Annuity Account B

In our opinion, the accompanying statements of assets and liabilities, the related statements of operations, and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of the NML Variable Annuity Account B and its Growth Stock Division, Focused Appreciation Division, Large Cap Core Stock Division, Large Cap Blend Division, Index 500 Stock Division, Large Company Value Division, Domestic Equity Division, Equity Income Division, Mid Cap Growth Stock Division, Index 400 Stock Division, Mid Cap Value Division, Small Cap Growth Stock Division, Index 600 Stock Division, Small Cap Value Division, International Growth Division, Research International Core Division, International Equity Division, Emerging Markets Equity Division, Money Market Division, Short-Term Bond Division, Select Bond Division, Long Term U.S. Government Bond Division, Inflation Protection Division, High Yield Bond Division, Multi-Sector Bond Division, Balanced Division, Asset Allocation Division, Fidelity VIP Mid Cap Division, Fidelity VIP Contrafund Division, Neuberger Berman AMT Socially Responsive Division, Russell Multi-Style Equity Division, Russell Aggressive Equity Division, Russell Non-US Division, Russell Real Estate Securities Division, Russell Core Bond Division, Russell LifePoints Moderate Strategy Division, Russell LifePoints Balanced Strategy Division, Russell LifePoints Growth Strategy Division, and Russell LifePoints Equity Growth Strategy Division at December 31, 2008, and the results of each of their operations, the changes in each of their net assets and their financial highlights for the periods presented, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of The Northwestern Mutual Life Insurance Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included direct confirmation of securities owned at December 31, 2008 with Northwestern Mutual Series Fund, Inc., Fidelity Variable Insurance Products, Neuberger Berman Advisers Management Trust and the Russell Investment Funds, provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

February 17, 2009

The following financial statements of Northwestern Mutual should be considered only as bearing upon the ability of Northwestern Mutual to meet its obligations under the Contracts.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Consolidated Statement of Financial Position (in millions)

	December 31,	
	2008	2007
Assets:		
Bonds	\$ 79,314	\$ 76,842
Mortgage loans	21,677	20,833
Policy loans	12,884	11,797
Common and preferred stocks	5,744	9,525
Real estate	1,528	1,499
Other investments	9,185	8,749
Cash and temporary investments	4,807	2,547
Total investments	135,139	131,792
Due and accrued investment income	1,498	1,395
Income taxes recoverable	73	-
Net deferred tax assets	2,696	1,461
Deferred premium and other assets	2,361	2,195
Separate account assets	13,387	19,704
Total assets	\$ 155,154	\$ 156,547
Liabilities and Surplus:		
Reserves for policy benefits	\$ 117,954	\$ 109,573
Policyowner dividends payable	4,555	5,024
Interest maintenance reserve	192	709
Asset valuation reserve	1,023	3,687
Income taxes payable	-	683
Other liabilities	5,642	5,061
Separate account liabilities	13,387	19,704
Total liabilities	142,753	144,441
Surplus	12,401	12,106
Total liabilities and surplus	\$ 155,154	\$ 156,547

The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Consolidated Statement of Operations (in millions)

	For the year ended		
	December 31,		
	2008	2007	2006
Revenue:			
Premiums	\$ 13,551	\$ 13,242	\$ 12,149
Net investment income	7,835	7,568	7,073
Other income	537	545	511
	21,923	21,355	19,733
Benefits and expenses:			
Benefit payments to policyowners and beneficiaries	6,071	5,544	4,979
Net additions to policy benefit reserves	8,491	7,904	7,304
Net transfers to (from) separate accounts	(102)	484	492
	14,460	13,932	12,775
Commissions and operating expenses	2,070	2,009	1,894
	16,530	15,941	14,669
Gain from operations before dividends and taxes	5,393	5,414	5,064
Policyowner dividends	4,547	5,012	4,628
	846	402	436
Income tax expense (benefit)	(304)	21	17
	1,150	381	419
Net gain from operations	1,150	381	419
Net realized capital gains (losses)	(667)	619	410
	\$ 483	\$ 1,000	\$ 829
Net income	\$ 483	\$ 1,000	\$ 829

The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company
Consolidated Statement of Changes in Surplus
(in millions)

	For the year ended		
	December 31,		
	2008	2007	2006
Beginning of year balance	\$ 12,106	\$ 11,684	\$ 10,381
Net income	483	1,000	829
Change in net unrealized capital gains (losses)	(3,483)	(12)	581
Change in net deferred tax assets	(20)	165	337
Change in nonadmitted assets and other	(178)	(137)	70
Change in asset valuation reserve	2,664	(594)	(514)
Change in accounting principle	829	-	-
	<hr/>	<hr/>	<hr/>
Net increase in surplus	295	422	1,303
	<hr/>	<hr/>	<hr/>
End of year balance	<u>\$ 12,401</u>	<u>\$ 12,106</u>	<u>\$ 11,684</u>

The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Consolidated Statement of Cash Flows (in millions)

	For the year ended December 31,		
	2008	2007	2006
Cash flows from operating activities:			
Premiums and other income received	\$ 9,198	\$ 9,495	\$ 8,634
Investment income received	7,838	7,424	6,893
Benefit payments to policyowners and beneficiaries	(6,442)	(5,904)	(5,274)
Net transfers from (to) separate accounts	121	(474)	(482)
Commissions, expenses and taxes paid	(2,115)	(2,148)	(2,202)
	<u>8,600</u>	<u>8,393</u>	<u>7,569</u>
Cash flows from investing activities:			
Proceeds from investments sold or matured:			
Bonds	42,698	64,980	51,695
Common and preferred stocks	5,527	6,099	6,088
Mortgage loans	1,811	2,940	3,413
Real estate	199	177	65
Other investments	1,669	1,175	1,693
	<u>51,904</u>	<u>75,371</u>	<u>62,954</u>
Cost of investments acquired:			
Bonds	46,592	70,890	56,372
Common and preferred stocks	5,121	5,594	5,777
Mortgage loans	2,659	4,422	4,659
Real estate	118	151	107
Other investments	2,712	2,401	2,099
	<u>57,202</u>	<u>83,458</u>	<u>69,014</u>
Disbursement of policy loans, net of repayments	1,087	802	730
Net cash applied to investing activities	<u>(6,385)</u>	<u>(8,889)</u>	<u>(6,790)</u>
Cash flows from financing and miscellaneous sources:			
Net inflows (outflows) on deposit-type contracts	(84)	198	69
Other cash provided (applied)	129	(40)	(87)
	<u>45</u>	<u>158</u>	<u>(18)</u>
Net cash provided by (applied to) financing and other activities:	<u>45</u>	<u>158</u>	<u>(18)</u>
Net increase (decrease) in cash and temporary investments	2,260	(338)	761

The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

**The Northwestern Mutual Life Insurance Company
Consolidated Statement of Cash Flows
(in millions)**

Cash and temporary investments, beginning of year	<u>2,547</u>	<u>2,885</u>	<u>2,124</u>
Cash and temporary investments, end of year	<u>\$ 4,807</u>	<u>\$ 2,547</u>	<u>\$ 2,885</u>

The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

1. Basis of Presentation

The accompanying consolidated statutory financial statements include the accounts of The Northwestern Mutual Life Insurance Company and its wholly owned subsidiary, Northwestern Long Term Care Insurance Company (together, “the Company”). All intercompany balances and transactions have been eliminated. The Company offers life, annuity, disability and long-term care insurance products to the personal, business and estate markets.

The consolidated financial statements were prepared in accordance with accounting practices prescribed or permitted by the Office of the Commissioner of Insurance of the State of Wisconsin (“statutory basis of accounting”), which are generally based on the *Accounting Practices and Procedures Manual* of the National Association of Insurance Commissioners (“NAIC”). Financial statements prepared on the statutory basis of accounting differ from financial statements prepared in accordance with generally accepted accounting principles (“GAAP”), primarily because on a GAAP basis: (1) certain policy acquisition costs are deferred and amortized, (2) most bond and preferred stock investments are reported at fair value, (3) policy benefit reserves are established using different actuarial methods and assumptions, (4) deposit-type contracts, for which premiums, benefits and reserve changes are not included in revenue or benefits as reported in the statement of operations, are defined differently, (5) majority-owned, non-insurance subsidiaries are consolidated, (6) changes in deferred taxes are reported as a component of net income and (7) no deferral of realized investment gains and losses is permitted. The effects on the financial statements of the Company attributable to the differences between the statutory basis of accounting and GAAP are material.

Certain accounting practices used by the Company vary from the *Accounting Practices and Procedures Manual* of the NAIC with the permission of the Office of the Commissioner of Insurance of the State of Wisconsin (“permitted practices”). Permitted practices are used in situations where the NAIC does not provide accounting guidance specific to a transaction entered into by the Company or where the Company and the Office of the Commissioner agree that an alternative accounting practice would be more appropriate in the Company’s circumstances.

During 2008, the Company adopted new permitted practices regarding valuation of net deferred tax assets (see Note 10) and the Company’s equity method accounting for its investment in Frank Russell Company common stock (see Note 11).

2. Summary of Significant Accounting Policies

The preparation of financial statements in accordance with the statutory basis of accounting requires management to make estimates or assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the annual periods presented. Actual future results could differ from these estimates and assumptions.

Investments

See Notes 3 and 14 regarding the statement value and fair value of the Company’s investments in bonds, common and preferred stocks, mortgage loans and real estate.

Policy Loans

Policy loans represent amounts borrowed from the Company by life insurance policyowners, secured by the cash value of the related policies, and are reported at unpaid principal balance, which approximates fair value.

Other Investments

Other investments consist primarily of partnership investments (including real estate, venture capital and leveraged buyout fund limited partnerships), real estate joint ventures and unconsolidated non-insurance subsidiaries organized as limited liability companies. These investments are reported using the equity method of accounting.

Other investments also include \$107 million and \$113 million of investments in oil and natural gas production at December 31, 2008 and 2007, respectively. These oil and gas investments are reported using the full cost method, under which all exploration and development costs, whether successful or not, are capitalized and amortized as a reduction of net investment income as oil and natural gas reserves are produced. This method is permitted by the Office of the Commissioner of Insurance of the State of Wisconsin (“OCI”). The *Accounting Practices and Procedures Manual* of the NAIC does not provide accounting guidance for oil and gas investments.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

Other investments also include low income housing tax credit investments, leveraged leases and derivative financial instruments. See Note 3 for a description of the Company's investments in leveraged leases and Note 4 regarding the Company's use of derivatives.

Temporary Investments

Temporary investments represent securities that had maturities of one year or less at purchase and are reported at amortized cost, which approximates fair value.

Separate Accounts

Separate account assets and related reserve liabilities represent the segregation of balances attributable to variable life insurance and variable annuity products, including a group annuity separate account used to fund certain of the Company's employee and representative benefit plan obligations. Policyowners bear the investment performance risk associated with variable products unless otherwise guaranteed by the Company. Separate account assets are invested at the direction of the policyowner in a variety of mutual fund options. Variable annuity policyowners also have the option to invest in a fixed rate group annuity issued by the general account of the Company. Separate account assets are reported at fair value based primarily on quoted market prices. See Note 7 for more information about the Company's separate accounts and Note 8 for more information about the Company's employee and representative benefit plans.

Reserves for Policy Benefits

Reserves for policy benefits represent the net present value of future policy benefits less future policy premiums, estimated using actuarial methods, mortality and morbidity experience tables and valuation interest rates prescribed or permitted by the OCI. These actuarial tables and methods include assumptions regarding future mortality and morbidity experience. Actual future experience could differ from the assumptions used to make these reserve estimates. See Note 5 for more information about the Company's reserves for policy benefits.

Policyowner Dividends

Nearly all life, disability and long-term care insurance policies and certain annuity policies issued by the Company are participating. Annually, the Company's Board of Trustees approves dividends payable on participating policies during the subsequent fiscal year, which are accrued and charged to operations when approved. Participating policyowners generally have the option to direct their dividends to be paid in cash, used to reduce future premiums due or used to purchase additional insurance benefits. Dividends used by policyowners to purchase additional insurance benefits are reported as premiums in the consolidated statement of operations, but are not included in premiums received or benefit payments in the consolidated statement of cash flows.

Interest Maintenance Reserve

The Company is required to maintain an interest maintenance reserve ("IMR"). The IMR is used to defer realized capital gains and losses, net of income tax, on fixed income investments and derivatives that are attributable to changes in market interest rates, including both changes in risk-free market interest rates and market credit spreads. Net realized capital gains and losses deferred to the IMR are amortized into investment income over the estimated remaining term to maturity of the investment sold or the asset/liability hedged by an interest rate-related derivative contract.

Asset Valuation Reserve

The Company is required to maintain an asset valuation reserve ("AVR"). The AVR represents a reserve for invested asset valuation using a formula prescribed by the NAIC. The AVR is intended to protect surplus against potential declines in the value of the Company's investments that are not related to changes in interest rates. Increases or decreases in the AVR are reported as direct adjustments to surplus in the consolidated statement of changes in surplus.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

Premium Revenue

Most life insurance premiums are recognized as revenue at the beginning of each respective policy year. Universal life insurance and annuity premiums are recognized as revenue when received. Considerations received on supplementary annuity contracts without life contingencies are deposit-type transactions and thereby excluded from revenue in the consolidated statement of operations. Disability and long-term care insurance premiums are recognized as revenue when due. Premium revenue is reported net of ceded reinsurance. See Note 9 for more information about the Company's use of reinsurance.

Net Investment Income

Net investment income primarily represents interest and dividends received or accrued on bonds, common and preferred stocks, mortgage loans, policy loans and other investments. Accrued investment income more than 90 days past due is nonadmitted and reported as a direct reduction of surplus in the consolidated statement of changes in surplus. Accrued investment income that is ultimately deemed uncollectible is included as a reduction of net investment income in the period that such determination is made. Net investment income also includes dividends paid to the Company from accumulated earnings of joint ventures, partnerships and unconsolidated non-insurance subsidiaries and prepayment fees on bonds and mortgage loans. Net investment income is reduced by investment management expenses, real estate depreciation, depletion related to oil and natural gas investments and interest costs associated with securities lending.

Other Income

Other income primarily represents ceded reinsurance expense allowances and various insurance policy charges. See Note 9 for more information about the Company's use of reinsurance.

Benefit Payments to Policyowners and Beneficiaries

Benefit payments to policyowners and beneficiaries include death, surrender, disability and long-term care benefits, as well as matured endowments and payments on supplementary annuity contracts that include life contingencies. Benefit payments on supplementary annuity contracts without life contingencies are deposit-type transactions and thereby excluded from benefits in the consolidated statement of operations. Benefit payments are reported net of ceded reinsurance recoveries. See Note 9 for more information about the Company's use of reinsurance.

Commissions and Operating Expenses

Commissions and other operating costs, including costs of acquiring new insurance policies, are generally charged to expense as incurred.

Information Technology Equipment and Software

The cost of information technology ("IT") equipment and operating system software is generally capitalized and depreciated over three years using the straight-line method. Non-operating system software is generally capitalized and depreciated over a maximum of five years. IT equipment and operating software assets of \$43 million and \$36 million at December 31, 2008 and 2007, respectively, are included in other assets in the consolidated statement of financial position and are net of accumulated depreciation of \$143 million and \$120 million, respectively. Non-operating software costs, net of accumulated depreciation, are nonadmitted assets and thereby excluded from assets and surplus in the consolidated statement of financial position. Depreciation expense for IT equipment and software totaled \$78 million, \$78 million and \$77 million for the years ended December 31, 2008, 2007 and 2006, respectively.

Furniture, Fixtures and Equipment

The cost of furniture, fixtures and equipment, including leasehold improvements, is generally capitalized and depreciated over the useful life of the assets using the straight-line method. Furniture, fixtures and equipment costs, net of accumulated depreciation, are nonadmitted assets and thereby excluded from assets and surplus in the consolidated statement of financial position. Depreciation expense for furniture, fixtures and equipment totaled \$8 million, \$7 million and \$7 million for the years ended December 31, 2008, 2007 and 2006, respectively.

Investment Capital Gains and Losses

Realized capital gains and losses are recognized based upon specific identification of investment assets sold. Realized capital losses also include valuation adjustments for impairment of bonds, common and preferred stocks, mortgage loans, real estate and other investments that have experienced a decline in fair value that management considers to be other-than-temporary.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

Realized capital gains and losses as reported in the consolidated statement of operations exclude any IMR deferrals. See Note 3 for more information regarding investment impairments and other realized capital gains and losses.

Effective January 1, 2008, the Company adopted Statement of Statutory Accounting Principle No. 98, *Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, An Amendment to SSAP No. 43 – Loan Backed and Structured Securities* ("SSAP 98"). SSAP 98 requires that valuation adjustments for other-than-temporary impairment of loan-backed and structured securities be based on fair value. Previous statutory accounting guidance required that such valuation adjustments be based on undiscounted future cash flows. SSAP 98 was adopted prospectively and resulted in \$90 million of additional realized capital losses during 2008 than would have been required under previous accounting guidance.

Unrealized capital gains and losses primarily represent changes in the fair value of common stocks and other equity investments and changes in valuation adjustments made for bonds in or near default. Changes in the Company's equity method share of undistributed earnings of joint ventures, partnerships and unconsolidated non-insurance subsidiaries are also included in changes in unrealized capital gains and losses. See Note 3 for more information regarding unrealized capital gains and losses.

Nonadmitted Assets

Certain assets are designated as nonadmitted on the statutory basis of accounting. Such assets, principally related to pension funding, amounts advanced to or due from the Company's financial representatives, furniture, fixtures, equipment and non-operating software (net of accumulated depreciation), deferred tax assets in excess of statutory limits and certain investments are excluded from assets and surplus in the consolidated statement of financial position. Changes in nonadmitted assets are reported as a direct adjustment to surplus in the consolidated statement of changes in surplus.

Reclassifications

Certain amounts in prior year footnote disclosures have been reclassified to conform to the current year presentation.

3. Investments

Bonds

Investments in bonds rated "1" (highest quality), "2" (high quality), "3" (medium quality), "4" (low quality) or "5" (lower quality) by the Securities Valuation Office ("SVO") of the NAIC are reported at amortized cost, less any valuation adjustment. Bonds rated "6" (lowest quality) by the SVO are reported at the lower of amortized cost or fair value. The interest method is used to amortize any purchase premium or discount, including estimates of future prepayments obtained from independent sources. Prepayment assumptions are updated at least annually, using the retrospective method to adjust net investment income for changes in the estimated yield-to-maturity.

Disclosure of fair value for bonds is based primarily on values published by the SVO. In the absence of SVO-published values, fair value is based on quoted market prices of identical or similar assets, if available. For bonds without SVO-published values or quoted market prices, fair value is estimated using independent pricing services or internally developed pricing models. See Note 14 for more information regarding the fair value of the Company's investments in bonds.

Statement value and fair value of bonds at December 31, 2008 and 2007 were as follows:

<u>December 31, 2008</u>	Reconciliation to Fair Value			Fair Value
	Statement Value	Gross Unrealized Gains	Gross Unrealized Losses	
	(in millions)			
U.S. Governments	\$ 7,795	\$ 1,555	\$ (4)	\$ 9,346
States, territories and possessions	463	61	(7)	517
Special revenue and assessments	13,084	454	(44)	13,494
All foreign governments	1,313	319	-	1,632

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company
Notes to Consolidated Statutory Financial Statements
December 31, 2008, 2007 and 2006

Public utilities	6,821	94	(603)	6,312
Banks, trust and insurance companies	10,336	108	(1,485)	8,959
Industrial and miscellaneous	39,502	458	(5,484)	34,476
Total	<u>\$ 79,314</u>	<u>\$ 3,049</u>	<u>\$ (7,627)</u>	<u>\$ 74,736</u>

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

December 31, 2007

	Reconciliation to Fair Value			Fair Value
	Statement Value	Gross Unrealized Gains	Gross Unrealized Losses	
	(in millions)			
U.S. Governments	\$ 6,081	\$ 653	\$ (3)	\$ 6,731
States, territories and possessions	244	39	(3)	280
Special revenue and assessments	13,408	146	(115)	13,439
All foreign governments	342	28	(2)	368
Public utilities	6,407	177	(94)	6,490
Banks, trust and insurance companies	11,146	260	(263)	11,143
Industrial and miscellaneous	39,214	834	(849)	39,199
Total	\$ 76,842	\$ 2,137	\$ (1,329)	\$ 77,650

The increases in gross unrealized gains during 2008 on U.S. Governments and Special revenue and assessments bonds comprised primarily of residential mortgage-backed securities issued by government agencies were primarily due to significant declines in yields on debt backed by the full faith and credit of the U.S. Government. The increase in gross unrealized losses on other bonds during 2008 was due primarily to a significant increase in market credit spreads for both investment-grade and below investment grade bonds between December 31, 2007 and December 31, 2008, as well as the impact of rating downgrades, as discussed below. Credit spreads represent the yield premium in excess of risk-free market interest rates that market participants require for the perceived risks or uncertainties associated with the future contractual performance of a bond issuer. The credit and liquidity crisis in the U.S. and global financial markets during 2008 significantly increased the perceived risks and uncertainties of bond investors, which reduced market liquidity and increased market credit spreads for most bond investments to historically high levels.

FINANCIAL STATEMENTS OF NORTHWESTERN MUTUAL

The Northwestern Mutual Life Insurance Company Notes to Consolidated Statutory Financial Statements December 31, 2008, 2007 and 2006

Based on statement value, 89% of the Company's bond portfolio was rated as investment-grade (i.e., rated "1" or "2" by the SVO) at each of December 31, 2008 and 2007. Statement value of bonds by NAIC rating category at December 31, 2008 and 2007 were as follows:

	NAIC Rating						Total
	1	2	3	4	5	6	
(in millions)							
U.S. Governments	\$ 7,795	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 7,795
States, territories and possessions	363	100	-	-	-	-	463
Special revenue and assessments	12,904	180	-	-	-	-	13,084
All foreign governments	1,224	89	-	-	-	-	1,313
Public utilities	2,512	3,682	390	222	15	-	6,821
Banks, trust and insurance companies	6,694	2,914	266	273	134	55	10,336
Industrial and miscellaneous	17,226	14,680	3,168	2,813	1,535	80	39,502
Total	<u>\$ 48,718</u>	<u>\$ 21,645</u>	<u>\$ 3,824</u>	<u>\$ 3,308</u>	<u>\$ 1,684</u>	<u>\$ 135</u>	<u>\$ 79,314</u>
(in millions)							
NAIC Rating							
	1	2	3	4	5	6	Total
U.S. Governments	\$ 6,081	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 6,081
States, territories and possessions	210	34	-	-	-	-	244
Special revenue and assessments	13,408	-	-	-	-	-	13,408
All foreign governments	281	61	-	-	-	-	342
Public utilities	2,304	3,379	284	385	55	-	6,407
Banks, trust and insurance companies	7,647	2,626	464	340	69	-	11,146
Industrial and miscellaneous	18,347	14,102	2,408	3,038	1,315	4	39,214
Total	<u>\$ 48,278</u>	<u>\$ 20,202</u>	<u>\$ 3,156</u>	<u>\$ 3,763</u>	<u>\$ 1,439</u>	<u>\$ 4</u>	<u>\$ 76,842</u>

During 2008, certain bonds were subject to downgrades by the NAIC. As of December 31, 2008, the Company held bonds classified as below investment grade which had been classified as investment grade with a statement value of \$788 million at December 31, 2007. These bonds experienced declines in fair value of \$349 million as a result of these rating downgrades, as well as the widening of general credit spreads.

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Statement value and fair value of bonds by contractual maturity at December 31, 2008 are presented below. Estimated maturities may differ from contractual maturities because certain borrowers have the right to call or prepay obligations with or without call or prepayment premiums.

	Statement Value	Fair Value
(in millions)		
Due in one year or less	\$ 1,570	\$ 1,550
Due after one year through five years	14,768	13,879
Due after five years through ten years	22,914	20,251
Due after ten years	17,380	17,732
	56,632	53,412
Mortgage-backed and structured securities	22,682	21,324
Total	\$ 79,314	\$ 74,736

The table below summarizes the composition of the Company's investments in mortgage-backed and structured securities at December 31, 2008. The investment grade designation is based on an NAIC rating of "1" or "2" as of December 31, 2008. These ratings are subject to change based upon subsequent evaluations of credit quality by the NAIC Securities Valuation Office or other rating agencies. On a statement value basis, over 98% of the Company's investments in these securities are rated as investment grade as of December 31, 2008, with a significant concentration within residential mortgage-backed securities issued by government agencies:

	Investment Grade		Below Investment Grade		Total	
	Statement Value	Fair Value	Statement Value	Fair Value	Statement Value	Fair Value
	(in millions)		(in millions)		(in millions)	
Residential mortgage backed:						
Government agencies	\$ 13,570	\$ 14,046	\$ -	\$ -	\$ 13,570	\$ 14,046
Other prime	1,806	1,650	-	-	1,806	1,650
Other non-prime	643	535	198	117	841	652
Commercial mortgage backed	2,753	1,760	62	7	2,815	1,767
Other asset backed	3,230	3,059	11	12	3,241	3,071
Collateralized debt obligations:						
CMBS CDO's	220	64	31	4	251	68
Consumer debt CDO's	46	38	-	-	46	38
Other CDO's	67	24	45	8	112	32
Total structured securities	\$ 22,335	\$ 21,176	\$ 347	\$ 148	\$ 22,682	\$ 21,324

On a statement value basis, 93% of the mortgage-backed and structured securities included in Investment Grade were rated "AAA" as of December 31, 2008. Mortgage-backed securities issued by government agencies experienced favorable movements in fair value relative to statement value due to declining yields on securities backed by the U.S. government during 2008. Wider credit spreads on securities not backed by the U.S. government resulted in market value declines for all other mortgage-backed and structured securities, with commercial mortgage-backed securities experiencing the most significant declines.

Rating information as of December 31, 2008 for commercial mortgage-backed securities, by year of origination, is provided in the following table:

Rating

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	Aaa	Aa	A	Baa	Ba and below	Total
(in millions)						
2007	\$ 381	\$ 253	\$ 10	\$ 57	\$ 14	\$ 715
2006	462	87	40	22	-	611
2005	330	36	35	96	33	530
2004	156	5	15	29	12	217
2003 & prior	397	177	74	91	3	742
Total	<u>\$ 1,726</u>	<u>\$ 558</u>	<u>\$ 174</u>	<u>\$ 295</u>	<u>\$ 62</u>	<u>\$ 2,815</u>

Common and Preferred Stocks

Common stocks are generally reported at fair value, which is based primarily on values published by the SVO and quoted market prices. When SVO-published values or quoted market prices are not used, fair value is estimated using independent pricing services or internally developed pricing models. The equity method is generally used to report investments in common stock of unconsolidated non-insurance subsidiaries. See Note 11 regarding statement value of the Company's investment in Frank Russell Company common stock. See Note 14 for more information regarding the fair value of the Company's investments in common stock.

Preferred stocks rated "1" (highest quality), "2" (high quality) or "3" (medium quality) by the SVO are reported at amortized cost. Preferred stocks rated "4" (low quality), "5" (lower quality) or "6" (lowest quality) by the SVO are reported at the lower of amortized cost or fair value. Fair value is based primarily upon values published by the SVO. In the absence of SVO-published values, fair value is based upon quoted market prices, if available. For preferred stocks without SVO-published values or quoted market prices, fair value is estimated using independent pricing services or internally developed pricing models. See Note 14 for more information regarding the fair value of the Company's investments in preferred stock.

When necessary, valuation adjustments are made for preferred stocks with SVO quality ratings of "4", "5" or "6" and for common and preferred stocks with a decline in fair value that management considers to be other-than-temporary. If the impairment is considered to be temporary, the valuation adjustment is reported as an unrealized capital loss. Valuation adjustments for declines in value considered to be other-than-temporary are reported as realized capital losses.

Mortgage Loans

Mortgage loans consist solely of commercial mortgage loans and are reported at unpaid principal balance, less any valuation allowance or unamortized commitment or origination fees. Such fees are generally deferred upon receipt and amortized into net investment income using the interest method.

The maximum and minimum interest rates for mortgage loans originated during 2008 were 7.0% and 4.8%, respectively, while these rates during 2007 were 8.3% and 5.3%, respectively. The aggregate ratio of amounts loaned to the fair value of collateral for mortgage loans originated during each of 2008 and 2007 was 63%, with a maximum of 100% for any single loan during each of 2008 and 2007. As of December 31, 2008 and 2007, the aggregate weighted-average loan-to-value ratio for the mortgage loan portfolio was 66% and 58%, respectively. The increase in the loan-to-value ratio is primarily the result of declining fair values for the underlying collateral, based on current appraisals performed by the Company.

The following table provides information on the distribution of mortgage loan maturities as of December 31, 2008:

	Statement Value
Due in one year or less	546
Due after one year through two years	1,797
Due after two years through five years	6,437
Due after five years through eight years	5,883
Due after eight years	<u>7,014</u>

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21,677

Real Estate

Real estate investments are reported at cost, less any valuation adjustment, encumbrances and accumulated depreciation of buildings and other improvements, using a straight-line method over the estimated useful lives of the improvements. Fair value of real estate is based primarily on the present value of estimated future cash flow (for commercial properties) or the capitalization of stabilized net operating income (for multi-family residential properties).

The table below summarizes the geographical diversification of the Company's investments in real estate by property type as of December 31, 2008:

	East	Midwest	South (in millions)	West	Total
Apartment	\$ 277	\$ 40	\$ 27	\$ 294	\$ 638
Office	72	402	136	26	636
Industrial	12	-	54	172	238
Land	-	-	16	-	16
Total	\$ 361	\$ 442	\$ 233	\$ 492	\$ 1,528

The Company occupies property included in Midwest Office investments above, which have aggregate statement values of \$245 million at December 31, 2008.

Leveraged Leases

Leveraged leases primarily represent investments in commercial aircraft or real estate properties that are leased to third parties and serve as collateral for non-recourse borrowings. Leveraged leases are reported at the present value of future minimum lease payments plus the estimated residual value of the leased asset and included in other investments in the consolidated statement of financial position. At December 31, 2008 and 2007, the statement value of leveraged leases was \$331 million and \$335 million, respectively.

Impairments

On a quarterly basis, the Company performs a review of bonds, common and preferred stocks, mortgage loans, real estate and other investments to identify those that have experienced a decline in fair value that management considers to be other-than-temporary. Factors considered in evaluating whether a decline in fair value is other-than-temporary include: (1) the duration and extent to which fair value has been less than cost, (2) the financial condition and near-term financial prospects of the issuer and (3) the Company's ability and intent to retain the investment for a period of time sufficient to allow for an anticipated recovery in value.

For fixed maturity securities, emphasis is placed on evaluating the issuer's ability to service all contractual interest and principal payments and the Company's ability and intent to hold the security until the earlier of a recovery in value or until maturity. The Company's intent and ability to hold a security considers broad portfolio management objectives such as asset/liability duration management, issuer and industry segment exposures, interest rate views and the overall total return of the portfolio.

For equity securities, greater weight and consideration is given to the duration and extent of a decline in market value and the likelihood such market value decline will recover. An investment in real estate is considered to be impaired when the fair value of the property is lower than depreciated cost. Securities, real estate and other investments that are determined to have an other-than-temporary impairment are written down to fair value.

Mortgage loans determined to have an other-than-temporary impairment are written down to net realizable value based on appraisal of the collateral property. Realized capital losses recognized due to declines in fair value of investments that were considered to be other-than-temporary for the years ended December 31, 2008, 2007 and 2006 were \$960 million, \$156 million and \$74 million, respectively.

The following table provides additional detail for the valuation adjustments for the years ended December 31, 2008, 2007 and

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2006:

	For the year ended December 31,		
	2008	2007	2006
	(in millions)		
Bonds, preferred and common stocks:			
Financial industry	\$ (366)	\$ (26)	\$ (9)
Structured securities	(157)	(1)	(1)
Energy sector	(98)	(31)	-
Consumer discretionary	(82)	(3)	(12)
Health care	(41)	(14)	(6)
Industrials	(30)	(6)	(6)
Technology	(25)	(1)	(3)
Other	(53)	(2)	(1)
Subtotal	(852)	(84)	(38)
Other investments:			
Real estate and RE Funds	(88)	(46)	-
Energy holdings	(10)	-	-
Security partnerships	(10)	(26)	(36)
Subtotal	(108)	(72)	(36)
Total	\$ (960)	\$ (156)	\$ (74)

The \$852 million in security write downs during 2008 was comprised of \$445 million of bonds, \$231 million of common stocks, and \$176 million of preferred stocks. The \$157 million of structured securities write downs during 2008 was comprised of \$63 million of consumer debt and other CDOs and \$94 million of CMBS, including CMBS CDOs.

In addition to the realized losses discussed above, \$77 million, \$53 million and \$6 million of other-than-temporary impairments were recognized in the Company's unconsolidated non-insurance subsidiaries for the years ended December 31, 2008, 2007 and 2006, respectively. The decline in equity of these subsidiaries resulting from these valuation adjustments is included in changes in net unrealized capital gains (losses) in the consolidated statement of changes in surplus.

Investment Capital Gains and Losses

Realized capital gains and losses for the years ended December 31, 2008, 2007 and 2006 were as follows:

	For the year ended December 31, 2008			For the year ended December 31, 2007			For the year ended December 31, 2006		
	Realized Gains	Realized Losses	Net Realized Gains (Losses)	Realized Gains	Realized Losses	Net Realized Gains (Losses)	Realized Gains	Realized Losses	Net Realized Gains (Losses)
	(in millions)			(in millions)			(in millions)		
Bonds	\$ 518	\$(1,757)	\$(1,239)	\$ 465	\$ (327)	\$ 138	\$ 243	\$ (497)	\$ (254)
Common and preferred stocks	773	(1,342)	(569)	1,415	(246)	1,169	1,193	(241)	952
Mortgage loans	-	(2)	(2)	-	(10)	(10)	1	-	1
Real estate	82	(4)	78	65	-	65	18	-	18
Other investments	1,416	(1,205)	211	306	(568)	(262)	207	(357)	(150)
	\$ 2,789	\$(4,310)	(1,521)	\$ 2,251	\$(1,151)	1,100	\$ 1,662	\$(1,095)	567
Less: IMR gains (losses)			(705)			144			(261)
Less: Capital gains taxes (benefit)			(149)			337			418
Net realized capital gains (losses)			\$ (667)			\$ 619			\$ 410

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Realized losses include the impact of the other-than-temporary impairments discussed previously. The realized gain and loss activity within Other Investments is primarily due to derivative transactions. See Note 4. The remaining realized gain and loss activity is the result of normal trading activity undertaken to execute the Company's overall portfolio strategy including asset/liability duration management, sector exposure, total return and tax optimization. During 2008, \$439 million of realized losses were attributable to the sale of bonds with significant declines in credit quality. Proceeds from the sale of bond investments totaled \$34 billion, \$56 billion and \$44 billion for the years ended December 31, 2008, 2007 and 2006, respectively.

Changes in net unrealized capital gains and losses for the years ended December 31, 2008, 2007 and 2006 were as follows:

	For the year ended December 31,		
	2008	2007	2006
	(in millions)		
Bonds	\$ (356)	\$ 98	\$ 58
Common and preferred stocks	(3,604)	(367)	466
Other investments	(831)	178	264
	(4,791)	(91)	788
Change in deferred taxes	1,308	79	(207)
Change in net unrealized capital gains (losses)	\$ (3,483)	\$ (12)	\$ 581

The increase in net unrealized capital losses during 2008 was due primarily to declines in the fair value of common stocks and other investments that management considers to be temporary. Net unrealized capital losses included unrealized losses of (\$460) million, (\$386) million and (\$312) million for the years ended December 31, 2008, 2007 and 2006, respectively, related to distributions to the Company from unconsolidated non-insurance subsidiaries. The Company's share of the earnings or losses of these subsidiaries are reported as unrealized under the equity method of accounting until distributed to the Company, at which time net investment income is recognized and the previously unrealized gain is reversed.

Changes in net unrealized capital gains (losses) also included valuation adjustments for declines in fair value of investments held by unconsolidated non-insurance subsidiaries that were considered to be other-than-temporary.

The amortized cost and fair value of bonds and common and preferred stocks for which fair value had temporarily declined and remained below cost as of December 31, 2008 and 2007 were as follows:

	December 31, 2008					
	Decline For Less Than 12 Months			Decline For Greater Than 12 Months		
	Amortized Cost	Fair Value	Difference	Amortized Cost	Fair Value	Difference
	(in millions)					
Bonds	\$ 29,909	\$ 26,205	\$ (3,704)	\$ 16,589	\$ 12,454	\$ (4,135)
Common and preferred stocks	3,326	2,391	(935)	1,048	610	(438)
Total	\$ 33,235	\$ 28,596	\$ (4,639)	\$ 17,637	\$ 13,064	\$ (4,573)

	December 31, 2007					
	Decline For Less Than 12 Months			Decline For Greater Than 12 Months		
	Amortized Cost	Fair Value	Difference	Amortized Cost	Fair Value	Difference

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	(in millions)					
Bonds	\$ 13,098	\$ 12,466	\$ (632)	\$ 17,873	\$ 17,200	\$ (673)
Common and preferred stocks	1,895	1,609	(286)	160	127	(33)
Total	<u>\$ 14,993</u>	<u>\$ 14,075</u>	<u>\$ (918)</u>	<u>\$ 18,033</u>	<u>\$ 17,327</u>	<u>\$ (706)</u>

At December 31, 2008, the amount of bonds for which fair value had temporarily declined increased due primarily to a significant increase in market credit spreads from December 31, 2007. These bonds are current on interest and principal payments and are otherwise performing according to their contractual terms. Based on the review process described previously, management considers these declines in fair value, as well as declines in fair value of common and preferred stocks, to be temporary based on existing facts and circumstances. Changes in the fair value of common stocks are reflected in surplus through unrealized gains/losses as a result of being reported at fair value in the financial statements.

Sub-prime and other Below-prime Mortgage Risk

Sub-prime mortgages are residential loans to borrowers with weak credit profiles. Alt-A mortgages are residential loans to borrowers who have credit profiles above sub-prime but do not conform to traditional (“prime”) mortgage underwriting guidelines. The Company has invested in certain mortgage-backed and structured securities that include exposure to below-prime mortgage loans. These investments are included in bonds in the consolidated statement of financial position and reported at amortized cost, less any valuation adjustments. At December 31, 2008 and 2007, the statement value of sub-prime investments was \$8 million and \$22 million, respectively, and the statement value of Alt-A investments was \$826 million and \$783 million, respectively. At December 31, 2008 and 2007, the fair value of sub-prime investments was \$2 million and \$21 million, respectively, and the fair value of Alt-A investments was \$648 million and \$771 million, respectively. As of December 31, 2008, the Alt-A investments were comprised primarily of a portfolio of non-prime Alt-A floaters issued in 2006 and 2007 in the statement amount of \$303 million, substantially all first pay securities, and a portfolio of non-prime fixed rate pass-through and CMO securities of earlier vintages in the statement amount of \$496 million. The non-prime Alt-A floater and non-prime fixed-rate pass-through portfolios included \$106 million and \$333 million of AAA rated securities, respectively, at December 31, 2008.

A summary of the Company’s Alt-A investments at December 31, 2008 by year of origination is reflected in the table below:

	Investment Grade		Below Investment Grade		Total	
	Statement Value	Fair Value	Statement Value	Fair Value	Statement Value	Fair Value
	(in millions)		(in millions)		(in millions)	
2007	\$ 155	\$ 125	\$ 117	\$ 76	\$ 272	\$ 201
2006	148	130	72	36	220	166
2005	65	59	-	-	65	59
2004	137	117	-	-	137	117
2003	65	53	-	-	65	53
2002 and prior	60	47	7	5	67	52
Total	<u>\$ 630</u>	<u>\$ 531</u>	<u>\$ 196</u>	<u>\$ 117</u>	<u>\$ 826</u>	<u>\$ 648</u>

Securities Lending

The Company has entered into securities lending agreements whereby certain general account investment securities are loaned to third parties, primarily major brokerage firms. At December 31, 2008 and 2007, the aggregate statement value of loaned securities was \$2.5 billion and \$3.2 billion, respectively, while the aggregate fair value of these loaned securities was \$3.0 billion and \$3.4 billion, respectively. The Company’s policy requires a minimum of 102% of the fair value of the loaned securities, calculated on a daily basis, as collateral in the form of either cash or securities to be held by the Company or a trustee.

At December 31, 2008 and 2007, securities lending collateral held by the Company of \$2.9 billion and \$3.0 billion, respectively, is reported in the consolidated statement of financial position at amortized cost and included in cash and temporary investments, with the offsetting collateral liability of \$2.9 billion and \$3.0 billion included in other liabilities.

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These collateral assets included \$2.8 billion and \$2.7 billion, respectively, of collateral positions with open terms (i.e., positions for which the borrower may return the loaned security and request return of the collateral at any time), \$10 million and \$0, respectively, for collateral positions with terms of less than 30 days, and \$90 million and \$320 million, respectively, for collateral positions with terms exceeding 90 days. Additionally, at December 31, 2008 and 2007, the total fair value of all collateral positions was \$2.9 billion and \$3.0 billion, respectively.

At December 31, 2008 and 2007, additional non-cash collateral of \$219 million and \$593 million, respectively, with fair values of \$208 million and \$590 million, respectively, was held on the Company's behalf by a trustee and is not included in the consolidated statement of financial position.

The Company has also entered into securities lending arrangements for separate account investment securities, utilizing similar procedures and collateral requirements as those for general account loaned securities. At December 31, 2008 and 2007, the aggregate statement value of loaned securities held by the separate accounts was \$67 million and \$113 million, respectively.

4. Derivative Financial Instruments

In the normal course of business, the Company enters into derivative transactions, generally to mitigate (or "hedge") the risk to its assets, liabilities and surplus from fluctuations in interest rates, foreign currency exchange rates and other market risks. Derivatives used in hedging transactions are designated as either "cash flow" hedges, which mitigate the risk of variability in future cash flows associated with the asset or liability being hedged, or "fair value" hedges, which mitigate the risk of changes in fair value of the asset or liability being hedged. Derivatives that qualify for hedge accounting are reported on a basis consistent with the asset or liability being hedged (e.g., at amortized cost or fair value). Derivatives used as hedges that do not qualify for hedge accounting are reported at fair value.

The Company also uses derivatives for the purpose of investment "replication." A replication is a derivative transaction that, when entered into in conjunction with other cash market investments, replicates the risk and reward characteristics of otherwise permissible investment positions. Derivatives used as part of a replication are reported on a basis consistent with the investment position being replicated (e.g., at amortized cost or fair value).

During 2008, the Company also used derivatives for income generation purposes. Derivatives used for income generation purposes are reported on a basis consistent with the accounting treatment that would be used for the covering asset or underlying interest to which the derivative relates (e.g., at amortized cost or fair value). The cash premium received by the Company at the inception of the contract is deferred for accounting purposes until maturity of the contract or its exercise by the counterparty (if the term of the derivative is less than one year) or amortized over the life of the contract (if the term of the derivative is greater than one year).

Derivative transactions expose the Company to the risk that a counterparty may not be able to fulfill its obligations under the contract. The Company manages this risk by dealing only with counterparties that maintain a minimum credit rating, performing ongoing surveillance of counterparties' credit standing and adhering to established limits for credit exposure to any single counterparty. The Company also utilizes collateral support agreements that require the daily exchange of collateral assets if credit exposure exceeds certain limits.

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The Company held the following derivative positions at December 31, 2008 and 2007:

Derivative Instrument	December 31, 2008			December 31, 2007		
	Notional Amount	Statement Value	Fair Value	Notional Amount	Statement Value	Fair Value
	(in millions)					
<u>Cash Flow Hedges:</u>						
Interest rate floors	\$ 1,175	\$ 17	\$ 130	\$ 1,250	\$ 19	\$ 38
Swaptions	1,742	53	21	1,458	45	39
Foreign currency swaps	863	9	101	787	-	(76)
Foreign currency covers	2	-	2	19	-	19
Interest rate swaps	52	-	17	102	-	12
Interest rate basis swaps	-	-	-	40	-	-
Commodity swaps	-	-	-	4	(1)	(1)
<u>Fair Value Hedges:</u>						
Purchased credit default swaps	306	15	15	420	2	2
Foreign currency forwards	376	(8)	(8)	2,474	5	5
Foreign currency futures	1,299	-	-	-	-	-
Short fixed income futures	3,407	-	-	2,356	-	-
Short equity index futures	552	-	-	-	-	-
Purchased put options	-	-	-	-	-	-
Equity collars	11	1	1	11	-	-
Short total return swaps	265	(9)	(9)	283	(6)	(6)
<u>Replications:</u>						
Fixed income	10	-	-	489	-	17
Long fixed income futures	3,867	-	-	1,783	-	-
Long equity index futures	-	-	-	204	-	-
Long total return swaps	322	2	2	-	-	-
<u>Income Generation Transactions:</u>						
Written equity call options	-	-	-	-	-	-

The notional amounts shown above are used to denominate the derivative contracts and do not represent amounts exchanged between the Company and the derivative counterparties. The statement value of derivatives is included in other investments in the consolidated statement of financial position.

Fair value is the amount that the Company would expect to receive or pay in an arms-length settlement of the derivative contract as of the reporting date. The fair value of derivative instruments is based on quoted market prices, when available. In the absence of quoted market prices, fair value is estimated using third-party or internal pricing models. For derivatives reported at fair value, changes in fair value on open derivative positions are reported as an unrealized capital gain or loss. Upon maturity or termination of the derivative contract, a realized capital gain or loss is recognized.

Following are descriptions of the types of derivative instruments used by the Company:

Cash Flow Hedges:

Interest rate floors are used to mitigate the asset/liability management risk of a significant and sustained decrease in interest rates for certain of the Company's insurance products. Interest rate floors entitle the Company to receive payments from a counterparty if market interest rates decline below a specified level. The Company's use of interest rate floors qualifies for hedge accounting, with these instruments reported at amortized cost.

Swaptions are used to mitigate the asset/liability management risk of a significant and sustained increase in interest rates for

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certain of the Company's insurance products. Swaptions provide the Company an option to enter into an interest rate swap with a counterparty on predefined terms. The Company's use of swaptions qualifies for hedge accounting, with these instruments reported at amortized cost.

Foreign currency swaps are used to mitigate the foreign exchange risk for investments in bonds denominated in foreign currencies. Foreign currency swaps obligate the Company and a counterparty to exchange the currencies of two different countries at a specified exchange rate. The Company's use of foreign currency swaps qualifies for hedge accounting. These instruments are reported at amortized cost, with the exception of changes in fair value due to fluctuations in market currency exchange rates. Foreign currency translation gain or loss is reported as an unrealized capital gain or loss until the maturity or termination of the contract, at which time a realized capital gain or loss is recognized.

Foreign currency covers are used to mitigate foreign exchange risk pending settlement of executed trades for investments denominated in foreign currencies. Foreign currency covers obligate the Company to pay to or receive from a counterparty a specified amount of a foreign currency at a specified exchange rate at a future date. The Company's use of foreign currency covers qualifies for hedge accounting, with foreign currency translation gain or loss recorded as an adjustment to the cost basis of the hedged security.

Interest rate swaps are used to mitigate interest rate risk for investments in variable interest rate and fixed interest rate bonds. Interest rate swaps obligate the Company and a counterparty to exchange amounts based on the difference between a variable interest rate index and a specified fixed rate of interest applied to the notional amount of the contract. The Company's use of interest rate swaps qualifies for hedge accounting, with these instruments reported at amortized cost.

Interest rate basis swaps are used to mitigate the basis risk for investments in variable interest rate preferred stocks. Interest rate basis swaps obligate the Company and a counterparty to exchange amounts based on the difference between the rates of return on two different reference indices applied to the notional amount of the contract. The Company's use of interest rate basis swaps does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital gains and losses on these contracts were less than \$1 million during each of 2008 and 2007.

Commodity swaps are used to mitigate market risk for the anticipated sale of future oil or natural gas production. Commodity swaps obligate the Company and a counterparty to exchange amounts based on the difference between a variable energy commodity price and a specified fixed energy commodity price applied to the notional amount of the contract. The Company's use of commodity swaps does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital gains of \$1 million and unrealized capital losses of \$1 million were recognized during 2008 and 2007, respectively, on these contracts.

Fair Value Hedges:

Purchased credit default swaps are used to mitigate the credit risk for investments in bonds issued by specific debtors. Credit default swaps provide the Company an option to put a specific bond to a counterparty at par in the event of a "credit event" encountered by the bond issuer. A credit event is generally defined as a bankruptcy, failure to make required payments or acceleration of issuer obligations under the terms of the bond. In some cases the Company's use of credit default swaps qualifies for hedge accounting, while in other cases it does not. Credit default swaps that qualify for hedge accounting are reported at amortized cost. Swaps that do not qualify for hedge accounting are reported at fair value. Unrealized capital gains of \$14 million and \$3 million were recognized during 2008 and 2007, respectively, on contracts that did not qualify for hedge accounting.

Foreign currency forwards are used to mitigate the foreign exchange risk for investments in bonds denominated in foreign currencies or common stock or other equity investments in companies operating in foreign countries. Foreign currency forwards obligate the Company to pay to or receive from a counterparty a specified amount of a foreign currency at a future date. The Company's use of foreign currency forwards does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital losses of \$13 million and unrealized capital gains of \$23 million were recognized during 2008 and 2007, respectively, on these contracts.

Foreign currency futures are used to mitigate the foreign exchange risk for investments in bonds denominated in foreign currencies or common stock or other equity investments in companies operating in foreign countries. Foreign currency futures obligate the Company to exchange a specified amount of a foreign currency with a counterparty at a specified

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exchange rate at a future date. The Company's use of foreign currency futures does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital losses of \$73 million were recognized during 2008 on these contracts. The Company did not use these instruments prior to 2008.

Short fixed income futures are used to mitigate interest rate risk for investment in portfolios of fixed income securities. Short fixed income futures obligate the Company to sell to a counterparty a specified bond at a specified price at a future date. The Company's use of short fixed income futures contracts does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital losses of \$239 million and \$17 million were recognized during 2008 and 2007, respectively, on these contracts.

Short equity index futures are used to mitigate market risk for investments in portfolios of common stock. Short equity index futures obligate the Company to pay to or receive from a counterparty an amount based on a specified equity market index as of a future date applied to the notional amount of the contract. The Company's use of short equity index futures does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital losses of \$17 million and unrealized capital gains of \$2 million were recognized during 2008 and 2007, respectively, on these contracts.

Purchased put options are used to mitigate credit and market risk for investments in debt and equity securities issued by specific entities. Purchased put options provide the Company an option to put a specific security to a counterparty at a specified price at a future date. The Company's use of purchased put options does not qualify for hedge accounting, with these instruments reported at fair value. No unrealized capital gains or losses were recognized during 2008 or 2007 on these contracts.

Equity collars are used to mitigate market risk for investments in specific common stocks or other equity securities. Equity collars consist of both a purchased put option and a written call option on a specific equity security owned by the Company. The Company's use of equity collars does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital gains of \$1 million and unrealized capital losses of \$1 million were recognized during 2008 and 2007, respectively, on these contracts.

Short total return swaps are used to mitigate market risk for investment in portfolios of common stocks and other equity securities. Total return swaps obligate the Company and a counterparty to exchange amounts based on the difference between a variable equity index return and a specified fixed rate of return applied to the notional amount of the contract. The Company's use of total return swaps does not qualify for hedge accounting, with these instruments reported at fair value. Unrealized capital losses of \$9 million and \$6 million were recognized during 2008 and 2007, respectively, on these contracts.

Replications:

Fixed income replications are used to replicate a bond investment through the use of written credit default swaps, interest rate swaps, credit default indices and cash market instruments. Single-name credit default swap ("CDS") contracts replicate credit exposure to a specific entity and debt issue with terms to maturity of five to ten years. Upon the occurrence of a defined credit event, the Company would be required to purchase a notional amount of the referenced obligation from the counterparty at par value. The Company is not aware of any credit events on outstanding CDS contracts at December 31, 2008. The maximum amounts that the Company could potentially be required to pay on CDS contracts as of December 31, 2008 and 2007 was \$10 million and \$49 million, respectively. The fair value of CDS contracts outstanding as of December 31, 2008 and 2007 was less than \$1 million and \$1 million, respectively. Index credit default swap ("CDX") contracts replicate general corporate credit exposure in either investment-grade or high-yield markets with terms to maturity of five to ten years. Upon the occurrence of a defined credit event, the Company would be required to pay to the counterparty an amount equal to the affected entity's proportion to the overall index applied to the notional amount of the contract. The Company did not have any open positions in CDX contracts as of December 31, 2008 and 2007. Fixed income replications, including the derivative components, are reported at amortized cost. The average fair value of open contracts was \$2 million and \$3 million during 2008 and 2007, respectively. Realized capital losses of \$39 million and \$1 million were recognized during 2008 and 2007, respectively, upon termination of these contracts.

Long fixed income futures replications are used in conjunction with cash market instruments to manage the duration of investment in portfolios of fixed income securities and to mitigate interest rate risk for such portfolios. Long fixed income futures replications are reported at fair value, with changes in fair value reported as an unrealized capital gain or loss until the

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contracts mature or are terminated, at which time a realized capital gain or loss is recognized. The average fair value of open contracts was \$3.5 billion and \$1.4 billion during 2008 and 2007, respectively. Realized capital gains of \$274 million and \$56 million were recognized during 2008 and 2007, respectively, upon termination of these contracts.

Long equity index futures replications are used in conjunction with the purchase of cash market instruments to replicate investment in portfolios of common stocks and other equity securities. Long equity index futures replications are reported at fair value, with changes in fair value reported as an unrealized capital gain or loss until the contracts mature or are terminated, at which time a realized capital gain or loss is recognized. The average fair value of open contracts was \$248 million and \$225 million during 2008 and 2007, respectively. Realized capital losses of \$87 million and realized capital gains of \$4 million were recognized during 2008 and 2007, respectively, upon termination of these contracts.

Long total return swap replications are used in conjunction with the purchase of cash market instruments to replicate investment in portfolios of common stocks and other equity securities. Total return swaps obligate the Company and a counterparty to exchange amounts based on the difference between a variable equity index return and a specified fixed rate of return applied to the notional amount of the contract. The Company's use of total return swaps does not qualify for hedge accounting, with these instruments reported at fair value. The average fair value of open contracts was (\$10) million during 2008. Realized capital losses of \$143 million were recognized during 2008 on these contracts. The Company did not use these instruments prior to 2008.

Income Generation Transactions:

Written equity call options (covered) are used to generate income in exchange for potential future gains on a specific common stock owned by the Company. The Company receives a cash premium at the inception of the contract, and the counterparty has the right (but not the obligation) to purchase the underlying security from the Company at a predetermined price at any time during the term of the contract. Written equity call options are reported at fair value, with changes in fair value reported as an unrealized capital gain or loss until the contracts mature or are exercised by the counterparty, at which time a realized capital gain or loss is recognized. The average fair value of open contracts was (\$1) million during 2008. Realized capital gains of \$2 million were recognized during 2008 upon termination of these contracts. The Company did not use these instruments prior to 2008.

5. Reserves for Policy Benefits

General account reserves for policy benefits at December 31, 2008 and 2007 are summarized below:

	December 31,	
	2008	2007
	(in millions)	
Life insurance reserves	\$ 105,453	\$ 98,166
Annuity reserves and deposit liabilities	6,432	5,616
Disability and long-term care unpaid claims and claim reserves	3,744	3,612
Disability and long-term care active life reserves	2,325	2,179
Total reserves for policy benefits	\$ 117,954	\$ 109,573

Life insurance reserves on substantially all policies issued since 1978 are based on the Commissioner's Reserve Valuation Method ("CRVM") using the 1958, 1980 or 2001 CSO mortality tables with valuation interest rates ranging from 3.5% to 5.5%. Other life insurance reserves are based primarily on the net level premium method, using various mortality tables at interest rates ranging from 2.0% to 4.5%. As of December 31, 2008, the Company had \$1.1 trillion of total life insurance in-force, including \$25 billion of life insurance in-force for which gross premiums were less than net premiums according to the standard valuation methods and assumptions prescribed by the OCI.

Tabular cost has been determined from the basic data for the calculation of policy reserves. Tabular cost less actual reserves released has been determined from the basic data for the calculation of reserves and reserves released. Tabular interest has been determined from the basic data for the calculation of policy reserves. Tabular interest on funds not involving life

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contingencies is calculated as the product of the valuation interest rate times the mean of the amount of funds subject to such rate held at the beginning and end of the year of valuation.

Additional premiums are charged for substandard lives on policies issued after January 1, 1956. Net level premium or CRVM mean reserves are based on multiples of mortality tables or one-half the net flat or other extra mortality charge. The Company waives deduction of fractional premiums upon death of an insured and returns any portion of the final premium beyond the date of death. Cash values are not promised in excess of the legally computed reserves.

Deferred annuity reserves on policies issued since 1985 are based primarily on the Commissioner's Annuity Reserve Valuation Method with valuation interest rates ranging from 3.5% to 6.25%. Other deferred annuity reserves are based on policy value. Immediate annuity reserves are based on the present value of expected benefit payments with valuation interest rates ranging from 3.5% to 7.5%. Changes in future policy benefit reserves on supplementary contracts without life contingencies are deposit-type transactions and thereby excluded from net additions to policy benefit reserves in the consolidated statement of operations.

At December 31, 2008 and 2007, the withdrawal characteristics of the Company's general account annuity reserves and deposit liabilities were as follows:

	December 31,	
	2008	2007
	(in millions)	
Subject to discretionary withdrawal		
- with market value adjustment	\$ 801	\$ 638
- at book value less surrender charge of 5% or more	208	125
- at book value without adjustment	3,583	3,247
Not subject to discretionary withdrawal	1,840	1,606
Total	\$ 6,432	\$ 5,616

Unpaid claims and claim reserves for disability policies are based on the present value of expected benefit payments, primarily using the 1985 Commissioner's Individual Disability Table A ("CIDA"), modified for Company experience, with valuation interest rates ranging from 3.0% to 5.5%. Unpaid claims and claim reserves for long-term care policies are based on the present value of expected benefit payments using industry-based long-term care experience with valuation interest rates ranging from 4.0% to 4.5%.

Reserves for unpaid claims, losses and loss adjustment expenses on disability and long-term care policies were \$3.7 billion and \$3.6 billion at December 31, 2008 and 2007, respectively. The table below provides a summary of the changes in these reserves for the years ended December 31, 2008 and 2007.

	For the year ended	
	December 31,	
	2008	2007
	(in millions)	
Balance at January 1	\$ 3,612	\$ 3,555
Incurred related to:		
Current year	472	462
Prior years	112	31
Total incurred	584	493
Paid related to:		
Current year	(18)	(17)
Prior years	(434)	(419)

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Total paid	(452)	(436)
Balance at December 31	\$ 3,744	\$ 3,612

Changes in reserves for incurred claims related to prior years are generally the result of differences between actual and assumed claim experience.

Active life reserves for disability policies issued since 1987 are based primarily on the two-year preliminary term method using the 1985 CIDA for morbidity with a 4.0% valuation interest rate. Active life reserves for prior disability policies are based on the net level premium method, using the 1964 Commissioner's Disability Table for morbidity with valuation interest rates ranging from 3.0% to 4.0%.

Active life reserves for long-term care policies consist of mid-terminal reserves and unearned premiums. Mid-terminal reserves are based on the one-year preliminary term method and industry-based morbidity experience. For policies issued prior to March, 2002, reserves are based on a 4.0% valuation interest rate and total terminations based on the 1983 Individual Annuitant Mortality table without lapses. For policies issued March, 2002 and later, minimum reserves are based on valuation interest rates of 4.0% or 4.5% and total terminations based on either the 1983 Group Annuity Mortality table or the 1994 Group Annuity Mortality table with lapses. A separate calculation is performed using valuation interest rates ranging from 5.2% to 6.0% and assuming no lapses. Reserves from the separate calculation are compared in the aggregate to the minimum reserves as estimated above and the greater of the two is reported.

6. Premium and Annuity Considerations Deferred and Uncollected

Gross deferred and uncollected insurance premiums represent life insurance premiums due to be received from policyowners through the next respective policy anniversary dates. Net deferred and uncollected premiums represent only the portion of gross premiums related to mortality charges and interest and are reported as an asset in the consolidated statement of financial position.

Deferred and uncollected premiums at December 31, 2008 and 2007 were as follows:

	December 31, 2008		December 31, 2007	
	Gross	Net	Gross	Net
	(in millions)			
Ordinary new business	\$ 171	\$ 72	\$ 169	\$ 80
Ordinary renewal	1,836	1,547	1,782	1,471
Total deferred and uncollected premiums	\$ 2,007	\$ 1,619	\$ 1,951	\$ 1,551

7. Separate Accounts

Following is a summary of separate account liabilities by withdrawal characteristic at December 31, 2008 and 2007:

	December 31,	
	2008	2007
	(in millions)	
Subject to discretionary withdrawal	\$ 11,047	\$ 16,526
Not subject to discretionary withdrawal	2,160	2,977
Non-policy liabilities	180	201
Total separate account liabilities	\$ 13,387	\$ 19,704

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While separate account liability values are not guaranteed by the Company, variable annuity and variable life insurance products do include guaranteed minimum death benefits (“GMDB”) underwritten by the Company. General account reserves for policy benefits included \$29 million and \$6 million attributable to GMDB at December 31, 2008 and 2007, respectively.

Premiums and other considerations received from variable life and variable annuity policyowners were \$1.4 billion and \$1.7 billion during the years ended December 31, 2008 and 2007, respectively. These amounts are reported as premiums in the consolidated statement of operations. The subsequent transfer of these receipts to the separate accounts is reported as transfers to separate accounts in the consolidated statement of operations, net of amounts received from the separate accounts to provide for policy benefit payments to variable product policyowners.

Following are amounts reported as transfers to and from separate accounts in the summary of operations of the Company’s NAIC Separate Account Annual Statement, which agree with the amounts reported as net transfers to separate accounts in the consolidated statement of operations for the years ended December 31, 2008, 2007 and 2006:

	For the year ended December 31,		
	2008	2007	2006
	(in millions)		
From Separate Account Annual Statement:			
Transfers to separate accounts	\$ 1,619	\$ 1,866	\$ 1,719
Transfers from separate accounts	(1,721)	(1,382)	(1,227)
Net transfers to separate accounts	<u>\$ (102)</u>	<u>\$ 484</u>	<u>\$ 492</u>

8. Employee and Representative Benefit Plans

The Company sponsors noncontributory defined benefit retirement plans (“plans”) for all eligible employees and financial representatives. These include tax-qualified plans, as well as nonqualified plans that provide benefits to certain participants in excess of limits set by the Employee Retirement Income Security Act (“ERISA”) for qualified plans. The Company’s funding policy for the tax qualified plans is to make annual contributions that are no less than the minimum amount needed to comply with the requirements of ERISA and no greater than the maximum amount deductible for federal income tax purposes. The Company contributed \$35 million and \$41 million to the qualified employee retirement plan during the years ended December 31, 2008 and 2007, respectively, and expects to contribute \$70 million in 2009.

In addition to defined pension benefits, the Company provides certain health care and life insurance benefits (“postretirement benefits”) to retired employees, financial representatives and eligible dependents. Substantially all employees and financial representatives will become eligible for these benefits if they reach retirement age while working for the Company.

Aggregate assets and projected benefit obligations of the defined benefit plans and postretirement benefit plans at December 31, 2008 and 2007, and changes in assets and obligations for the years then ended, were as follows:

	Defined Benefit Plans		Postretirement Benefit Plans	
	2008	2007	2008	2007
	(in millions)			
Fair value of plan assets at January 1	\$ 2,741	\$ 2,533	\$ 89	\$ 85
Changes in plan assets:				
Actual return on plan assets	(728)	216	(24)	7
Company contributions	35	41	-	-
Actual plan benefits paid	(56)	(49)	(3)	(3)
Fair value of plan assets at December 31	<u>\$ 1,992</u>	<u>\$ 2,741</u>	<u>\$ 62</u>	<u>\$ 89</u>
Projected benefit obligation at January 1	\$ 2,455	\$ 2,310	\$ 244	\$ 211
Changes in benefit obligation:				
Service cost of benefits earned	90	86	29	27

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Interest cost on projected obligations	147	136	14	12
Projected gross plan benefits paid	(65)	(57)	(14)	(13)
Projected Medicare Part D reimbursement	-	-	2	2
Experience losses (gains)	(259)	(20)	(6)	5
Projected benefit obligation at December 31	\$ 2,368	\$ 2,455	\$ 269	\$ 244

Plan assets consist of a share of a group annuity separate account (“GASA”) issued by the Company, which invests primarily in public common stocks and a diversified mix of corporate, government and mortgage-backed debt securities. The investment objective of the plans is to maximize long-term total rate of return, consistent with prudent investment risk management and in accordance with ERISA requirements. Plan investments are managed for the sole benefit of the plans’ participants.

While significant exposure to public and private equity securities is warranted by the long-term duration of expected benefit payments, diversification across asset classes is maintained to provide a risk/reward profile consistent with the objectives of the plans’ participants. Diversified equity investments are subject to an aggregate maximum exposure of 75% of total assets, with holdings in any one corporate issuer not to exceed 3% of total assets. Asset mix is rebalanced regularly to maintain holdings within target asset allocation ranges. The measurement date for plan assets is December 31, with the fair value of plan assets based primarily on quoted market values.

The table below presents the fair value of the plans’ ratable share of the GASA by asset class at December 31, 2008 and 2007:

	Defined Benefit Plans				Postretirement Benefit Plans			
	2008	% of Total	2007	% of Total	2008	% of Total	2007	% of Total
	(in millions)							
Bonds	\$ 1,004	50%	\$ 1,142	42%	\$ 31	50%	\$ 37	42%
Preferred stock	4	0%	9	0%	-	0%	-	0%
Public common stock	825	42%	1,477	54%	26	42%	48	54%
Private equities and other	159	8%	113	4%	5	8%	4	4%
Total assets	\$ 1,992	100%	\$ 2,741	100%	\$ 62	100%	\$ 89	100%

The projected benefit obligation (“PBO”) represents the actuarial net present value of estimated future benefit obligations. For defined benefit plans, PBO includes assumptions for future salary increases. This method is consistent with the going concern assumption and is prescribed for measurement of pension obligations. The accumulated benefit obligation (“ABO”) is similar to the PBO, but is based only on current salaries with no assumption of future salary increases. The aggregate ABO for the defined benefit plans was \$2.0 billion at each of December 31, 2008 and 2007.

The PBO and ABO amounts above represent the estimated obligations for benefits to vested participants only, as required by the statutory basis of accounting. The additional obligations estimated for participants that have not yet vested in the defined pension plans and the postretirement plans at December 31, 2008 and 2007 are as follows:

	Defined Benefit Plans		Postretirement Benefit Plans	
	2008	2007	2008	2007
	(in millions)			
PBO	\$ 60	\$ 56	\$ 228	\$ 224
ABO	35	33	-	-

The following table summarizes the assumptions used in estimating the projected benefit obligations and the net benefit cost at December 31, 2008, 2007 and 2006 and for the years then ended:

	Defined Benefit Plans		Postretirement Benefit Plans	
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	2008	2007	2006	2008	2007	2006
Projected benefit obligation:						
Discount rate	6.25%	6.00%	6.00%	6.25%	6.00%	6.00%
Annual increase in compensation	3.75%	4.50%	4.50%	3.75%	4.50%	4.50%
Net periodic benefit cost:						
Discount rate	6.00%	6.00%	5.75%	6.00%	6.00%	5.75%
Annual increase in compensation	4.50%	4.50%	4.50%	4.50%	4.50%	4.50%
Long-term rate of return on plan assets	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%

The long-term rate of return on plan assets is estimated assuming an allocation of plan assets among asset classes consistent with December 31, 2008. Returns are estimated by asset class based on the current risk-free interest rate plus a risk premium. The risk premium is based on historical returns and other factors such as expected reinvestment returns and asset manager performance.

The PBO for postretirement benefits at December 31, 2008 assumed an annual increase in future retiree medical costs of 7.0%, grading down to 5% over five years and remaining level thereafter. At December 31, 2007 the comparable assumption was for an annual increase in future retiree medical costs of 7.5% grading down to 5% over six years and remaining level thereafter. A further increase in the assumed health care cost trend of 1% in each year would increase the accumulated postretirement benefit obligation at December 31, 2008 by \$29 million and net periodic postretirement benefit expense for the year ended December 31, 2008 by \$6 million. A decrease in the assumed health care cost trend of 1% in each year would reduce the accumulated postretirement benefit obligation as of December 31, 2008 and net periodic postretirement benefit expense for the year ended December 31, 2008 by the same amounts.

Following is an aggregate reconciliation of the funded status of the plans to the related financial statement liability reported by the Company at December 31, 2008 and 2007:

	Defined Benefit Plans		Postretirement Benefit Plans	
	2008	2007	2008	2007
	(in millions)			
Fair value of plan assets	\$ 1,992	\$ 2,741	\$ 62	\$ 89
Projected benefit obligation	2,368	2,455	269	244
Funded status	(376)	286	(207)	(155)
Unrecognized net experience losses	986	298	49	25
Unrecognized initial net asset	(544)	(544)	-	-
Additional minimum liability	(9)	(13)	-	-
Nonadmitted asset	(485)	(433)	-	-
Net pension liability	<u>\$ (428)</u>	<u>\$ (406)</u>	<u>\$ (158)</u>	<u>\$ (130)</u>

Unrecognized net experience gains or losses represent cumulative amounts by which plan experience for return on plan assets or growth in estimated benefit obligations have varied from related assumptions. These differences accumulate without recognition in the Company's financial statements unless they exceed 10% of plan assets or 10% of the projected benefit obligation, whichever is greater. If they exceed this limit, they are amortized into net periodic benefit cost over the remaining average years of service until retirement of the plan participants, which is currently fourteen years for employee plans and twelve years for financial representative plans.

Unrecognized initial asset represents the amount by which the fair value of plan assets exceeded the projected benefit obligation for funded pension plans upon the adoption of new statutory accounting guidance for defined benefit plans as of

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January 1, 2001. The Company has elected not to record a direct credit to surplus for this excess, electing instead to amortize this unrecognized initial asset as a credit to net periodic benefit cost in a systematic manner until exhausted.

An additional minimum liability is required if a plan's ABO exceeds plan assets or accrued pension liabilities. This additional liability was \$9 million, \$13 million and \$14 million at December 31, 2008, 2007 and 2006, respectively. Changes in the additional minimum liability are reported as a direct adjustment to surplus in the consolidated statement of changes in surplus.

Any net pension assets for funded plans are nonadmitted and are thereby excluded from assets and surplus in the consolidated statement of financial position.

The components of net periodic benefit cost for the years ended December 31, 2008, 2007 and 2006 were as follows:

	Defined Benefit Plans			Postretirement Benefit Plans		
	2008	2007	2006	2008	2007	2006
	(in millions)					
Components of net periodic benefit cost:						
Service cost of benefits earned	\$ 90	\$ 85	\$ 79	\$ 29	\$ 27	\$ 23
Interest cost on projected obligations	147	136	127	15	12	11
Amortization of experience gains and losses	4	4	20	-	1	1
Amortization of initial net asset	-	-	(13)	-	-	-
Expected return on plan assets	(218)	(202)	(180)	(7)	(7)	(5)
Net periodic benefit cost	<u>\$ 23</u>	<u>\$ 23</u>	<u>\$ 33</u>	<u>\$ 37</u>	<u>\$ 33</u>	<u>\$ 30</u>

The expected benefit payments by the defined benefit plans and the postretirement plans for the years 2009 through 2018 are as follows:

	Defined Benefit Plans	Postretirement Benefit Plans
	(in millions)	
2009	\$ 77	\$ 15
2010	86	17
2011	95	19
2012	105	22
2013	116	24
2014-2018	793	160
	<u>\$ 1,272</u>	<u>\$ 257</u>

The Company also sponsors a contributory 401(k) plan for eligible employees and a noncontributory defined contribution plan for financial representatives. For the years ended December 31, 2008, 2007 and 2006 the Company expensed total contributions to these plans of \$29 million, \$28 million and \$27 million, respectively.

9. Reinsurance

The Company limits its exposure to life insurance death benefits by ceding insurance coverage to various reinsurers. The Company retains a maximum of \$35 million of individual life coverage and a maximum of \$50 million of joint life coverage. The Company also participates in a life insurance catastrophic risk sharing pool.

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The Company cedes 60% of the morbidity risk on group disability plans. The Company ceased reinsuring new individual disability policies in 1999 and new long-term care policies in 2002, but has maintained the reinsurance ceded on policies issued prior to those dates.

Amounts in the consolidated financial statements are reported net of the impact of reinsurance. Reserves for policy benefits at December 31, 2008 and 2007 were reported net of ceded reserves of \$1.6 billion and \$1.5 billion, respectively.

The effects of reinsurance on premium revenue and benefit expense for the years ended December 31, 2008, 2007 and 2006 were as follows:

	For the year ended December 31,		
	2008	2007	2006
	(in millions)		
Direct premium revenue	\$ 14,356	\$ 14,007	\$ 12,890
Premiums ceded	(805)	(765)	(741)
Net premium revenue	\$ 13,551	\$ 13,242	\$ 12,149
Direct benefit expense	\$ 15,027	\$ 14,518	\$ 13,263
Benefits ceded	(567)	(586)	(488)
Net benefit expense	\$ 14,460	\$ 13,932	\$ 12,775

In addition, the Company received \$184 million, \$182 million and \$180 million in allowances from reinsurers for reimbursement of commissions and other expenses on ceded business for the years ended December 31, 2008, 2007 and 2006, respectively. These amounts are included in other income in the consolidated statement of operations.

Reinsurance contracts do not relieve the Company from its obligations to policyowners. Failure of reinsurers to honor their obligations could result in losses to the Company. The Company mitigates this risk by dealing only with reinsurers that meet its financial strength standards, while adhering to concentration limits that would limit losses in the event of one or more reinsurer failures. Most significant reinsurance treaties contain financial protection provisions should a reinsurer's credit rating fall below a prescribed level. There were no reinsurance recoverables at December 31, 2008 and 2007 that were considered by management to be uncollectible.

10. Income Taxes

The Company files a consolidated federal income tax return including the following subsidiaries:

Northwestern Mutual Investment Services, LLC	Frank Russell Company and subsidiaries
Northwestern International Holdings, Inc.	Bradford, Inc.
NML Real Estate Holdings, LLC and subsidiaries	Mason Street Advisors, LLC
NML Securities Holdings, LLC and subsidiaries	NML – CBO, LLC
Northwestern Investment Management Company, LLC	JYD Assets, LLC
Northwestern Mutual Wealth Management Company	NM GP Holdings, LLC

The Company collects from or refunds to these subsidiaries their share of consolidated federal income taxes determined under written tax-sharing agreements.

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The major components of current income tax expense in the consolidated statement of operations were as follows:

	For the year ended December 31,		
	2008	2007	2006
		(in millions)	
Tax payable on ordinary income	\$ 97	\$ 50	\$ 66
Tax credits	(122)	(110)	(86)
Increase (decrease) in contingent tax liabilities	(279)	81	37
Total current tax expense (benefit)	\$ (304)	\$ 21	\$ 17

The Company's taxable income can vary significantly from gain from operations before taxes reported in the consolidated statement of operations due to temporary and permanent differences in revenue recognition and expense deduction between tax and financial statement bases of reporting. The Company's financial statement effective tax rates were 91%, 16% and 1% for the years ended December 31, 2008, 2007 and 2006, respectively.

The effective tax rate is not the rate of tax applied to the Company's federal taxable income or loss by the Internal Revenue Service ("IRS"). It is a financial statement relationship that represents the ratio between the sum of total tax expense or benefit incurred, including current tax expense or benefit on realized capital gains and losses and changes in deferred taxes not related to unrealized gains and losses on investments, to the sum of gain from operations before taxes and pretax net realized capital gains or losses. These financial statement effective rates were different than the applicable federal income tax rate of 35% due primarily to net investment income eligible for dividends received deduction, changes in non-admitted deferred tax assets, certain investment transactions, amortization of the IMR, leveraged leases, tax credits, pension contributions, tax losses of subsidiaries not eligible for refunds under intercompany tax-sharing agreements, interest accrued or released on contingent tax liabilities and adjustments to estimated current tax liabilities upon subsequent filing of tax returns.

The Company made payments to the IRS for federal income taxes of \$72 million, \$252 million and \$412 million during the years ended December 31, 2008, 2007 and 2006, respectively. Income taxes paid in 2008 and prior years of \$1.6 billion are available at December 31, 2008 for refund claims in the event of future tax losses.

Federal income tax returns for 2005 and prior years are closed as to further assessment of tax. Income taxes recoverable or payable in the consolidated statement of financial position represents taxes recoverable or payable at the respective reporting date, adjusted for an estimate of additional taxes that may become due with respect to tax years that remained open to examination by the IRS at the respective reporting date ("contingent tax liabilities").

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Changes in the amount of contingent tax liabilities for the year ended December 31, 2008 were as follows (in millions):

Balance at January 1, 2008	\$ 664
Additions based on tax positions related to the current year	-
Additions for tax positions of prior years	-
Reductions for tax positions of prior years	(279)
Balance at December 31, 2008	\$ 385

Included in the balance at December 31, 2008 are \$350 million of tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of the deductions. Because of the impact of deferred tax accounting for amounts other than interest, the timing of the ultimate deduction would not affect the effective tax rate in future periods.

The Company recognizes interest accrued or released related to contingent tax liabilities in current income tax expense (benefit). During the years ended December 31, 2008, 2007 and 2006, the Company recognized \$(38) million, \$34 million and \$(7) million, respectively, in interest-related expense (benefit). The Company had \$35 million and \$73 million accrued for the payment of interest at December 31, 2008 and 2007, respectively.

The Company accounts for deferred tax assets and liabilities, which represent the financial statement impact of cumulative temporary differences between the tax and financial statement bases of assets and liabilities. The significant components of the net deferred tax asset at December 31, 2008 and 2007 were as follows:

	December 31,		Change
	2008	2007	
	(in millions)		
Deferred tax assets:			
Policy acquisition costs	\$ 925	\$ 885	\$ 40
Investments	440	40	400
Policy benefit liabilities	1,645	1,893	(248)
Benefit plan obligations	444	434	10
Guaranty fund assessments	11	11	-
Nonadmitted assets	75	65	10
Other	111	157	(46)
Gross deferred tax assets	3,651	3,485	166
Nonadmitted deferred tax assets	(74)	-	(74)
Admitted deferred tax assets	3,577	3,485	92
Deferred tax liabilities:			
Premiums and other receivables	591	572	19
Investments	284	1,450	(1,166)
Other	6	2	4
Gross deferred tax liabilities	881	2,024	(1,143)
Net admitted deferred tax assets	\$ 2,696	\$ 1,461	\$ 1,235

The statutory basis of accounting limits the amount of gross deferred tax assets that can be included in Company surplus. This limit is based on a formula that takes into consideration available loss carryback and carryforward capacity, expected timing of reversal for existing temporary differences, gross deferred tax liabilities and the level of Company surplus. Beginning in 2008, the Company adopted a permitted practice relating to the valuation of its net deferred tax assets. This

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permitted practice, which is effective through September 30, 2009, differs from the NAIC *Accounting Practices and Procedures Manual* in that it extends the reversal period for carryforward of temporary differences in Statement of Statutory Accounting Principles No. 10, *Accounting for Income Taxes* ("SSAP 10"), from one year to three years and increases the level of surplus limitation from 10% to 15%.

At December 31, 2008, the Company's gross deferred tax assets exceeded this permitted practice limit by \$74 million. If the Company had not received permission for this alternative accounting treatment, the Company's gross deferred tax assets would have exceeded the SSAP 10 limit by \$844 million, thereby reducing surplus in the consolidated statement of financial position by \$770 million at December 31, 2008 compared to the result under the permitted practice. At December 31, 2007, the Company's gross deferred tax assets were less than the SSAP 10 limit by \$445 million.

Changes in deferred tax assets and liabilities related to unrealized gains and losses on investments are included in changes in unrealized capital gains and losses in the consolidated statement of changes in surplus. Other net changes in deferred tax assets and liabilities are direct adjustments to surplus and separately reported in the consolidated statement of changes in surplus.

11. Frank Russell Company

The Company acquired Frank Russell Company ("Russell") effective January 1, 1999. Russell, a global leader in multi-manager investment services, provides investment products and services in over 40 countries. The initial purchase price of approximately \$1.0 billion was funded with a combination of cash, senior notes issued by Russell and bank debt. The purchase agreement also called for additional contingent consideration to be paid to the former owners of Russell based upon its financial performance during the five year period ended December 31, 2003.

At the time of acquisition, the Company received permission from the OCI for a permitted practice regarding the valuation of its equity investment in Russell, whereby all GAAP acquisition goodwill, including any subsequent additions to goodwill resulting from payment of contingent purchase consideration, was charged off from the statutory cost basis of the acquisition as a direct reduction of Company surplus. At December 31, 2007, the Company had made cumulative direct reductions of surplus for goodwill associated with the Russell acquisition of \$981 million which exceeded the Company's equity method accounting basis in Russell. As a result, the Company's investment in Russell was reported at a negative \$464 million, which was included as a reduction of the Company's investment in common stocks in the consolidated statement of financial position at December 31, 2007. During 2008, the Company received permission from the OCI to amend the original permitted practice to be in accordance with Statement of Statutory Accounting Principle No. 97, *Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 88* ("SSAP 97"), using the statutory equity method based on Russell's audited GAAP book equity, exclusive of any adjustment for Russell's GAAP goodwill as would otherwise be required by SSAP 97. This new permitted practice was adopted as a change in accounting principle effective January 1, 2008 and resulted in an \$829 million direct increase to surplus. At December 31, 2008, the Company's investment in Russell common stock was reported at \$67 million, compared with a fair value of approximately \$1 billion at that date.

If the Company had not received permission for this alternative accounting treatment, surplus as reported in the consolidated statement of financial position would have been lower by \$730 million and higher by \$130 million at December 31, 2008 and December 31, 2007, respectively, and net income as reported in the consolidated statement of operations would have been lower by \$63 million for each of the years then ended.

During 2007, the Company received common stock dividends from Russell in the amount of \$56 million, which are included in net investment income in the consolidated statement of operations. No dividends were received from Russell during 2008.

In July 2008, a subsidiary of the Company sold common stock representing a 5% ownership interest in Russell to a third party, resulting in an immaterial after-tax gain that is reported as an unrealized capital gain pending distribution of the net proceeds to the Company by the subsidiary.

In conjunction with the financing of the Russell acquisition in 1999, the Company guaranteed the repayment of \$350 million of senior notes issued to third parties by Russell. During December 2008, the Company purchased, at par, perpetual senior preferred stock issued by Russell in the amount of \$350 million. These securities are callable under certain conditions and

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will pay preferred dividends at a rate of 8.0%, payable semi-annually. Russell used the proceeds of the senior preferred stock issuance to retire the senior notes upon their maturity on January 15, 2009.

During 2008, Russell entered into capital support agreements with money market funds it sponsors in order to assure the realizable value of \$764 million of Lehman Brothers Holdings Inc. securities held by the funds. The Company guaranteed Russell's obligations under those agreements. The Company subsequently entered into a loan agreement with Russell under which Russell could borrow up to \$764 million to purchase the Lehman securities or to otherwise meet its obligations to the funds under the capital support agreements. The loan bears interest at prime plus 2% and has a term of three years. At December 31, 2008, there was no outstanding balance under this loan agreement. On January 12, 2009, the loan agreement was terminated, and the Company entered into an agreement to purchase, at par, up to \$764 million of perpetual junior preferred stock and warrants issued by Russell. The junior preferred stock is callable under certain conditions and will pay preferred dividends at a rate of 10.0%, payable semi-annually. The purchase of the first issuance of junior preferred stock and warrants, which occurred on January 12, 2009, was \$82 million. It is expected that additional junior preferred stock and warrants will be issued and purchased during 2009, with the proceeds used by Russell to fulfill its remaining obligations to its sponsored funds under the capital support agreements.

During 2008, the Company purchased \$654 million of short-term notes issued by third parties from money market funds sponsored by Russell. These notes were purchased at amortized cost, which approximated fair value, and had varying interest rates and maturity dates. At December 31, 2008, the Company held \$342 million of these notes, which are reported at amortized cost and included in cash and temporary investments in the consolidated statement of financial position.

The Company also invests in other notes issued by Russell, which bear interest at rates from 6.1% to 7.0% and mature in 2014. At each of December 31, 2008 and 2007, the Company held \$180 million of other notes issued by Russell, which are reported at amortized cost and included in bonds in the consolidated statement of financial position.

The Company has guaranteed the repayment of up to \$250 million of bank borrowings by Russell under a revolving line of credit that expires on April 30, 2009. Russell's borrowings under this facility were \$222 million and \$26 million at December 31, 2008 and 2007, respectively.

12. Contingencies and Guarantees

In the normal course of business, the Company has guaranteed certain obligations of other affiliates and made guarantees of operating leases or future minimum compensation payments on behalf of its financial representatives. The terms of these guarantees range from 5 years to 19 years at December 31, 2008. If these affiliates or financial representatives are not able to meet their obligations, the Company would be required to make payments to fulfill its guarantees. The maximum aggregate exposure under these guarantees was \$469 million at December 31, 2008. The Company believes that the likelihood is remote that payments will be required under these guarantees and therefore has not accrued a contingent liability in the consolidated statement of financial position. In addition, the Company routinely makes commitments to fund mortgage loans or other investments in the normal course of business. These commitments aggregated to \$3.0 billion at December 31, 2008 and were extended at market interest rates and terms.

The Company is engaged in various legal actions in the course of its investment and insurance operations. The status of these legal actions is actively monitored by management. If management believed, based on available information, that an adverse outcome upon resolution of a given legal action was probable and the amount of that adverse outcome was reasonable to estimate, a loss would be recognized and a related liability recorded. No such liabilities were recorded by the Company at December 31, 2008 and 2007.

Legal actions are subject to inherent uncertainties, and future events could change management's assessment of the probability or estimated amount of potential losses from pending or threatened legal actions. Based on available information, it is the opinion of management that the ultimate resolution of pending or threatened legal actions, both individually and in the aggregate, will not result in losses having a material effect on the Company's financial position at December 31, 2008.

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13. Related Party Transactions

During each of 2008 and 2007, the Company transferred certain investments from its general account to unconsolidated subsidiaries as a capital contribution. The aggregate statement value and fair value of investments transferred during 2008 was \$102 million and \$449 million, respectively. The aggregate statement value and fair value of investments transferred during 2007 were each \$45 million. These capital contributions were accounted for at statement value, and no capital gain or loss was reported by the Company or its subsidiaries as a result of these transfers.

During 2007, the Company invested \$300 million of seed money in 15 new variable annuity mutual funds managed by a subsidiary. At December 31, 2008 and 2007, these investments had a fair value of \$250 million and \$321 million, respectively, and are included in common stocks in the consolidated statement of financial position.

During March 2006, the Company completed a reorganization transaction whereby the Mason Street Funds, a family of mutual funds sponsored and managed by a subsidiary of the Company, were combined with new or existing mutual funds sponsored by two unaffiliated third parties ("successor funds"). Prior to the reorganization transaction, the Company and its subsidiaries redeemed \$289 million and \$21 million, respectively, of mutual fund investments from the Mason Street Funds at fair value, with aggregate realized and unrealized capital gains of \$68 million reported by the Company during 2006 from these redemptions. Under the terms of the reorganization transaction, the remaining Mason Street Fund shares owned by the Company and its subsidiaries, with an aggregate fair value of \$970 million, were exchanged for mutual fund shares in the successor funds of equal fair value. In connection with the reorganization, the Company and its subsidiaries agreed not to redeem their investment in the successor funds for a period of up to three years after the reorganization transaction. During 2008 the Company and its subsidiaries redeemed \$258 million and \$40 million, respectively, of mutual fund shares in the successor funds with net realized capital gains of \$27 million and unrealized capital losses of \$14 million reported by the Company on these redemptions. The Company held shares in the successor funds with aggregate fair values of \$376 million and \$830 million at December 31, 2008 and 2007, respectively, which are included in common stocks in the consolidated statement of financial position. At December 31, 2008 and 2007, the Company's unconsolidated subsidiaries held additional shares in the successor funds with aggregate fair values of \$162 million and \$288 million, respectively. The Company has been notified that in February, 2009 several of the successor funds held by the Company and an unconsolidated subsidiary are scheduled to be liquidated. The Company and an unconsolidated subsidiary expect to receive distributions from these funds of approximately \$198 million and \$41 million, respectively, with realized capital losses of approximately \$53 million and unrealized capital losses of approximately \$22 million to be reported by the Company in 2009 on these distributions.

14. Fair Value of Financial Instruments

The fair value of an asset or liability is the amount at which the asset or liability could be purchased or sold in a current transaction between willing parties, other than in a forced sale or liquidation situation.

The fair value of investment assets and certain policy liabilities at December 31, 2008 and 2007 were as follows:

	December 31, 2008		December 31, 2007	
	Statement Value	Fair Value	Statement Value	Fair Value
	(in millions)			
Assets:				
Bonds	\$ 79,314	\$ 74,736	\$ 76,842	\$ 77,650
Mortgage loans	21,677	18,620	20,833	21,160
Policy loans	12,884	12,884	11,797	11,797
Common and preferred stocks	5,744	6,646	9,525	13,626
Real estate	1,528	2,402	1,499	2,653
Other investments	9,185	10,624	8,749	10,838
Cash and temporary investments	4,807	4,807	2,547	2,547
Liabilities:				
Investment-type insurance reserves	\$ 4,563	\$ 4,226	\$ 4,336	\$ 4,121

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The statutory basis of accounting generally requires that fair value disclosures for bonds and certain preferred stocks, as well as statement value for common stocks and certain preferred stocks, be based on values published by the SVO, when available. The Company understands that SVO values are based on quoted market prices, when available, or SVO-developed pricing models.

The fair value of bonds is generally based on values published by the SVO or quoted market prices of identical or similar securities when no SVO value is available. For bonds without SVO-published values or quoted market prices, fair value is estimated using independent pricing services or internally developed pricing models. The fair value of common and preferred stocks and other equity securities is generally based on values published by the SVO and quoted market prices. When SVO-published values or quoted market prices are not used, fair value is estimated using independent pricing services or internally developed pricing models. The fair value of the Company's investment in Russell common stock is determined using a multiple, reflective of comparable public companies, of Russell's earnings before interest, taxes, depreciation and amortization. See Note 11 regarding the statement value of the Company's investment in Russell common stock. The fair value of mortgage loans is based on estimated future cash flows discounted using market interest rates for debt with comparable credit risk and maturities. The fair value of real estate is based on estimated future cash flows discounted using market interest or capitalization rates. The fair value of policy loans is based on unpaid principal balance, which approximates fair value. Other investments include: real estate joint ventures, for which fair value is based on estimated future cash flows discounted using market interest rates; other joint ventures and partnerships, for which statement value approximates fair value; investments in low income housing tax credits, for which fair value is based on estimated future tax benefits discounted using market interest rates, and derivatives, for which fair value is based on quoted market prices, where available, or third party and internally developed pricing models.

Investment-type insurance reserves only include individual fixed annuity policies, supplementary contracts without life contingencies and amounts left on deposit with the Company. The fair value of investment-type insurance reserves is based on estimated future cash flows discounted at market interest rates for similar instruments with comparable maturities.

The statutory basis of accounting requires that certain bonds and preferred stocks, most common stocks, certain derivative instruments and most separate account assets be reported at fair value. Estimates of fair value can be categorized into three levels based on the nature of the inputs to the valuation estimates:

Level 1 – Fair value is based on quoted prices for identical assets or liabilities in active markets that are accessible to the Company.

Level 2 – Fair value is based on quoted prices for similar assets in active markets or quoted prices for identical or similar assets in non-active markets.

Level 3 – Fair value is estimated by the Company using one or more significant unobservable inputs.

The table below presents the common stocks and separate account assets reported at fair value in the consolidated statement of financial position, in aggregate, as of December 31, 2008. The statement value of bonds rated "6" by the NAIC and preferred stocks rated "4", "5" and "6" by the NAIC, which are reported at the lower of amortized cost or fair value, and the statement value of derivatives reported at fair value as of December 31, 2008 are considered immaterial for the purpose of this disclosure and are thereby not included below.

Common stocks reported at fair value exclude investments in unconsolidated subsidiaries, as they are reported using the equity method. Separate account assets reported at fair value exclude short-term investments and real estate joint ventures, as they are reported at amortized cost and using the equity method, respectively.

	December 31, 2008			Total
	Level 1	Level 2	Level 3	
	(in millions)			
Common stocks	\$ 3,951	\$ -	\$ 1,064	\$ 5,015
Separate accounts	12,206	703	19	12,928

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The following table summarizes the changes in fair value of assets utilizing Level 3 inputs for the year ended December 31, 2008.

	For the year ended December 31, 2008	
	Common Stocks	Separate Accounts
	(in millions)	
Fair value, beginning of period	\$ 1,361	\$ 24
Realized investment gains/(losses)	(35)	(1)
Unrealized gains/(losses)	(310)	(2)
Purchases, sales, settlements	48	(2)
Fair value, end of period	\$ 1,064	\$ 19

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Report of Independent Auditors

To the Board of Trustees and Policyowners of
The Northwestern Mutual Life Insurance Company

We have audited the accompanying statutory consolidated statements of financial position of The Northwestern Mutual Life Insurance Company and its subsidiary (the "Company") as of December 31, 2008 and 2007, and the related consolidated statutory statements of operations, of changes in surplus, and of cash flows for each of the three years in the period ended December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As described in Note 1 to the financial statements, the Company prepared these consolidated financial statements using accounting practices prescribed or permitted by the Office of the Commissioner of Insurance of the State of Wisconsin (statutory basis of accounting), which practices differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between the statutory basis of accounting and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Company as of December 31, 2008 and 2007 or the results of its operations or its cash flows for each of the three years in the period ended December 31, 2008.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2008 and 2007, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2008, on the basis of accounting described in Note 1, which includes permitted departures from codified statutory accounting as disclosed in Notes 10 and 11.

/s/PRICEWATERHOUSECOOPERS LLP
February 25, 2009