

LINCOLN NATIONAL CORP  
Form 10-Q  
November 03, 2011

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

\_\_\_\_\_  
FORM 10-Q  
\_\_\_\_\_

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2011  
OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-6028

\_\_\_\_\_  
LINCOLN NATIONAL CORPORATION  
(Exact name of registrant as specified in its charter)

Indiana  
(State or other jurisdiction of  
incorporation or organization)

35-1140070  
(I.R.S. Employer  
Identification No.)

150 N. Radnor Chester Road, Suite A305, Radnor,  
Pennsylvania  
(Address of principal executive offices)

19087  
(Zip Code)

(484) 583-1400  
(Registrant's telephone number, including area code)

Not Applicable  
(Former name, former address and former fiscal year, if changed since last report.)

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

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

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

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

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

As of October 31, 2011, there were 301,664,558 shares of the registrant's common stock outstanding.

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## Lincoln National Corporation

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

LINCOLN NATIONAL CORPORATION  
CONSOLIDATED BALANCE SHEETS  
(in millions, except share data)

|  | As of<br>September<br>30,<br>2011<br>(Unaudited) | As of<br>December 31,<br>2010 |
|--|--|-------------------------------|
| <b>ASSETS</b>  |  |                               |
| Investments:   |  |                               |
| Available-for-sale securities, at fair value:  |  |                               |
| Fixed maturity securities (amortized cost: 2011 - \$68,382; 2010 - \$65,175)                       | \$ 74,591  | \$ 68,030                     |
| Variable interest entities' fixed maturity securities (amortized cost: 2011 - \$672; 2010 - \$570) | 700  | 584                           |
| Equity securities (cost: 2011 - \$131; 2010 - \$179)   | 137  | 197                           |
| Trading securities   | 2,726  | 2,596                         |
| Mortgage loans on real estate  | 6,893  | 6,752                         |
| Real estate  | 136  | 202                           |
| Policy loans   | 2,874  | 2,865                         |
| Derivative investments   | 3,029  | 1,076                         |
| Other investments  | 1,105  | 1,038                         |
| Total investments  | 92,191   | 83,340                        |
| Cash and invested cash   | 4,833  | 2,741                         |
| Deferred acquisition costs and value of business acquired  | 8,130  | 8,930                         |
| Premiums and fees receivable   | 383  | 335                           |
| Accrued investment income  | 1,023  | 933                           |
| Reinsurance recoverables   | 6,659  | 6,527                         |
| Goodwill   | 3,019  | 3,019                         |
| Other assets   | 3,314  | 3,369                         |
| Separate account assets  | 78,195   | 84,630                        |
| Total assets   | \$ 197,747                                       | \$ 193,824                    |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |  |                               |
| Liabilities  |  |                               |
| Future contract benefits   | \$ 19,969  | \$ 17,460                     |
| Other contract holder funds  | 68,581   | 66,478                        |
| Short-term debt  | 550  | 351                           |
| Long-term debt   | 5,348  | 5,399                         |
| Reinsurance related embedded derivatives   | 177  | 102                           |
| Funds withheld reinsurance liabilities   | 1,072  | 1,149                         |
| Deferred gain on business sold through reinsurance   | 412  | 468                           |
| Payables for collateral on investments   | 3,855  | 1,659                         |
| Variable interest entities' liabilities  | 203  | 132                           |
| Other liabilities  | 4,466  | 3,190                         |
| Separate account liabilities   | 78,195   | 84,630                        |
| Total liabilities  | 182,828  | 181,018                       |

Contingencies and Commitments (See Note 10)

Stockholders' Equity

|  |            |            |
|--|------------|------------|
| Preferred stock - 10,000,000 shares authorized; Series A - 10,854 and 10,914 shares issued and outstanding as of September 30, 2011, and December 31, 2010, respectively | -          | -          |
| Common stock - 800,000,000 shares authorized; 301,659,175 and 315,718,554 shares issued and outstanding as of September 30, 2011, and December 31, 2010, respectively    | 7,792      | 8,124      |
| Retained earnings  | 4,664      | 3,934      |
| Accumulated other comprehensive income (loss)  | 2,463      | 748        |
| Total stockholders' equity   | 14,919     | 12,806     |
| Total liabilities and stockholders' equity   | \$ 197,747 | \$ 193,824 |

See accompanying Notes to Consolidated Financial Statements

LINCOLN NATIONAL CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME (LOSS)  
(Unaudited, in millions, except per share data)

|   | For the Three<br>Months Ended<br>September 30, |         | For the Nine<br>Months Ended<br>September 30, |          |
|---|--|---------|---|----------|
|   | 2011   | 2010    | 2011  | 2010     |
| Revenues  |  |         |   |          |
| Insurance premiums  | \$ 559   | \$ 538  | \$ 1,721                                      | \$ 1,621 |
| Insurance fees  | 864  | 769     | 2,582   | 2,351    |
| Net investment income   | 1,151  | 1,132   | 3,522   | 3,358    |
| Realized gain (loss):   |  |         |   |          |
| Total other-than-temporary impairment losses on securities                              | (42)   | (99)    | (133)   | (187)    |
| Portion of loss recognized in other comprehensive income                                | 17   | 53      | 39  | 77       |
| Net other-than-temporary impairment losses on securities<br>recognized in earnings      | (25)   | (46)    | (94)  | (110)    |
| Realized gain (loss), excluding other-than-temporary<br>impairment losses on securities | (138)  | 89      | (83)  | 132      |
| Total realized gain (loss)  | (163)  | 43      | (177)   | 22       |
| Amortization of deferred gain on business sold through reinsurance                      | 19   | 19      | 56  | 56       |
| Other revenues and fees   | 118  | 112     | 361   | 337      |
| Total revenues  | 2,548  | 2,613   | 8,065   | 7,745    |
| Benefits and Expenses   |  |         |   |          |
| Interest credited   | 625  | 623     | 1,864   | 1,855    |
| Benefits  | 665  | 924     | 2,527   | 2,541    |
| Underwriting, acquisition, insurance and other expenses                                 | 1,040  | 689     | 2,401   | 2,155    |
| Interest and debt expense   | 79   | 74      | 223   | 212      |
| Total benefits and expenses   | 2,409  | 2,310   | 7,015   | 6,763    |
| Income (loss) from continuing operations before taxes                                   | 139  | 303     | 1,050   | 982      |
| Federal income tax expense (benefit)  | (12)   | 55      | 234   | 226      |
| Income (loss) from continuing operations  | 151  | 248     | 816   | 756      |
| Income (loss) from discontinued operations, net of federal<br>income taxes              | (8)  | (2)     | (8)   | 29       |
| Net income (loss)   | 143  | 246     | 808   | 785      |
| Preferred stock dividends and accretion of<br>discount                                  | -  | -       | -   | (168)    |
| Net income (loss) available to<br>common stockholders                                   | \$ 143   | \$ 246  | \$ 808  | \$ 617   |
| Earnings (Loss) Per Common Share - Basic  |  |         |   |          |
| Income (loss) from continuing operations  | \$ 0.50  | \$ 0.79 | \$ 2.63                                       | \$ 1.92  |
| Income (loss) from discontinued operations  | (0.03)   | (0.01)  | (0.03)  | 0.09     |
| Net income (loss)   | \$ 0.47  | \$ 0.78 | \$ 2.60                                       | \$ 2.01  |
| Earnings (Loss) Per Common Share - Diluted  |  |         |   |          |
| Income (loss) from continuing operations  | \$ 0.47  | \$ 0.76 | \$ 2.55                                       | \$ 1.85  |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Income (loss) from discontinued operations | (0.03)  | (0.01)  | (0.03)  | 0.09    |
| Net income (loss)                          | \$ 0.44 | \$ 0.75 | \$ 2.52 | \$ 1.94 |

See accompanying Notes to Consolidated Financial Statements



LINCOLN NATIONAL CORPORATION  
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY  
(Unaudited, in millions, except per share data)

|   | For the Nine<br>Months Ended<br>September 30, |           |
|---|---|-----------|
|   | 2011  | 2010      |
| <b>Preferred Stock</b>  |   |           |
| Balance as of beginning-of-year                                 | \$ -  | \$ 806    |
| Issuance (redemption) of Series B preferred stock               | -   | (950)     |
| Accretion of discount on Series B preferred stock               | -   | 144       |
| Balance as of end-of-period                                     | -   | -         |
| <b>Common Stock</b>   |   |           |
| Balance as of beginning-of-year                                 | 8,124   | 7,840     |
| Issuance of common stock  | -   | 368       |
| Issuance (repurchase and cancellation) of common stock warrants | -   | (48)      |
| Stock compensation/issued for benefit plans                     | 13  | 11        |
| Effect of amendment to deferred compensation plans              | -   | (29)      |
| Retirement of common stock/cancellation of shares               | (345)   | -         |
| Balance as of end-of-period                                     | 7,792   | 8,142     |
| <b>Retained Earnings</b>  |   |           |
| Balance as of beginning-of-year                                 | 3,934   | 3,316     |
| Cumulative effect from adoption of new accounting standards     | -   | (169)     |
| Comprehensive income (loss)                                     | 2,523   | 2,528     |
| Less other comprehensive income (loss), net of tax              | 1,715   | 1,743     |
| Net income (loss)   | 808   | 785       |
| Retirement of common stock                                      | (30)  | -         |
| Dividends declared: Common (2011 - \$0.150; 2010 - \$0.030)     | (48)  | (9)       |
| Dividends on preferred stock                                    | -   | (24)      |
| Accretion of discount on Series B preferred stock               | -   | (144)     |
| Balance as of end-of-period                                     | 4,664   | 3,755     |
| <b>Accumulated Other Comprehensive Income (Loss)</b>            |   |           |
| Balance as of beginning-of-year                                 | 748   | (262)     |
| Cumulative effect from adoption of new accounting standards     | -   | 181       |
| Other comprehensive income (loss), net of tax                   | 1,715   | 1,743     |
| Balance as of end-of-period                                     | 2,463   | 1,662     |
| Total stockholders' equity as of end-of-period                  | \$ 14,919                                     | \$ 13,559 |

See accompanying Notes to Consolidated Financial Statements

LINCOLN NATIONAL CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited, in millions)

|  | For the Nine<br>Months Ended<br>September 30, |          |
|--|---|----------|
|  | 2011  | 2010     |
| <b>Cash Flows from Operating Activities</b>  |   |          |
| Net income (loss)  | \$ 808  | \$ 785   |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |   |          |
| Deferred acquisition costs, value of business acquired, deferred sales inducements       |   |          |
| and deferred front-end loads deferrals and interest, net of amortization                 | (110)   | (186)    |
| Trading securities purchases, sales and maturities, net                                  | 33  | 15       |
| Change in premiums and fees receivable   | (48)  | 13       |
| Change in accrued investment income  | (90)  | (100)    |
| Change in future contract benefits and other contract holder funds                       | 141   | 671      |
| Change in reinsurance related assets and liabilities                                     | (210)   | (119)    |
| Change in federal income tax accruals  | 275   | 261      |
| Realized (gain) loss   | 177   | (22)     |
| (Gain) loss on early extinguishment of debt  | 8   | -        |
| Amortization of deferred gain on business sold through reinsurance                       | (56)  | (56)     |
| (Gain) loss on disposal of discontinued operations                                       | 3   | (65)     |
| Other  | 3   | (53)     |
| Net cash provided by (used in) operating activities                                      | 934   | 1,144    |
| <b>Cash Flows from Investing Activities</b>  |   |          |
| Purchases of available-for-sale securities   | (8,540)                                       | (10,449) |
| Sales of available-for-sale securities   | 1,274   | 2,595    |
| Maturities of available-for-sale securities  | 3,988   | 3,093    |
| Purchases of other investments   | (2,202)                                       | (2,390)  |
| Sales or maturities of other investments   | 2,336   | 2,307    |
| Increase (decrease) in payables for collateral on investments                            | 2,196   | 660      |
| Proceeds from sale of subsidiaries/businesses, net of cash disposed                      | -   | 321      |
| Other  | (63)  | (49)     |
| Net cash provided by (used in) investing activities                                      | (1,011)                                       | (3,912)  |
| <b>Cash Flows from Financing Activities</b>  |   |          |
| Payment of long-term debt, including current maturities                                  | (275)   | (250)    |
| Issuance of long-term debt, net of issuance costs  | 298   | 749      |
| Increase (decrease) in commercial paper, net   | (100)   | 1        |
| Deposits of fixed account values, including the fixed portion of variable                | 8,187   | 8,247    |
| Withdrawals of fixed account values, including the fixed portion of variable             | (3,750)                                       | (3,858)  |
| Transfers to and from separate accounts, net   | (1,763)                                       | (2,087)  |
| Common stock issued for benefit plans and excess tax benefits                            | (6)   | (2)      |

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|  |       |          |
|--|-------|----------|
| Issuance (redemption) of Series B preferred stock                                    | -     | (998)    |
| Issuance of common stock   | -     | 368      |
| Repurchase of common stock   | (375) | -        |
| Dividends paid to common and preferred stockholders                                  | (47)  | (39)     |
| Net cash provided by (used in) financing activities                                  | 2,169 | 2,131    |
| Net increase (decrease) in cash and invested cash, including discontinued operations | 2,092 | (637)    |
| Cash and invested cash, including discontinued operations, as of beginning-of-year   | 2,741 | 4,184    |
| Cash and invested cash, including discontinued operations, as of end-of-period \$    | 4,833 | \$ 3,547 |

See accompanying Notes to Consolidated Financial Statements

LINCOLN NATIONAL CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

1. Nature of Operations and Basis of Presentation

Nature of Operations

Lincoln National Corporation and its majority-owned subsidiaries (“LNC” or the “Company,” which also may be referred to as “we,” “our” or “us”) operate multiple insurance businesses through four business segments. See Note 15 for additional details. The collective group of businesses uses “Lincoln Financial Group” as its marketing identity. Through our business segments, we sell a wide range of wealth protection, accumulation and retirement income products. These products include institutional and/or retail fixed and indexed annuities, variable annuities, universal life insurance (“UL”), variable universal life insurance (“VUL”), linked-benefit UL, term life insurance, mutual funds and group life, disability and dental.

Basis of Presentation

The accompanying unaudited consolidated financial statements are prepared in accordance with United States of America generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions for the Securities and Exchange Commission (“SEC”) Quarterly Report on Form 10-Q, including Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. Therefore, the information contained in the Notes to Consolidated Financial Statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2010 (“2010 Form 10-K”), should be read in connection with the reading of these interim unaudited consolidated financial statements.

Certain GAAP policies, which significantly affect the determination of financial position, results of operations and cash flows, are summarized in our 2010 Form 10-K.

In the opinion of management, these statements include all normal recurring adjustments necessary for a fair presentation of the Company’s results. Operating results for the nine month period ended September 30, 2011, are not necessarily indicative of the results that may be expected for the full year ending December 31, 2011. All material intercompany accounts and transactions have been eliminated in consolidation.

Certain amounts reported in prior years’ consolidated financial statements have been reclassified to conform to the presentation adopted in the current year. These reclassifications had no effect on net income or stockholders’ equity of the prior years.

2. New Accounting Standards

Adoption of New Accounting Standards

Fair Value Measurements and Disclosures Topic

In January 2010, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2010-06, “Improving Disclosures about Fair Value Measurements” (“ASU 2010-06”), which requires additional disclosure related to the three-level fair value hierarchy. For a more detailed description of ASU 2010-06, see “Adoption of New

Accounting Standards – Fair Value Measurements and Disclosures Topic” in Note 2 of our 2010 Form 10-K. We adopted the remaining disclosure requirements in ASU 2010-06 effective January 1, 2011, and have prospectively included the disclosures related to purchases, sales, issuances and settlements for Level 3 fair value measurements in Note 14 for the period ended September 30, 2011.

#### Financial Services – Insurance Industry Topic

In April 2010, the FASB issued ASU No. 2010-15, “How Investments Held through Separate Accounts Affect an Insurer’s Consolidation Analysis of Those Investments” (“ASU 2010-15”), to clarify a consolidation issue for insurance entities that hold a controlling interest in an investment fund either partially or completely through separate accounts. For a more detailed description of ASU 2010-15, see “Future Adoption of New Accounting Standards – Financial Services – Insurance Industry Topic” in Note 2 of our 2010 Form 10-K. We adopted the accounting guidance in ASU 2010-15 effective January 1, 2011. The adoption did not have a material effect on our consolidated financial condition and results of operations.

#### Intangibles – Goodwill and Other Topic

In December 2010, the FASB issued ASU No. 2010-28, “When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts” (“ASU 2010-28”). For a more detailed description of ASU 2010-28, see “Future Adoption of New Accounting Standards – Intangibles – Goodwill and Other Topic” in Note 2 of our 2010 Form 10-K. We adopted ASU 2010-28 effective January 1, 2011, and evaluated the reporting units within scope under this new accounting guidance. The adoption did not have a material effect on our consolidated financial condition and results of operations.

#### Receivables Topic

In July 2010, the FASB issued ASU No. 2010-20, “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses” (“ASU 2010-20”), in order to enhance and expand the financial statement disclosures. For a more detailed description of ASU 2010-20, see “Adoption of New Accounting Standards – Receivables Topic” in Note 2 of our 2010 Form 10-K. We adopted the remaining disclosure requirements in ASU 2010-20 effective January 1, 2011, and have prospectively included the required financial statement disclosures related to the activity in our allowance for mortgage loan on real estate losses in Note 5 for the period ended September 30, 2011.

#### Future Adoption of New Accounting Standards

##### Comprehensive Income Topic

In June 2011, the FASB issued ASU No. 2011-05, “Presentation of Comprehensive Income” (“ASU 2011-05”), with an objective of increasing the prominence of items reported in other comprehensive income (“OCI”). The amendments in ASU 2011-05 provide entities with the option to present the total of comprehensive income, the components of net income and the components of OCI in either a single continuous statement of comprehensive income or in two separate but consecutive statements. In addition, entities must present on the face of the financial statement, items reclassified from OCI to net income in the section of the financial statement where the components of net income and OCI are presented, regardless of the option selected to present comprehensive income. ASU 2011-05 is applicable retrospectively and is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. Early adoption is permitted. We will adopt the provisions of ASU 2011-05 effective January 1, 2012, and are currently evaluating our options for the presentation of comprehensive income upon adoption.

##### Fair Value Measurements and Disclosures Topic

In May 2011, the FASB issued ASU No. 2011-04, “Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards” (“ASU 2011-04”), which was issued to create a consistent framework for the application of fair value measurement across jurisdictions. The amendments include wording changes to GAAP in order to clarify the FASB’s intent about the application of existing fair value measurements and disclosure requirements, as well as to change a particular principle or existing requirement for measuring fair value or disclosing information about fair value measurements. There are no additional fair value measurements required upon the adoption of ASU 2011-04. The amendments are effective, prospectively, for interim and annual reporting periods beginning after December 15, 2011. Early adoption is prohibited. We will adopt the provisions of ASU 2011-04 effective January 1, 2012, and are currently evaluating the effect of adoption on our consolidated financial condition and results of operations.

##### Financial Services – Insurance Industry Topic

In October 2010, the FASB issued ASU No. 2010-26, “Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts” (“ASU 2010-26”), which clarifies the types of costs incurred by an insurance entity that can be capitalized in the acquisition of insurance contracts. For a more detailed description of ASU 2010-26, see “Future Adoption of New Accounting Standards – Financial Services – Insurance Industry Topic” in Note 2 of our 2010 Form 10-K. We will adopt the provisions of ASU 2010-26 effective January 1, 2012, and currently estimate that retrospective adoption will result in the restatement of all years presented with a cumulative effect adjustment to the opening balance of retained earnings for the earliest period presented of approximately \$950 million to \$1.15 billion. In addition, the adoption of this accounting guidance will result in a lower deferred acquisition costs (“DAC”) adjustment associated with unrealized gains and losses on available-for-sale (“AFS”) securities and certain derivatives;

therefore, we will also adjust these DAC balances as of January 1, 2012, through a cumulative effect adjustment to the opening balance of accumulated other comprehensive income (loss) ("AOCI"). This adjustment is dependent on our unrealized position as of the date of adoption.

#### Intangibles – Goodwill and Other Topic

In September 2011, the FASB issued ASU No. 2011-08, "Testing Goodwill for Impairment" ("ASU 2011-08"), which provides an option to first assess qualitative factors to determine if it is necessary to complete the two-step goodwill impairment test. If an assessment of the relevant events and circumstances leads to a conclusion that it is not more likely than not that the fair value of a reporting unit is less than its carrying value, then performing the two-step impairment test is unnecessary. However, if a conclusion is reached otherwise, the two-step impairment test, that is currently required under the FASB ASC, must be completed. An entity has an unconditional option to bypass the qualitative assessment for any reporting unit and proceed directly to the two-

step goodwill impairment test, and resume qualitative assessment for the same reporting unit in the subsequent reporting period. The amendments in ASU 2011-08 will be effective for interim and annual goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. We will adopt the provisions of ASU 2011-08 effective January 1, 2012, and do not expect the adoption will have a material effect on our consolidated financial condition and results of operations.

#### Transfers and Servicing Topic

In April 2011, the FASB issued ASU No. 2011-03, "Reconsideration of Effective Control for Repurchase Agreements" ("ASU 2011-03"), which revises the criteria for assessing effective control for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The determination of whether the transfer of a financial asset subject to a repurchase agreement is a sale is based, in part, on whether the entity maintains effective control over the financial asset. ASU 2011-03 removes from the assessment of effective control: the criterion requiring the transferor to have the ability to repurchase or redeem the financial asset on substantially the agreed terms, even in the event of default by the transferee, and the related requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. The amendments in ASU 2011-03 will be effective for interim and annual reporting periods beginning on or after December 15, 2011, early adoption is prohibited, and the amendments will be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. We will adopt the provisions of ASU 2011-03 effective January 1, 2012, and do not expect the adoption will have a material effect on our consolidated financial condition and results of operations.

### 3. Dispositions

#### Discontinued Investment Management Operations

On January 4, 2010, we closed on the stock sale of our subsidiary Delaware Management Holdings, Inc. ("Delaware"), which provided investment products and services to individuals and institutions, to Macquarie Bank Limited. Net of tax proceeds were approximately \$405 million.

We have reclassified the results of operations of Delaware into income (loss) from discontinued operations, net of federal income taxes, for all periods presented on our Consolidated Statements of Income (Loss), and selected amounts (in millions) were as follows:

|  | For the<br>Three<br>Months<br>Ended<br>September<br>30,<br>2011 |      | For the Nine<br>Months Ended<br>September 30,<br>2010 |         |
|--|---|------|---|---------|
| Discontinued Operations Before Disposal  |   |      |   |         |
| Revenues - gain (loss) on sale of business   | \$ -  | \$ - | \$ -  | \$ 4    |
| Income (loss) from discontinued operations before disposal,<br>before federal income taxes | \$ -  | \$ - | \$ -  | \$ (13) |
| Federal income tax expense (benefit)   | -   | -    | -   | (2)     |
| Income (loss) from discontinued operations before disposal                                 | -   | -    | -   | (11)    |



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Disposal

|  |        |      |        |       |
|--|--------|------|--------|-------|
| Gain (loss) on disposal, before federal income taxes | (3)    | -    | (3)    | 37    |
| Federal income tax expense (benefit)                 | 5      | -    | 5      | 13    |
| Gain (loss) on disposal                              | (8)    | -    | (8)    | 24    |
| Income (loss) from discontinued operations           | \$ (8) | \$ - | \$ (8) | \$ 13 |

The loss from discontinued operations for the three and nine months ended September 30, 2011, related to an unfavorable tax return true-up from the prior year.

The income from discontinued operations for the nine months ended September 30, 2010, included final cash received toward the purchase price for certain institutional taxable fixed income business sold during the fourth quarter 2007, and also reflected stock compensation expense attributable to the acceleration of vesting of equity awards for certain Delaware employees upon the sale of Delaware.

## Discontinued Lincoln UK Operations

On October 1, 2009, we closed on the stock sale of Lincoln National (UK) plc (“Lincoln UK”), our subsidiary, which focused primarily on providing life and retirement income products in the United Kingdom to SLF of Canada UK Limited, and we retained Lincoln UK’s pension plan assets and liabilities.

We have reclassified the results of operations of Lincoln UK into income (loss) from discontinued operations, net of federal income taxes, for all periods presented on our Consolidated Statements of Income (Loss), and selected amounts (in millions) were as follows:

|  | For<br>the<br>Three<br>Months<br>Ended | For<br>the<br>Nine<br>Months<br>Ended |
|--|--|---------------------------------------|
|  | September<br>30,<br>2010               | September<br>30,<br>2010              |
| Disposal   |  |                                       |
| Gain (loss) on disposal, before federal income taxes | \$ 1                                   | \$ 28                                 |
| Federal income tax expense (benefit)                 | 3                                      | 12                                    |
| Gain (loss) on disposal                              | (2)                                    | 16                                    |
| Income (loss) from discontinued operations           | \$ (2)                                 | \$ 16                                 |

The loss from discontinued operations for the three months ended September 30, 2010, related to an unfavorable tax return true-up from the prior year, partially offset by the estimated transaction cost being lower than anticipated. In addition, the income from discontinued operations for the nine months ended September 30, 2010, included additional consideration received attributable to a post-closing adjustment of the purchase price based upon a final actuarial appraisal of the value of the business as set forth in the share purchase agreement, partially offset by the items mentioned above.

## 4. Variable Interest Entities (“VIEs”)

Our involvement with VIEs is primarily to invest in assets that allow us to gain exposure to a broadly diversified portfolio of asset classes. A VIE is an entity which does not have sufficient equity to finance its own activities without additional financial support or where investors lack certain characteristics of a controlling financial interest. We perform an ongoing qualitative assessment of our involvement with VIEs to determine whether we have a controlling financial interest and would therefore be considered the primary beneficiary of the VIE. If we determine we are the primary beneficiary of a VIE, we consolidate the assets and liabilities of the VIE in our consolidated financial statements.

## Consolidated VIEs

## Credit-Linked Notes

We have invested in the Class 1 Notes of two credit-linked note (“CLN”) structures, which represent special purpose trusts combining asset-backed securities with credit default swaps to produce multi-class structured securities. The

CLN structures also include subordinated Class 2 Notes, which are held by third parties, and, together with the Class 1 Notes, represent 100% of the outstanding notes of the CLN structures. The entities that issued the CLNs are financed by the note holders, and, as such, the note holders participate in the expected losses and residual returns of the entities. Because the note holders do not have voting rights or similar rights, we determined the entities issuing the CLNs are VIEs, and as a note holder, our interest represented a variable interest. We have the power to direct the most significant activity affecting the performance of both CLN structures, as we have the ability to actively manage the reference portfolio underlying the credit default swaps. As a result, we have concluded we are the primary beneficiary of the VIEs associated with the CLNs and have consolidated the assets and liabilities of both CLN structures in our Consolidated Balance Sheets.

As a result of consolidating the CLNs, we also consolidate the derivative instruments in the CLN structures. The credit default swaps create variability in the CLN structures and expose the note holders to the credit risk of the referenced portfolio. The contingent forwards transfer a portion of the loss in the underlying fixed maturity corporate asset-backed credit card loan securities back to the counterparty after credit losses reach our attachment point.

The following summarizes information regarding the CLN structures (dollars in millions) as of September 30, 2011:

|  | Amount and Date of Issuance |                        |
|--|-----------------------------|------------------------|
|  | \$400<br>December<br>2006   | \$200<br>April<br>2007 |
| Original attachment point (subordination)        | 5.50 %                      | 2.05 %                 |
| Current attachment point (subordination)         | 4.17 %                      | 1.48 %                 |
| Maturity   | 12/20/2016                  | 3/20/2017              |
| Current rating of tranche                        | B+                          | Ba2                    |
| Current rating of underlying collateral pool     | Aa1-B3                      | Aaa-Caa1               |
| Number of defaults in underlying collateral pool | 2                           | 2                      |
| Number of entities                               | 123                         | 99                     |
| Number of countries                              | 19                          | 22                     |

There has been no event of default on the CLNs themselves. Based upon our analysis, the remaining subordination as represented by the attachment point should be sufficient to absorb future credit losses, subject to changing market conditions. Similar to other debt market instruments, our maximum principal loss is limited to our original investment.

The following summarizes the exposure of the CLN structures' underlying collateral by industry and rating as of September 30, 2011:

| Industry                               | AAA   | AA     | A      | BBB    | BB    | B     | CCC   | Total   |
|--|-------|--------|--------|--------|-------|-------|-------|---------|
| Telecommunications                     | - %   | - %    | 5.5 %  | 5.1 %  | 0.6 % | - %   | - %   | 11.2 %  |
| Financial intermediaries               | 0.3 % | 4.0 %  | 5.7 %  | 0.5 %  | - %   | - %   | - %   | 10.5 %  |
| Oil and gas                            | - %   | 1.0 %  | 1.2 %  | 4.1 %  | - %   | - %   | - %   | 6.3 %   |
| Utilities                              | - %   | - %    | 3.1 %  | 1.4 %  | - %   | - %   | - %   | 4.5 %   |
| Chemicals and plastics                 | - %   | - %    | 2.3 %  | 1.2 %  | 0.4 % | - %   | - %   | 3.9 %   |
| Drugs                                  | 0.3 % | 2.2 %  | 1.2 %  | - %    | - %   | - %   | - %   | 3.7 %   |
| Retailers (except food<br>and drug)    | - %   | - %    | 1.6 %  | 1.4 %  | 0.5 % | - %   | - %   | 3.5 %   |
| Industrial equipment                   | - %   | - %    | 3.0 %  | 0.3 %  | - %   | - %   | - %   | 3.3 %   |
| Sovereign                              | - %   | 0.7 %  | 1.6 %  | 1.0 %  | - %   | - %   | - %   | 3.3 %   |
| Food products                          | - %   | 0.3 %  | 1.8 %  | 1.1 %  | - %   | - %   | - %   | 3.2 %   |
| Conglomerates                          | - %   | 2.6 %  | 0.5 %  | - %    | - %   | - %   | - %   | 3.1 %   |
| Forest products                        | - %   | - %    | - %    | 1.6 %  | 1.4 % | - %   | - %   | 3.0 %   |
| Other industry < 3%<br>(27 industries) | - %   | 2.5 %  | 15.4 % | 17.3 % | 3.6 % | 1.4 % | 0.3 % | 40.5 %  |
| Total                                  | 0.6 % | 13.3 % | 42.9 % | 35.0 % | 6.5 % | 1.4 % | 0.3 % | 100.0 % |

#### Statutory Trust Note

In August 2011, we purchased a \$100 million note issued by a statutory trust ("Issuer") in a private placement offering. The proceeds were used by the Issuer to purchase U.S. Treasury securities to be held as collateral assets supporting an excess mortality swap. Our maximum exposure to loss is limited to our original investment in the notes. We have concluded that the Issuer of the note is a VIE as the entity does not have sufficient equity to support

its activities without additional financial support. In our evaluation of the primary beneficiary, we concluded that our economic interest was disproportionately greater than our stated power, and as a result, we concluded that we are the primary beneficiary of the Issuer and as of August 1, 2011, have consolidated all of the assets and liabilities of the Issuer in our consolidated financial statements.

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Asset and liability information (dollars in millions) for these consolidated VIEs included on our Consolidated Balance Sheets was as follows:

|   | As of September 30,<br>2011 |                     |                   | As of December 31,<br>2010 |                     |                   |
|---|-----------------------------|---------------------|-------------------|----------------------------|---------------------|-------------------|
|   | Number<br>of Instruments    | Notional<br>Amounts | Carrying<br>Value | Number<br>of Instruments   | Notional<br>Amounts | Carrying<br>Value |
| <b>Assets</b>   |                             |                     |                   |                            |                     |                   |
| <b>Fixed maturity securities:</b>   |                             |                     |                   |                            |                     |                   |
| Asset-backed credit card loan   | N/A                         | \$ -                | \$ 593            | N/A                        | \$ -                | \$ 584            |
| U.S. Government bonds   | N/A                         | -                   | 107               | N/A                        | -                   | -                 |
| Excess mortality swap   | 1                           | 100                 | -                 | -                          | -                   | -                 |
| Total assets (1)  | 1                           | \$ 100              | \$ 700            | -                          | \$ -                | \$ 584            |
| <b>Liabilities</b>  |                             |                     |                   |                            |                     |                   |
| <b>Derivative instruments not designated<br/>and not qualifying as hedging<br/>instruments:</b> |                             |                     |                   |                            |                     |                   |
| Credit default swaps  | 2                           | \$ 600              | \$ 312            | 2                          | \$ 600              | \$ 215            |
| Contingent forwards   | 2                           | -                   | (5)               | 2                          | -                   | (6)               |
| Total derivative instruments not<br>designated and not qualifying<br>as hedging instruments     | 4                           | 600                 | 307               | 4                          | 600                 | 209               |
| Federal income tax  | N/A                         | -                   | (104)             | N/A                        | -                   | (77)              |
| Total liabilities (2)   | 4                           | \$ 600              | \$ 203            | 4                          | \$ 600              | \$ 132            |

(1) Reported in VIEs' fixed maturity securities on our Consolidated Balance Sheets.

(2) Reported in VIEs' liabilities on our Consolidated Balance Sheets.

For details related to the fixed maturity AFS securities for these VIEs, see Note 5.

As described more fully in Note 1 of our 2010 Form 10-K, we regularly review our investment holdings for other-than-temporary impairment ("OTTI"). Based upon this review, we believe that the fixed maturity securities were not other-than-temporarily impaired as of September 30, 2011.

The gains (losses) for these consolidated VIEs (in millions) recorded on our Consolidated Statements of Income (Loss) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |       | For the Nine<br>Months Ended<br>September 30, |         |
|--|--|-------|---|---------|
|  | 2011   | 2010  | 2011  | 2010    |
| <b>Derivative Instruments Not Designated and<br/>Not Qualifying as Hedging Instruments</b>   |  |       |   |         |
| Credit default swaps   | \$ (105)                                       | \$ 60 | \$ (92)                                       | \$ (10) |
| Contingent forwards  | 2  | (4)   | 1   | (7)     |
| Total derivative instruments not designated and<br>not qualifying as hedging instruments (1) | \$ (103)                                       | \$ 56 | \$ (91)                                       | \$ (17) |

(1) Reported in realized gain (loss) on our Consolidated Statements of Income (Loss).

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## Unconsolidated VIEs

See Note 4 in our 2010 Form 10-K for a detailed discussion of our unconsolidated VIEs.

## 5. Investments

## AFS Securities

Pursuant to the Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification™ (“ASC”), we have categorized AFS securities into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in Note 1 in our 2010 Form 10-K, which also includes additional disclosures regarding our fair value measurements.

The amortized cost, gross unrealized gains, losses and OTTI and fair value of AFS securities (in millions) were as follows:

|  | As of September 30, 2011 |             |                   |        | Fair Value |
|--|--------------------------|-------------|-------------------|--------|------------|
|  | Amortized Cost           | Gross Gains | Unrealized Losses | OTTI   |            |
| <b>Fixed Maturity Securities</b>               |                          |             |                   |        |            |
| Corporate bonds                                | \$ 52,926                | \$ 5,955    | \$ 551            | \$ 67  | \$ 58,263  |
| U.S. Government bonds                          | 239                      | 47          | -                 | -      | 286        |
| Foreign government bonds                       | 590                      | 53          | 1                 | -      | 642        |
| Mortgage-backed securities ("MBS"):            |                          |             |                   |        |            |
| Collateralized mortgage obligations ("CMOs")   | 5,001                    | 404         | 73                | 124    | 5,208      |
| Mortgage pass through securities ("MPTS")      | 3,052                    | 188         | -                 | -      | 3,240      |
| Commercial mortgage-backed securities ("CMBS") | 1,719                    | 70          | 105               | 14     | 1,670      |
| ABS CDOs                                       | 131                      | -           | 20                | -      | 111        |
| State and municipal bonds                      | 3,407                    | 571         | 9                 | -      | 3,969      |
| Hybrid and redeemable preferred securities     | 1,317                    | 55          | 170               | -      | 1,202      |
| VIEs' fixed maturity securities                | 672                      | 28          | -                 | -      | 700        |
| Total fixed maturity securities                | 69,054                   | 7,371       | 929               | 205    | 75,291     |
| <b>Equity Securities</b>                       |                          |             |                   |        |            |
| Banking securities                             | 2                        | -           | 1                 | -      | 1          |
| Insurance securities                           | 29                       | 1           | 3                 | -      | 27         |
| Other financial services securities            | 17                       | 8           | -                 | -      | 25         |
| Other securities                               | 83                       | 7           | 6                 | -      | 84         |
| Total equity securities                        | 131                      | 16          | 10                | -      | 137        |
| Total AFS securities                           | \$ 69,185                | \$ 7,387    | \$ 939            | \$ 205 | \$ 75,428  |



|  | As of December 31, 2010 |             |                   |        | Fair Value |
|--|-------------------------|-------------|-------------------|--------|------------|
|  | Amortized Cost          | Gross Gains | Unrealized Losses | OTTI   |            |
| Fixed Maturity Securities                  |                         |             |                   |        |            |
| Corporate bonds                            | \$ 48,863               | \$ 3,571    | \$ 607            | \$ 87  | \$ 51,740  |
| U.S. Government bonds                      | 150                     | 17          | 2                 | -      | 165        |
| Foreign government bonds                   | 473                     | 38          | 3                 | -      | 508        |
| MBS:                                       |                         |             |                   |        |            |
| CMOs                                       | 5,693                   | 324         | 114               | 146    | 5,757      |
| MPTS                                       | 2,980                   | 106         | 5                 | -      | 3,081      |
| CMBS                                       | 2,144                   | 95          | 180               | 6      | 2,053      |
| ABS CDOs                                   | 174                     | 22          | 13                | 9      | 174        |
| State and municipal bonds                  | 3,222                   | 27          | 94                | -      | 3,155      |
| Hybrid and redeemable preferred securities | 1,476                   | 56          | 135               | -      | 1,397      |
| VIEs' fixed maturity securities            | 570                     | 14          | -                 | -      | 584        |
| Total fixed maturity securities            | 65,745                  | 4,270       | 1,153             | 248    | 68,614     |
| Equity Securities                          |                         |             |                   |        |            |
| Banking securities                         | 61                      | -           | 3                 | -      | 58         |
| Insurance securities                       | 33                      | 4           | -                 | -      | 37         |
| Other financial services securities        | 18                      | 14          | -                 | -      | 32         |
| Other securities                           | 67                      | 7           | 4                 | -      | 70         |
| Total equity securities                    | 179                     | 25          | 7                 | -      | 197        |
| Total AFS securities                       | \$ 65,924               | \$ 4,295    | \$ 1,160          | \$ 248 | \$ 68,811  |

The amortized cost and fair value of fixed maturity AFS securities by contractual maturities (in millions) were as follows:

|  | As of September 30, 2011 |            |
|--|--------------------------|------------|
|  | Amortized Cost           | Fair Value |
| Due in one year or less  | \$ 2,330                 | \$ 2,369   |
| Due after one year through five years                                    | 12,515                   | 13,390     |
| Due after five years through ten years                                   | 21,789                   | 23,809     |
| Due after ten years  | 22,517                   | 25,494     |
| Subtotal   | 59,151                   | 65,062     |
| MBS  | 9,772                    | 10,118     |
| Asset-backed securities ("ABS") collateralized debt obligations ("CDOs") | 131                      | 111        |
| Total fixed maturity AFS securities                                      | \$ 69,054                | \$ 75,291  |

Actual maturities may differ from contractual maturities because issuers may have the right to call or pre-pay obligations.

The fair value and gross unrealized losses, including the portion of OTTI recognized in OCI, of AFS securities (dollars in millions), aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were as follows:

|   | As of September 30, 2011               |  |                               |  |               |  |
|---|--|--|-------------------------------|--|---------------|--|
|   | Less Than or Equal<br>to Twelve Months |  | Greater Than<br>Twelve Months |  | Total         |  |
|   | Fair<br>Value                          | Gross<br>Unrealized<br>Losses<br>and<br>OTTI | Fair<br>Value                 | Gross<br>Unrealized<br>Losses<br>and<br>OTTI | Fair<br>Value | Gross<br>Unrealized<br>Losses<br>and<br>OTTI |
| <b>Fixed Maturity Securities</b>                              |  |  |                               |  |               |  |
| Corporate bonds   | \$ 3,576                               | \$ 184                                       | \$ 1,405                      | \$ 434                                       | \$ 4,981      | \$ 618                                       |
| U.S. Government bonds   | 14                                     | -  | 2                             | -  | 16            | -  |
| Foreign government bonds                                      | 86                                     | 1  | -                             | -  | 86            | 1  |
| <b>MBS:</b>   |  |  |                               |  |               |  |
| CMOs  | 573                                    | 107  | 492                           | 90   | 1,065         | 197  |
| MPTS  | 2                                      | -  | 1                             | -  | 3             | -  |
| CMBS  | 221                                    | 21   | 154                           | 98   | 375           | 119  |
| ABS CDOs  | 3                                      | 1  | 87                            | 19   | 90            | 20   |
| State and municipal bonds                                     | 5                                      | -  | 28                            | 9  | 33            | 9  |
| Hybrid and redeemable<br>preferred securities                 | 277                                    | 23   | 396                           | 147  | 673           | 170  |
| Total fixed maturity securities                               | 4,757                                  | 337  | 2,565                         | 797  | 7,322         | 1,134  |
| <b>Equity Securities</b>                                      |  |  |                               |  |               |  |
| Banking securities  | 1                                      | 1  | -                             | -  | 1             | 1  |
| Insurance securities  | 24                                     | 3  | -                             | -  | 24            | 3  |
| Other securities  | 6                                      | 6  | -                             | -  | 6             | 6  |
| Total equity securities                                       | 31                                     | 10   | -                             | -  | 31            | 10   |
| Total AFS securities  | \$ 4,788                               | \$ 347                                       | \$ 2,565                      | \$ 797                                       | \$ 7,353      | \$ 1,144                                     |
| Total number of AFS securities in an unrealized loss position |  |  |                               |  |               | 952  |

|   | As of December 31, 2010                |  |                               |  |               |  |
|---|--|--|-------------------------------|--|---------------|--|
|   | Less Than or Equal<br>to Twelve Months |  | Greater Than<br>Twelve Months |  | Total         |  |
|   | Fair<br>Value                          | Gross<br>Unrealized<br>Losses<br>and<br>OTTI | Fair<br>Value                 | Gross<br>Unrealized<br>Losses<br>and<br>OTTI | Fair<br>Value | Gross<br>Unrealized<br>Losses<br>and<br>OTTI |
| Fixed Maturity Securities                     |  |  |                               |  |               |  |
| Corporate bonds                               | \$ 5,271                               | \$ 297                                       | \$ 2,007                      | \$ 397                                       | \$ 7,278      | \$ 694                                       |
| U.S. Government bonds                         | 28                                     | 2  | 2                             | -  | 30            | 2  |
| Foreign government bonds                      | 19                                     | -  | 9                             | 3  | 28            | 3  |
| MBS:  |  |  |                               |  |               |  |
| CMOs  | 465                                    | 121  | 748                           | 139  | 1,213         | 260  |
| MPTS  | 190                                    | 5  | 2                             | -  | 192           | 5  |
| CMBS  | 75                                     | 8  | 304                           | 178  | 379           | 186  |
| ABS CDOs                                      | -                                      | -  | 147                           | 22   | 147           | 22   |
| State and municipal bonds                     | 1,889                                  | 84   | 27                            | 10   | 1,916         | 94   |
| Hybrid and redeemable<br>preferred securities | 203                                    | 10   | 568                           | 125  | 771           | 135  |
| Total fixed maturity securities               | 8,140                                  | 527  | 3,814                         | 874  | 11,954        | 1,401  |
| Equity Securities                             |  |  |                               |  |               |  |
| Banking securities                            | 57                                     | 3  | -                             | -  | 57            | 3  |
| Other securities                              | 3                                      | 4  | -                             | -  | 3             | 4  |
| Total equity securities                       | 60                                     | 7  | -                             | -  | 60            | 7  |
| Total AFS securities                          | \$ 8,200                               | \$ 534                                       | \$ 3,814                      | \$ 874                                       | \$ 12,014     | \$ 1,408                                     |

Total number of AFS securities in an unrealized loss position 1,237

For information regarding our investments in VIEs, see Note 4.

We perform detailed analysis on the AFS securities backed by pools of residential and commercial mortgages that are most at risk of impairment based on factors discussed in Note 1 in our 2010 Form 10-K. Selected information for these securities in a gross unrealized loss position (in millions) was as follows:

|   | As of September 30, 2011 |               |                    |
|---|--------------------------|---------------|--------------------|
|   | Amortized<br>Cost        | Fair<br>Value | Unrealized<br>Loss |
| Total   |                          |               |                    |
| AFS securities backed by pools of residential mortgages | \$ 2,120                 | \$ 1,650      | \$ 470             |
| AFS securities backed by pools of commercial mortgages  | 532                      | 399           | 133                |
| Total   | \$ 2,652                 | \$ 2,049      | \$ 603             |
| Subject to Detailed Analysis                            |                          |               |                    |
| AFS securities backed by pools of residential mortgages | \$ 2,097                 | \$ 1,627      | \$ 470             |
| AFS securities backed by pools of commercial mortgages  | 132                      | 67            | 65                 |
| Total   | \$ 2,229                 | \$ 1,694      | \$ 535             |



|   | As of December 31, 2010 |               |                    |
|---|-------------------------|---------------|--------------------|
|   | Amortized<br>Cost       | Fair<br>Value | Unrealized<br>Loss |
| Total   |                         |               |                    |
| AFS securities backed by pools of residential mortgages | \$ 2,539                | \$ 2,006      | \$ 533             |
| AFS securities backed by pools of commercial mortgages  | 611                     | 410           | 201                |
| Total   | \$ 3,150                | \$ 2,416      | \$ 734             |
| Subject to Detailed Analysis                            |                         |               |                    |
| AFS securities backed by pools of residential mortgages | \$ 2,303                | \$ 1,776      | \$ 527             |
| AFS securities backed by pools of commercial mortgages  | 185                     | 76            | 109                |
| Total   | \$ 2,488                | \$ 1,852      | \$ 636             |

For the nine months ended September 30, 2011 and 2010, we recorded OTTI for AFS securities backed by pools of residential and commercial mortgages of \$42 million and \$114 million, pre-tax, respectively, and before associated amortization expense for DAC, value of business acquired (“VOBA”), deferred sales inducements (“DSI”) and deferred front-end loads (“DFEL”), of which \$9 million and \$25 million, respectively, was recognized in OCI and \$33 million and \$89 million, respectively, was recognized in net income (loss).

The fair value, gross unrealized losses, the portion of OTTI recognized in OCI (in millions) and number of AFS securities where the fair value had declined and remained below amortized cost by greater than 20% were as follows:

|   | As of September 30, 2011 |                               |        |                                   |
|---|--------------------------|-------------------------------|--------|-----------------------------------|
|   | Fair<br>Value            | Gross<br>Unrealized<br>Losses | OTTI   | Number<br>of<br>Securities<br>(1) |
| Less than six months                                | \$ 444                   | \$ 156                        | \$ 31  | 82                                |
| Six months or greater, but less than nine months    | 2                        | -                             | 2      | 5                                 |
| Nine months or greater, but less than twelve months | 21                       | 6                             | 3      | 9                                 |
| Twelve months or greater                            | 630                      | 450                           | 120    | 174                               |
| Total   | \$ 1,097                 | \$ 612                        | \$ 156 | 270                               |

|   | As of December 31, 2010 |                               |        |                                   |
|---|-------------------------|-------------------------------|--------|-----------------------------------|
|   | Fair<br>Value           | Gross<br>Unrealized<br>Losses | OTTI   | Number<br>of<br>Securities<br>(1) |
| Less than six months                                | \$ 170                  | \$ 73                         | \$ 5   | 41                                |
| Six months or greater, but less than nine months    | 60                      | 22                            | -      | 13                                |
| Nine months or greater, but less than twelve months | 42                      | 17                            | 1      | 13                                |
| Twelve months or greater                            | 929                     | 520                           | 184    | 224                               |
| Total   | \$ 1,201                | \$ 632                        | \$ 190 | 291                               |

(1) We may reflect a security in more than one aging category based on various purchase dates.

We regularly review our investment holdings for OTTI. Our gross unrealized losses on AFS securities decreased \$264 million for the nine months ended September 30, 2011. This change was attributable primarily to a decline in overall market yields, which was driven by market uncertainty and weakening economic activity. As discussed further below, we believe the unrealized loss position as of September 30, 2011, did not represent OTTI as we did not intend to sell these fixed maturity AFS securities, it is not more likely than not that we will be required to sell the fixed maturity AFS securities before recovery of their amortized cost basis, the estimated future cash flows were equal to or greater than the amortized cost basis of the debt securities, or we had the ability and intent to hold the equity AFS securities for a period of time sufficient for recovery.

Based upon this evaluation as of September 30, 2011, management believed we had the ability to generate adequate amounts of cash from our normal operations (e.g., insurance premiums and fees and investment income) to meet cash requirements with a prudent margin of safety without requiring the sale of our temporarily-impaired securities.

As of September 30, 2011, the unrealized losses associated with our corporate bond securities were attributable primarily to securities that were backed by commercial loans and individual issuer companies. For our corporate bond securities with commercial loans as the underlying collateral, we evaluated the projected credit losses in the underlying collateral and concluded that we had sufficient subordination or other credit enhancement when compared with our estimate of credit losses for the individual security and we expected to recover the entire amortized cost for each security. For individual issuers, we performed detailed analysis of the financial performance of the issuer and determined that we expected to recover the entire amortized cost for each security.

As of September 30, 2011, the unrealized losses associated with our MBS and ABS CDOs were attributable primarily to collateral losses and credit spreads. We assessed for credit impairment using a cash flow model as discussed above. The key assumptions included default rates, severities and prepayment rates. We estimated losses for a security by forecasting the underlying loans in each transaction. The forecasted loan performance was used to project cash flows to the various tranches in the structure, as applicable. Our forecasted cash flows also considered, as applicable, independent industry analyst reports and forecasts, sector credit ratings and other independent market data. Based upon our assessment of the expected credit losses of the security given the performance of the underlying collateral compared to our subordination or other credit enhancement, we expected to recover the entire amortized cost basis of each security.

As of September 30, 2011, the unrealized losses associated with our hybrid and redeemable preferred securities were attributable primarily to wider credit spreads caused by illiquidity in the market and subordination within the capital structure, as well as credit risk of specific issuers. For our hybrid and redeemable preferred securities, we evaluated the financial performance of the issuer based upon credit performance and investment ratings and determined we expected to recover the entire amortized cost of each security.

Changes in the amount of credit loss of OTTI recognized in net income (loss) where the portion related to other factors was recognized in OCI (in millions) on fixed maturity AFS securities were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        | For the Nine<br>Months Ended<br>September 30, |        |
|--|--|--------|---|--------|
|  | 2011   | 2010   | 2011  | 2010   |
| Balance as of beginning-of-period  | \$ 340   | \$ 293 | \$ 319  | \$ 268 |
| Increases attributable to:   |  |        |   |        |
| Credit losses on securities for which an OTTI was not previously<br>recognized | 11   | 6      | 40  | 7      |
| Credit losses on securities for which an OTTI was previously<br>recognized     | 17   | 14     | 57  | 53     |
| Decreases attributable to:   |  |        |   |        |
| Securities sold  | (6)  | (6)    | (54)  | (21)   |
| Balance as of end-of-period  | \$ 362   | \$ 307 | \$ 362  | \$ 307 |

During the three and nine months ended September 30, 2011, we recorded credit losses on securities for which an OTTI was not previously recognized as we determined the cash flows expected to be collected would not be sufficient to recover the entire amortized cost basis of the debt security. The credit losses we recorded on securities for which an OTTI was not previously recognized were attributable primarily to one or a combination of the following reasons:

- Failure of the issuer of the security to make scheduled payments;
- Deterioration of creditworthiness of the issuer;
- Deterioration of conditions specifically related to the security;
- Deterioration of fundamentals of the industry in which the issuer operates;
- Deterioration of fundamentals in the economy including, but not limited to, higher unemployment and lower housing prices; and
- Deterioration of the rating of the security by a rating agency.



We recognize the OTTI attributed to the noncredit portion as a separate component in OCI referred to as unrealized OTTI on AFS securities.

Details of the amount of credit loss of OTTI recognized in net income (loss) where the portion related to other factors was recognized in OCI (in millions), were as follows:

|                 |       | As of September 30, 2011 |       |          |            | OTTI             |
|-----------------|-------|--------------------------|-------|----------|------------|------------------|
|                 |       | Gross Unrealized Losses  |       |          | Fair Value | in Credit Losses |
|                 |       | Amortized Cost           | Gains | and OTTI |            |                  |
| Corporate bonds |       | \$ 168                   | \$ 1  | \$ 66    | \$ 103     | \$ 46            |
| MBS:            |       |                          |       |          |            |                  |
|                 | CMOs  | 640                      | 1     | 118      | 523        | 288              |
|                 | CMBS  | 21                       | -     | 14       | 7          | 28               |
|                 | Total | \$ 829                   | \$ 2  | \$ 198   | \$ 633     | \$ 362           |

|                 |       | As of December 31, 2010 |       |          |            | OTTI             |
|-----------------|-------|-------------------------|-------|----------|------------|------------------|
|                 |       | Gross Unrealized Losses |       |          | Fair Value | in Credit Losses |
|                 |       | Amortized Cost          | Gains | and OTTI |            |                  |
| Corporate bonds |       | \$ 204                  | \$ 3  | \$ 76    | \$ 131     | \$ 60            |
| MBS:            |       |                         |       |          |            |                  |
|                 | CMOs  | 509                     | 2     | 126      | 385        | 258              |
|                 | CMBS  | 6                       | -     | 5        | 1          | 1                |
|                 | Total | \$ 719                  | \$ 5  | \$ 207   | \$ 517     | \$ 319           |

Mortgage Loans on Real Estate

Mortgage loans on real estate principally involve commercial real estate. The commercial loans are geographically diversified throughout the U.S. with the largest concentrations in California and Texas, which accounted for approximately 33% and 30% of mortgage loans on real estate as of September 30, 2011, and December 31, 2010, respectively.

The following provides the current and past due composition of our mortgage loans on real estate (in millions):

|  | As of September 30, 2011 | As of December 31, 2010 |
|--|--------------------------|-------------------------|
| Current  | \$ 6,806                 | \$ 6,697                |
| 60 to 90 days past due   | 26                       | 8                       |
| Greater than 90 days past due  | 68                       | 40                      |
| Valuation allowance associated with impaired mortgage loans on real estate | (22)                     | (13)                    |
| Unamortized premium (discount)   | 15                       | 20                      |
| Total carrying value   | \$ 6,893                 | \$ 6,752                |



The number of impaired mortgage loans on real estate, each of which had an associated specific valuation allowance, and the carrying value of impaired mortgage loans on real estate (dollars in millions) were as follows:

|  | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|--|-----------------------------------|----------------------------------|
| Number of impaired mortgage loans on real estate                           | 10                                | 9                                |
| Principal balance of impaired mortgage loans on real estate                | \$ 79                             | \$ 75                            |
| Valuation allowance associated with impaired mortgage loans on real estate | (22)                              | (13)                             |
| Carrying value of impaired mortgage loans on real estate                   | \$ 57                             | \$ 62                            |

Changes in the valuation allowance for credit losses associated with impaired mortgage loans on real estate (in millions) were as follows:

|                                 | For<br>the<br>Nine<br>Months<br>Ended<br>September<br>30,<br>2011 |
|---------------------------------|---|
| Balance as of beginning-of-year | \$ 13   |
| Additions                       | 14  |
| Charge-offs                     | (5)   |
| Balance as of end-of-period     | \$ 22   |

Information for our impaired mortgage loans on real estate (in millions) was as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |
|--|--|-------|---|-------|
| Average carrying value for impaired mortgage loans on real estate    | \$ 58  | \$ 61 | \$ 55   | \$ 53 |
| Interest income recognized on impaired mortgage loans on real estate | -  | -     | 2   | 1     |
| Interest income collected on impaired mortgage loans on real estate  | -  | -     | 2   | 1     |

As described in Note 1 in our 2010 Form 10-K, we use the loan-to-value and debt-service coverage ratios as credit quality indicators for our mortgage loans on real estate, which were as follows (dollars in millions):

|               | As of September 30, 2011 |        |                                       | As of December 31, 2010 |        |                                       |
|---------------|--------------------------|--------|---------------------------------------|-------------------------|--------|---------------------------------------|
|               | Principal<br>Amount      | %      | Debt-<br>Service<br>Coverage<br>Ratio | Principal<br>Amount     | %      | Debt-<br>Service<br>Coverage<br>Ratio |
| Loan-to-Value |                          |        |                                       |                         |        |                                       |
| Less than 65% | \$ 5,343                 | 77.4 % | 1.60                                  | \$ 4,863                | 72.1 % | 1.62                                  |
| 65% to 74%    | 1,148                    | 16.7 % | 1.37                                  | 1,484                   | 22.0 % | 1.40                                  |

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|                                     |          |         |      |          |         |      |
|-------------------------------------|----------|---------|------|----------|---------|------|
| 75% to 100%                         | 319      | 4.6 %   | 0.86 | 179      | 2.7 %   | 0.85 |
| Greater than 100%                   | 90       | 1.3 %   | 0.26 | 219      | 3.2 %   | 1.06 |
| Total mortgage loans on real estate | \$ 6,900 | 100.0 % |      | \$ 6,745 | 100.0 % |      |

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## Alternative Investments

As of September 30, 2011, and December 31, 2010, alternative investments included investments in approximately 97 and 95 different partnerships, respectively, and the portfolio represented less than 1% of our overall invested assets.

## Realized Gain (Loss) Related to Certain Investments

The detail of the realized gain (loss) related to certain investments (in millions) was as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |         | For the Nine<br>Months Ended<br>September 30,<br>2010 |         |
|--|--|---------|---|---------|
| Fixed maturity AFS securities:   |  |         |   |         |
| Gross gains  | \$ 17  | \$ 12   | \$ 84   | \$ 96   |
| Gross losses   | (63)   | (61)    | (177)   | (174)   |
| Equity AFS securities:   |  |         |   |         |
| Gross gains  | -  | 3       | 10  | 9       |
| Gross losses   | -  | -       | -   | (4)     |
| Gain (loss) on other investments   | (3)  | (2)     | 1   | (33)    |
| Associated amortization of DAC, VOBA, DSI and DFEL<br>and changes in other contract holder funds | 5  | 22      | (13)  | 20      |
| Total realized gain (loss) related to certain<br>investments                                     | \$ (44)  | \$ (26) | \$ (95)   | \$ (86) |

Details underlying write-downs taken as a result of OTTI (in millions) that were recognized in net income (loss) and included in realized gain (loss) on AFS securities above, and the portion of OTTI recognized in OCI (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30,<br>2011 |         | For the Nine<br>Months Ended<br>September 30,<br>2010 |         |
|---|--|---------|---|---------|
| OTTI Recognized in Net Income (Loss)                  |  |         |   |         |
| Fixed maturity securities:                            |  |         |   |         |
| Corporate bonds                                       | \$ (3)   | \$ (34) | \$ (9)  | \$ (80) |
| MBS:  |  |         |   |         |
| CMOs  | (22)   | (16)    | (65)  | (52)    |
| CMBS  | (8)  | (4)     | (47)  | (4)     |
| ABS CDOs  | -  | -       | (1)   | (1)     |
| Hybrid and redeemable preferred securities            | -  | -       | (2)   | (5)     |
| Total fixed maturity securities                       | (33)   | (54)    | (124)   | (142)   |
| Equity securities:                                    |  |         |   |         |
| Other financial services securities                   | -  | -       | -   | (3)     |
| Total equity securities                               | -  | -       | -   | (3)     |
| Gross OTTI recognized in net income (loss)            | (33)   | (54)    | (124)   | (145)   |
| Associated amortization of DAC, VOBA, DSI and<br>DFEL | 8  | 8       | 30  | 35      |

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|  |                                   |         |         |          |
|--|-----------------------------------|---------|---------|----------|
|  | Net OTTI recognized in net income |         |         |          |
|  | (loss), pre-tax                   |         |         |          |
|  | \$ (25)                           | \$ (46) | \$ (94) | \$ (110) |
| Portion of OTTI Recognized in OCI              |                                   |         |         |          |
| Gross OTTI recognized in OCI                   | \$ 21                             | \$ 62   | \$ 48   | \$ 84    |
| Change in DAC, VOBA, DSI and DFEL              | (4)                               | (9)     | (9)     | (7)      |
| Net portion of OTTI recognized in OCI, pre-tax | \$ 17                             | \$ 53   | \$ 39   | \$ 77    |

### Determination of Credit Losses on Corporate Bonds and ABS CDOs

As of September 30, 2011, and December 31, 2010, we reviewed our corporate bond and ABS CDO portfolios for potential shortfall in contractual principal and interest based on numerous subjective and objective inputs. The factors used to determine the amount of credit loss for each individual security, include, but are not limited to, near term risk, substantial discrepancy between book and market value, sector or company-specific volatility, negative operating trends and trading levels wider than peers.

Credit ratings express opinions about the credit quality of a security. Securities rated investment grade, that is those rated BBB- or higher by Standard & Poor's ("S&P") Rating Services or Baa3 or higher by Moody's Investors Service ("Moody's"), are generally considered by the rating agencies and market participants to be low credit risk. As of September 30, 2011, and December 31, 2010, 97% and 95%, respectively, of the fair value of our corporate bond portfolio was rated investment grade. As of September 30, 2011, and December 31, 2010, the portion of our corporate bond portfolio rated below investment grade had an amortized cost of \$2.3 billion and \$2.6 billion and a fair value of \$2.1 billion and \$2.4 billion, respectively. As of September 30, 2011, and December 31, 2010, 89% and 91%, respectively, of the fair value of our ABS CDO portfolio was rated investment grade. As of September 30, 2011, and December 31, 2010, the portion of our ABS CDO portfolio rated below investment grade had an amortized cost of \$25 million and \$24 million and fair value of \$13 million and \$16 million, respectively. Based upon the analysis discussed above, we believed as of September 30, 2011, and December 31, 2010, that we would recover the amortized cost of each investment grade corporate bond and ABS CDO security.

For securities where we recorded an OTTI recognized in net income (loss) for the nine months ended September 30, 2011 and 2010, the recovery as a percentage of amortized cost was 98% and 80% for corporate bonds, respectively, and 0% for ABS CDOs for both periods.

### Determination of Credit Losses on MBS

As of September 30, 2011, and December 31, 2010, default rates were projected by considering underlying MBS loan performance and collateral type. Projected default rates on existing delinquencies vary between 25% to 100% depending on loan type and severity of delinquency status. In addition, we estimate the potential contributions of currently performing loans that may become delinquent in the future based on the change in delinquencies and loan liquidations experienced in the recent history. Finally, we develop a default rate timing curve by aggregating the defaults for all loans (delinquent loans, foreclosure and real estate owned and new delinquencies from currently performing loans) in the pool to project the future expected cash flows.

We use certain available loan characteristics such as lien status, loan sizes and occupancy to estimate the loss severity of loans. Second lien loans are assigned 100% severity, if defaulted. For first lien loans, we assume a minimum of 30% severity with higher severity assumed for investor properties and further housing price depreciation.

### Payables for Collateral on Investments

The carrying values of the payables for collateral on investments (in millions) included on our Consolidated Balance Sheets and the fair value of the related investments or collateral consisted of the following:

|  | As of September<br>30, 2011 |               | As of December<br>31, 2010 |               |
|--|-----------------------------|---------------|----------------------------|---------------|
|  | Carrying<br>Value           | Fair<br>Value | Carrying<br>Value          | Fair<br>Value |
| Collateral payable held for derivative investments (1) | \$ 2,593                    | \$ 2,593      | \$ 800                     | \$ 800        |

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|  |          |          |          |          |
|--|----------|----------|----------|----------|
| Securities pledged under securities lending agreements (2)                                 | 198      | 191      | 199      | 192      |
| Securities pledged under reverse repurchase agreements (3)                                 | 280      | 295      | 280      | 294      |
| Securities pledged for Term Asset-Backed Securities<br>Loan Facility ("TALF") (4)          | 184      | 211      | 280      | 318      |
| Investments pledged for Federal Home Loan Bank of<br>Indianapolis Securities ("FHLBI") (5) | 600      | 1,037    | 100      | 115      |
| Total payables for collateral on investments   | \$ 3,855 | \$ 4,327 | \$ 1,659 | \$ 1,719 |

- (1) We obtain collateral based upon contractual provisions with our counterparties. These agreements take into consideration the counterparties' credit rating as compared to ours, the fair value of the derivative investments and specified thresholds that once exceeded result in the receipt of cash that is typically invested in cash and invested cash. See Note 6 for details about maximum collateral potentially required to post on our credit default swaps.



- (2) Our pledged securities under securities lending agreements are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We generally obtain collateral in an amount equal to 102% and 105% of the fair value of the domestic and foreign securities, respectively. We value collateral daily and obtain additional collateral when deemed appropriate. The cash received in our securities lending program is typically invested in cash and invested cash or fixed maturity AFS securities.
- (3) Our pledged securities under reverse repurchase agreements are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We obtain collateral in an amount equal to 95% of the fair value of the securities, and our agreements with third parties contain contractual provisions to allow for additional collateral to be obtained when necessary. The cash received in our reverse repurchase program is typically invested in fixed maturity AFS securities.
- (4) Our pledged securities for TALF are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We obtain collateral in an amount that has typically averaged 90% of the fair value of the TALF securities. The cash received in these transactions is invested in fixed maturity AFS securities.
- (5) Our pledged investments for FHLBI are included in fixed maturity AFS securities and mortgage loans on real estate on our Consolidated Balance Sheets. We generally obtain collateral in an amount equal to 85% to 95% of the fair value of the FHLBI securities. The cash received in these transactions is typically invested in cash and invested cash or fixed maturity AFS securities.

Increase (decrease) in payables for collateral on investments (in millions) included on the Consolidated Statements of Cash Flows consisted of the following:

|  | For the Nine<br>Months Ended<br>September 30, |          |
|--|---|----------|
|  | 2011  | 2010     |
| Collateral payable held for derivative investments                     | \$ 1,793                                      | \$ 1,053 |
| Securities pledged under securities lending agreements                 | (1)   | (301)    |
| Securities pledged under reverse repurchase agreements                 | -   | (64)     |
| Securities pledged for TALF  | (96)  | (28)     |
| Securities pledged for FHLBI   | 500   | -        |
| Total increase (decrease) in payables for<br>collateral on investments | \$ 2,196                                      | \$ 660   |

#### Investment Commitments

As of September 30, 2011, our investment commitments were \$627 million, which included \$271 million of limited partnerships ("LPs"), \$194 million of private placements and \$162 million of mortgage loans on real estate.

#### Concentrations of Financial Instruments

As of September 30, 2011, and December 31, 2010, our most significant investments in one issuer were our investments in securities issued by the Federal Home Loan Mortgage Corporation with a fair value of \$5.1 billion and \$5.0 billion, or 6% of our invested assets portfolio, respectively, and our investments in securities issued by Fannie Mae with a fair value of \$2.8 billion and \$2.9 billion, or 3% of our invested assets portfolio, respectively. These investments are included in corporate bonds in the tables above.

As of September 30, 2011, and December 31, 2010, our most significant investments in one industry were our investment securities in the electric industry with a fair value of \$7.6 billion and \$6.7 billion, or 8% of our invested assets portfolio, respectively, and our investment securities in the CMO industry with a fair value of \$5.9 billion and

\$6.5 billion, or 6% and 8% of our invested assets portfolio, respectively. We utilized the industry classifications to obtain the concentration of financial instruments amount; as such, this amount will not agree to the AFS securities table above.

## 6. Derivative Instruments

### Types of Derivative Instruments and Derivative Strategies

We maintain an overall risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate risk, foreign currency exchange risk, equity market risk, default risk, basis risk and credit risk. We assess these risks by continually identifying and monitoring changes in interest rate exposure, foreign currency exposure, equity market exposure and credit exposure that may adversely affect expected future cash flows and by evaluating hedging opportunities. Derivative instruments that are used as part of our interest rate risk management strategy include interest rate swap agreements, interest rate cap agreements, interest rate futures, forward-starting interest rate swaps, consumer price index swaps, interest rate cap corridors, treasury locks and reverse treasury locks. Derivative instruments that are used as part of our foreign currency risk management strategy include foreign currency swaps, currency futures and foreign currency forwards. Call options based on our stock, call options based on the S&P 500 Index® (“S&P 500”), total return swaps, variance swaps, equity collars, put options and equity futures are used as part of our equity market risk management strategy. We also use credit default swaps as part of our credit risk management strategy.

We evaluate and recognize our derivative instruments in accordance with the Derivatives and Hedging Topic of the FASB ASC. As of September 30, 2011, we had derivative instruments that were designated and qualifying as cash flow hedges and fair value hedges. We also had embedded derivatives that were economic hedges, but were not designed to meet the requirements for hedge accounting treatment. See Note 1 in our 2010 Form 10-K for a detailed discussion of the accounting treatment for derivative instruments.

Our derivative instruments are monitored by our Asset Liability Management Committee and our Equity Risk Management Committee as part of those committees’ oversight of our derivative activities. Our committees are responsible for implementing various hedging strategies that are developed through their analysis of financial simulation models and other internal and industry sources. The resulting hedging strategies are incorporated into our overall risk management strategies.

We use a hedging strategy designed to mitigate the risk and income statement volatility caused by changes in the equity markets, interest rates and volatility associated with living benefit guarantees offered in our variable annuity products, including products with guaranteed withdrawal benefit (“GWB”) features and guaranteed income benefit (“GIB”) features. See “Guaranteed Living Benefit (“GLB”) Reserves Embedded Derivatives” below for further details.

See Note 14 for additional disclosures related to the fair value of our financial instruments and see Note 4 for derivative instruments related to our consolidated VIEs.

We have derivative instruments with off-balance-sheet risks whose notional or contract amounts exceed the credit exposure. Outstanding derivative instruments with off-balance-sheet risks (dollars in millions) were as follows:

|   | As of September 30, 2011 |           |                |          |               |            |
|---|--------------------------|-----------|----------------|----------|---------------|------------|
|   | Number                   | Notional  | Asset Carrying |          | (Liability)   |            |
|   | of                       | Amounts   | or Fair Value  | Loss     | or Fair Value | Loss       |
|   | Instruments              |           | Gain           |          | Gain          |            |
| <b>Derivative Instruments</b>                 |                          |           |                |          |               |            |
| Designated and Qualifying                     |                          |           |                |          |               |            |
| as Hedging Instruments                        |                          |           |                |          |               |            |
| Cash flow hedges:                             |                          |           |                |          |               |            |
| Interest rate swap agreements (1)             | 148                      | \$ 877    | \$ 34          | \$ (222) | \$ -          | \$ -       |
| Forward-starting interest rate swaps (1)      | 3                        | 60        | -              | -        | -             | -          |
| Foreign currency swaps (1)                    | 13                       | 340       | 47             | (14)     | -             | -          |
| Treasury and reverse treasury locks (1)       | 12                       | 1,600     | 320            | (10)     | -             | -          |
| Total cash flow hedges                        | 176                      | 2,877     | 401            | (246)    | -             | -          |
| Fair value hedges:                            |                          |           |                |          |               |            |
| Interest rate swap agreements (2)             | 11                       | 1,675     | 277            | -        | -             | (277)      |
| Total fair value hedges                       | 11                       | 1,675     | 277            | -        | -             | (277)      |
| Total derivative instruments                  |                          |           |                |          |               |            |
| designated and qualifying as                  |                          |           |                |          |               |            |
| hedging instruments                           | 187                      | 4,552     | 678            | (246)    | -             | (277)      |
| <b>Derivative Instruments Not</b>             |                          |           |                |          |               |            |
| Designated and Not Qualifying                 |                          |           |                |          |               |            |
| as Hedging Instruments                        |                          |           |                |          |               |            |
| Interest rate futures (1)                     | 5,241                    | 935       | -              | -        | -             | -          |
| Equity futures (1)                            | 28,409                   | 1,724     | -              | -        | -             | -          |
| Interest rate swap agreements (1)             | 106                      | 10,076    | 887            | (505)    | -             | -          |
| Credit default swaps - buying protection (1)  | 3                        | 35        | 6              | -        | -             | -          |
| Credit default swaps - selling protection (3) | 9                        | 148       | -              | -        | -             | (15)       |
| Total return swaps (1)                        | 24                       | 2,597     | 101            | (12)     | -             | -          |
| Put options (1)                               | 172                      | 6,477     | 1,878          | (18)     | -             | -          |
| Call options (based on S&P 500) (1)           | 545                      | 4,778     | 118            | -        | -             | -          |
| Variance swaps (1)                            | 74                       | 40        | 125            | (14)     | -             | -          |
| Currency futures (1)                          | 18                       | 3         | -              | -        | -             | -          |
| Consumer price index swaps (1)                | 98                       | 51        | -              | (3)      | -             | -          |
| Interest rate cap corridors (1)               | 88                       | 16,625    | 34             | -        | -             | -          |
| Embedded derivatives:                         |                          |           |                |          |               |            |
| Deferred compensation plans (3)               | 6                        | -         | -              | -        | -             | (325)      |
| Indexed annuity contracts (4)                 | 145,862                  | -         | -              | -        | -             | (342)      |
| GLB reserves (4)                              | 330,244                  | -         | -              | -        | 503           | (2,846)    |
| Reinsurance related (5)                       | -                        | -         | -              | -        | -             | (177)      |
| Total derivative instruments not              |                          |           |                |          |               |            |
| designated and not qualifying as              |                          |           |                |          |               |            |
| hedging instruments                           | 510,899                  | 43,489    | 3,149          | (552)    | 503           | (3,705)    |
| Total derivative                              |                          |           |                |          |               |            |
| instruments                                   | 511,086                  | \$ 48,041 | \$ 3,827       | \$ (798) | \$ 503        | \$ (3,982) |



|   | As of December 31, 2010 |           |                |          |               |            |
|---|-------------------------|-----------|----------------|----------|---------------|------------|
|   | Number                  | Notional  | Asset Carrying |          | (Liability)   |            |
|   | of                      | Amounts   | or Fair Value  | Loss     | Carrying      |            |
|   | Instruments             |           | Gain           |          | or Fair Value | Loss       |
| Derivative Instruments  |                         |           |                |          |               |            |
| Designated and Qualifying<br>as Hedging Instruments   |                         |           |                |          |               |            |
| Cash flow hedges:   |                         |           |                |          |               |            |
| Interest rate swap agreements (1)   | 151                     | \$ 926    | \$ 24          | \$ (71)  | \$ -          | \$ -       |
| Forward-starting interest rate swaps (1)  | 2                       | 150       | 1              | -        | -             | -          |
| Foreign currency swaps (1)  | 13                      | 340       | 43             | (13)     | -             | -          |
| Reverse treasury locks (1)  | 5                       | 1,000     | 11             | (5)      | -             | -          |
| Total cash flow hedges  | 171                     | 2,416     | 79             | (89)     | -             | -          |
| Fair value hedges:  |                         |           |                |          |               |            |
| Interest rate swap agreements (2)   | 11                      | 1,675     | 106            | (51)     | -             | (55)       |
| Total fair value hedges   | 11                      | 1,675     | 106            | (51)     | -             | (55)       |
| Total derivative instruments<br>designated and qualifying as<br>hedging instruments         | 182                     | 4,091     | 185            | (140)    | -             | (55)       |
| Derivative Instruments Not<br>Designated and Not Qualifying<br>as Hedging Instruments       |                         |           |                |          |               |            |
| Interest rate cap agreements (1)  | 3                       | 150       | -              | -        | -             | -          |
| Interest rate futures (1)   | 15,881                  | 2,251     | -              | -        | -             | -          |
| Equity futures (1)  | 13,375                  | 907       | -              | -        | -             | -          |
| Interest rate swap agreements (1)   | 81                      | 7,955     | 34             | (511)    | -             | -          |
| Credit default swaps (3)  | 9                       | 145       | -              | -        | -             | (16)       |
| Total return swaps (1)  | 9                       | 900       | -              | (21)     | -             | -          |
| Put options (1)   | 145                     | 5,602     | 1,151          | -        | -             | -          |
| Call options (based on S&P 500) (1)   | 544                     | 4,083     | 301            | -        | -             | -          |
| Variance swaps (1)  | 50                      | 30        | 46             | (34)     | -             | -          |
| Currency futures (1)  | 1,589                   | 219       | -              | -        | -             | -          |
| Consumer price index swaps (1)  | 100                     | 55        | -              | (2)      | -             | -          |
| Interest rate cap corridors (1)   | 73                      | 8,050     | 52             | -        | -             | -          |
| Embedded derivatives:   |                         |           |                |          |               |            |
| Deferred compensation plans (3)   | 6                       | -         | -              | -        | -             | (363)      |
| Indexed annuity contracts (4)   | 132,260                 | -         | -              | -        | -             | (497)      |
| GLB reserves (4)  | 305,962                 | -         | -              | -        | 518           | (926)      |
| Reinsurance related (5)   | -                       | -         | -              | -        | -             | (102)      |
| AFS securities (1)  | 1                       | -         | 15             | -        | -             | -          |
| Total derivative instruments not<br>designated and not qualifying as<br>hedging instruments | 470,088                 | 30,347    | 1,599          | (568)    | 518           | (1,904)    |
| Total derivative<br>instruments   | 470,270                 | \$ 34,438 | \$ 1,784       | \$ (708) | \$ 518        | \$ (1,959) |

(1) Reported in derivative investments on our Consolidated Balance Sheets.

(2)

The asset is reported in derivative investments and the liability in long-term debt on our Consolidated Balance Sheets.

- (3) Reported in other liabilities on our Consolidated Balance Sheets.
- (4) Reported in future contract benefits on our Consolidated Balance Sheets.
- (5) Reported in reinsurance related embedded derivatives on our Consolidated Balance Sheets.

The maturity of the notional amounts of derivative instruments (in millions) was as follows:

|  | Remaining Life as of September 30, 2011 |                |                 |                  |                     | Total     |
|--|---|----------------|-----------------|------------------|---------------------|-----------|
|  | Less Than<br>1 Year                     | 1 – 5<br>Years | 6 – 10<br>Years | 11 – 30<br>Years | Over<br>30<br>Years |           |
| Derivative Instruments   |   |                |                 |                  |                     |           |
| Designated and Qualifying<br>as Hedging Instruments  |   |                |                 |                  |                     |           |
| Cash flow hedges:  |   |                |                 |                  |                     |           |
| Interest rate swap agreements  | \$ -                                    | \$ 59          | \$ 264          | \$ 547           | \$ 7                | \$ 877    |
| Forward-starting interest rate swaps   | -                                       | -              | 60              | -                | -                   | 60        |
| Foreign currency swaps   | -                                       | 154            | 105             | 81               | -                   | 340       |
| Treasury and reverse treasury locks  | 300                                     | 1,090          | 210             | -                | -                   | 1,600     |
| Total cash flow hedges   | 300                                     | 1,303          | 639             | 628              | 7                   | 2,877     |
| Fair value hedges:   |   |                |                 |                  |                     |           |
| Interest rate swap agreements  | 300                                     | 500            | -               | 875              | -                   | 1,675     |
| Total fair value hedges  | 300                                     | 500            | -               | 875              | -                   | 1,675     |
| Total derivative instruments<br>designated and qualifying as<br>hedging instruments            | 600                                     | 1,803          | 639             | 1,503            | 7                   | 4,552     |
| Derivative Instruments Not<br>Designated and Not Qualifying<br>as Hedging Instruments          |   |                |                 |                  |                     |           |
| Interest rate futures  | 935                                     | -              | -               | -                | -                   | 935       |
| Equity futures   | 1,724                                   | -              | -               | -                | -                   | 1,724     |
| Interest rate swap agreements  | 258                                     | 1,594          | 1,970           | 6,254            | -                   | 10,076    |
| Credit default swaps - buying protection   | -                                       | 35             | -               | -                | -                   | 35        |
| Credit default swaps - selling protection  | -                                       | 40             | 108             | -                | -                   | 148       |
| Total return swaps   | 2,447                                   | 150            | -               | -                | -                   | 2,597     |
| Put options  | -                                       | 1,814          | 4,663           | -                | -                   | 6,477     |
| Call options (based on S&P 500)  | 3,786                                   | 992            | -               | -                | -                   | 4,778     |
| Variance swaps   | -                                       | 3              | 37              | -                | -                   | 40        |
| Currency futures   | 3                                       | -              | -               | -                | -                   | 3         |
| Consumer price index swaps   | 4                                       | 15             | 13              | 17               | 2                   | 51        |
| Interest rate cap corridors  | -                                       | 7,750          | 8,875           | -                | -                   | 16,625    |
| Total derivative instruments<br>not designated and not<br>qualifying as hedging<br>instruments | 9,157                                   | 12,393         | 15,666          | 6,271            | 2                   | 43,489    |
| Total derivative instruments<br>with notional amounts  | \$ 9,757                                | \$ 14,196      | \$ 16,305       | \$ 7,774         | \$ 9                | \$ 48,041 |



The change in our unrealized gain (loss) on derivative instruments in accumulated OCI (in millions) was as follows:

|   | For the Nine<br>Months Ended<br>September 30, |         |
|---|---|---------|
|   | 2011  | 2010    |
| Unrealized Gain (Loss) on Derivative Instruments                              |   |         |
| Balance as of beginning-of-year   | \$ (15)                                       | \$ 11   |
| Other comprehensive income (loss):  |   |         |
| Unrealized holding gains (losses) arising during the period:                  |   |         |
| Cash flow hedges:   |   |         |
| Interest rate swap agreements   | (147)   | (91)    |
| Forward-starting interest rate swaps  | (2)   | -       |
| Foreign currency swaps  | 7   | 20      |
| Treasury and reverse treasury locks   | 327   | (29)    |
| Fair value hedges:  |   |         |
| Interest rate swap agreements   | 3   | 3       |
| Change in foreign currency exchange rate adjustment                           | (1)   | 8       |
| Change in DAC, VOBA, DSI and DFEL   | (1)   | (10)    |
| Income tax benefit (expense)  | (65)  | 35      |
| Less:   |   |         |
| Reclassification adjustment for gains (losses) included in net income (loss): |   |         |
| Cash flow hedges:   |   |         |
| Interest rate swap agreements (1)   | (6)   | 5       |
| Foreign currency swaps (1)  | 3   | 2       |
| Treasury and reverse treasury locks (2)                                       | (3)   | 3       |
| Fair value hedges:  |   |         |
| Interest rate swap agreements (2)   | 3   | 3       |
| Associated amortization of DAC, VOBA, DSI and DFEL                            | -   | (1)     |
| Income tax benefit (expense)  | 1   | (4)     |
| Balance as of end-of-period   | \$ 108  | \$ (61) |

(1) The OCI offset is reported within net investment income on our Consolidated Statements of Income (Loss).

(2) The OCI offset is reported within interest and debt expense on our Consolidated Statements of Income (Loss).

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The gains (losses) on derivative instruments (in millions) recorded within income (loss) from continuing operations on our Consolidated Statements of Income (Loss) were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |         | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |
|--|--|---------|---|-------|
| Derivative Instruments Designated and<br>Qualifying as Hedging Instruments               |  |         |   |       |
| Cash flow hedges:  |  |         |   |       |
| Interest rate swap agreements (1)  | \$   | (2)     | \$  | (3)   |
| Foreign currency swaps (1)   |  | 2       |   | 1     |
| Total cash flow hedges   |  | -       |   | (2)   |
| Fair value hedges:   |  |         |   |       |
| Interest rate swap agreements (2)  |  | 13      |   | 12    |
| Equity collars (3)   |  | -       |   | 15    |
| Total fair value hedges  |  | 13      |   | 27    |
| Total derivative instruments designated<br>and qualifying as hedging instruments         |  | 13      |   | 25    |
| Derivative Instruments Not Designated and<br>Not Qualifying as Hedging Instruments       |  |         |   |       |
| Interest rate futures (3)  |  | 132     |   | 134   |
| Equity futures (3)   |  | 105     |   | (184) |
| Interest rate swap agreements (3)  |  | 850     |   | 10    |
| Foreign currency forwards (3)  |  | -       |   | -     |
| Credit default swaps - fees (1)  |  | -       |   | -     |
| Credit default swaps - buying protection - marked-to-market (1)                          |  | (1)     |   | -     |
| Credit default swaps - selling protection - marked-to-market (3)                         |  | (8)     |   | 12    |
| Total return swaps (4)   |  | 154     |   | (110) |
| Put options (3)  |  | 606     |   | (148) |
| Call options (based on S&P 500) (3)  |  | (140)   |   | 70    |
| Variance swaps (3)   |  | 126     |   | (56)  |
| Currency futures (3)   |  | (5)     |   | (8)   |
| Consumer price index swaps (3)   |  | (3)     |   | (4)   |
| Interest rate cap corridors (1)  |  | (25)    |   | (4)   |
| Embedded derivatives:  |  |         |   |       |
| Deferred compensation plans (4)  |  | 22      |   | (14)  |
| Indexed annuity contracts (3)  |  | 135     |   | (70)  |
| GLB reserves (3)   |  | (2,065) |   | 188   |
| Reinsurance related (3)  |  | (58)    |   | (40)  |
| AFS securities (1)   |  | -       |   | 1     |
| Total derivative instruments not designated<br>and not qualifying as hedging instruments |  | (175)   |   | (223) |
| Total derivative instruments   | \$   | (162)   | \$  | (198) |
|  |  |         | \$  | (255) |
|  |  |         | \$  | (145) |

- (1) Reported in net investment income on our Consolidated Statements of Income (Loss).  
(2) Reported in interest and debt expense on our Consolidated Statements of Income (Loss).  
(3) Reported in realized gain (loss) on our Consolidated Statements of Income (Loss).  
(4)

Reported in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income (Loss).

The location in the Consolidated Statements of Income (Loss) where the gains (losses) are recorded for each of the derivative instruments discussed below is specified in the table above.

## Derivative Instruments Designated and Qualifying as Cash Flow Hedges

Gains (losses) (in millions) on derivative instruments designated and qualifying as cash flow hedges were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |      |
|--|--|--------|---|------|
| Gain (loss) recognized as a component of OCI with the offset<br>to net investment income | \$ -   | \$ (3) | \$ (4)  | \$ 7 |

As of September 30, 2011, \$21 million of the deferred net losses on derivative instruments in accumulated OCI were expected to be reclassified to earnings during the next twelve months. This reclassification would be due primarily to the interest rate variances related to the interest rate swap agreements.

For the three and nine months ended September 30, 2011 and 2010, there were no material reclassifications to earnings due to hedged firm commitments no longer deemed probable or due to hedged forecasted transactions that had not occurred by the end of the originally specified time period.

## Interest Rate Swap Agreements

We use a portion of our interest rate swap agreements to hedge the interest rate risk of our exposure to floating rate bond coupon payments, replicating a fixed rate bond. An interest rate swap is a contractual agreement to exchange payments at one or more times based on the actual or expected price level, performance or value of one or more underlying interest rates. We are required to pay the counterparty the stream of variable interest payments based on the coupon payments from the hedged bonds, and in turn, receive a fixed payment from the counterparty at a predetermined interest rate. The gains or losses on interest rate swaps hedging our interest rate exposure on floating rate bond coupon payments are reclassified from accumulated OCI to net income (loss) as the related bond interest is accrued.

In addition, we use interest rate swap agreements to hedge our exposure to fixed rate bond coupon payments and the change in underlying asset values as interest rates fluctuate.

As of September 30, 2011, the latest maturity date for which we were hedging our exposure to the variability in future cash flows for these instruments was June 2042.

## Forward-Starting Interest Rate Swaps

We use forward-starting interest rate swaps to hedge our exposure to interest rate fluctuations related to the forecasted purchase of certain AFS securities. The gains or losses resulting from the swap agreements are recorded in OCI. The gains or losses are reclassified from accumulated OCI to earnings over the life of the assets once the assets are purchased.

## Foreign Currency Swaps

We use foreign currency swaps, which are traded over-the-counter, to hedge some of the foreign exchange risk of investments in fixed maturity securities denominated in foreign currencies. A foreign currency swap is a contractual agreement to exchange the currencies of two different countries at a specified rate of exchange in the future. The gains or losses on foreign currency swaps hedging foreign exchange risk exposure on foreign currency bond coupon

payments are reclassified from accumulated OCI to net income (loss) as the related bond interest is accrued.

As of September 30, 2011, the latest maturity date for which we were hedging our exposure to the variability in future cash flows for these instruments was July 2022.

#### Treasury and Reverse Treasury Locks

We use treasury locks to hedge the interest rate exposure related to our issuance of fixed rate securities or the anticipated future cash flows of floating rate fixed maturity securities due to changes in interest rates. In addition, we use reverse treasury locks to hedge the interest rate exposure related to the purchase of fixed rate securities or the anticipated future cash flows of floating rate fixed maturity securities due to changes in interest rates. These derivatives are primarily structured to hedge interest rate risk

inherent in the assumptions used to price certain liabilities. The gains or losses resulting from these derivatives are recorded in OCI and are reclassified from accumulated OCI to earnings over the life of the securities once they are purchased or issued.

#### Derivative Instruments Designated and Qualifying as Fair Value Hedges

Gains (losses) (in millions) on derivative instruments designated and qualifying as fair value hedges were as follows:

|   | For the Three<br>Months Ended<br>September 30, |      | For the Nine<br>Months Ended<br>September 30, |      |
|---|--|------|---|------|
|   | 2011   | 2010 | 2011  | 2010 |
| Ineffective portion recognized in realized gain (loss)                              | \$ -   | \$ - | \$ -  | \$ 1 |
| Gain (loss) recognized as a component of OCI with the offset<br>to interest expense | 1  | 1    | 3   | 3    |

#### Interest Rate Swap Agreements

We used a portion of our interest rate swap agreements to hedge the risk of paying a higher fixed rate of interest on junior subordinated debentures issued to affiliated trusts, which were redeemed during 2010, and on senior debt that would be paid on long-term debt based on current interest rates in the marketplace. We are required to pay the counterparty a stream of variable interest payments based on the referenced index, and in turn, we receive a fixed payment from the counterparty at a predetermined interest rate. The net receipts or payments earned or owed from these interest rate swap agreements are recorded as an adjustment to the interest expense for the debt being hedged in the period it occurs. The changes in fair value of the interest rate swap agreements are recorded as an offsetting adjustment to derivative investments and long-term debt on our Consolidated Balance Sheets.

#### Equity Collars

We used an equity collar on four million shares of our Bank of America (“BOA”) stock holdings. On September 7, 2010, we settled the equity collar by delivering four million shares of BOA stock, which resulted in a \$15 million gain, reported within realized gain (loss) on our Consolidated Statements of Income (Loss).

#### Derivative Instruments Not Designated and Not Qualifying as Hedging Instruments

We use various other derivative instruments for risk management and income generation purposes that either do not qualify for hedge accounting treatment or have not currently been designated by us for hedge accounting treatment.

#### Interest Rate Cap Agreements

We use interest rate cap agreements to provide a level of protection from the effect of rising interest rates for our annuity business, within our Annuities and Defined Contribution segments. Interest rate cap agreements entitle us to receive quarterly payments from the counterparties on specified future reset dates, contingent on future interest rates. For each cap, the amount of such quarterly payments, if any, is determined by the excess of a market interest rate over a specified cap rate, multiplied by the notional amount divided by four. Our interest rate cap agreements provide an economic hedge of our annuity business.

#### Interest Rate Futures and Equity Futures

We use interest rate futures and equity futures contracts to hedge the liability exposure on certain options in variable annuity products. These futures contracts require payment between our counterparty and us on a daily basis for changes in the futures index price.

#### Interest Rate Swap Agreements

We use interest rate swap agreements to hedge the liability exposure on certain options in variable annuity products.

#### Foreign Currency Forwards

We used foreign currency forward contracts to hedge the liability exposure on certain options in the variable annuity products. The foreign currency forward contracts obligated us to deliver a specified amount of currency at a future date and a specified exchange rate.

## Credit Default Swaps

We buy credit default swaps to hedge against a drop in bond prices due to credit concerns of certain bond issuers. A credit default swap allows us to put the bond back to the counterparty at par upon a default event by the bond issuer. A default event is defined as bankruptcy, failure to pay, obligation acceleration or restructuring.

We sold credit default swaps to offer credit protection to contract holders and investors. The credit default swaps hedge the contract holders and investors against a drop in bond prices due to credit concerns of certain bond issuers. A credit default swap allows the investor to put the bond back to us at par upon a default event by the bond issuer. A default event is defined as bankruptcy, failure to pay, obligation acceleration or restructuring.

Information related to our open credit default swap liabilities for which we are the seller (dollars in millions) was as follows:

| As of September 30, 2011 |            |           |  |                       |            |                          |
|--------------------------|------------|-----------|--|-----------------------|------------|--------------------------|
|                          | Reason for | Nature of | Credit Rating of Underlying Obligation | Number of Instruments | Fair Value | Maximum Potential Payout |
| Maturity                 | Entering   | Recourse  | (1)                                    |                       | (2)        |                          |
| 12/20/2012 (3)           | (5)        | (6)       | BBB+                                   | 4                     | \$ -       | \$ 40                    |
| 12/20/2016 (4)           | (5)        | (6)       | A-                                     | 3                     | (10)       | 68                       |
| 03/20/2017 (4)           | (5)        | (6)       | BBB                                    | 2                     | (5)        | 40                       |
|                          |            |           |  | 9                     | \$ (15)    | \$ 148                   |

| As of December 31, 2010 |            |           |  |                       |            |                          |
|-------------------------|------------|-----------|--|-----------------------|------------|--------------------------|
|                         | Reason for | Nature of | Credit Rating of Underlying Obligation | Number of Instruments | Fair Value | Maximum Potential Payout |
| Maturity                | Entering   | Recourse  | (1)                                    |                       | (2)        |                          |
| 12/20/2012 (3)          | (5)        | (6)       | BBB+                                   | 4                     | \$ -       | \$ 40                    |
| 12/20/2016 (4)          | (5)        | (6)       | BBB                                    | 3                     | (12)       | 65                       |
| 03/20/2017 (4)          | (5)        | (6)       | BBB-                                   | 2                     | (4)        | 40                       |
|                         |            |           |  | 9                     | \$ (16)    | \$ 145                   |

- (1) Represents average credit ratings based on the midpoint of the applicable ratings among Moody's, S&P and Fitch Ratings, as scaled to the corresponding S&P ratings.
- (2) Broker quotes are used to determine the market value of credit default swaps.
- (3) These credit default swaps were sold to our contract holders where we determined there was a spread versus premium mismatch.
- (4) These credit default swaps were sold to a counter-party of the consolidated VIEs as discussed in Note 4 in our 2010 Form 10-K.
- (5) Credit default swap was entered into in order to generate income by providing default protection in return for a quarterly payment.
- (6) Seller does not have the right to demand indemnification or compensation from third parties in case of a loss (payment) on the contract.





Details underlying the associated collateral of our open credit default swaps for which we are the seller, if credit risk related contingent features were triggered (in millions) are as follows:

|   | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|---|-----------------------------------|----------------------------------|
| Maximum potential payout                        | \$ 148                            | \$ 145                           |
| Less:   |                                   |                                  |
| Counterparty thresholds                         | -                                 | 10                               |
| Maximum collateral potentially required to post | \$ 148                            | \$ 135                           |

Certain of our credit default swap agreements contain contractual provisions that allow for the netting of collateral with our counterparties related to all of our collateralized financing transactions that we have outstanding. If these netting agreements were not in place, we would have been required to post approximately \$15 million as of September 30, 2011, after considering the fair values of the associated investments counterparties' credit ratings as compared to ours and specified thresholds that once exceeded result in the payment of cash.

#### Total Return Swaps

We use total return swaps to hedge a portion of the liability related to our deferred compensation plans. We receive the total return on a portfolio of indexes and pay a floating rate of interest.

In addition, we use total return swaps to hedge the liability exposure on certain options in variable annuity products. We receive the total return on a portfolio of indexes and pay a floating rate of interest.

#### Put Options

We use put options to hedge the liability exposure on certain options in variable annuity products. Put options are contracts that require counterparties to pay us at a specified future date the amount, if any, by which a specified equity index is less than the strike rate stated in the agreement, applied to a notional amount.

#### Call Options (Based on S&P 500)

We use indexed annuity contracts to permit the holder to elect an interest rate return or an equity market component, where interest credited to the contracts is linked to the performance of the S&P 500. Contract holders may elect to rebalance index options at renewal dates, either annually or biannually. As of each renewal date, we have the opportunity to re-price the indexed component by establishing participation rates, subject to minimum guarantees. We purchase call options that are highly correlated to the portfolio allocation decisions of our contract holders, such that we are economically hedged with respect to equity returns for the current reset period. The mark-to-market of the options held generally offsets the change in value of the embedded derivative within the indexed annuity.

#### Variance Swaps

We use variance swaps to hedge the liability exposure on certain options in variable annuity products. Variance swaps are contracts entered into at no cost and whose payoff is the difference between the realized variance rate of an underlying index and the fixed variance rate determined as of inception.

#### Currency Futures

We use currency futures to hedge foreign exchange risk associated with certain options in variable annuity products. Currency futures exchange one currency for another at a specified date in the future at a specified exchange rate.

#### Consumer Price Index Swaps

We use consumer price index swaps to hedge the liability exposure on certain options in fixed/indexed annuity products. Consumer price index swaps are contracts entered into at no cost and whose payoff is the difference between the consumer price index inflation rate and the fixed rate determined as of inception.

### Interest Rate Cap Corridors

We use interest rate cap corridors to provide a level of protection from the effect of rising interest rates for our annuity business, within our Annuities and Defined Contribution segments. Interest rate cap corridors involve purchasing an interest rate cap at a specific cap rate and selling an interest rate cap with a higher cap rate. For each corridor, the amount of quarterly payments, if any, is determined by the rate at which the underlying index rate resets above the original capped rate. The corridor limits the benefit the purchaser can receive as the related interest rate index rises above the higher capped rate. There is no additional liability to us other than the purchase price associated with the interest rate cap corridor. Our interest rate cap corridors provide an economic hedge of our annuity business.

### Deferred Compensation Plans Embedded Derivatives

We have certain deferred compensation plans that have embedded derivative instruments. The liability related to these plans varies based on the investment options selected by the participants. The liability related to certain investment options selected by the participants is marked-to-market through net income (loss).

### Indexed Annuity Contracts Embedded Derivatives

We distribute indexed annuity contracts that permit the holder to elect an interest rate return or an equity market component, where interest credited to the contracts is linked to the performance of the S&P 500. This feature represents an embedded derivative under the Derivatives and Hedging Topic of the FASB ASC. Contract holders may elect to rebalance index options at renewal dates, either annually or biannually. As of each renewal date, we have the opportunity to re-price the indexed component by establishing participation rates, subject to minimum guarantees. We purchase S&P 500 call options that are highly correlated to the portfolio allocation decisions of our contract holders, such that we are economically hedged with respect to equity returns for the current reset period. The mark-to-market of the options held generally offsets the change in value of the embedded derivative within the indexed annuity.

### GLB Reserves Embedded Derivatives

We have certain GLB variable annuity products with GWB and GIB features that are embedded derivatives. Certain features of these guarantees have elements of both insurance benefits accounted for under the Financial Services – Insurance – Claim Costs and Liabilities for Future Policy Benefits Subtopic of the FASB ASC (“benefit reserves”) and embedded derivatives accounted for under the Derivatives and Hedging and the Fair Value Measurements and Disclosures Topics of the FASB ASC (“embedded derivative reserves”). We calculate the value of the embedded derivative reserve and the benefit reserve based on the specific characteristics of each GLB feature. As of September 30, 2011, we had \$29.6 billion of account values that were attributable to variable annuities with a GWB feature and \$11.5 billion of account values that were attributable to variable annuities with a GIB feature.

We use a hedging strategy designed to mitigate the risk and income statement volatility caused by changes in the equity markets, interest rates and volatility associated with GWB and GIB features. The hedging strategy is designed such that changes in the value of the hedge contracts due to changes in equity markets, interest rates and implied volatilities move in the opposite direction of changes in embedded derivative reserves of the GWB and GIB caused by those same factors. As part of our current hedging program, equity markets, interest rates and volatility in market conditions are monitored on a daily basis. We rebalance our hedge positions based upon changes in these factors as needed. While we actively manage our hedge positions, these hedge positions may not be totally effective in offsetting changes in the embedded derivative reserve due to, among other things, differences in timing between when a market exposure changes and corresponding changes to the hedge positions, extreme swings in the equity markets and interest rates, market volatility, contract holder behavior, divergence between the performance of the underlying funds and the hedging indices, divergence between the actual and expected performance of the hedge instruments and

our ability to purchase hedging instruments at prices consistent with our desired risk and return trade-off.

#### Reinsurance Related Embedded Derivatives

We have certain modified coinsurance arrangements and coinsurance with funds withheld reinsurance arrangements with embedded derivatives related to the withheld assets of the related funds. These derivatives are considered total return swaps with contractual returns that are attributable to various assets and liabilities associated with these reinsurance arrangements. Changes in the estimated fair value of these derivatives as they occur are recorded through net income (loss). Offsetting these amounts are corresponding changes in the estimated fair value of trading securities in portfolios that support these arrangements.

## AFS Securities Embedded Derivatives

We own various debt securities that either contain call options to exchange the debt security for other specified securities of the borrower, usually common stock, or contain call options to receive the return on equity-like indexes. The change in fair value of these embedded derivatives flows through net income (loss).

## Credit Risk

We are exposed to credit loss in the event of nonperformance by our counterparties on various derivative contracts and reflect assumptions regarding the credit or nonperformance risk. The nonperformance risk is based upon assumptions for each counterparty's credit spread over the estimated weighted average life of the counterparty exposure less collateral held. As of September 30, 2011, the nonperformance risk adjustment was \$19 million. The credit risk associated with such agreements is minimized by purchasing such agreements from financial institutions with long-standing, superior performance records. Additionally, we maintain a policy of requiring all derivative contracts to be governed by an International Swaps and Derivatives Association ("ISDA") Master Agreement. We are required to maintain minimum ratings as a matter of routine practice in negotiating ISDA agreements. Under some ISDA agreements, our insurance subsidiaries have agreed to maintain certain financial strength or claims-paying ratings. A downgrade below these levels could result in termination of the derivatives contract, at which time any amounts payable by us would be dependent on the market value of the underlying derivative contract. In certain transactions, we and the counterparty have entered into a collateral support agreement requiring either party to post collateral when net exposures exceed pre-determined thresholds. These thresholds vary by counterparty and credit rating. We do not believe the inclusion of termination or collateralization events pose any material threat to the liquidity position of any insurance subsidiary of the Company. The amount of such exposure is essentially the net replacement cost or market value less collateral held for such agreements with each counterparty if the net market value is in our favor. As of September 30, 2011, the exposure was \$110 million.

The amounts recognized (in millions) by S&P credit rating of counterparty, for which we had the right to reclaim cash collateral or were obligated to return cash collateral, were as follows:

| S&P<br>Credit<br>Rating of<br>Counterparty | As of September 30,<br>2011   |   | As of December 31,<br>2010  |   |
|--|---|---|---|---|
|  | Collateral<br>Posted<br>by<br>Counter-<br>Party<br>(Held by<br>LNC) | Collateral<br>Posted<br>by<br>LNC<br>(Held by<br>Counter-<br>Party) | Collateral<br>Posted<br>by<br>Counter-<br>Party<br>(Held by<br>LNC) | Collateral<br>Posted<br>by<br>LNC<br>(Held by<br>Counter-<br>Party) |
| AAA  | \$ 37   | \$ -  | \$ 1  | \$ -  |
| AA   | 249   | -   | 99  | -   |
| AA-  | 224   | (1)   | 65  | -   |
| A+   | 1,067   | (88)  | 548   | (76)  |
| A  | 1,454   | (43)  | 436   | (223)   |
|  | \$ 3,031  | \$ (132)  | \$ 1,149  | \$ (299)  |

## 7. Federal Income Taxes

The effective tax rate is a ratio of tax expense over pre-tax income (loss). Because the pre-tax income of \$139 million resulted in a tax benefit of \$12 million for the three months ended September 30, 2011, the effective tax rate was not

meaningful. The effective tax rate on pre-tax income from continuing operations was 22% for the nine months ended September 30, 2011. The effective tax rate on pre-tax income from continuing operations was 18% and 23% for the three and nine months ended September 30, 2010, respectively. The effective tax rate on pre-tax income from continuing operations was lower than the prevailing corporate federal income tax rate. Differences in the effective rates and the U.S. statutory rate of 35% were the result of certain tax preferred investment income, separate account dividends-received deduction ("DRD"), foreign tax credits and other tax preference items.

Federal income tax expense for the first nine months of 2011 was decreased by \$28 million related to favorable adjustments from the 2010 tax return, filed in the third quarter of 2011, relating primarily to the separate account DRD, foreign tax credits and other tax preference items. Federal income tax expense for the first nine months of 2010 was decreased by \$13 million related to favorable adjustments from the 2009 tax return, filed in the third quarter of 2010, relating primarily to the separate account DRD, foreign tax credits and other tax preference items.

## 8. DAC, VOBA, DSI and DFEL

Changes in DAC (in millions) were as follows:

|   | For the Nine<br>Months Ended<br>September 30, |          |
|---|---|----------|
|   | 2011  | 2010     |
| Balance as of beginning-of-year                 | \$ 7,552                                      | \$ 7,424 |
| Deferrals                                       | 1,240   | 1,179    |
| Amortization, net of interest:                  |   |          |
| Prospective unlocking - assumption changes      | (339)   | (26)     |
| Prospective unlocking - model refinements       | 171   | 183      |
| Retrospective unlocking                         | 75  | 41       |
| Other amortization                              | (705)   | (676)    |
| Adjustment related to realized (gains) losses   | (38)  | (32)     |
| Adjustment related to unrealized (gains) losses | (837)   | (1,223)  |
| Balance as of end-of-period                     | \$ 7,119                                      | \$ 6,870 |

Changes in VOBA (in millions) were as follows:

|   | For the Nine<br>Months Ended<br>September 30, |          |
|---|---|----------|
|   | 2011  | 2010     |
| Balance as of beginning-of-year                 | \$ 1,378                                      | \$ 2,086 |
| Business acquired through reinsurance           | 2   | -        |
| Deferrals                                       | 15  | 19       |
| Amortization:                                   |   |          |
| Prospective unlocking - assumption changes      | 28  | (40)     |
| Prospective unlocking - model refinements       | 102   | (30)     |
| Retrospective unlocking                         | 16  | -        |
| Other amortization                              | (235)   | (270)    |
| Accretion of interest (1)                       | 59  | 68       |
| Adjustment related to realized (gains) losses   | (5)   | 2        |
| Adjustment related to unrealized (gains) losses | (349)   | (787)    |
| Balance as of end-of-period                     | \$ 1,011                                      | \$ 1,048 |

(1) The interest accrual rates utilized to calculate the accretion of interest ranged from 3.45% to 4.70%.



Changes in DSI (in millions) were as follows:

|   | For the Nine<br>Months Ended<br>September 30, |        |
|---|---|--------|
|   | 2011  | 2010   |
| Balance as of beginning-of-year                 | \$ 286  | \$ 323 |
| Deferrals                                       | 29  | 53     |
| Amortization, net of interest:                  |   |        |
| Prospective unlocking - assumption changes      | (2)   | 2      |
| Retrospective unlocking                         | 11  | 6      |
| Other amortization                              | (42)  | (43)   |
| Adjustment related to realized (gains) losses   | (3)   | (8)    |
| Adjustment related to unrealized (gains) losses | (11)  | (64)   |
| Balance as of end-of-period                     | \$ 268  | \$ 269 |

Changes in DFEL (in millions) were as follows:

|   | For the Nine<br>Months Ended<br>September 30, |          |
|---|---|----------|
|   | 2011  | 2010     |
| Balance as of beginning-of-year                 | \$ 1,502                                      | \$ 1,338 |
| Deferrals                                       | 411   | 411      |
| Amortization, net of interest:                  |   |          |
| Prospective unlocking - assumption changes      | (6)   | (53)     |
| Prospective unlocking - model refinements       | 28  | 62       |
| Retrospective unlocking                         | 7   | (14)     |
| Other amortization                              | (127)   | (126)    |
| Adjustment related to realized (gains) losses   | (10)  | (4)      |
| Adjustment related to unrealized (gains) losses | (467)   | (312)    |
| Balance as of end-of-period                     | \$ 1,338                                      | \$ 1,302 |

## 9. Guaranteed Benefit Features

Information on the guaranteed death benefit (“GDB”) features outstanding (dollars in millions) was as follows (our variable contracts with guarantees may offer more than one type of guarantee in each contract; therefore, the amounts listed are not mutually exclusive):

|  | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|--|-----------------------------------|----------------------------------|
| <b>Return of Net Deposits</b>            |                                   |                                  |
| Total account value                      | \$ 50,472                         | \$ 52,211                        |
| Net amount at risk (1)                   | 2,364                             | 816                              |
|  | 59                                | 58                               |
| Average attained age of contract holders | years                             | years                            |
| <b>Minimum Return</b>                    |                                   |                                  |
| Total account value                      | \$ 150                            | \$ 187                           |
| Net amount at risk (1)                   | 56                                | 46                               |
|  | 71                                | 70                               |
| Average attained age of contract holders | years                             | years                            |
| Guaranteed minimum return                | 5 %                               | 5 %                              |
| <b>Anniversary Contract Value</b>        |                                   |                                  |
| Total account value                      | \$ 20,640                         | \$ 23,483                        |
| Net amount at risk (1)                   | 4,172                             | 2,183                            |
|  | 67                                | 66                               |
| Average attained age of contract holders | years                             | years                            |

(1) Represents the amount of death benefit in excess of the account balance. The increase in net amount at risk when comparing September 30, 2011, to December 31, 2010, was attributable primarily to the decline in equity markets and associated decrease in the account values.

The determination of GDB liabilities is based on models that involve a range of scenarios and assumptions, including those regarding expected market rates of return and volatility, contract surrender rates and mortality experience. The following summarizes the balances of and changes in the liabilities for GDB (in millions), which were recorded in future contract benefits on our Consolidated Balance Sheets:

|                                 | For the Nine<br>Months Ended<br>September 30, |       |
|---------------------------------|---|-------|
|                                 | 2011  | 2010  |
| Balance as of beginning-of-year | \$ 44   | \$ 71 |
| Changes in reserves             | 108   | 59    |
| Benefits paid                   | (34)  | (68)  |
| Balance as of end-of-period     | \$ 118  | \$ 62 |

Account balances of variable annuity contracts with guarantees (in millions) were invested in separate account investment options as follows:

| Asset Type  | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|---|-----------------------------------|----------------------------------|
| Domestic equity   | \$1,476                           | \$5,659                          |
| International equity                                      | 12,169                            | 14,172                           |
| Bonds   | 16,951                            | 15,913                           |
| Money market  | 5,799                             | 5,725                            |
| Total   | \$6,395                           | \$1,469                          |
| Percent of total variable annuity separate account values | 98 %                              | 98 %                             |

Future contract benefits also includes reserves for our products with secondary guarantees for our products sold through our Insurance Solutions – Life Insurance segment. These UL and VUL products with secondary guarantees represented approximately 38% of permanent life insurance in force as of September 30, 2011, and approximately 46% and 49% of total sales for these products for the three and nine months ended September 30, 2011, respectively.

#### 10. Contingencies and Commitments

See “Contingencies and Commitments” in Note 14 to the consolidated financial statements in our 2010 Form 10-K for a discussion of commitments and contingencies, which information is incorporated herein by reference.

Regulatory bodies, such as state insurance departments, the SEC, Financial Industry Regulatory Authority and other regulatory bodies regularly make inquiries and conduct examinations or investigations concerning our compliance with, among other things, insurance laws, securities laws, laws governing the activities of broker-dealers and unclaimed property laws.

In the ordinary course of its business, LNC and its subsidiaries are involved in various pending or threatened legal proceedings, including purported class actions, arising from the conduct of business. In some instances, these proceedings include claims for unspecified or substantial punitive damages and similar types of relief in addition to amounts for alleged contractual liability or requests for equitable relief. After consultation with legal counsel and a review of available facts, it is management’s opinion that these proceedings, after consideration of any reserves and rights to indemnification, ultimately will be resolved without materially affecting the consolidated financial position of LNC. However, given the large and indeterminate amounts sought in certain of these proceedings and the inherent difficulty in predicting the outcome of such legal proceedings, it is possible that an adverse outcome in certain matters could be material to our operating results for any particular reporting period.

Our life insurance subsidiaries are currently being audited on behalf of multiple states' treasury and controllers' offices for compliance with laws and regulations concerning the identification, reporting and escheatment of unclaimed contract benefits or abandoned funds. The audits focus on insurance company processes and procedures for identifying unreported death claims, and their use of the Social Security Master Death File to identify deceased policy and contract holders. In addition, our life insurance subsidiaries are the subject of multiple state Insurance Department inquiries and market conduct examinations with a similar focus on the handling of unreported claims and abandoned property. The audits and related examination activity may result in additional payments to beneficiaries, escheatment of funds deemed abandoned under state laws, administrative penalties and changes in our procedures for

the identification of unreported claims and handling of escheatable property. We are not currently able to estimate the amount of benefits which may become payable as a result of any such unreported claims or the potential increase in the cost of implementing related changes in procedures.

## 11. Shares and Stockholders' Equity

## Common and Preferred Shares

The changes in our preferred and common stock (number of shares) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |             | For the Nine<br>Months Ended<br>September 30, |             |
|---|--|-------------|---|-------------|
|   | 2011   | 2010        | 2011  | 2010        |
| <b>Series A Preferred Stock</b>                   |  |             |   |             |
| Balance as of beginning-of-period                 | 10,854   | 11,365      | 10,914  | 11,497      |
| Conversion of convertible preferred stock (1)     | -  | (451)       | (60)  | (583)       |
| Balance as of end-of-period                       | 10,854   | 10,914      | 10,854  | 10,914      |
| <b>Series B Preferred Stock</b>                   |  |             |   |             |
| Balance as of beginning-of-period                 | -  | -           | -   | 950,000     |
| Issuance (redemption) of Series B preferred stock | -  | -           | -   | (950,000)   |
| Balance as of end-of-period                       | -  | -           | -   | -           |
| <b>Common Stock</b>                               |  |             |   |             |
| Balance as of beginning-of-period                 | 308,339,163                                    | 316,662,480 | 315,718,554                                   | 302,223,281 |
| Stock issued                                      | -  | -           | -   | 14,137,615  |
| Conversion of convertible preferred stock (1)     | -  | 7,216       | 960   | 9,328       |
| Stock compensation/issued for benefit plans       | 32,712   | 84,385      | 215,618                                       | 401,950     |
| Retirement/cancellation of shares                 | (6,712,700)                                    | -           | (14,275,957)                                  | (18,093)    |
| Balance as of end-of-period                       | 301,659,175                                    | 316,754,081 | 301,659,175                                   | 316,754,081 |
| <b>Common Stock as of End-of-Period</b>           |  |             |   |             |
| Assuming conversion of preferred stock            | 301,832,839                                    | 316,928,705 | 301,832,839                                   | 316,928,705 |
| Diluted basis                                     | 306,899,902                                    | 324,290,798 | 306,899,902                                   | 324,290,798 |

(1) Represents the conversion of Series A preferred stock into common stock.

Our common, Series A and Series B preferred stocks are without par value.

## Average Shares

A reconciliation of the denominator (number of shares) in the calculations of basic and diluted earnings (loss) per common share (“EPS”) was as follows:

|   | For the Three<br>Months Ended<br>September 30, |             | For the Nine<br>Months Ended<br>September 30, |             |
|---|--|-------------|---|-------------|
|   | 2011   | 2010        | 2011  | 2010        |
| Weighted-average shares, as used in basic calculation   | 304,779,641                                    | 316,726,409 | 310,357,508                                   | 307,863,690 |
| Shares to cover exercise of outstanding warrants  | 10,150,292                                     | 12,791,748  | 10,150,292                                    | 12,963,550  |
| Shares to cover conversion of preferred stock   | 173,664  | 175,095     | 174,293                                       | 180,101     |
| Shares to cover non-vested stock  | 815,594  | 584,206     | 801,261                                       | 602,443     |
| Average stock options outstanding during the period   | 500,578  | 580,067     | 698,054                                       | 728,250     |
| Assumed acquisition of shares with assumed<br>proceeds from exercising outstanding warrants   | (5,153,660)                                    | (5,805,269) | (4,223,290)                                   | (5,416,234) |
| Assumed acquisition of shares with assumed<br>proceeds and benefits from exercising stock<br>options (at average market price for the period) | (342,848)                                      | (383,607)   | (459,168)                                     | (478,222)   |
| Shares repurchaseable from measured but<br>unrecognized stock option expense  | (31,025)                                       | (97,164)    | (80,317)                                      | (150,846)   |
| Average deferred compensation shares  | 1,105,447                                      | 1,112,284   | 1,070,549                                     | 1,221,257   |
| Weighted-average shares, as used in<br>diluted calculation  | 311,997,683                                    | 325,683,769 | 318,489,182                                   | 317,513,989 |

In the event the average market price of LNC common stock exceeds the issue price of stock options, such options would be dilutive to our EPS and will be shown in the table above.

We have participants in our deferred compensation plans, with the exception of the non-employee directors’ deferred compensation plan, who selected LNC stock as the measure for the investment return attributable to their deferral amounts. For the three and nine months ended September 30, 2011 and 2010, the effect of settling this obligation in LNC stock (“equity classification”) was more dilutive than the scenario of settling it in cash (“liability classification”). Therefore, for our EPS calculation for these periods, we added these shares to the denominator and adjusted the numerator to present net income as if the shares had been accounted for under equity classification by removing the mark-to-market adjustment included in net income attributable to these deferred units of LNC stock. The amount of this adjustment was \$5 million for the three and nine months ended September 30, 2011, \$1 million for the three months ended September 30, 2010, and \$3 million for the nine months ended September 30, 2010.

The income used in the calculation of our diluted EPS is our net income (loss), reduced by preferred stock dividends and accretion of discount. These amounts are presented on our Consolidated Statements of Income (Loss).

## Accumulated OCI

The following summarizes the components and changes in accumulated OCI (in millions):

|   | For the Nine<br>Months Ended<br>September 30, |          |
|---|---|----------|
|   | 2011  | 2010     |
| Unrealized Gain (Loss) on AFS Securities  |   |          |
| Balance as of beginning-of-year   | \$ 1,072                                      | \$ 49    |
| Cumulative effect from adoption of new accounting standards                                 | -   | 181      |
| Unrealized holding gains (losses) arising during the period                                 | 3,232   | 4,742    |
| Change in foreign currency exchange rate adjustment   | 2   | (5)      |
| Change in DAC, VOBA, DSI and other contract holder funds                                    | (885)   | (1,799)  |
| Income tax benefit (expense)  | (841)   | (1,053)  |
| Less:   |   |          |
| Reclassification adjustment for gains (losses) included in net income (loss)                | (83)  | (73)     |
| Reclassification adjustment for gains (losses) on derivatives included in net income (loss) | -   | 135      |
| Associated amortization of DAC, VOBA, DSI and DFEL  | (13)  | 21       |
| Income tax benefit (expense)  | 34  | (29)     |
| Balance as of end-of-period   | \$ 2,642                                      | \$ 2,061 |
| Unrealized OTTI on AFS Securities   |   |          |
| Balance as of beginning-of-year   | \$ (129)                                      | \$ (115) |
| (Increases) attributable to:  |   |          |
| Gross OTTI recognized in OCI during the period  | (48)  | (84)     |
| Change in DAC, VOBA, DSI and DFEL   | 9   | 7        |
| Income tax benefit (expense)  | 14  | 27       |
| Decreases attributable to:  |   |          |
| Sales, maturities or other settlements of AFS securities                                    | 91  | 64       |
| Change in DAC, VOBA, DSI and DFEL   | (19)  | (12)     |
| Income tax benefit (expense)  | (25)  | (18)     |
| Balance as of end-of-period   | \$ (107)                                      | \$ (131) |
| Unrealized Gain (Loss) on Derivative Instruments  |   |          |
| Balance as of beginning-of-year   | \$ (15)                                       | \$ 11    |
| Unrealized holding gains (losses) arising during the period                                 | 188   | (97)     |
| Change in foreign currency exchange rate adjustment   | (1)   | 8        |
| Change in DAC, VOBA, DSI and DFEL   | (1)   | (10)     |
| Income tax benefit (expense)  | (65)  | 35       |
| Less:   |   |          |
| Reclassification adjustment for gains (losses) included in net income (loss)                | (3)   | 13       |
| Associated amortization of DAC, VOBA, DSI and DFEL  | -   | (1)      |
| Income tax benefit (expense)  | 1   | (4)      |
| Balance as of end-of-period   | \$ 108  | \$ (61)  |
| Foreign Currency Translation Adjustment   |   |          |
| Balance as of beginning-of-year   | \$ 1  | \$ 3     |
| Foreign currency translation adjustment arising during the period                           | 3   | (1)      |

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|   |          |          |
|---|----------|----------|
| Income tax benefit (expense)            | (1)      | -        |
| Balance as of end-of-period             | \$ 3     | \$ 2     |
| Funded Status of Employee Benefit Plans |          |          |
| Balance as of beginning-of-year         | \$ (181) | \$ (210) |
| Adjustment arising during the period    | (3)      | 2        |
| Income tax benefit (expense)            | 1        | (1)      |
| Balance as of end-of-period             | \$ (183) | \$ (209) |



## 12. Realized Gain (Loss)

Details underlying realized gain (loss) (in millions) reported on our Consolidated Statements of Income (Loss) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |         | For the Nine<br>Months Ended<br>September 30, |         |
|---|--|---------|---|---------|
|   | 2011   | 2010    | 2011  | 2010    |
| Total realized gain (loss) related to certain investments (1)   | \$ (44)  | \$ (26) | \$ (95)                                       | \$ (86) |
| Realized gain (loss) related to certain derivative instruments,<br>including those associated with our consolidated VIEs, and<br>trading securities (2) | (105)  | 105     | (96)  | 72      |
| Indexed annuity net derivative results: (3)   |  |         |   |         |
| Gross gain (loss)   | (5)  | 1       | 3   | 8       |
| Associated amortization of DAC, VOBA, DSI and DFEL  | 1  | -       | (2)   | (3)     |
| Guaranteed living benefits: (4)   |  |         |   |         |
| Gross gain (loss)   | (34)   | 36      | 26  | 117     |
| Associated amortization of DAC, VOBA, DSI and DFEL  | 4  | (27)    | (20)  | (53)    |
| Guaranteed death benefits: (5)  |  |         |   |         |
| Gross gain (loss)   | 22   | (52)    | 8   | (38)    |
| Associated amortization of DAC, VOBA, DSI and DFEL  | (2)  | 6       | (1)   | 5       |
| Total realized gain (loss)  | \$ (163)                                       | \$ 43   | \$ (177)                                      | \$ 22   |

- (1) See “Realized Gain (Loss) Related to Certain Investments” section in Note 5.
- (2) Represents changes in the fair values of certain derivative investments (including the credit default swaps, contingent forwards and excess mortality swap associated with our consolidated VIEs), total return swaps (embedded derivatives that are theoretically included in our various modified coinsurance and coinsurance with funds withheld reinsurance arrangements that have contractual returns related to various assets and liabilities associated with these arrangements) and trading securities.
- (3) Represents the net difference between the change in the fair value of the S&P 500 call options that we hold and the change in the fair value of the embedded derivative liabilities of our indexed annuity products along with changes in the fair value of embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations applicable to future reset periods for our indexed annuity products.
- (4) Represents the net difference in the change in embedded derivative reserves of our GLB products and the change in the fair value of the derivative instruments we own to hedge, including the cost of purchasing the hedging instruments.
- (5) Represents the change in the fair value of the derivatives used to hedge our GDB riders.

## 13. Stock-Based Incentive Compensation Plans

We sponsor various incentive plans for our employees and directors, and for the employees and agents of our subsidiaries that provide for the issuance of stock options, performance shares (performance-vested shares as opposed to time-vested shares), stock appreciation rights (“SARs”) and restricted stock units.

LNC stock-based awards granted were as follows:

|                                 | For the<br>Three<br>Months<br>Ended<br>September<br>30,<br>2011 | For the<br>Nine<br>Months<br>Ended<br>September<br>30,<br>2011 |
|---------------------------------|---|--|
| Awards                          |   |  |
| 10-year LNC stock options       | -   | 459,093  |
| Performance shares              | -   | 215,137  |
| SARs                            | -   | 106,966  |
| Restricted stock units          | 12,869  | 524,273  |
| Non-employee:                   |   |  |
| Agent stock options             | -   | 95,451   |
| Director stock options          | -   | 32,560   |
| Director restricted stock units | 17,547  | 36,961   |

## 14. Fair Value of Financial Instruments

The carrying values and estimated fair values of our financial instruments (in millions) were as follows:

|  | As of September 30,<br>2011 |               | As of December 31,<br>2010 |               |
|--|-----------------------------|---------------|----------------------------|---------------|
|  | Carrying<br>Value           | Fair<br>Value | Carrying<br>Value          | Fair<br>Value |
| <b>Assets</b>  |                             |               |                            |               |
| AFS securities:  |                             |               |                            |               |
| Fixed maturity securities                              | \$ 74,591                   | \$ 74,591     | \$ 68,030                  | \$ 68,030     |
| VIEs' fixed maturity securities                        | 700                         | 700           | 584                        | 584           |
| Equity securities                                      | 137                         | 137           | 197                        | 197           |
| Trading securities                                     | 2,726                       | 2,726         | 2,596                      | 2,596         |
| Mortgage loans on real estate                          | 6,893                       | 7,596         | 6,752                      | 7,183         |
| Derivative investments                                 | 3,029                       | 3,029         | 1,076                      | 1,076         |
| Other investments                                      | 1,105                       | 1,105         | 1,038                      | 1,038         |
| Cash and invested cash                                 | 4,833                       | 4,833         | 2,741                      | 2,741         |
| Separate account assets                                | 78,195                      | 78,195        | 84,630                     | 84,630        |
| <b>Liabilities</b>                                     |                             |               |                            |               |
| Future contract benefits:                              |                             |               |                            |               |
| Indexed annuity contracts embedded<br>derivatives      | (342)                       | (342)         | (497)                      | (497)         |
| GLB reserves embedded derivatives                      | (2,343)                     | (2,343)       | (408)                      | (408)         |
| Other contract holder funds:                           |                             |               |                            |               |
| Remaining guaranteed interest and similar<br>contracts | (1,115)                     | (1,115)       | (1,119)                    | (1,119)       |
| Account values of certain investment contracts         | (27,190)                    | (29,888)      | (26,130)                   | (27,142)      |
| Short-term debt (1)                                    | (550)                       | (564)         | (351)                      | (364)         |
| Long-term debt   | (5,348)                     | (4,898)       | (5,399)                    | (5,512)       |
| Reinsurance related embedded derivatives               | (177)                       | (177)         | (102)                      | (102)         |
| VIEs' liabilities - derivative instruments             | (307)                       | (307)         | (209)                      | (209)         |
| Other liabilities:                                     |                             |               |                            |               |
| Deferred compensation plans embedded<br>derivatives    | (325)                       | (325)         | (363)                      | (363)         |
| Credit default swaps                                   | (15)                        | (15)          | (16)                       | (16)          |

(1) The difference between the carrying value and fair value of short-term debt as of September 30, 2011, and December 31, 2010, related to current maturities of long-term debt.

## Valuation Methodologies and Associated Inputs for Financial Instruments Not Carried at Fair Value

The following discussion outlines the methodologies and assumptions used to determine the fair value of our financial instruments not carried at fair value on our Consolidated Balance Sheets. Considerable judgment is required to develop these assumptions used to measure fair value. Accordingly, the estimates shown are not necessarily indicative of the amounts that would be realized in a one-time, current market exchange of all of our financial instruments.

Mortgage Loans on Real Estate

The fair value of mortgage loans on real estate is established using a discounted cash flow method based on credit rating, maturity and future income. The ratings for mortgages in good standing are based on property type, location, market conditions, occupancy, debt-service coverage, loan-to-value, quality of tenancy, borrower and payment record. The fair value for impaired mortgage loans on real estate is based on the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's market price or the fair value of the collateral if the loan is collateral dependent.

#### Other Investments

The carrying value of our assets classified as other investments approximates their fair value. Other investments include LPs and other privately held investments that are accounted for using the equity method of accounting.

#### Other Contract Holder Funds

Other contract holder funds include remaining guaranteed interest and similar contracts and account values of certain investment contracts. The fair value for the remaining guaranteed interest and similar contracts is estimated using discounted cash flow calculations as of the balance sheet date. These calculations are based on interest rates currently offered on similar contracts with maturities that are consistent with those remaining for the contracts being valued. As of September 30, 2011, and December 31, 2010, the remaining guaranteed interest and similar contracts carrying value approximates fair value. The fair value of the account values of certain investment contracts is based on their approximate surrender value as of the balance sheet date.

#### Short-term and Long-term Debt

The fair value of long-term debt is based on quoted market prices or estimated using discounted cash flow analysis determined in conjunction with our incremental borrowing rate as of the balance sheet date for similar types of borrowing arrangements where quoted prices are not available. For short-term debt, excluding current maturities of long-term debt, the carrying value approximates fair value.

#### Financial Instruments Carried at Fair Value

We did not have any assets or liabilities measured at fair value on a nonrecurring basis as of September 30, 2011, or December 31, 2010, and we noted no changes in our valuation methodologies between these periods.

The following summarizes our financial instruments carried at fair value (in millions) on a recurring basis by the fair value hierarchy levels described in “Summary of Significant Accounting Policies” in Note 1 of the 2010 Form 10-K:

|  | As of September 30, 2011  |  |  |                        |
|--|---|--|--|------------------------|
|  | Quoted<br>Prices<br>in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
| <b>Assets</b>                                    |   |  |  |                        |
| <b>Investments:</b>                              |   |  |  |                        |
| Fixed maturity AFS securities:                   |   |  |  |                        |
| Corporate bonds                                  | \$ 63   | \$ 56,700  | \$ 1,500   | \$ 58,263              |
| U.S. Government bonds                            | 267   | 18   | 1  | 286                    |
| Foreign government bonds                         | -   | 537  | 105  | 642                    |
| MBS:   |   |  |  |                        |
| CMOs   | -   | 5,189  | 19   | 5,208                  |
| MPTS   | -   | 3,120  | 120  | 3,240                  |
| CMBS   | -   | 1,633  | 37   | 1,670                  |
| ABS CDOs   | -   | -  | 111  | 111                    |
| State and municipal bonds                        | -   | 3,969  | -  | 3,969                  |
| Hybrid and redeemable preferred securities       | 15  | 1,095  | 92   | 1,202                  |
| VIEs' fixed maturity securities                  | 107   | 593  | -  | 700                    |
| Equity AFS securities:                           |   |  |  |                        |
| Banking securities                               | -   | 1  | -  | 1                      |
| Insurance securities                             | 3   | -  | 24   | 27                     |
| Other financial services securities              | -   | 7  | 18   | 25                     |
| Other securities                                 | 34  | -  | 50   | 84                     |
| Trading securities                               | 2   | 2,655  | 69   | 2,726                  |
| Derivative investments                           | -   | 503  | 2,526  | 3,029                  |
| Cash and invested cash                           | -   | 4,833  | -  | 4,833                  |
| Separate account assets                          | -   | 78,195   | -  | 78,195                 |
|  |   | <b>Total assets</b>                              |  | <b>\$ 164,211</b>      |
|  | <b>\$ 491</b>   | <b>\$ 159,048</b>                                | <b>\$ 4,672</b>                                    |                        |
| <b>Liabilities</b>                               |   |  |  |                        |
| <b>Future contract benefits:</b>                 |   |  |  |                        |
| Indexed annuity contracts embedded derivatives   | \$ -  | \$ -   | \$ (342)   | \$ (342)               |
| GLB reserves embedded derivatives                | -   | -  | (2,343)  | (2,343)                |
| Long-term debt - interest rate swap agreements   | -   | (277)  | -  | (277)                  |
| Reinsurance related embedded derivatives         | -   | (177)  | -  | (177)                  |
| VIEs' liabilities - derivative instruments       | -   | -  | (307)  | (307)                  |
| <b>Other liabilities:</b>                        |   |  |  |                        |
| Deferred compensation plans embedded derivatives | -   | -  | (325)  | (325)                  |
| Credit default swaps                             | -   | -  | (15)   | (15)                   |

|                   |    |   |    |       |    |         |    |         |
|-------------------|----|---|----|-------|----|---------|----|---------|
| Total liabilities | \$ | - | \$ | (454) | \$ | (3,332) | \$ | (3,786) |
|-------------------|----|---|----|-------|----|---------|----|---------|

|  | As of December 31, 2010   |  |  |                        |
|--|---|--|--|------------------------|
|  | Quoted<br>Prices<br>in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
| <b>Assets</b>                                    |   |  |  |                        |
| <b>Investments:</b>                              |   |  |  |                        |
| Fixed maturity AFS securities:                   |   |  |  |                        |
| Corporate bonds                                  | \$ 60   | \$ 49,864  | \$ 1,816   | \$ 51,740              |
| U.S. Government bonds                            | 160   | 3  | 2  | 165                    |
| Foreign government bonds                         | -   | 395  | 113  | 508                    |
| MBS:   |   |  |  |                        |
| CMOs   | -   | 5,734  | 23   | 5,757                  |
| MPTS   | -   | 2,985  | 96   | 3,081                  |
| CMBS   | -   | 1,944  | 109  | 2,053                  |
| ABS CDOs   | -   | 2  | 172  | 174                    |
| State and municipal bonds                        | -   | 3,155  | -  | 3,155                  |
| Hybrid and redeemable preferred securities       | 18  | 1,260  | 119  | 1,397                  |
| VIEs' fixed maturity securities                  | -   | 584  | -  | 584                    |
| Equity AFS securities:                           |   |  |  |                        |
| Banking securities                               | -   | 58   | -  | 58                     |
| Insurance securities                             | 3   | -  | 34   | 37                     |
| Other financial services securities              | -   | 8  | 24   | 32                     |
| Other securities                                 | 34  | 2  | 34   | 70                     |
| Trading securities                               | 2   | 2,518  | 76   | 2,596                  |
| Derivative investments                           | -   | (419)  | 1,495  | 1,076                  |
| Cash and invested cash                           | -   | 2,741  | -  | 2,741                  |
| Separate account assets                          | -   | 84,630   | -  | 84,630                 |
| Total assets                                     | \$ 277  | \$ 155,464                                       | \$ 4,113   | \$ 159,854             |
| <b>Liabilities</b>                               |   |  |  |                        |
| <b>Future contract benefits:</b>                 |   |  |  |                        |
| Indexed annuity contracts embedded derivatives   | \$ -  | \$ -   | \$ (497)   | \$ (497)               |
| GLB reserves embedded derivatives                | -   | -  | (408)  | (408)                  |
| Long-term debt - interest rate swap agreements   | -   | (55)   | -  | (55)                   |
| Reinsurance related embedded derivatives         | -   | (102)  | -  | (102)                  |
| VIEs' liabilities - derivative instruments       | -   | -  | (209)  | (209)                  |
| <b>Other liabilities:</b>                        |   |  |  |                        |
| Deferred compensation plans embedded derivatives | -   | -  | (363)  | (363)                  |
| Credit default swaps                             | -   | -  | (16)   | (16)                   |
| Total liabilities                                | \$ -  | \$ (157)   | \$ (1,493)   | \$ (1,650)             |





The following summarizes changes to our financial instruments carried at fair value (in millions) and classified within Level 3 of the fair value hierarchy. This summary excludes any effect of amortization of DAC, VOBA, DSI and DFEL. The gains and losses below may include changes in fair value due in part to observable inputs that are a component of the valuation methodology.

|  | For the Three Months Ended September 30, 2011 |            |          |              |           |          |
|--|---|------------|----------|--------------|-----------|----------|
|  | Beginning                                     | Items      | Gains    | Issuances,   | Transfers | Ending   |
|  | Fair  | Included   | (Losses) | Sales,       | In or     | Fair     |
|  | Value   | in         | in       | Maturities,  | Out       | Value    |
|  |   | Net        | OCI      | Settlements, | of        |          |
|  |   | Income     | and      | Calls,       | Level     |          |
|  |   |            | Other    | Net          | 3,        |          |
|  |   |            | (1)      | Net          | Net (2)   |          |
| Investments: (3)                                     |   |            |          |              |           |          |
| Fixed maturity AFS securities:                       |   |            |          |              |           |          |
| Corporate bonds                                      | \$ 1,573                                      | \$ (18)    | \$ (33)  | \$ (11)      | \$ (11)   | \$ 1,500 |
| U.S. Government bonds                                | 2   | -          | -        | (1)          | -         | 1        |
| Foreign government bonds                             | 96  | 1          | 9        | (1)          | -         | 105      |
| MBS:   |   |            |          |              |           |          |
| CMOs   | 28  | (1)        | -        | (1)          | (7)       | 19       |
| MPTS   | 133   | -          | 2        | 25           | (40)      | 120      |
| CMBS   | 53  | (7)        | 3        | (12)         | -         | 37       |
| ABS CDOs   | 126   | 5          | (8)      | (12)         | -         | 111      |
| Hybrid and redeemable preferred securities           | 106   | -          | (12)     | (18)         | 16        | 92       |
| Equity AFS securities:                               |   |            |          |              |           |          |
| Insurance securities                                 | 30  | -          | (6)      | -            | -         | 24       |
| Other financial services securities                  | 22  | -          | (4)      | -            | -         | 18       |
| Other securities                                     | 44  | -          | (4)      | 10           | -         | 50       |
| Trading securities                                   | 71  | 1          | 1        | (5)          | 1         | 69       |
| Derivative investments                               | 1,492   | 684        | 340      | 10           | -         | 2,526    |
| Future contract benefits: (4)                        |   |            |          |              |           |          |
| Indexed annuity contracts embedded derivatives       | (506)   | 135        | -        | 29           | -         | (342)    |
| GLB reserves embedded derivatives                    | (278)   | (2,065)    | -        | -            | -         | (2,343)  |
| VIEs' liabilities - derivative instruments (5)       | (198)   | (109)      | -        | -            | -         | (307)    |
| Other liabilities:                                   |   |            |          |              |           |          |
| Deferred compensation plans embedded derivatives (6) | (360)   | 22         | -        | 13           | -         | (325)    |
| Credit default swaps (7)                             | (7)   | (8)        | -        | -            | -         | (15)     |
| Total, net   | \$ 2,427                                      | \$ (1,360) | \$ 288   | \$ 26        | \$ (41)   | \$ 1,340 |

For the Three Months Ended September 30, 2010

|   | Beginning<br>Fair<br>Value | Items<br>Included<br>in<br>Net<br>Income | Gains<br>(Losses)<br>in<br>OCI<br>and<br>Other<br>(1) | Issuances,<br>Sales<br>Maturities,<br>Settlements,<br>Calls,<br>Net | Transfers<br>In or<br>Out<br>of<br>Level 3,<br>Net (2) | Ending<br>Fair<br>Value |
|---|----------------------------|--|---|---|--|-------------------------|
| Investments: (3)  |                            |  |   |   |  |                         |
| Fixed maturity AFS securities:                          |                            |  |   |   |  |                         |
| Corporate bonds   | \$ 1,907                   | \$ (31)                                  | \$ 81   | \$ (84)   | \$ (78)  | \$ 1,795                |
| U.S. Government bonds                                   | 4                          | -  | -   | (2)   | -  | 2                       |
| Foreign government bonds                                | 92                         | -  | 8   | (1)   | (1)  | 98                      |
| MBS:  |                            |  |   |   |  |                         |
| CMOs  | 27                         | (3)                                      | 3   | 19  | -  | 46                      |
| MPTS  | 101                        | -  | 1   | (2)   | -  | 100                     |
| CMBS  | 119                        | (4)                                      | 13  | (4)   | (1)  | 123                     |
| ABS CDOs  | 156                        | -  | 7   | (3)   | -  | 160                     |
| State and municipal bonds                               | 20                         | -  | -   | -   | (20)   | -                       |
| Hybrid and redeemable<br>preferred securities           | 97                         | -  | 6   | -   | -  | 103                     |
| Equity AFS securities:                                  |                            |  |   |   |  |                         |
| Insurance securities                                    | 26                         | -  | 5   | 1   | -  | 32                      |
| Other financial services securities                     | 23                         | 3  | 1   | (4)   | -  | 23                      |
| Other securities  | 34                         | -  | (1)   | -   | -  | 33                      |
| Trading securities                                      | 77                         | 1  | -   | (1)   | (1)  | 76                      |
| Derivative investments                                  | 2,005                      | (244)                                    | 1   | 75  | -  | 1,837                   |
| Future contract benefits: (4)                           |                            |  |   |   |  |                         |
| Indexed annuity contracts embedded<br>derivatives       | (383)                      | (70)                                     | -   | (3)   | -  | (456)                   |
| GLB reserves embedded derivatives                       | (1,669)                    | 188                                      | -   | -   | -  | (1,481)                 |
| VIEs' liabilities - derivative<br>instruments (5)       | (297)                      | 51                                       | -   | -   | -  | (246)                   |
| Other liabilities:                                      |                            |  |   |   |  |                         |
| Deferred compensation plans embedded<br>derivatives (6) | (319)                      | (14)                                     | -   | (5)   | -  | (338)                   |
| Credit default swaps (7)                                | (30)                       | 12                                       | -   | -   | -  | (18)                    |
| Total, net  | \$ 1,990                   | \$ (111)                                 | \$ 125  | \$ (14)   | \$ (101)   | \$ 1,889                |

For the Nine Months Ended September 30, 2011

|   | Beginning<br>Fair<br>Value | Items<br>Included<br>in<br>Net<br>Income | Gains<br>(Losses)<br>in<br>OCI<br>and<br>Other<br>(1) | Issuances,<br>Sales,<br>Maturities,<br>Settlements,<br>Calls,<br>Net | Transfers<br>In or<br>Out<br>of<br>Level 3,<br>Net (2) | Ending<br>Fair<br>Value |
|---|----------------------------|--|---|--|--|-------------------------|
| Investments: (3)  |                            |  |   |  |  |                         |
| Fixed maturity AFS securities:                          |                            |  |   |  |  |                         |
| Corporate bonds   | \$ 1,816                   | \$ 5                                     | \$ 10   | \$ (247)   | \$ (84)  | \$ 1,500                |
| U.S. Government bonds                                   | 2                          | -  | -   | (1)  | -  | 1                       |
| Foreign government bonds                                | 113                        | -  | 12  | (3)  | (17)   | 105                     |
| MBS:  |                            |  |   |  |  |                         |
| CMOs  | 23                         | (3)                                      | 3   | (4)  | -  | 19                      |
| MPTS  | 96                         | -  | 4   | 20   | -  | 120                     |
| CMBS  | 109                        | (53)                                     | 57  | (75)   | (1)  | 37                      |
| ABS CDOs  | 172                        | 19                                       | (17)  | (63)   | -  | 111                     |
| Hybrid and redeemable<br>preferred securities           | 119                        | -  | (5)   | (18)   | (4)  | 92                      |
| Equity AFS securities:                                  |                            |  |   |  |  |                         |
| Insurance securities                                    | 34                         | 1  | (6)   | (5)  | -  | 24                      |
| Other financial services securities                     | 24                         | 7  | (5)   | (8)  | -  | 18                      |
| Other securities  | 34                         | -  | (2)   | 16   | 2  | 50                      |
| Trading securities                                      | 76                         | -  | 4   | (8)  | (3)  | 69                      |
| Derivative investments                                  | 1,495                      | 600                                      | 335   | 96   | -  | 2,526                   |
| Future contract benefits: (4)                           |                            |  |   |  |  |                         |
| Indexed annuity contracts embedded<br>derivatives       | (497)                      | 80                                       | -   | 75   | -  | (342)                   |
| GLB reserves embedded derivatives                       | (408)                      | (1,935)                                  | -   | -  | -  | (2,343)                 |
| VIEs' liabilities - derivative<br>instruments (5)       | (209)                      | (98)                                     | -   | -  | -  | (307)                   |
| Other liabilities:                                      |                            |  |   |  |  |                         |
| Deferred compensation plans embedded<br>derivatives (6) | (363)                      | 10                                       | -   | 28   | -  | (325)                   |
| Credit default swaps (7)                                | (16)                       | (5)                                      | -   | 6  | -  | (15)                    |
| Total, net  | \$ 2,620                   | \$ (1,372)                               | \$ 390  | \$ (191)   | \$ (107)   | \$ 1,340                |

For the Nine Months Ended September 30, 2010

|   | Beginning<br>Fair<br>Value | Items<br>Included<br>in<br>Net<br>Income | Gains<br>(Losses)<br>in<br>OCI<br>and<br>Other<br>(1) | Issuances,<br>Sales,<br>Maturities,<br>Settlements,<br>Calls,<br>Net | Transfers<br>In or<br>Out<br>of<br>Level 3,<br>Net (2) | Ending<br>Fair<br>Value |
|---|----------------------------|--|---|--|--|-------------------------|
| Investments: (3)  |                            |  |   |  |  |                         |
| Fixed maturity AFS securities:                          |                            |  |   |  |  |                         |
| Corporate bonds   | \$ 2,070                   | \$ (37)                                  | \$ 86   | \$ (234)   | \$ (90)  | \$ 1,795                |
| U.S. Government bonds                                   | 3                          | -  | -   | (4)  | 3  | 2                       |
| Foreign government bonds                                | 92                         | -  | 10  | (4)  | -  | 98                      |
| MBS:  |                            |  |   |  |  |                         |
| CMOs  | 35                         | (5)                                      | 4   | 16   | (4)  | 46                      |
| MPTS  | 101                        | -  | 5   | (6)  | -  | 100                     |
| CMBS  | 259                        | (6)                                      | 36  | (48)   | (118)  | 123                     |
| ABS:  |                            |  |   |  |  |                         |
| CDOs  | 153                        | -  | 18  | (11)   | -  | 160                     |
| CLNs  | 322                        | -  | 278   | -  | (600)  | -                       |
| Hybrid and redeemable<br>preferred securities           | 156                        | 3  | (26)  | (30)   | -  | 103                     |
| Equity AFS securities:                                  |                            |  |   |  |  |                         |
| Insurance securities                                    | 43                         | -  | -   | (11)   | -  | 32                      |
| Other financial services securities                     | 22                         | -  | 6   | (5)  | -  | 23                      |
| Other securities  | 23                         | -  | (1)   | 11   | -  | 33                      |
| Trading securities                                      | 91                         | 2  | (10)  | (6)  | (1)  | 76                      |
| Derivative investments                                  | 1,368                      | 242                                      | 9   | 218  | -  | 1,837                   |
| Future contract benefits: (4)                           |                            |  |   |  |  |                         |
| Indexed annuity contracts embedded<br>derivatives       | (419)                      | (19)                                     | -   | (18)   | -  | (456)                   |
| GLB reserves embedded derivatives                       | (676)                      | (805)                                    | -   | -  | -  | (1,481)                 |
| VIEs' liabilities - derivative<br>instruments (5)       | -                          | (21)                                     | -   | -  | (225)  | (246)                   |
| Other liabilities:                                      |                            |  |   |  |  |                         |
| Deferred compensation plans embedded<br>derivatives (6) | (332)                      | (14)                                     | -   | 8  | -  | (338)                   |
| Credit default swaps (7)                                | (65)                       | 4  | -   | 43   | -  | (18)                    |
| Total, net  | \$ 3,246                   | \$ (656)                                 | \$ 415  | \$ (81)  | \$ (1,035)   | \$ 1,889                |

- (1) The changes in fair value of the interest rate swaps are offset by an adjustment to derivative investments. See "Derivatives Instruments Designated and Qualifying as Fair Value Hedges" section in Note 6.
- (2) Transfers in or out of Level 3 for AFS and trading securities are displayed at amortized cost as of the beginning-of-period. For AFS and trading securities, the difference between beginning-of-period amortized cost and beginning-of-period fair value was included in OCI and earnings, respectively, in prior periods.
- (3) Amortization and accretion of premiums and discounts are included in net investment income on our Consolidated Statements of Income (Loss). Gains (losses) from sales, maturities, settlements and calls and OTTI are included in realized gain (loss) on our Consolidated Statements of Income (Loss).
- (4)

Gains (losses) from sales, maturities, settlements and calls are included in realized gain (loss) on our Consolidated Statements of Income (Loss).

- (5) The changes in fair value of the credit default swaps, contingency forwards and excess mortality swap are included in realized gain (loss) on our Consolidated Statements of Income (Loss).

- (6) Deferrals and subsequent changes in fair value for the participants' investment options are reported in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income (Loss).
- (7) Gains (losses) from sales, maturities, settlements and calls are included in net investment income on our Consolidated Statements of Income (Loss).

The following provides the components of the items included in issuances, sales, maturities, settlements, calls, net, excluding any effect of amortization of DAC, VOBA, DSI and DFEL and changes in future contract benefits, (in millions) as reported above:

For the Three Months Ended September 30, 2011  
 Issuances Sales Maturities Settlements Calls Total

Investments:

|  |        |         |         |        |        |         |
|--|--------|---------|---------|--------|--------|---------|
| Fixed maturity AFS securities:                   |        |         |         |        |        |         |
| Corporate bonds                                  | \$ 22  | \$ (14) | \$ (10) | \$ (9) | \$ -   | \$ (11) |
| U.S. Government bonds                            | -      | -       | -       | (1)    | -      | (1)     |
| Foreign government bonds                         | -      | -       | -       | -      | (1)    | (1)     |
| MBS:   |        |         |         |        |        |         |
| CMOs   | -      | -       | -       | (1)    | -      | (1)     |
| MPTS   | 28     | (1)     | -       | (2)    | -      | 25      |
| CMBS   | -      | -       | -       | (12)   | -      | (12)    |
| ABS CDOs   | -      | -       | -       | (12)   | -      | (12)    |
| Hybrid and redeemable preferred securities       | -      | (18)    | -       | -      | -      | (18)    |
| Equity AFS securities:                           |        |         |         |        |        |         |
| Other securities                                 | 10     | -       | -       | -      | -      | 10      |
| Trading securities                               | -      | (2)     | -       | (3)    | -      | (5)     |
| Derivative investments                           | 87     | 6       | (83)    | -      | -      | 10      |
| Future contract benefits:                        |        |         |         |        |        |         |
| Indexed annuity contracts embedded derivatives   | (11)   | -       | -       | 40     | -      | 29      |
| Other liabilities:                               |        |         |         |        |        |         |
| Deferred compensation plans embedded derivatives | -      | -       | -       | 13     | -      | 13      |
| Total, net                                       | \$ 136 | \$ (29) | \$ (93) | \$ 13  | \$ (1) | \$ 26   |

For the Nine Months Ended September 30, 2011  
 Issuances Sales Maturities Settlements Calls Total

|  |        |          |          |         |         |          |
|--|--------|----------|----------|---------|---------|----------|
| Investments:                                     |        |          |          |         |         |          |
| Fixed maturity AFS securities:                   |        |          |          |         |         |          |
| Corporate bonds                                  | \$ 45  | \$ (146) | \$ (11)  | \$ (46) | \$ (89) | \$ (247) |
| U.S. Government bonds                            | -      | -        | -        | (1)     | -       | (1)      |
| Foreign government bonds                         | -      | (2)      | -        | -       | (1)     | (3)      |
| MBS:   |        |          |          |         |         |          |
| CMOs   | -      | -        | -        | (4)     | -       | (4)      |
| MPTS   | 28     | (1)      | -        | (7)     | -       | 20       |
| CMBS   | -      | (53)     | -        | (22)    | -       | (75)     |
| ABS CDOs   | -      | (34)     | -        | (29)    | -       | (63)     |
| Hybrid and redeemable preferred securities       | -      | (18)     | -        | -       | -       | (18)     |
| Equity AFS securities:                           |        |          |          |         |         |          |
| Insurance securities                             | 2      | (7)      | -        | -       | -       | (5)      |
| Other financial services securities              | -      | (8)      | -        | -       | -       | (8)      |
| Other securities                                 | 16     | -        | -        | -       | -       | 16       |
| Trading securities                               | -      | (3)      | -        | (5)     | -       | (8)      |
| Derivative investments                           | 362    | (27)     | (239)    | -       | -       | 96       |
| Future contract benefits:                        |        |          |          |         |         |          |
| Indexed annuity contracts embedded derivatives   | (49)   | -        | -        | 124     | -       | 75       |
| Other liabilities:                               |        |          |          |         |         |          |
| Deferred compensation plans embedded derivatives | -      | -        | -        | 28      | -       | 28       |
| Credit default swaps                             | -      | 6        | -        | -       | -       | 6        |
| Total, net                                       | \$ 404 | \$ (293) | \$ (250) | \$ 38   | \$ (90) | \$ (191) |

The following summarizes changes in unrealized gains (losses) included in net income, excluding any effect of amortization of DAC, VOBA, DSI and DFEL and changes in future contract benefits, related to financial instruments carried at fair value classified within Level 3 that we still held (in millions):

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |          | For the Nine<br>Months Ended<br>September 30,<br>2010 |          |
|--|--|----------|---|----------|
| Investments: (1)                                     |  |          |   |          |
| Derivative investments                               | \$ 696   | \$ (267) | \$ 574  | \$ 222   |
| Future contract benefits: (1)                        |  |          |   |          |
| Indexed annuity contracts embedded derivatives       | (4)  | 105      | -   | 35       |
| GLB reserves embedded derivatives                    | (2,011)  | 221      | (1,781)   | (688)    |
| VIEs' liabilities - derivative instruments (1)       | (108)  | 51       | (98)  | (21)     |
| Other liabilities:                                   |  |          |   |          |
| Deferred compensation plans embedded derivatives (2) | 22   | (14)     | 10  | (14)     |
| Credit default swaps (3)                             | (8)  | 11       | (7)   | (15)     |
| Total, net   | \$ (1,413)   | \$ 107   | \$ (1,302)  | \$ (481) |

(1) Included in realized gain (loss) on our Consolidated Statements of Income (Loss).



- (2) Included in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income (Loss).
- (3) Included in net investment income on our Consolidated Statements of Income (Loss).

The following provides the components of the transfers in and out of Level 3 (in millions) as reported above:

|  | For the Three Months<br>Ended September 30,<br>2011 |                   |         | For the Three Months<br>Ended September 30,<br>2010 |                   |          |
|--|---|-------------------|---------|---|-------------------|----------|
|  | Transfers   |                   | Total   | Transfers   |                   | Total    |
|  | In to<br>Level<br>3                                 | Out of<br>Level 3 |         | In to<br>Level<br>3                                 | Out of<br>Level 3 |          |
|  |   |                   |         |   |                   |          |
| Investments:                               |   |                   |         |   |                   |          |
| Fixed maturity AFS securities:             |   |                   |         |   |                   |          |
| Corporate bonds                            | \$ 4  | \$ (15)           | \$ (11) | \$ 6  | \$ (84)           | \$ (78)  |
| Foreign government bonds                   | -   | -                 | -       | -   | (1)               | (1)      |
| MBS:                                       |   |                   |         |   |                   |          |
| CMOs                                       | -   | (7)               | (7)     | -   | -                 | -        |
| MPTS                                       | -   | (40)              | (40)    | -   | -                 | -        |
| CMBS                                       | -   | -                 | -       | -   | (1)               | (1)      |
| State and municipal bonds                  | -   | -                 | -       | -   | (20)              | (20)     |
| Hybrid and redeemable preferred securities | 16  | -                 | 16      | -   | -                 | -        |
| Trading securities                         | 1   | -                 | 1       | -   | (1)               | (1)      |
| Total, net                                 | \$ 21   | \$ (62)           | \$ (41) | \$ 6  | \$ (107)          | \$ (101) |

|  | For the Nine Months<br>Ended September 30,<br>2011 |                   |          | For the Nine Months<br>Ended September 30, 2010 |                   |            |
|--|--|-------------------|----------|---|-------------------|------------|
|  | Transfers  |                   | Total    | Transfers                                       |                   | Total      |
|  | In to<br>Level<br>3                                | Out of<br>Level 3 |          | In to<br>Level<br>3                             | Out of<br>Level 3 |            |
|  |  |                   |          |   |                   |            |
| Investments:                               |  |                   |          |   |                   |            |
| Fixed maturity AFS securities:             |  |                   |          |   |                   |            |
| Corporate bonds                            | \$ 33  | \$ (117)          | \$ (84)  | \$ 117  | \$ (207)          | \$ (90)    |
| U.S. Government bonds                      | -  | -                 | -        | 3   | -                 | 3          |
| Foreign government bonds                   | -  | (17)              | (17)     | -   | -                 | -          |
| MBS:                                       |  |                   |          |   |                   |            |
| CMOs                                       | -  | -                 | -        | -   | (4)               | (4)        |
| CMBS                                       | -  | (1)               | (1)      | 3   | (121)             | (118)      |
| ABS CLNs                                   | -  | -                 | -        | -   | (600)             | (600)      |
| Hybrid and redeemable preferred securities | 18   | (22)              | (4)      | -   | -                 | -          |
| Equity AFS securities:                     |  |                   |          |   |                   |            |
| Other securities                           | 2  | -                 | 2        | -   | -                 | -          |
| Trading securities                         | 1  | (4)               | (3)      | -   | (1)               | (1)        |
| VIEs' liabilities - derivative instruments | -  | -                 | -        | (225)   | -                 | (225)      |
| Total, net                                 | \$ 54  | \$ (161)          | \$ (107) | \$ (102)  | \$ (933)          | \$ (1,035) |

For the three and nine months ended September 30, 2011, our corporate bonds transfers in and out were attributable primarily to the securities' observable market information being available or no longer being available. For the three

and nine months ended September 30, 2010, our corporate bonds transfers in and out were attributable primarily to the securities' observable market information being available or no longer being available and the ABS CLNs transfer out of Level 3 and VIEs' liabilities – derivative instruments transfer into Level 3 were related to new accounting guidance that is discussed in Note 4 of our 2010 Form 10-K. For the three and nine months ended September 30, 2011 and 2010, there were no significant transfers between Level 1 and 2 of the fair value hierarchy.

## 15. Segment Information

We provide products and services in two operating businesses and report results through four business segments as follows:

|            |                |
|------------|----------------|
| Business   | Corresponding  |
| Retirement | Segments       |
| Solutions  | Annuities      |
|            | Defined        |
|            | Contribution   |
| Insurance  |                |
| Solutions  | Life Insurance |
|            | Group          |
|            | Protection     |

We also have Other Operations, which includes the financial data for operations that are not directly related to the business segments. Our reporting segments reflect the manner by which our chief operating decision makers view and manage the business. The following is a brief description of these segments and Other Operations.

### Retirement Solutions

The Retirement Solutions business provides its products through two segments: Annuities and Defined Contribution. The Annuities segment provides tax-deferred investment growth and lifetime income opportunities for its clients by offering individual fixed annuities, including indexed annuities and variable annuities. The Defined Contribution segment provides employer-sponsored variable and fixed annuities, defined benefit, individual retirement accounts and mutual-fund based programs in the retirement plan marketplaces.

### Insurance Solutions

The Insurance Solutions business provides its products through two segments: Life Insurance and Group Protection. The Life Insurance segment offers wealth protection and transfer opportunities through term insurance, a linked-benefit product (which is a UL policy linked with riders that provide for long-term care costs) and both single (including corporate-owned UL and VUL and bank-owned UL and VUL) and survivorship versions of UL and VUL insurance products. The Group Protection segment offers group life, disability and dental insurance to employers. These offices develop business through employee benefit brokers, third-party administrators and other employee benefit firms.

### Other Operations

Other Operations includes investments related to the excess capital in our insurance subsidiaries; investments in media properties and other corporate investments; benefit plan net liability; the unamortized deferred gain on indemnity reinsurance related to the sale of reinsurance to Swiss Re in 2001; the results of certain disability income business due to the rescission of a reinsurance agreement with Swiss Re; the Institutional Pension business, which is a closed-block of pension business, the majority of which was sold on a group annuity basis, and is currently in run-off; and debt costs. We are actively managing our remaining radio station clusters to maximize performance and future value.

Segment operating revenues and income (loss) from operations are internal measures used by our management and Board of Directors to evaluate and assess the results of our segments. Income (loss) from operations is GAAP net income excluding the after-tax effects of the following items, as applicable:

- Realized gains and losses associated with the following (“excluded realized gain (loss)”):
  - § Sale or disposal of securities;
  - § Impairments of securities;
- § Change in the fair value of derivative investments, embedded derivatives within certain reinsurance arrangements and our trading securities;
  - § Change in the fair value of the derivatives we own to hedge our GDB riders within our variable annuities;
- § Change in the GLB embedded derivative reserves, net of the change in the fair value of the derivatives we own to hedge the changes in the embedded derivative reserves; and
- § Changes in the fair value of the embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations applicable to future reset periods for our indexed annuity products accounted for under the Derivatives and Hedging and the Fair Value Measurements and Disclosures Topics of the FASB ASC;
- Change in reserves accounted for under the Financial Services – Insurance – Claim Costs and Liabilities for Future Policy Benefits Subtopic of the FASB ASC resulting from benefit ratio unlocking on our GDB and GLB riders (“benefit ratio unlocking”);
- Income (loss) from the initial adoption of new accounting standards;

- Income (loss) from reserve changes (net of related amortization) on business sold through reinsurance;
- Gain (loss) on early extinguishment of debt;
- Losses from the impairment of intangible assets; and
- Income (loss) from discontinued operations.

Operating revenues represent GAAP revenues excluding the pre-tax effects of the following items, as applicable:

- Excluded realized gain (loss);
- Amortization of DFEL arising from changes in GDB and GLB benefit ratio unlocking;
- Amortization of deferred gains arising from the reserve changes on business sold through reinsurance; and
- Revenue adjustments from the initial adoption of new accounting standards.

We use our prevailing corporate federal income tax rate of 35% while taking into account any permanent differences for events recognized differently in our financial statements and federal income tax returns when reconciling our non-GAAP measures to the most comparable GAAP measure. Operating revenues and income (loss) from operations do not replace revenues and net income as the GAAP measures of our consolidated results of operations.

Segment information (in millions) was as follows:

|   | For the Three<br>Months Ended<br>September 30, |          | For the Nine<br>Months Ended<br>September 30, |          |
|---|--|----------|---|----------|
|   | 2011   | 2010     | 2011  | 2010     |
| Revenues  |  |          |   |          |
| Operating revenues:   |  |          |   |          |
| Retirement Solutions:   |  |          |   |          |
| Annuities   | \$ 710   | \$ 660   | \$ 2,175                                      | \$ 1,935 |
| Defined Contribution  | 248  | 245      | 771   | 730      |
| Total Retirement Solutions  | 958  | 905      | 2,946   | 2,665    |
| Insurance Solutions:  |  |          |   |          |
| Life Insurance  | 1,176  | 1,108    | 3,552   | 3,372    |
| Group Protection  | 479  | 451      | 1,458   | 1,367    |
| Total Insurance Solutions   | 1,655  | 1,559    | 5,010   | 4,739    |
| Other Operations  | 120  | 122      | 351   | 367      |
| Excluded realized gain (loss), pre-tax  | (185)  | 25       | (243)   | (27)     |
| Amortization of deferred gain arising from reserve<br>changes on business sold through reinsurance, pre-tax | 1  | 1        | 2   | 2        |
| Amortization of DFEL associated with<br>benefit ratio unlocking, pre-tax                                    | (1)  | 1        | (1)   | (1)      |
| Total revenues  | \$ 2,548                                       | \$ 2,613 | \$ 8,065                                      | \$ 7,745 |

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |        |
|--|--|--------|---|--------|
| Net Income (Loss)  |  |        |   |        |
| Income (loss) from operations:   |  |        |   |        |
| Retirement Solutions:  |  |        |   |        |
| Annuities  | \$ 162   | \$ 126 | \$ 459  | \$ 361 |
| Defined Contribution   | 40   | 50     | 132   | 122    |
| Total Retirement Solutions   | 202  | 176    | 591   | 483    |
| Insurance Solutions:   |  |        |   |        |
| Life Insurance   | 132  | 60     | 450   | 348    |
| Group Protection   | 28   | 9      | 78  | 54     |
| Total Insurance Solutions  | 160  | 69     | 528   | 402    |
| Other Operations   | (45)   | (40)   | (104)   | (113)  |
| Excluded realized gain (loss), after-tax   | (120)  | 17     | (158)   | (17)   |
| Gain (loss) on early extinguishment of debt, after-tax   | (5)  | -      | (5)   | -      |
| Income (expense) from reserve changes (net of related<br>amortization) on business sold through reinsurance, after-tax | -  | 1      | 1   | 1      |
| Benefit ratio unlocking, after-tax   | (41)   | 25     | (37)  | -      |
| Income (loss) from continuing operations,<br>after-tax   | 151  | 248    | 816   | 756    |
| Income (loss) from discontinued operations,<br>after-tax   | (8)  | (2)    | (8)   | 29     |
| Net income (loss)  | \$ 143   | \$ 246 | \$ 808  | \$ 785 |

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following Management’s Discussion and Analysis (“MD&A”) is intended to help the reader understand the financial condition as of September 30, 2011, compared with December 31, 2010, and the results of operations for the three and nine months ended September 30, 2011, compared with the corresponding periods in 2010 of Lincoln National Corporation and its consolidated subsidiaries. Unless otherwise stated or the context otherwise requires, “LNC,” “Lincoln,” “Company,” “we,” “our” or “us” refers to Lincoln National Corporation and its consolidated subsidiaries. The MD&A is provided as a supplement to, and should be read in conjunction with our consolidated financial statements and the accompanying notes to the consolidated financial statements (“Notes”) presented in “Part I – Item 1. Financial Statements”; our Form 10-K for the year ended December 31, 2010 (“2010 Form 10-K”), including the sections entitled “Part I – Item 1A. Risk Factors,” as updated in “Part II – Item 1A. Risk Factors” below, “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Part II – Item 8. Financial Statements and Supplementary Data”; our quarterly reports on Form 10-Q filed in 2011; and our current reports on Form 8-K filed in 2011.

In this report, in addition to providing consolidated revenues and net income (loss), we also provide segment operating revenues and income (loss) from operations because we believe they are meaningful measures of revenues and the profitability of our operating segments. Income (loss) from operations is net income recorded in accordance with United States of America generally accepted accounting principles (“GAAP”) excluding the after-tax effects of the following items, as applicable:

- Realized gains and losses associated with the following (“excluded realized gain (loss)”):
  - § Sales or disposals of securities;
  - § Impairments of securities;
- § Change in the fair value of derivative investments, embedded derivatives within certain reinsurance arrangements and our trading securities;
- § Change in the fair value of the derivatives we own to hedge our guaranteed death benefit (“GDB”) riders within our variable annuities, which is referred to as “GDB derivatives results”;
- § Change in the fair value of the embedded derivatives of our guaranteed living benefit (“GLB”) riders within our variable annuities accounted for under the Derivatives and Hedging and the Fair Value Measurements and Disclosures Topics of the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification™ (“ASC”) (“embedded derivative reserves”), net of the change in the fair value of the derivatives we own to hedge the changes in the embedded derivative reserves, the net of which is referred to as “GLB net derivative results”; and
- § Changes in the fair value of the embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations applicable to future reset periods for our indexed annuity products accounted for under the Derivatives and Hedging and the Fair Value Measurements and Disclosures Topics of the FASB ASC (“indexed annuity forward-starting option”);
- Change in reserves accounted for under the Financial Services – Insurance – Claim Costs and Liabilities for Future Policy Benefits Subtopic of the FASB ASC resulting from benefit ratio unlocking on our GDB and GLB riders (“benefit ratio unlocking”);
- Income (loss) from the initial adoption of new accounting standards;
- Income (loss) from reserve changes (net of related amortization) on business sold through reinsurance;
- Gain (loss) on early extinguishment of debt;
- Losses from the impairment of intangible assets; and
- Income (loss) from discontinued operations.

Income (loss) from operations available to common stockholders is net income (loss) available to common stockholders (used in the calculation of earnings (loss) per share) in accordance with GAAP, excluding the after-tax effects of the items above and the acceleration of our Series B preferred stock discount as a result of redemption prior



to five years from the date of issuance.

Operating revenues represent GAAP revenues excluding the pre-tax effects of the following items, as applicable:

- Excluded realized gain (loss);
- Amortization of deferred front-end loads (“DFEL”) arising from changes in GDB and GLB benefit ratio unlocking;
- Amortization of deferred gains arising from the reserve changes on business sold through reinsurance; and
- Revenue adjustments from the initial adoption of new accounting standards.

Operating revenues and income (loss) from operations are the financial performance measures we use to evaluate and assess the results of our segments. Accordingly, we report operating revenues and income (loss) from operations by segment in Note 15. Our management believes that operating revenues and income (loss) from operations explain the results of our ongoing businesses in a manner that allows for a better understanding of the underlying trends in our current businesses because the excluded items are unpredictable and not necessarily indicative of current operating fundamentals or future performance of the business segments,

and, in many instances, decisions regarding these items do not necessarily relate to the operations of the individual segments. In addition, we believe that our definitions of operating revenues and income (loss) from operations will provide investors with a more valuable measure of our performance because it better reveals trends in our business.

We use our prevailing corporate federal income tax rate of 35% while taking into account any permanent differences for events recognized differently in our financial statements and federal income tax returns when reconciling our non-GAAP measures to the most comparable GAAP measure. Operating revenues and income (loss) from operations do not replace revenues and net income as the GAAP measures of our consolidated results of operations.

Certain reclassifications have been made to prior periods' financial information.

#### FORWARD-LOOKING STATEMENTS – CAUTIONARY LANGUAGE

Certain statements made in this report and in other written or oral statements made by us or on our behalf are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 (“PSLRA”). A forward-looking statement is a statement that is not a historical fact and, without limitation, includes any statement that may predict, forecast, indicate or imply future results, performance or achievements, and may contain words like: “believe,” “anticipate,” “expect,” “estimate,” “project,” “will,” “shall” and other words or phrases with similar meaning in connection with a discussion of future operating or financial performance. In particular, these include statements relating to future actions, trends in our businesses, prospective services or products, future performance or financial results and the outcome of contingencies, such as legal proceedings. We claim the protection afforded by the safe harbor for forward-looking statements provided by the PSLRA.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from the results contained in the forward-looking statements. Risks and uncertainties that may cause actual results to vary materially, some of which are described within the forward-looking statements, include, among others:

- Deterioration in general economic and business conditions that may affect account values, investment results, guaranteed benefit liabilities, premium levels, claims experience and the level of pension benefit costs, funding and investment results;
- Adverse global capital and credit market conditions could affect our ability to raise capital, if necessary, and may cause us to realize impairments on investments and certain intangible assets, including goodwill and a valuation allowance against deferred tax assets, which may reduce future earnings and/or affect our financial condition and ability to raise additional capital or refinance existing debt as it matures;
- Because of our holding company structure, the inability of our subsidiaries to pay dividends to the holding company in sufficient amounts could harm the holding company's ability to meet its obligations;
- Legislative, regulatory or tax changes, both domestic and foreign, that affect the cost of, or demand for, our subsidiaries' products, the required amount of reserves and/or surplus, or otherwise affect our ability to conduct business, including changes to statutory reserve requirements related to secondary guarantees under universal life such as a reinterpretation of reserve calculations under Actuarial Guideline 38 (also known as The Application of the Valuation of Life Insurance Policies Model Regulation, or “AG38”); changes to risk-based capital (“RBC”) requirements; restrictions on revenue sharing and 12b-1 payments; and the potential for U.S. federal tax reform;
- Uncertainty about the effect of rules and regulations to be promulgated under the Dodd-Frank Wall Street Reform and Consumer Protection Act on us and the economy and the financial services sector in particular;
- The initiation of legal or regulatory proceedings against us, and the outcome of any legal or regulatory proceedings, such as: adverse actions related to present or past business practices common in businesses in which we compete; adverse decisions in significant actions including, but not limited to, actions brought by federal and state authorities and class action cases; new decisions that result in changes in law; and unexpected trial court rulings;
-

Changes in or sustained low interest rates causing a reduction in investment income, a reduction in the interest margins of our businesses and a related reduction in estimated gross profits, and demand for our products;

- A decline in the equity markets causing a reduction in the sales of our subsidiaries' products, a reduction of asset-based fees that our subsidiaries charge on various investment and insurance products, an acceleration of the net amortization of deferred acquisition costs ("DAC"), value of business acquired ("VOBA"), deferred sales inducements ("DSI") and DFEL and an increase in liabilities related to guaranteed benefit features of our subsidiaries' variable annuity products;
- Ineffectiveness of our risk management policies and procedures, including various hedging strategies used to offset the effect of changes in the value of liabilities due to changes in the level and volatility of the equity markets and interest rates;
- A deviation in actual experience regarding future persistency, mortality, morbidity, interest rates or equity market returns from the assumptions used in pricing our subsidiaries' products, in establishing related insurance reserves and in the net amortization of DAC, VOBA, DSI and DFEL, which may reduce future earnings;
- Changes in GAAP, including moving to International Financial Reporting Standards, that may result in unanticipated changes to our net income;

- Lowering of one or more of our debt ratings issued by nationally recognized statistical rating organizations and the adverse effect such action may have on our ability to raise capital and on our liquidity and financial condition;
- Lowering of one or more of the insurer financial strength ratings of our insurance subsidiaries and the adverse effect such action may have on the premium writings, policy retention, profitability of our insurance subsidiaries and liquidity;
- Significant credit, accounting, fraud, corporate governance or other issues that may adversely affect the value of certain investments in our portfolios, as well as counterparties to which we are exposed to credit risk, requiring that we realize losses on investments;
- The effect of acquisitions and divestitures, restructurings, product withdrawals and other unusual items;
- The adequacy and collectibility of reinsurance that we have purchased;
- Acts of terrorism, a pandemic, war or other man-made and natural catastrophes that may adversely affect our businesses and the cost and availability of reinsurance;
- Competitive conditions, including pricing pressures, new product offerings and the emergence of new competitors, that may affect the level of premiums and fees that our subsidiaries can charge for their products;
- The unknown effect on our subsidiaries' businesses resulting from changes in the demographics of their client base, as aging baby-boomers move from the asset-accumulation stage to the asset-distribution stage of life; and
- Loss of key management, financial planners or wholesalers.

The risks included here are not exhaustive. Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other documents filed with the Securities and Exchange Commission ("SEC") include additional factors that could affect our business and financial performance. Moreover, we operate in a rapidly changing and competitive environment. New risk factors emerge from time to time, and it is not possible for management to predict all such risk factors.

Further, it is not possible to assess the effect of all risk factors on our businesses or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. In addition, we disclaim any obligation to update any forward-looking statements to reflect events or circumstances that occur after the date of this report.

## INTRODUCTION

### Executive Summary

We are a holding company that operates multiple insurance and retirement businesses through subsidiary companies. Through our business segments, we sell a wide range of wealth protection, accumulation and retirement income products and solutions. These products include fixed and indexed annuities, variable annuities, universal life insurance ("UL"), variable universal life insurance ("VUL"), linked-benefit UL, term life insurance, mutual funds and group life, disability and dental.

We provide products and services in two operating businesses and report results through four business segments as follows:

|            |               |
|------------|---------------|
| Business   | Corresponding |
| Retirement | Segments      |
| Solutions  | Annuities     |
|            | Defined       |
|            | Contribution  |

Insurance  
Solutions      Life Insurance  
                    Group  
                    Protection

These operating businesses and their segments are described in “Part I – Item 1. Business” of our 2010 Form 10-K. We also have Other Operations, which includes the financial data for operations that are not directly related to the business segments.

For information on how we derive our revenues, see the discussion in results of operations by segment below.

#### Current Market Conditions

Recent unfavorable market conditions including, but not limited to, the following concerns are weighing on and threatening the financial stability of the U.S. economy:

- The effects of the European debt crisis;
- Volatile equity markets during the recent quarter;
- Uncertainty regarding the long-term effect of the recently passed Budget Control Act of 2011 and pending American Jobs Act;

- Downgrade by Standard and Poor's ("S&P") for the first time in history of the long-term credit rating of the U.S. sovereign debt to AA+ in August 2011; a credit rating review for the first time since 1996 by Moody's Investors Service ("Moody's") followed by placing the rating of the U.S. sovereign debt on negative outlook in August 2011; and warnings of possible downgrades of the U.S. sovereign debt by Fitch Ratings ("Fitch") in August 2011;
- The interest rate on overnight loans between banks controlled by the Federal Reserve Board remaining unchanged in August 2011 at 0% to 0.25%, with low rates expected to continue at least through mid-2013, in anticipation of weakening economic conditions and a subdued outlook on inflation, an indicator of general interest rate trends;
- Persistent high unemployment, shrinking unemployment benefits and weak job creation;
- Continued slow and unpredictable U.S. housing market;
- Declining consumer confidence as the August 2011 Consumer Confidence Index fell to a level not seen since April 2009 when the U.S. was still officially in recession, reflecting the lowest percentile since the inception of the index; and
- Ongoing conflicts in the Middle East.

The Federal Reserve's projections for the remainder of 2011 and 2012 announced in the second quarter of 2011 reflect weak growth and a slowing economic recovery. In the face of these economic challenges, we continue to focus on building our businesses through these difficult markets and beyond by developing and introducing high quality products, expanding distribution into new and existing key accounts and channels and targeting market segments that have high growth potential while maintaining a disciplined approach to managing our expenses.

As a result of our focus on building strong liquidity and capital positions and improving earnings in our core businesses, Moody's improved its outlook on our company to positive from stable on June 22, 2011. For more information about ratings, see "Part I – Item 1. Business – Ratings" in our 2010 Form 10-K.

### Significant Operational Matters

#### Earnings from Account Values

The Annuities and Defined Contribution segments are the most sensitive to the equity markets, as well as, to a lesser extent, our Life Insurance segment. We discuss the earnings effect of the equity markets on account values and the related asset-based earnings below in "Part I – Item 3. Quantitative and Qualitative Disclosures About Market Risk – Equity Market Risk – Effect of Equity Market Sensitivity." From December 31, 2010, to September 30, 2011, our account values were down \$4.6 billion driven primarily by a decrease in equity markets during the third quarter of 2011, partially offset by positive net flows during the first nine months of 2011.

#### Improvement of Return on Equity

One of our highest priorities continues to be increasing our return on equity ("ROE"). Growth in ROE will be driven by a number of items including:

- Earnings mix shift to businesses with higher returns;
- Continued sales of products that have higher returns than the products already in force; and
- Capital management actions consisting of redeployment of excess capital (including returning capital to common stockholders) and further generation of excess capital.

#### Strategic Investments

We continue to make strategic investments in our businesses to grow revenues, further spur productivity and improve our efficiency and service to our customers. These efforts include investments in technology and system upgrades,

new products for the voluntary market and expanded distribution focus.

#### Industry Trends

We continue to be influenced by a variety of trends that affect the industry. For information on these trends, see “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Introduction – Executive Summary – Industry Trends” in our 2010 Form 10-K.

## Issues and Outlook

For the remainder of 2011 and the near term, significant issues include:

- Increased actions by government and regulatory authorities to introduce regulations or interpret existing regulations or guidance in a manner that could have a significant effect on our earnings and/or business models, such as reinterpreting long-standing reserving methods for life insurance products with guarantee features;
- Continuation of the low interest rate environment in comparison to historical periods;
- Implementation of new accounting requirements in 2012 that could have a significant effect on the earnings and/or business models of companies within the insurance industry, including Lincoln; and
- Loss ratios remaining volatile in our Group Protection segment given the economic conditions.

In the face of these issues and potential issues, we expect to focus on the following:

- Closely monitoring our capital and liquidity positions taking into account the uncertain economic recovery and changing statutory accounting and reserving practices;
- Continuing to explore additional financing strategies addressing the statutory reserve strain related to our secondary guarantee UL products in order to manage our capital position effectively;
  - Taking actions to manage the risk of a continuation of lower interest rates;
- Closely monitoring ongoing activities in the legal and regulatory environment and taking an active role in the legislative and/or regulatory process;
- Controlling our non-medical loss ratios through continued focus on claims risk management;
- Increasing our product development activities together with identifying future product development initiatives;
- Evaluating opportunities for strategic investments in our businesses to grow revenues and further spur productivity; and
- Managing our expenses aggressively through process improvement initiatives combined with continued financial discipline and execution excellence throughout our operations.

For additional factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language.”

## Critical Accounting Policies and Estimates

The MD&A included in our 2010 Form 10-K contains a detailed discussion of our critical accounting policies and estimates. The following information updates the “Critical Accounting Policies and Estimates” provided in our 2010 Form 10-K and, accordingly, should be read in conjunction with the “Critical Accounting Policies and Estimates” discussed in our 2010 Form 10-K.

### DAC, VOBA, DSI and DFEL

#### New DAC Methodology

In October 2010, the FASB issued Accounting Standards Update No. 2010-26, “Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts” (referred to herein as the “new DAC methodology”), which clarifies the types of costs incurred by an insurance entity that can be capitalized in the acquisition of insurance contracts. Only those costs incurred that result directly from and are essential to the successful acquisition of new or renewal insurance contracts may be capitalized as deferrable acquisition costs. This analysis must be done on a contract-level basis. This new guidance contrasts to the existing guidance we follow that defines deferrable acquisition costs as



costs that vary with and are related primarily to new or renewal business, regardless of whether the acquisition efforts were successful or unsuccessful.

Some examples of acquisition costs that remain subject to deferral as part of the new DAC methodology include the following:

- Employee, agent or broker commissions for successful contract acquisitions;
- Wholesaler production bonuses for successful contract acquisitions;
- Renewal commissions and bonuses to agents or brokers;
- Medical and inspection fees for successful contract acquisitions;
- Premium-related taxes and assessments; and
- A portion of the salaries and benefits of certain employees involved in the underwriting, contract issuance and processing, medical and inspection and sales force contract selling functions related to the successful issuance or renewal of an insurance contract.

All other acquisition-related costs, including costs incurred by the insurer for soliciting potential customers, market research, training, administration, management of distribution and underwriting functions, unsuccessful acquisition or renewal efforts and product development, are considered non-deferrable acquisition costs and must be expensed in the period incurred.

In addition, the following indirect costs are considered non-deferrable acquisition costs as part of the new DAC methodology and must be charged to expense in the period incurred:

- Administrative costs;
- Rent;
- Depreciation;
- Occupancy costs;
- Equipment costs (including data processing equipment dedicated to acquiring insurance contracts); and
- Other general overhead.

We will adopt the new DAC methodology effective January 1, 2012, and have elected to apply the guidance retrospectively. We expect that our adoption of the new DAC methodology will result in an overall reduction in deferrable acquisition costs, partially offset by lower DAC amortization, in each of our business segments. We currently estimate that retrospective adoption will result in the restatement of all years presented with a cumulative effect adjustment to the opening balance of retained earnings for the earliest period presented of approximately \$950 million to \$1.15 billion. In addition, the adoption of this accounting guidance will result in a lower DAC adjustment associated with unrealized gains and losses on available-for-sale (“AFS”) securities and certain derivatives; therefore, we will also adjust these DAC balances as of January 1, 2012, through a cumulative effect adjustment to the opening balance of accumulated other comprehensive income (loss) (“AOCI”). This adjustment is dependent on our unrealized position as of the date of adoption. We believe that the total of our segment results would have declined by approximately 5% to 7% for the first nine months of 2011 had we applied the provisions of the new DAC methodology during 2011. This estimate does not include changes that management may make to mitigate the effects of this new DAC methodology.

#### Unlocking

As discussed and defined in our 2010 Form 10-K, we may record retrospective unlocking, prospective unlocking – assumption changes and prospective unlocking – model refinements on a quarterly basis that result in increases or decreases to the carrying values of DAC, VOBA, DSI, DFEL, embedded derivatives and reserves for life insurance and annuity products with living benefit and death benefit guarantees. The primary distinction between retrospective and prospective unlocking is that retrospective unlocking is driven by the difference between actual gross profits compared to estimated gross profits (“EGPs”) each period, while prospective unlocking is driven by changes in assumptions or projection models related to our expectations of future EGPs.

Details underlying the increase (decrease) to income from continuing operations from our prospective unlocking as a result of our annual comprehensive review (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |         |
|---|--|---------|
|   | 2011   | 2010    |
| Insurance fees:   |  |         |
| Annuities   | \$ 6   | \$ (3)  |
| Life Insurance  | (13)   | (6)     |
| Total insurance fees  | (7)  | (9)     |
| Realized gain (loss):   |  |         |
| Indexed annuity forward-starting option                       | -  | 2       |
| GLB   | (117)  | (1)     |
| Total realized gain (loss)                                    | (117)  | 1       |
| Total revenues  | (124)  | (8)     |
| Interest credited:  |  |         |
| Annuities   | 2  | (2)     |
| Total interest credited                                       | 2  | (2)     |
| Benefits:   |  |         |
| Annuities   | 43   | (1)     |
| Life Insurance  | (322)  | 153     |
| Total benefits  | (279)  | 152     |
| Underwriting, acquisition, insurance and other expenses:      |  |         |
| Annuities   | (13)   | 3       |
| Defined Contribution  | 3  | (17)    |
| Life Insurance  | 285  | (34)    |
| Total underwriting, acquisition, insurance and other expenses | 275  | (48)    |
| Total benefits and expenses                                   | (2)  | 102     |
| Income from continuing operations before taxes                | (122)  | (110)   |
| Federal income tax expense                                    | (43)   | (38)    |
| Income from continuing operations                             | \$ (79)  | \$ (72) |

For a discussion of the drivers of our prospective unlocking, see the results of operations by segment and "Realized Gain (Loss) and Benefit Ratio Unlocking" below.

#### Reversion to the Mean

As equity markets do not move in a systematic manner, we reset the baseline of account values from which EGPs are projected, which we refer to as our "reversion to the mean" ("RTM") process, as discussed in our 2010 Form 10-K.

As of September 30, 2011, our long-term equity market growth rate assumption, which is used in the determination of DAC, VOBA, DSI and DFEL amortization for the variable component of our variable annuity and VUL products, is an immediate drop of approximately 4% followed by growth going forward of 8% to 9% depending on the block of business and reflecting differences in contract holder fund allocations between fixed income and equity-type investments. If we were to have unlocked our RTM assumption in the corridor as of September 30, 2011, we would have recorded a favorable prospective unlocking of approximately \$100 million, pre-tax, for our Retirement Solutions business, and approximately \$10 million, pre-tax, for our Insurance Solutions business, as a result of improved market conditions since our last unlock of RTM in the fourth quarter of 2008.



## Goodwill and Other Intangible Assets

As discussed in our 2010 Form 10-K, our stock price trading below book value requires us to evaluate and reassess each reporting period whether or not there is an indicator that would require us to perform an impairment test. We believe that our stock price has been unfavorably affected by macroeconomic events and concerns about the economic recovery and other concerns about the global economy as discussed above in “Current Market Conditions,” and has experienced increased volatility in recent quarters and continues to be lower than our book value. We believe that our stock price is not representative of the underlying fair value of our reporting units and do not believe there is an indicator that requires us to perform an interim impairment test since our annual evaluation as of October 1, 2010. During the fourth quarter of 2011, we will be completing our annual evaluation of the recoverability of goodwill as of October 1, 2011.

Unfavorable changes to assumptions as compared to our prior year analysis or factors that could result in impairment include, but are not limited to, the following:

- Lower expectations for future sales levels or future sales profitability;
- Higher discount rates on new business assumptions; and
- Weakened expectations for the ability to execute future reinsurance transactions for life insurance business over the long-term or expectations for significant increases in the associated costs.

## Investments

## Investment Valuation

The following summarizes our investments carried at fair value by pricing source and the Fair Value Measurements and Disclosures Topic of the FASB ASC hierarchy level (in millions):

|   | As of September 30, 2011   |  |  |                        |
|---|--|--|--|------------------------|
|   | Quoted<br>Prices<br>in Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
| Priced by third party pricing services  | \$ 490   | \$ 66,797  | \$ -   | \$ 67,287              |
| Priced by independent broker quotations | -  | -  | 3,254  | 3,254                  |
| Priced by matrices                      | -  | 9,225  | -  | 9,225                  |
| Priced by other methods (1)             | -  | -  | 1,417  | 1,417                  |
| Total                                   | \$ 490   | \$ 76,022  | \$ 4,671   | \$ 81,183              |
| Percent of total                        | 1%   | 94%  | 5%   | 100%                   |

(1) Represents primarily securities for which pricing models were used to compute the fair values.

For more information about the three-level hierarchy that we use to categorize our financial instruments carried at fair value, see “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations –

Introduction – Critical Accounting Policies and Estimates – Investments – Investment Valuation” in our 2010 Form 10-K and Note 14.

As of September 30, 2011, we evaluated the markets that our securities trade in and concluded that none were inactive. We will continue to re-evaluate this conclusion, as needed, based on market conditions. We use an internationally recognized pricing service as our primary pricing source, and we generally do not obtain multiple prices for our financial instruments. We generally use prices from the pricing service rather than broker quotes as we have documentation from the pricing service on the observable market inputs that they use to determine the prices in contrast to the broker quotes where we have limited information on the pricing inputs. As of September 30, 2011, we only obtained multiple prices for 41 AFS and trading securities. These multiple prices were related primarily to instances where the vendor was providing a price for the first time and we also received a broker quote. In these instances, we used the price from the pricing service due to the higher reliability as discussed above. As of September 30, 2011, we used broker quotes for 105 securities as our final price source, representing approximately 2% of total securities owned.

## Derivatives

Our accounting policies for derivatives and the potential effect on interest spreads in a falling rate environment are discussed in Note 6 of this report and “Part II – Item 7A. Quantitative and Qualitative Disclosures About Market Risk” in our 2010 Form 10-K.

## Guaranteed Living Benefits

As of September 30, 2011, the fair value of our derivative assets, which hedge both our GLB and GDB features, and including margins generated by futures contracts, was \$3.0 billion. As of September 30, 2011, the sum of all GLB liabilities at fair value, excluding the non-performance risk (“NPR”) adjustment, and GDB reserves was \$2.8 billion, comprised of \$2.7 billion for GLB liabilities and \$0.1 billion for the GDB reserves. The fair value of the hedge assets exceeded the estimated liabilities by approximately \$200 million. However, the relationship of hedge assets to the liabilities for the guarantees may vary in any given reporting period due to market conditions, hedge performance and/or changes to the hedging strategy.

Approximately 47% of our variable annuity account values contained a guaranteed withdrawal benefit (“GWB”) rider as of September 30, 2011. Declines in the equity markets increase our exposure to potential benefits under the GWB contracts, leading to an increase in our existing liability for those benefits. The decrease in the equity markets over the recent months has increased our existing liability. For example, a GWB contract is “in the money” if the contract holder’s account balance falls below the guaranteed amount. As of September 30, 2011 and 2010, 91% and 45% respectively, of all GWB in-force contracts were “in the money,” and our exposure to the guaranteed amounts, after reinsurance, as of September 30, 2011 and 2010, was \$3.8 billion and \$1.7 billion, respectively. Our exposure before reinsurance for these same periods was \$4.1 billion and \$2.0 billion, respectively.

For information on our variable annuity hedging results, see our discussion in “Realized Gain (Loss) and Benefit Ratio Unlocking” below.

The following table presents our estimates of the potential instantaneous effect to realized gain (loss), which could result from sudden changes that may occur in equity markets, interest rates and implied market volatilities (in millions) at the levels indicated in the table and excludes the net cost of operating the hedging program. The amounts represent the estimated difference between the change in the portion of GLB reserves that is calculated on a fair value basis and the change in the value of the underlying hedge instruments after the amortization of DAC, VOBA, DSI and DFEL and taxes. These effects do not include any estimate of retrospective or prospective unlocking that could occur, nor do they estimate any change in the NPR component of the GLB reserve or any estimate of effects to our GLB benefit ratio unlocking. These estimates are based upon the recorded reserves as of October 6, 2011, and the related hedge instruments in place as of that date. The effects presented in the table below are not representative of the aggregate impacts that could result if a combination of such changes to equity market returns, interest rates and implied volatilities occurred.

|                                   | In-Force Sensitivities |         |        |        |
|-----------------------------------|------------------------|---------|--------|--------|
|                                   | -20%                   | -10%    | -5%    | 5%     |
| Equity Market Return              |                        |         |        |        |
| Hypothetical effect to net income | \$ (55)                | \$ (12) | \$ (3) | \$ (4) |
|                                   |                        |         | +25    | +50    |
| Interest Rates                    | -50 bps                | -25 bps | bps    | bps    |
| Hypothetical effect to net income | \$ (7)                 | \$ (2)  | \$ (3) | \$ (9) |
|                                   |                        |         | 2%     | 4%     |
| Implied Volatilities              | -4%                    | -2%     | 2%     | 4%     |

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Hypothetical effect to net income \$ 20 \$ 11 \$ (14) \$ (30)

The following table shows the effect (dollars in millions) of indicated changes in instantaneous shifts in equity market returns, interest rate scenarios and market implied volatilities:

|            | Assumptions of Changes In  |                            |                                   | Hypothetical               |
|------------|----------------------------|----------------------------|-----------------------------------|----------------------------|
|            | Equity<br>Market<br>Return | Interest<br>Rate<br>Yields | Market<br>Implied<br>Volatilities | Effect to<br>Net<br>Income |
| Scenario 1 | -5%                        | -12.5<br>bps               | +1%                               | \$ (13)                    |
| Scenario 2 | -10%                       | -25.0<br>bps               | +2%                               | (43)                       |
| Scenario 3 | -20%                       | -50.0<br>bps               | +4%                               | (157)                      |



The actual effects of the results illustrated in the two tables above could vary significantly depending on a variety of factors, many of which are out of our control, and consideration should be given to the following:

- The analysis is only valid as of October 6, 2011, due to changing market conditions, contract holder activity, hedge positions and other factors;
- The analysis assumes instantaneous shifts in the capital market factors and no ability to rebalance hedge positions prior to the market changes;
- The analysis assumes constant exchange rates and implied dividend yields;
- Assumptions regarding shifts in the market factors, such as assuming parallel shifts in interest rate and implied volatility term structures, may be overly simplistic and not indicative of actual market behavior in stress scenarios;
- It is very unlikely that one capital market sector (e.g., equity markets) will sustain such a large instantaneous movement without affecting other capital market sectors; and
- The analysis assumes that there is no tracking or basis risk between the funds and/or indices affecting the GLBs and the instruments utilized to hedge these exposures.

#### Acquisitions and Dispositions

For information about acquisitions and divestitures, see Note 3 in this report and “Part I – Item 1. Business – Acquisitions and Dispositions,” “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Acquisitions and Dispositions” and Note 3 in our 2010 Form 10-K.

## RESULTS OF CONSOLIDATED OPERATIONS

Details underlying the consolidated results, deposits, net flows and account values (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|---|--|--------|--------|---|----------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010     | Change |
| Revenues  |  |        |        |   |          |        |
| Insurance premiums  | \$ 559   | \$ 538 | 4%     | \$ 1,721                                      | \$ 1,621 | 6%     |
| Insurance fees  | 864  | 769    | 12%    | 2,582   | 2,351    | 10%    |
| Net investment income   | 1,151  | 1,132  | 2%     | 3,522   | 3,358    | 5%     |
| Realized gain (loss):   |  |        |        |   |          |        |
| Total OTTI losses on securities   | (42)   | (99)   | 58%    | (133)   | (187)    | 29%    |
| Portion of loss recognized in OCI   | 17   | 53     | -68%   | 39  | 77       | -49%   |
| Net OTTI losses on securities<br>recognized in earnings                       | (25)   | (46)   | 46%    | (94)  | (110)    | 15%    |
| Realized gain (loss), excluding OTTI<br>losses on securities                  | (138)  | 89     | NM     | (83)  | 132      | NM     |
| Total realized gain (loss)  | (163)  | 43     | NM     | (177)   | 22       | NM     |
| Amortization of deferred gain on business<br>sold through reinsurance         | 19   | 19     | 0%     | 56  | 56       | 0%     |
| Other revenues and fees   | 118  | 112    | 5%     | 361   | 337      | 7%     |
| Total revenues  | 2,548  | 2,613  | -2%    | 8,065   | 7,745    | 4%     |
| Benefits and Expenses   |  |        |        |   |          |        |
| Interest credited   | 625  | 623    | 0%     | 1,864   | 1,855    | 0%     |
| Benefits  | 665  | 924    | -28%   | 2,527   | 2,541    | -1%    |
| Underwriting, acquisition, insurance and<br>other expenses                    | 1,040  | 689    | 51%    | 2,401   | 2,155    | 11%    |
| Interest and debt expense   | 79   | 74     | 7%     | 223   | 212      | 5%     |
| Total benefits and expenses   | 2,409  | 2,310  | 4%     | 7,015   | 6,763    | 4%     |
| Income (loss) from continuing<br>operations before taxes                      | 139  | 303    | -54%   | 1,050   | 982      | 7%     |
| Federal income tax expense (benefit)  | (12)   | 55     | NM     | 234   | 226      | 4%     |
| Income (loss) from continuing<br>operations                                   | 151  | 248    | -39%   | 816   | 756      | 8%     |
| Income (loss) from discontinued<br>operations, net of federal<br>income taxes | (8)  | (2)    | NM     | (8)   | 29       | NM     |
| Net income (loss)   | \$ 143   | \$ 246 | -42%   | \$ 808  | \$ 785   | 3%     |

|  | For the Three<br>Months Ended<br>September 30, |          |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|--|--|----------|--------|---|----------|--------|
|  | 2011   | 2010     | Change | 2011  | 2010     | Change |
| Revenues   |  |          |        |   |          |        |
| Operating revenues:  |  |          |        |   |          |        |
| Retirement Solutions:  |  |          |        |   |          |        |
| Annuities  | \$ 710   | \$ 660   | 8%     | \$ 2,175                                      | \$ 1,935 | 12%    |
| Defined Contribution   | 248  | 245      | 1%     | 771   | 730      | 6%     |
| Total Retirement Solutions   | 958  | 905      | 6%     | 2,946   | 2,665    | 11%    |
| Insurance Solutions:   |  |          |        |   |          |        |
| Life Insurance   | 1,176  | 1,108    | 6%     | 3,552   | 3,372    | 5%     |
| Group Protection   | 479  | 451      | 6%     | 1,458   | 1,367    | 7%     |
| Total Insurance Solutions  | 1,655  | 1,559    | 6%     | 5,010   | 4,739    | 6%     |
| Other Operations   | 120  | 122      | -2%    | 351   | 367      | -4%    |
| Excluded realized gain (loss), pre-tax   | (185)  | 25       | NM     | (243)   | (27)     | NM     |
| Amortization of deferred gain arising<br>from reserve changes on business sold<br>through reinsurance, pre-tax | 1  | 1        | 0%     | 2   | 2        | 0%     |
| Amortization of DFEL associated with<br>benefit ratio unlocking, pre-tax                                       | (1)  | 1        | NM     | (1)   | (1)      | 0%     |
| Total revenues   | \$ 2,548                                       | \$ 2,613 | -2%    | \$ 8,065                                      | \$ 7,745 | 4%     |

|   | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|--------|--------|---|--------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Net Income (Loss)   |  |        |        |   |        |        |
| Income (loss) from operations:  |  |        |        |   |        |        |
| Retirement Solutions:   |  |        |        |   |        |        |
| Annuities   | \$ 162   | \$ 126 | 29%    | \$ 459  | \$ 361 | 27%    |
| Defined Contribution  | 40   | 50     | -20%   | 132   | 122    | 8%     |
| Total Retirement Solutions  | 202  | 176    | 15%    | 591   | 483    | 22%    |
| Insurance Solutions:  |  |        |        |   |        |        |
| Life Insurance  | 132  | 60     | 120%   | 450   | 348    | 29%    |
| Group Protection  | 28   | 9      | 211%   | 78  | 54     | 44%    |
| Total Insurance Solutions   | 160  | 69     | 132%   | 528   | 402    | 31%    |
| Other Operations  | (45)   | (40)   | -13%   | (104)   | (113)  | 8%     |
| Excluded realized gain (loss), after-tax  | (120)  | 17     | NM     | (158)   | (17)   | NM     |
| Gain (loss) on early extinguishment of<br>debt, after-tax   | (5)  | -      | NM     | (5)   | -      | NM     |
| Income (expense) from reserve changes<br>(net of related amortization) on business<br>sold through reinsurance, after-tax | -  | 1      | -100%  | 1   | 1      | 0%     |
| Benefit ratio unlocking, after-tax  | (41)   | 25     | NM     | (37)  | -      | NM     |
| Income (loss) from continuing<br>operations, after-tax  | 151  | 248    | -39%   | 816   | 756    | 8%     |
| Income (loss) from discontinued<br>operations, after-tax  | (8)  | (2)    | NM     | (8)   | 29     | NM     |
| Net income (loss)   | \$ 143   | \$ 246 | -42%   | \$ 808  | \$ 785 | 3%     |

|                                      | For the Three<br>Months Ended<br>September 30, |          |        | For the Nine<br>Months Ended<br>September 30, |           |        |
|--------------------------------------|--|----------|--------|---|-----------|--------|
|                                      | 2011   | 2010     | Change | 2011  | 2010      | Change |
| Deposits                             |  |          |        |   |           |        |
| Retirement Solutions:                |  |          |        |   |           |        |
| Annuities                            | \$ 2,709                                       | \$ 2,978 | -9%    | \$ 8,275                                      | \$ 8,077  | 2%     |
| Defined Contribution                 | 1,456  | 1,262    | 15%    | 3,996   | 3,943     | 1%     |
| Insurance Solutions - Life Insurance | 1,343  | 1,230    | 9%     | 3,887   | 3,370     | 15%    |
| Total deposits                       | \$ 5,508                                       | \$ 5,470 | 1%     | \$ 16,158                                     | \$ 15,390 | 5%     |

|                                      |          |          |      |          |          |      |
|--------------------------------------|----------|----------|------|----------|----------|------|
| Net Flows                            |          |          |      |          |          |      |
| Retirement Solutions:                |          |          |      |          |          |      |
| Annuities                            | \$ 663   | \$ 1,284 | -48% | \$ 1,846 | \$ 3,012 | -39% |
| Defined Contribution                 | 329      | (278)    | 218% | 285      | 13       | NM   |
| Insurance Solutions - Life Insurance | 963      | 725      | 33%  | 2,652    | 1,977    | 34%  |
| Total net flows                      | \$ 1,955 | \$ 1,731 | 13%  | \$ 4,783 | \$ 5,002 | -4%  |

|                                      | As of September 30, |            |        |
|--------------------------------------|---------------------|------------|--------|
|                                      | 2011                | 2010       | Change |
| Account Values                       |                     |            |        |
| Retirement Solutions:                |                     |            |        |
| Annuities                            | \$ 81,230           | \$ 80,229  | 1%     |
| Defined Contribution                 | 37,020              | 37,088     | 0%     |
| Insurance Solutions - Life Insurance | 34,419              | 32,654     | 5%     |
| Total account values                 | \$ 152,669          | \$ 149,971 | 2%     |

## Comparison of the Three Months Ended September 30, 2011 to 2010

Net income decreased due primarily to the following:

- Realized losses in 2011 as compared to realized gains in 2010 attributable primarily to less favorable results on the mark-to-market on certain instruments and variable annuity net derivatives results both attributable primarily to the volatility experienced during 2011 (see “Realized Gain (Loss) and Benefit Ratio Unlocking” below for more information);
- An \$11 million unfavorable retrospective unlocking of DAC, VOBA, DSI, DFEL and the reserves for life insurance and annuity products with living benefit and death benefit guarantees, compared to a \$37 million favorable retrospective unlocking during the third quarter of 2010:
  - § The unfavorable retrospective unlocking during the third quarter of 2011 was due primarily to the increase in the change in GDB reserves due to our GDB benefit ratio unlocking, partially offset by higher equity markets and expense assessments and lower lapses than our model projections assumed; and
  - § The favorable retrospective unlocking during the third quarter of 2010 was due primarily to the decrease in the change in GDB reserves due to our GDB benefit ratio unlocking and higher equity markets and expense assessments and lower lapses than our model projections assumed;
- Higher benefits, excluding unlocking, driven primarily by:
  - § Higher death claims; and
- § An increase in secondary guarantee life insurance product reserves from model refinements and continued growth in the business;
  - partially offset by:
    - § More favorable non-medical loss ratio experience within our Group Protection segment;
- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to:
  - § Higher incentive compensation accruals as a result of higher earnings and production performance relative to targets;
    - § Higher average account values driving higher trail commissions; and
  - § Investments in strategic initiatives related to updating information technology and expanding distribution and support during the third quarter of 2011;
    - partially offset by:
      - § Legal and merger-related expenses in 2010; and
- A \$79 million unfavorable prospective unlocking of DAC, VOBA, DSI, DFEL and the reserves for life insurance and annuity products with living benefit and death benefit guarantees during the third quarter of 2011 compared to a \$72 million unfavorable prospective unlocking during the third quarter of 2010 (see “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” for more information):
  - § The unfavorable prospective unlocking during the third quarter of 2011 was due to an \$88 million unfavorable unlocking from assumption changes related primarily to our lapse, long-term equity market growth rate and interest margin assumptions, partially offset by changes in our assumptions for long-term volatility, net of a \$9 million favorable unlocking from model refinements;

- § The prospective unlocking reflected in our Life Insurance segment during the third quarter of 2011 created significant line item fluctuations as underwriting, acquisition, insurance and other expenses was increased by \$285 million, pre-tax, and benefits was decreased by \$322 million, pre-tax; and
- § The unfavorable prospective unlocking during the third quarter of 2010 was due to a \$2 million unfavorable unlocking from model refinements and a \$70 million unfavorable unlocking from assumption changes due primarily to lower investment margins attributable primarily to lowering our new money investment yield assumption to reflect the then current new money rates and to approximate the forward curve for interest rates relevant at such time, as this effect alone represented \$114 million unfavorable unlocking within our Life Insurance segment, as well as higher lapses than our model projections assumed, partially offset by lower surrenders and death claims than our model projections assumed.

The decrease in net income was partially offset by the following:

- Higher earnings from our variable annuity and mutual fund (within our Defined Contribution segment) products as a result of higher average account values driven by increases in the equity markets, and an increase in insurance fees, excluding unlocking, attributable primarily to growth in insurance in force;
- More favorable tax return true-ups recorded in the third quarter of 2011; and
- Higher net investment income and relatively flat interest credited, excluding unlocking, driven primarily by:
  - § Higher average fixed account values, including the fixed portion of variable annuity contracts, attributable primarily to positive net flows and interest credited to contract holders, partially offset by transfers from fixed to variable; and

§ Reductions in crediting rates after the third quarter of 2010;

partially offset by:

§ New money rates averaging below our portfolio yields.

Comparison of the Nine Months Ended September 30, 2011 to 2010

Net income increased due primarily to the following:

- Higher earnings from our variable annuity and mutual fund (within our Defined Contribution segment) products as a result of higher average account values driven by increases in the equity markets, and an increase in insurance fees, excluding unlocking, attributable primarily to growth in insurance in force;
- Higher net investment income and relatively flat interest credited, excluding unlocking, driven primarily by:
  - § Higher average fixed account values, including the fixed portion of variable annuity contracts, attributable primarily to positive net flows and interest credited to contract holders, partially offset by transfers from fixed to variable;
  - § Higher prepayment and bond makewhole premiums, more favorable investment income on alternative investments and higher portfolio yields on surplus (see “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” and “Consolidated Investments – Alternative Investments” below for more information); and

§ Reductions in crediting rates after the third quarter of 2010;

partially offset by:

§ New money rates averaging below our portfolio yields;

- A lower DAC, VOBA, DSI and DFEL amortization rate, net of interest, excluding unlocking, during the first nine months of 2011 and a \$25 million favorable retrospective unlocking of DAC, VOBA, DSI, DFEL and the reserves for life insurance and annuity products with living benefit and death benefit guarantees during the first nine months of 2011, compared to a \$42 million favorable retrospective unlocking during the first nine months of 2010:
  - § The lower amortization rate during the first nine months of 2011 was due primarily to higher EGPs attributable to rider fees related to our products with living benefit guarantees and an overall shift in business mix towards products with lower deferrable expense rates;
  - § The favorable retrospective unlocking during the first nine months of 2011 was due primarily to higher equity markets, expense assessments and prepayment and bond makewhole premiums and lower lapses than our model projections assumed, partially offset by the increase in the change in GDB reserves due to our GDB benefit ratio unlocking and lower premiums received and higher death claims than our model projections assumed; and
  - § The favorable retrospective unlocking during the first nine months of 2010 was due primarily to the decrease in the change in GDB reserves due to our GDB benefit ratio unlocking and higher equity markets and expense assessments and lower lapses than our model projections assumed; and
- More favorable tax return true-ups recorded in the first nine months of 2011.

The increase in net income was partially offset by the following:

- The effect of realized losses in 2011 as compared to realized gains in 2010 discussed above;
  - Higher benefits, excluding unlocking, driven primarily by:
    - § Higher death claims; and
  - § An increase in secondary guarantee life insurance product reserves from model refinements and continued growth in the business;
- partially offset by:
- § A decrease in the change in GDB reserves from a decrease in our expected GDB benefit payments attributable primarily to the increase in account values above guaranteed levels due to the more favorable equity markets and favorable mortality experience on single-premium immediate annuities (“SPIA”); and
    - § More favorable non-medical loss ratio experience within our Group Protection segment;
  - Loss from discontinued operations of \$8 million during the first nine months of 2011 due to an unfavorable tax return true-up related to our former Investment Management segment compared to income from discontinued operations of \$29 million during the first nine months of 2010 related to our former Lincoln UK and Investment Management segments (see Note 3 for



more information on our discontinued operations);

- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to:

- § Higher average account values driving higher trail commissions;

- § Higher incentive compensation accruals as a result of higher earnings and production performance relative to targets;

- § An increase in expenses associated with reserve financing supporting our secondary guarantee UL and term business due primarily to higher pricing that has occurred in reaction to the unfavorable market conditions experienced during the recession and our continued efforts to reduce the strain of these statutory reserves (see “Results of Insurance Solutions – Life Insurance – Income (Loss) from Operations – Strategies to Address Statutory Reserve Strain” below for more information); and

- § Investments in strategic initiatives related to updating information technology and expanding distribution and support during the first nine months of 2011;

partially offset by:

- § Higher legal and merger-related expenses during the first nine months of 2010;

- The effect of prospective unlocking discussed above and a \$20 million favorable prospective unlocking of DAC, VOBA, DSI, DFEL and reserves for life insurance and annuity products with living benefit and death benefit guarantees during the first six months of 2011 compared to a \$26 million favorable prospective unlocking during the first six months of 2010 (see “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” for more information);

- § The favorable prospective unlocking during the first six months of 2011 was recorded in the Life Insurance segment and was due to an \$18 million favorable unlocking from model refinements and a \$2 million favorable unlocking from assumption changes; and

- § The favorable prospective unlocking during the first six months of 2010 was due to assumption changes in the Annuities segment; and

- A \$5 million loss associated with the early extinguishment of long-term debt in 2011 and higher interest and debt expenses as a result of higher average balances of outstanding debt in 2011.

The foregoing items are discussed in further detail in results of operations by segment discussions and “Realized Gain (Loss) and Benefit Ratio Unlocking” below. In addition, for a discussion of the earnings effect of the equity markets, see “Item 3. Quantitative and Qualitative Disclosures About Market Risk – Equity Market Risk – Effect of Equity Market Sensitivity.”

## RESULTS OF RETIREMENT SOLUTIONS

The Retirement Solutions business provides its products through two segments: Annuities and Defined Contribution. The Annuities segment provides tax-deferred investment growth and lifetime income opportunities for its clients by offering individual fixed annuities, including indexed annuities, and variable annuities. The Defined Contribution segment provides employer-sponsored variable and fixed annuities, defined benefit, individual retirement accounts and mutual-fund based programs in the retirement plan marketplaces.

For factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language” above.

## Annuities

## Income (Loss) from Operations

Details underlying the results for Annuities (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Operating Revenues   |  |        |        |   |        |        |
| Insurance premiums (1)                                     | \$ 15  | \$ 16  | -6%    | \$ 60   | \$ 35  | 71%    |
| Insurance fees   | 317  | 269    | 18%    | 948   | 799    | 19%    |
| Net investment income                                      | 271  | 282    | -4%    | 837   | 824    | 2%     |
| Operating realized gain (loss)                             | 22   | 18     | 22%    | 66  | 49     | 35%    |
| Other revenues and fees (2)                                | 85   | 75     | 13%    | 264   | 228    | 16%    |
| Total operating revenues                                   | 710  | 660    | 8%     | 2,175   | 1,935  | 12%    |
| Operating Expenses   |  |        |        |   |        |        |
| Interest credited  | 177  | 184    | -4%    | 530   | 537    | -1%    |
| Benefits   | 87   | 43     | 102%   | 164   | 128    | 28%    |
| Underwriting, acquisition, insurance<br>and other expenses | 273  | 297    | -8%    | 932   | 839    | 11%    |
| Total operating expenses                                   | 537  | 524    | 2%     | 1,626   | 1,504  | 8%     |
| Income (loss) from operations before<br>taxes              | 173  | 136    | 27%    | 549   | 431    | 27%    |
| Federal income tax expense (benefit)                       | 11   | 10     | 10%    | 90  | 70     | 29%    |
| Income (loss) from operations                              | \$ 162   | \$ 126 | 29%    | \$ 459  | \$ 361 | 27%    |

(1) Includes primarily our SPIA, which have a corresponding offset in benefits for changes in reserves.

(2) Consists primarily of fees attributable to broker-dealer services that are subject to market volatility.

## Comparison of the Three Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- Higher insurance fees driven primarily by higher average daily variable account values due to more favorable equity markets;
- A \$34 million favorable retrospective unlocking of DAC, VOBA, DSI, DFEL and reserves for our guarantee riders during the third quarter of 2011, compared to a \$19 million favorable retrospective unlocking during the third quarter of 2010:
  - § The favorable retrospective unlocking during the third quarter of 2011 was due primarily to higher equity markets, expense assessments and prepayment and bond makewhole premiums and lower lapses than our model projections assumed; and
  - § The favorable retrospective unlocking during the third quarter of 2010 was due primarily to higher equity markets and expense assessments and lower lapses than our model projections assumed; and
- Favorable tax return true-ups during the third quarter of 2011 driven by the separate account dividends-received deduction (“DRD”) and other items.

The increase in income from operations was partially offset by the following:

- A \$17 million unfavorable prospective unlocking of DAC, VOBA, DSI, DFEL and reserves for our guarantee riders during the third quarter of 2011 compared to a \$2 million unfavorable prospective unlocking during the third quarter of 2010 (see “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” for more information):
- § The unfavorable prospective unlocking during the third quarter of 2011 was due to a \$48 million unfavorable unlocking from assumption changes related primarily to our long-term equity market growth rate and interest margin assumptions, partially offset by changes related to our lapse assumptions, net of a \$31 million favorable unlocking from model refinements; and

§ The unfavorable prospective unlocking during the third quarter of 2010 was due to assumption changes attributable primarily to the \$16 million unfavorable unlocking for the estimated effect of the planned conversion of our actuarial valuation systems to a uniform platform for certain blocks of business, net of a \$14 million favorable unlocking from assumption changes related primarily to our lapse assumptions;

- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to:

§ Higher average account values driving higher trail commissions; and

§ Investments in strategic initiatives related to updating information technology and expanding distribution and support during the third quarter of 2011; and

- Lower net investment income partially offset by lower interest credited, excluding unlocking, driven primarily by:

§ New money rates averaging below our portfolio yields; and

§ Reductions in crediting rates after the third quarter of 2010;

partially offset by:

§ Higher average fixed account values, including the fixed portion of variable annuity contracts, attributable primarily to positive net flows and interest credited to contract holders, partially offset by transfers from fixed to variable since the third quarter of 2010.

#### Comparison of the Nine Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- Higher insurance fees driven primarily by higher average daily variable account values due to more favorable equity markets;

- A lower DAC, VOBA, DSI and DFEL amortization rate, net of interest, excluding unlocking, and a \$91 million favorable retrospective unlocking of DAC, VOBA, DSI, DFEL and reserves for our guarantee riders during the first nine months of 2011, compared to a \$63 million favorable retrospective unlocking during the first nine months of 2010:

§ The lower amortization rate during the first nine months of 2011 was due primarily to higher EGPs attributable to rider fees related to our products with living benefit guarantees;

§ The favorable retrospective unlocking during the first nine months of 2011 was due primarily to higher equity markets, expense assessments and prepayment and bond makewhole premiums and lower lapses than our model projections assumed; and

§ The favorable retrospective unlocking during the first nine months of 2010 was due primarily to higher equity markets and expense assessments and lower lapses than our model projections assumed;

- Lower benefits, excluding SPIA (see footnote one above) and unlocking, due primarily to a decrease in the change in GDB reserves from a decrease in our expected GDB benefit payments attributable primarily to the increase in account values above guaranteed levels due to the more favorable equity markets and favorable mortality experience on SPIA;

- Higher net investment income and relatively flat interest credited, excluding unlocking, driven primarily by:

§ Higher average fixed account values, including the fixed portion of variable annuity contracts, attributable primarily to positive net flows and interest credited to contract holders, partially offset by transfers from fixed to variable since the third quarter of 2010;

§ Higher prepayment and bond makewhole premiums, an increase in surplus investments allocated to this segment, higher portfolio yields on surplus and more favorable investment income on alternative investments within our surplus portfolio (see “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” and “Consolidated Investments – Alternative Investments” below for more information); and

§ Reductions in crediting rates after the third quarter of 2010;

partially offset by:

§ New money rates averaging below our portfolio yields.

The increase in income from operations was partially offset by the following:

- The effect of prospective unlocking discussed above and a \$26 million favorable prospective unlocking of DAC, VOBA, DSI, DFEL and reserves for our guarantee riders during the first six months of 2010 from assumption changes due to including an estimate in our models for rider fees related to our annuity products with living benefit guarantees; and
- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to:
  - § Higher account values driving higher trail commissions; and
  - § Investments in strategic initiatives related to updating information technology and expanding distribution and support during the first nine months of 2011.

#### Additional Information

During 2010, we completed the planned conversion of our actuarial valuation systems to a uniform platform for certain blocks of business. We have other blocks of business that we intend to convert. Although we expect some differences to emerge as a result

of the planned conversion of the other blocks of business, based upon the current status of these efforts, we are not able to provide an estimate or range of the effects to our results of operations until completion of the conversion. See “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” in our 2010 Form 10-K for information on our actuarial system conversion.

We expect our investments in strategic initiatives for this segment during the fourth quarter of 2011 will be higher than those made in the third quarter of 2011.

New deposits are an important component of net flows and key to our efforts to grow our business. Although deposits do not significantly affect current period income from operations, they are an important indicator of future profitability.

The other component of net flows relates to the retention of the business. An important measure of retention is the lapse rate, which compares the amount of withdrawals to the average account values. The overall lapse rate for our annuity products was 8% for the three and nine months ended September 30, 2011, compared to 7% for the corresponding periods in 2010.

See Note 8 for information on contractual guarantees to contract holders related to GDB features for our Retirement Solutions business.

Our fixed annuity business includes products with discretionary crediting rates that are reset on an annual basis and are not subject to surrender charges. Our ability to retain annual reset annuities will be subject to current competitive conditions at the time interest rates for these products reset. We expect to manage the effects of spreads on near-term income from operations through portfolio management and, to a lesser extent, crediting rate actions, which assumes no significant changes in net flows into or out of our fixed accounts or other changes that may cause interest rate spreads to differ from our expectations. For information on interest rate spreads and the interest rate risk due to falling interest rates, see “Item 3. Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk – Interest Rate Risk on Fixed Insurance Businesses – Falling Rates” and “Part II – Item 1A. Risk Factors – Changes in interest rates and sustained low interest rates may cause interest rate spreads to decrease and changes in interest rates may also result in increased contract withdrawals” herein.

We provide information about this segment’s operating revenue and operating expense line items, the period in which amounts are recognized, key drivers of changes and historical details underlying the line items and their associated drivers below. For detail on the operating realized gain (loss), see “Realized Gain (Loss) and Benefit Ratio Unlocking” below.

#### Insurance Fees

Details underlying insurance fees, account values and net flows (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |        |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |        |        | Change |      |        |
|--|--|--------|--------|---|--------|--------|--------|------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change | 2011   | 2010 | Change |
| Insurance Fees                           |  |        |        |   |        |        |        |      |        |
| Mortality, expense and other assessments | \$ 316   | \$ 277 | 14%    | \$ 950  | \$ 812 | 17%    |        |      |        |
| Surrender charges                        | 8  | 9      | -11%   | 29  | 30     | -3%    |        |      |        |
| DFEL:                                    |  |        |        |   |        |        |        |      |        |

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|  |        |        |       |        |        |      |
|--|--------|--------|-------|--------|--------|------|
| Deferrals  | (16)   | (19)   | 16%   | (51)   | (56)   | 9%   |
| Amortization, net of interest:                     |        |        |       |        |        |      |
| Prospective unlocking - assumption changes         | 6      | (3)    | 300%  | 6      | (3)    | 300% |
| Retrospective unlocking                            | (2)    | (1)    | -100% | (3)    | -      | NM   |
| Amortization, net of interest, excluding unlocking | 5      | 6      | -17%  | 17     | 16     | 6%   |
| Total insurance fees                               | \$ 317 | \$ 269 | 18%   | \$ 948 | \$ 799 | 19%  |

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|  | As of September 30,                      |           |        |   |           |        |
|--|--|-----------|--------|---|-----------|--------|
|  | 2011                                     | 2010      | Change |   |           |        |
| <b>Account Values</b>  |  |           |        |   |           |        |
| Variable portion of variable annuities                                 | \$ 60,774                                | \$ 60,132 | 1%     |   |           |        |
| Fixed portion of variable annuities                                    | 3,366                                    | 3,771     | -11%   |   |           |        |
| Total variable annuities   | 64,140                                   | 63,903    | 0%     |   |           |        |
| Fixed annuities, including indexed                                     | 18,010                                   | 17,304    | 4%     |   |           |        |
| Fixed annuities ceded to reinsurers                                    | (920)                                    | (978)     | 6%     |   |           |        |
| Total fixed annuities  | 17,090                                   | 16,326    | 5%     |   |           |        |
| Total account values   | \$ 81,230                                | \$ 80,229 | 1%     |   |           |        |
| <b>Averages</b>  |  |           |        |   |           |        |
|  | For the Three Months Ended September 30, |           | Change | For the Nine Months Ended September 30, |           | Change |
|  | 2011                                     | 2010      |        | 2011                                    | 2010      |        |
| Daily variable account values, excluding the fixed portion of variable | \$ 65,169                                | \$ 57,255 | 14%    | \$ 66,625                               | \$ 56,623 | 18%    |
| Daily S&P 500 Index® (“S&P 500”)                                       | 1,227.42                                 | 1,094.32  | 12%    | 1,282.45                                | 1,116.63  | 15%    |
| <b>Net Flows on Account Values</b>                                     |  |           |        |   |           |        |
|  | For the Three Months Ended September 30, |           | Change | For the Nine Months Ended September 30, |           | Change |
|  | 2011                                     | 2010      |        | 2011                                    | 2010      |        |
| Variable portion of variable annuity deposits                          | \$ 1,415                                 | \$ 1,204  | 18%    | \$ 4,558                                | \$ 3,664  | 24%    |
| Variable portion of variable annuity withdrawals                       | (1,456)                                  | (1,209)   | -20%   | (4,801)                                 | (3,638)   | -32%   |
| Variable portion of variable annuity net flows                         | (41)                                     | (5)       | NM     | (243)                                   | 26        | NM     |
| Fixed portion of variable annuity deposits                             | 740                                      | 817       | -9%    | 2,137                                   | 2,408     | -11%   |
| Fixed portion of variable annuity withdrawals                          | (82)                                     | (99)      | 17%    | (259)                                   | (299)     | 13%    |
| Fixed portion of variable annuity net flows                            | 658                                      | 718       | -8%    | 1,878                                   | 2,109     | -11%   |
| Total variable annuity deposits  | 2,155                                    | 2,021     | 7%     | 6,695                                   | 6,072     | 10%    |
| Total variable annuity withdrawals                                     | (1,538)                                  | (1,308)   | -18%   | (5,060)                                 | (3,937)   | -29%   |
| Total variable annuity net flows                                       | 617                                      | 713       | -13%   | 1,635                                   | 2,135     | -23%   |
| Fixed indexed annuity deposits   | 462                                      | 853       | -46%   | 1,320                                   | 1,700     | -22%   |
| Fixed indexed annuity withdrawals                                      | (190)                                    | (130)     | -46%   | (501)                                   | (365)     | -37%   |
| Fixed indexed annuity net flows  | 272                                      | 723       | -62%   | 819                                     | 1,335     | -39%   |
| Other fixed annuity deposits   | 92                                       | 104       | -12%   | 260                                     | 305       | -15%   |
| Other fixed annuity withdrawals  | (318)                                    | (256)     | -24%   | (868)                                   | (763)     | -14%   |
| Other fixed annuity net flows  | (226)                                    | (152)     | -49%   | (608)                                   | (458)     | -33%   |
| Total annuity deposits   | 2,709                                    | 2,978     | -9%    | 8,275                                   | 8,077     | 2%     |
| Total annuity withdrawals  | (2,046)                                  | (1,694)   | -21%   | (6,429)                                 | (5,065)   | -27%   |
|  | \$ 663                                   | \$ 1,284  | -48%   | \$ 1,846                                | \$ 3,012  | -39%   |



Total annuity net  
flows

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |          |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |          |        |
|--|--|----------|--------|---|----------|--------|
|  | 2011   | 2010     | Change | 2011  | 2010     | Change |
| Other Changes to Account Values  |  |          |        |   |          |        |
| Change in market value on variable,<br>excluding the fixed portion of variable   | \$ (8,345)   | \$ 5,334 | NM     | \$ (5,981)  | \$ 2,284 | NM     |
| Transfers to the variable portion of<br>variable annuity products from the fixed<br>portion of variable annuity products | 609  | 882      | -31%   | 2,140   | 2,454    | -13%   |

We charge contract holders mortality and expense assessments on variable annuity accounts to cover insurance and administrative expenses. These assessments are a function of the rates priced into the product and the average daily variable account values. Average daily account values are driven by net flows and the equity markets. In addition, for our fixed annuity contracts and for some variable contracts, we collect surrender charges when contract holders surrender their contracts during their surrender charge periods to protect us from premature withdrawals. Insurance fees include charges on both our variable and fixed annuity products, but exclude the attributed fees on our GLB products; see “Realized Gain (Loss) and Benefit Ratio Unlocking – Operating Realized Gain (Loss)” below for discussion of these attributed fees.

#### Net Investment Income and Interest Credited

Details underlying net investment income, interest credited (in millions) and our interest rate spread were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |        |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Net Investment Income  |  |        |        |   |        |        |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | \$ 243   | \$ 254 | -4%    | \$ 735  | \$ 746 | -1%    |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums (1)                               | 6  | 6      | 0%     | 23  | 11     | 109%   |
| Alternative investments (2)  | -  | -      | NM     | -   | 1      | -100%  |
| Surplus investments (3)  | 22   | 22     | 0%     | 79  | 66     | 20%    |
| Total net investment income  | \$ 271   | \$ 282 | -4%    | \$ 837  | \$ 824 | 2%     |
| Interest Credited  |  |        |        |   |        |        |
| Amount provided to contract holders  | \$ 176   | \$ 190 | -7%    | \$ 525  | \$ 555 | -5%    |
| DSI deferrals  | (10)   | (16)   | 38%    | (29)  | (53)   | 45%    |
| Interest credited before DSI<br>amortization   | 166  | 174    | -5%    | 496   | 502    | -1%    |
| DSI amortization:  |  |        |        |   |        |        |
| Prospective unlocking - assumption<br>changes  | 2  | (2)    | 200%   | 2   | (2)    | 200%   |
| Retrospective unlocking  | (4)  | (2)    | -100%  | (11)  | (6)    | -83%   |
| Amortization, excluding unlocking  | 13   | 14     | -7%    | 43  | 43     | 0%     |

|                         |        |        |     |        |        |     |
|-------------------------|--------|--------|-----|--------|--------|-----|
| Total interest credited | \$ 177 | \$ 184 | -4% | \$ 530 | \$ 537 | -1% |
|-------------------------|--------|--------|-----|--------|--------|-----|

- (1) See “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” below for additional information.
- (2) See “Consolidated Investments – Alternative Investments” below for additional information.
- (3) Represents net investment income on the required statutory surplus for this segment and includes the effect of investment income on alternative investments for such assets that are held in the portfolios supporting statutory surplus versus the

portfolios supporting product liabilities.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |        |
|--|--|-------|--------|---|-------|--------|
|  | 2011   | 2010  | Change | 2011  | 2010  | Change |
| <b>Interest Rate Spread</b>  |  |       |        |   |       |        |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | 5.08%  | 5.48% | (40)   | 5.18%   | 5.53% | (35)   |
| Commercial mortgage loan prepayment<br>and bond make whole premiums                                  | 0.12%  | 0.13% | (1)    | 0.16%   | 0.08% | 8      |
| Net investment income yield on reserves  | 5.20%  | 5.61% | (41)   | 5.34%   | 5.61% | (27)   |
| Interest rate credited to contract holders   | 3.33%  | 3.57% | (24)   | 3.34%   | 3.53% | (19)   |
| Interest rate spread   | 1.87%  | 2.04% | (17)   | 2.00%   | 2.08% | (8)    |

Note: The yields, rates and spreads above are calculated using whole dollars instead of dollars rounded to millions.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |           |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |           |        |
|--|--|-----------|--------|---|-----------|--------|
|  | 2011   | 2010      | Change | 2011  | 2010      | Change |
| <b>Other Information</b>   |  |           |        |   |           |        |
| Average invested assets on reserves  | \$ 19,160  | \$ 18,565 | 3%     | \$ 18,947   | \$ 18,064 | 5%     |
| Average fixed account values, including<br>the fixed portion of variable   | 20,905   | 20,305    | 3%     | 20,687  | 19,863    | 4%     |
| Transfers to the fixed portion of variable<br>annuity products from the variable<br>portion of variable annuity products | (609)  | (882)     | 31%    | (2,140)   | (2,454)   | 13%    |
| Net flows for fixed annuities, including<br>the fixed portion of variable  | 704  | 1,289     | -45%   | 2,089   | 2,986     | -30%   |

A portion of our investment income earned is credited to the contract holders of our fixed annuity products, including the fixed portion of variable annuity contracts. We expect to earn a spread between what we earn on the underlying general account investments supporting the fixed annuity product line, including the fixed portion of variable annuity contracts, and what we credit to our fixed annuity contract holders' accounts, including the fixed portion of variable annuity contracts. The interest rate spread for this segment represents the excess of the yield on invested assets on reserves over the average crediting rate. The yield on invested assets on reserves is calculated as net investment income, excluding the amounts attributable to our surplus investments, reverse repurchase agreement interest expense, inter-segment cash management program interest expense and interest on collateral divided by average invested assets on reserves. The average invested assets on reserves is calculated based upon total invested assets, excluding hedge derivatives and collateral. The average crediting rate is calculated as interest credited before DSI amortization, plus the immediate annuity reserve change (included within benefits) divided by the average fixed account values, including the fixed portion of variable annuity contracts, net of coinsured account values. Fixed account values reinsured under modified coinsurance agreements are included in account values for this calculation. Changes in commercial mortgage loan prepayments and bond makewhole premiums, investment income on alternative investments and surplus investment income can vary significantly from period to period due to a number of factors and, therefore, may contribute to investment income results that are not indicative of the underlying trends.

Benefits

Benefits for this segment include changes in reserves of immediate annuity account values driven by premiums, changes in GDB and GLB benefit reserves and our expected costs associated with purchases of derivatives used to hedge our GDB benefit ratio unlocking.

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## Underwriting, Acquisition, Insurance and Other Expenses

Details underlying underwriting, acquisition, insurance and other expenses (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Underwriting, Acquisition, Insurance<br>and Other Expenses                               |  |        |        |   |        |        |
| Commissions:   |  |        |        |   |        |        |
| Deferrable   | \$ 122   | \$ 134 | -9%    | \$ 359  | \$ 358 | 0%     |
| Non-deferrable   | 60   | 55     | 9%     | 193   | 158    | 22%    |
| General and administrative expenses  | 85   | 86     | -1%    | 265   | 246    | 8%     |
| Inter-segment reimbursement associated<br>with reserve financing and LOC<br>expenses (1) | (1)  | -      | NM     | (1)   | -      | NM     |
| Taxes, licenses and fees   | 5  | 2      | 150%   | 20  | 15     | 33%    |
| Total expenses incurred, excluding<br>broker-dealer                                      | 271  | 277    | -2%    | 836   | 777    | 8%     |
| DAC deferrals  | (160)  | (171)  | 6%     | (476)   | (467)  | -2%    |
| Total pre-broker-dealer expenses<br>incurred, excluding amortization,<br>net of interest | 111  | 106    | 5%     | 360   | 310    | 16%    |
| DAC and VOBA amortization, net of<br>interest:   |  |        |        |   |        |        |
| Prospective unlocking - assumption<br>changes  | (13)   | (6)    | NM     | (13)  | (45)   | 71%    |
| Prospective unlocking - model<br>refinements   | -  | 9      | -100%  | -   | 9      | -100%  |
| Retrospective unlocking  | (41)   | (20)   | NM     | (103)   | (67)   | -54%   |
| Amortization, net of interest,<br>excluding unlocking                                    | 130  | 129    | 1%     | 419   | 400    | 5%     |
| Broker-dealer expenses incurred  | 86   | 79     | 9%     | 269   | 232    | 16%    |
| Total underwriting, acquisition,<br>insurance and other<br>expenses                      | \$ 273   | \$ 297 | -8%    | \$ 932  | \$ 839 | 11%    |
| DAC Deferrals  |  |        |        |   |        |        |
| As a percentage of sales/deposits  | 5.9%   | 5.7%   |        | 5.8%  | 5.8%   |        |

(1) Represents reimbursements to Annuities from the Life Insurance segment for reserve financing, net of expenses incurred by Annuities for its use of LOCs. The inter-segment amounts are not reported on our Consolidated Statements of Income (Loss).

Commissions and other costs that vary with and are related primarily to the production of new business are deferred to the extent recoverable and are amortized over the lives of the contracts in relation to EGPs. Certain of our commissions, such as trail commissions that are based on account values, are expensed as incurred rather than deferred and amortized.

Broker-dealer expenses that vary with and are related to sales are expensed as incurred and not deferred and amortized. Fluctuations in these expenses correspond with fluctuations in other revenues and fees.

## Defined Contribution

## Income (Loss) from Operations

Details underlying the results for Defined Contribution (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |        |        | Change |
|--|--|-------|--------|---|--------|--------|--------|
|  | 2011   | 2010  | Change | 2011  | 2010   | Change |        |
| Operating Revenues   |  |       |        |   |        |        |        |
| Insurance fees   | \$ 51  | \$ 48 | 6%     | \$ 161  | \$ 148 | 9%     |        |
| Net investment income                                      | 193  | 192   | 1%     | 598   | 569    | 5%     |        |
| Other revenues and fees (1)                                | 4  | 5     | -20%   | 12  | 13     | -8%    |        |
| Total operating revenues                                   | 248  | 245   | 1%     | 771   | 730    | 6%     |        |
| Operating Expenses   |  |       |        |   |        |        |        |
| Interest credited  | 110  | 110   | 0%     | 326   | 331    | -2%    |        |
| Benefits   | 2  | -     | NM     | 2   | 1      | 100%   |        |
| Underwriting, acquisition, insurance and<br>other expenses | 81   | 66    | 23%    | 257   | 229    | 12%    |        |
| Total operating expenses                                   | 193  | 176   | 10%    | 585   | 561    | 4%     |        |
| Income (loss) from operations before<br>taxes              | 55   | 69    | -20%   | 186   | 169    | 10%    |        |
| Federal income tax expense (benefit)                       | 15   | 19    | -21%   | 54  | 47     | 15%    |        |
| Income (loss) from operations                              | \$ 40  | \$ 50 | -20%   | \$ 132  | \$ 122 | 8%     |        |

(1) Consists primarily of mutual fund account program fees for mid-to-large employers.

## Comparison of the Three Months Ended September 30, 2011 to 2010

Income from operations for this segment decreased due primarily to the following:

- A \$2 million unfavorable prospective unlocking of DAC, VOBA and DSI during the third quarter of 2011 compared to an \$11 million favorable prospective unlocking during the third quarter of 2010 (see “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” for more information):
  - § The unfavorable prospective unlocking during the third quarter of 2011 was due to model refinements; and
  - § The favorable prospective unlocking during the third quarter of 2010 was due to assumption changes attributable primarily to the \$10 million estimated effect of the planned conversion of our actuarial valuation systems to a uniform platform for certain blocks of business;
- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to the following:
  - § Investments in strategic initiatives related to updating information technology and expanding distribution and support during the third quarter of 2011, as discussed in “Additional Information” below; and
  - § Higher average account values driving higher trail commissions; and
- Higher benefits, excluding unlocking, driven primarily by an increase in the change in GDB reserves from an increase in our expected GDB benefit payments attributable primarily to the decrease in end of period account values as a result of the effect of unfavorable equity markets during the third quarter of 2011.

The decrease in income from operations was partially offset by:



- A \$6 million favorable retrospective unlocking of DAC, VOBA and DSI during the third quarter of 2011 due primarily to lower lapses than our model projections assumed and a reallocation of acquisition expenses related to our wholesaling distribution organization; and
- Higher insurance fees driven primarily by higher average daily variable account values due to higher equity markets, partially offset by an overall shift in business mix toward products with lower expense assessment rates and negative net flows.

Comparison of the Nine Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- Higher net investment income and relatively flat interest credited driven primarily by:
    - § Higher prepayment and bond makewhole premiums and more favorable investment income on alternative investments within our surplus portfolio (see “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” and “Consolidated Investments – Alternative Investments” below for more information);
    - § Higher average fixed account values, including the fixed portion of variable annuity contracts, attributable primarily to transfers from variable to fixed and interest credited to contract holders, partially offset by negative net flows, since the third quarter of 2010; and
      - § Reductions in crediting rates after the third quarter of 2010;
- partially offset by
- § New money rates averaging below our portfolio yields.
  - An \$8 million favorable retrospective unlocking of DAC, VOBA and DSI and a lower DAC, VOBA and DSI amortization rate, net of interest and excluding unlocking, during the first nine months of 2011 compared to a \$3 million unfavorable retrospective unlocking during the first nine months of 2010:
    - § The favorable retrospective unlocking during the first nine months of 2011 was due primarily to lower lapses and higher equity markets than our model projections assumed;
    - § The lower amortization rate during the first nine months of 2011 was due primarily to no VOBA amortization during the first nine months of 2011 as our VOBA balance became fully amortized during the fourth quarter of 2010; and
    - § The unfavorable retrospective unlocking during the first nine months of 2010 was due primarily to higher lapses than our model projections assumed, partially offset by higher equity markets than our model projections assumed; and
  - Higher insurance fees driven primarily by higher average daily variable account values due to higher equity markets, partially offset by an overall shift in business mix toward products with lower expense assessment rates and negative net flows.

The increase in income from operations was partially offset by:

- Higher underwriting, acquisition, insurance and other expenses, excluding amortization of DAC and VOBA, due primarily to the following:
  - § Investments in strategic initiatives related to updating information technology and expanding distribution and support during the first nine months of 2011, as discussed in “Additional Information” below; and
    - § Higher average account values driving higher trail commissions; and
- The effect of prospective unlocking discussed above.

Additional Information

We expect our investments in strategic initiatives for this segment during the fourth quarter of 2011 will be higher than those made in the third quarter of 2011.

Net flows in this business fluctuate based on the timing of larger plans rolling onto our platform and rolling off over the course of the year, and we expect this trend will continue for the remainder of 2011.

New deposits are an important component of net flows and key to our efforts to grow our business. Although deposits do not significantly affect current period income from operations, they are an important indicator of future

profitability. The other component of net flows relates to the retention of the business. An important measure of retention is the lapse rate, which compares the amount of withdrawals to the average account values. The overall lapse rate for our annuity and mutual fund products was 12% for the three and nine months ended September 30, 2011, compared to 17% and 15% for the corresponding periods in 2010.

Our lapse rate is negatively affected by the continued net outflows from our oldest blocks of annuities business (as presented on our Account Value Roll Forward table below as “Total Multi-Fund® and Other Variable Annuities”), which are also our higher margin product lines in this segment, due to the fact that they are mature blocks with much of the account values out of their surrender charge period. The proportion of these products to our total account values was 41% and 42% as of September 30, 2011, and 2010, respectively. Due to this expected overall shift in business mix toward products with lower returns, a significant increase in new deposit production will be necessary to maintain earnings at current levels.

See Note 8 for information on contractual guarantees to contract holders related to GDB features for our Retirement Solutions business.

Our fixed annuity business includes products with discretionary and index-based crediting rates that are reset on a quarterly basis.

Our ability to retain quarterly reset annuities will be subject to current competitive conditions at the time interest rates for these products reset. We expect to manage the effects of spreads on near-term income from operations through portfolio management and, to a lesser extent, crediting rate actions, which assumes no significant changes in net flows into or out of our fixed accounts or other changes that may cause interest rate spreads to differ from our expectations. For information on interest rate spreads and the interest rate risk due to falling interest rates, see “Item 3. Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk – Interest Rate Risk on Fixed Insurance Businesses – Falling Rates” and “Part II – Item 1A. Risk Factors – Changes in interest rates and sustained low interest rates may cause interest rate spreads to decrease and changes in interest rates may also result in increased contract withdrawals” herein.

We provide information about this segment’s operating revenue and operating expense line items, the period in which amounts are recognized, key drivers of changes and historical details underlying the line items and their associated drivers below.

### Insurance Fees

Details underlying insurance fees, account values and net flows (in millions) were as follows:

|                             | For the Three Months Ended |       |        | For the Nine Months Ended |        |        |
|-----------------------------|----------------------------|-------|--------|---------------------------|--------|--------|
|                             | September 30, 2011         | 2010  | Change | September 30, 2011        | 2010   | Change |
| Insurance Fees              |                            |       |        |                           |        |        |
| Annuity expense assessments | \$ 43                      | \$ 41 | 5%     | \$ 136                    | \$ 128 | 6%     |
| Mutual fund fees            | 7                          | 6     | 17%    | 23                        | 18     | 28%    |
| Total expense assessments   | 50                         | 47    | 6%     | 159                       | 146    | 9%     |
| Surrender charges           | 1                          | 1     | 0%     | 2                         | 2      | 0%     |
| Total insurance fees        | \$ 51                      | \$ 48 | 6%     | \$ 161                    | \$ 148 | 9%     |

| Averages   | For the Three Months Ended |           |        | For the Nine Months Ended |           |        |
|--|----------------------------|-----------|--------|---------------------------|-----------|--------|
|  | September 30, 2011         | 2010      | Change | September 30, 2011        | 2010      | Change |
| Daily variable annuity account values, excluding the fixed portion of variable | \$ 13,217                  | \$ 12,471 | 6%     | \$ 13,889                 | \$ 12,744 | 9%     |
| Daily S&P 500  | 1,227.42                   | 1,094.32  | 12%    | 1,282.45                  | 1,116.63  | 15%    |

|  | As of September 30, |           |        |
|--|---------------------|-----------|--------|
|  | 2011                | 2010      | Change |
| Account Values                         |                     |           |        |
| Variable portion of variable annuities | \$ 12,122           | \$ 12,956 | -6%    |
| Fixed portion of variable annuities    | 6,273               | 6,163     | 2%     |
| Total variable annuities               | 18,395              | 19,119    | -4%    |
| Fixed annuities                        | 7,122               | 6,571     | 8%     |
| Total annuities                        | 25,517              | 25,690    | -1%    |
| Mutual funds (1)                       | 11,503              | 11,398    | 1%     |
| Total annuities and mutual funds       | \$ 37,020           | \$ 37,088 | 0%     |

- (1) Includes mutual fund account values and other third-party trustee-held assets. These items are not included in the separate accounts reported on our Consolidated Balance Sheets as we do not have any ownership interest in them.

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|  | For the Three<br>Months Ended<br>September 30, |           |        | For the Nine<br>Months Ended<br>September 30, |           |        |
|--|--|-----------|--------|---|-----------|--------|
|  | 2011   | 2010      | Change | 2011  | 2010      | Change |
| <b>Account Value Roll Forward – By Product</b>             |  |           |        |   |           |        |
| <b>Total Micro – Small Segment:</b>                        |  |           |        |   |           |        |
| Balance as of beginning-of-period                          | \$ 6,566                                       | \$ 5,544  | 18%    | \$ 6,396                                      | \$ 5,863  | 9%     |
| Gross deposits   | 312  | 277       | 13%    | 953   | 884       | 8%     |
| Withdrawals and deaths                                     | (336)  | (291)     | -15%   | (1,045)                                       | (1,047)   | 0%     |
| Net flows  | (24)   | (14)      | -71%   | (92)  | (163)     | 44%    |
| Transfers between fixed and variable<br>accounts           | -  | (1)       | 100%   | (6)   | (2)       | NM     |
| Investment increase and change in market<br>value          | (686)  | 425       | NM     | (442)   | 256       | NM     |
| Balance as of end-of-period                                | \$ 5,856                                       | \$ 5,954  | -2%    | \$ 5,856                                      | \$ 5,954  | -2%    |
| <b>Total Mid – Large Segment:</b>                          |  |           |        |   |           |        |
| Balance as of beginning-of-period                          | \$ 17,333                                      | \$ 14,384 | 21%    | \$ 16,207                                     | \$ 13,653 | 19%    |
| Gross deposits   | 969  | 800       | 21%    | 2,504   | 2,489     | 1%     |
| Withdrawals and deaths                                     | (408)  | (858)     | 52%    | (1,463)                                       | (1,663)   | 12%    |
| Net flows  | 561  | (58)      | NM     | 1,041   | 826       | 26%    |
| Transfers between fixed and variable<br>accounts           | (19)   | 11        | NM     | (57)  | 29        | NM     |
| Other (1)  | -  | -         | NM     | -   | 186       | -100%  |
| Investment increase and change in market<br>value          | (1,769)  | 1,061     | NM     | (1,085)                                       | 704       | NM     |
| Balance as of end-of-period                                | \$ 16,106                                      | \$ 15,398 | 5%     | \$ 16,106                                     | \$ 15,398 | 5%     |
| <b>Total Multi-Fund® and Other Variable<br/>Annuities:</b> |  |           |        |   |           |        |
| Balance as of beginning-of-period                          | \$ 16,388                                      | \$ 15,112 | 8%     | \$ 16,221                                     | \$ 15,786 | 3%     |
| Gross deposits   | 175  | 185       | -5%    | 539   | 570       | -5%    |
| Withdrawals and deaths                                     | (383)  | (391)     | 2%     | (1,203)                                       | (1,220)   | 1%     |
| Net flows  | (208)  | (206)     | -1%    | (664)   | (650)     | -2%    |
| Investment increase and change in market<br>value          | (1,122)  | 830       | NM     | (499)   | 600       | NM     |
| Balance as of end-of-period                                | \$ 15,058                                      | \$ 15,736 | -4%    | \$ 15,058                                     | \$ 15,736 | -4%    |
| <b>Total Annuities and Mutual Funds:</b>                   |  |           |        |   |           |        |
| Balance as of beginning-of-period                          | \$ 40,287                                      | \$ 35,040 | 15%    | \$ 38,824                                     | \$ 35,302 | 10%    |
| Gross deposits   | 1,456  | 1,262     | 15%    | 3,996   | 3,943     | 1%     |
| Withdrawals and deaths                                     | (1,127)  | (1,540)   | 27%    | (3,711)                                       | (3,930)   | 6%     |
| Net flows  | 329  | (278)     | 218%   | 285   | 13        | NM     |
| Transfers between fixed and variable<br>accounts           | (19)   | 10        | NM     | (63)  | 27        | NM     |
| Other (1)  | -  | -         | NM     | -   | 186       | -100%  |
| Investment increase and change in market<br>value          | (3,577)  | 2,316     | NM     | (2,026)                                       | 1,560     | NM     |
| Balance as of end-of-period (2)                            | \$ 37,020                                      | \$ 37,088 | 0%     | \$ 37,020                                     | \$ 37,088 | 0%     |



- (1) Represents LINCOLN ALLIANCE® program assets held by a third-party trustee that were not previously included in the account value roll forward. Effective January 1, 2010, all such LINCOLN ALLIANCE® program activity was included in the account value roll forward.
- (2) Includes mutual fund account values and other third-party trustee-held assets. These items are not included in the separate accounts reported on our Consolidated Balance Sheets as we do not have any ownership interest in them.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |          |        | For the Nine<br>Months Ended<br>September 30,<br>2011 |          |        |
|--|--|----------|--------|---|----------|--------|
|  | 2011   | 2010     | Change | 2011  | 2010     | Change |
| Net Flows on Account Values                      |  |          |        |   |          |        |
| Variable portion of variable annuity deposits    | \$ 391   | \$ 368   | 6%     | \$ 1,199  | \$ 1,171 | 2%     |
| Variable portion of variable annuity withdrawals | (511)  | (473)    | -8%    | (1,614)   | (1,637)  | 1%     |
| Variable portion of variable annuity net flows   | (120)  | (105)    | -14%   | (415)   | (466)    | 11%    |
| Fixed portion of variable annuity deposits       | 77   | 77       | 0%     | 239   | 234      | 2%     |
| Fixed portion of variable annuity withdrawals    | (162)  | (163)    | 1%     | (490)   | (492)    | 0%     |
| Fixed portion of variable annuity net flows      | (85)   | (86)     | 1%     | (251)   | (258)    | 3%     |
| Total variable annuity deposits                  | 468  | 445      | 5%     | 1,438   | 1,405    | 2%     |
| Total variable annuity withdrawals               | (673)  | (636)    | -6%    | (2,104)   | (2,129)  | 1%     |
| Total variable annuity net flows                 | (205)  | (191)    | -7%    | (666)   | (724)    | 8%     |
| Fixed annuity deposits                           | 301  | 272      | 11%    | 803   | 758      | 6%     |
| Fixed annuity withdrawals                        | (194)  | (292)    | 34%    | (639)   | (710)    | 10%    |
| Fixed annuity net flows                          | 107  | (20)     | NM     | 164   | 48       | 242%   |
| Total annuity deposits                           | 769  | 717      | 7%     | 2,241   | 2,163    | 4%     |
| Total annuity withdrawals                        | (867)  | (928)    | 7%     | (2,743)   | (2,839)  | 3%     |
| Total annuity net flows                          | (98)   | (211)    | 54%    | (502)   | (676)    | 26%    |
| Mutual fund deposits                             | 687  | 545      | 26%    | 1,755   | 1,780    | -1%    |
| Mutual fund withdrawals                          | (260)  | (612)    | 58%    | (968)   | (1,091)  | 11%    |
| Mutual fund net flows                            | 427  | (67)     | NM     | 787   | 689      | 14%    |
| Total annuity and mutual fund deposits           | 1,456  | 1,262    | 15%    | 3,996   | 3,943    | 1%     |
| Total annuity and mutual fund withdrawals        | (1,127)  | (1,540)  | 27%    | (3,711)   | (3,930)  | 6%     |
| Total annuity and mutual fund net flows          | \$ 329   | \$ (278) | 218%   | \$ 285  | \$ 13    | NM     |



|   | For the Three<br>Months Ended<br>September 30, |          |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|----------|--------|---|--------|--------|
|   | 2011   | 2010     | Change | 2011  | 2010   | Change |
| Other Changes to Account Values   |  |          |        |   |        |        |
| Change in market value on variable,<br>excluding the fixed portion of variable  | \$ (1,888)                                     | \$ 1,173 | NM     | \$ (1,176)                                    | \$ 617 | NM     |
| Transfers to the variable portion of<br>variable annuity products from the<br>fixed<br>portion of variable annuity products | (124)  | (79)     | -57%   | (214)   | (148)  | -45%   |

We charge expense assessments to cover insurance and administrative expenses. Expense assessments are generally equal to a percentage of the daily variable account values. Average daily account values are driven by net flows and the equity markets. Our expense assessments include fees we earn for the services that we provide to our mutual fund programs. In addition, for both our fixed and variable annuity contracts, we collect surrender charges when contract holders surrender their contracts during the surrender charge periods to protect us from premature withdrawals.

#### Net Investment Income and Interest Credited

Details underlying net investment income, interest credited (in millions) and our interest rate spread were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Net Investment Income  |  |        |        |   |        |        |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | \$ 180   | \$ 179 | 1%     | \$ 536  | \$ 527 | 2%     |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums (1)                               | 1  | 1      | 0%     | 20  | 3      | NM     |
| Alternative investments (2)  | -  | -      | NM     | 1   | 2      | -50%   |
| Surplus investments (3)  | 12   | 12     | 0%     | 41  | 37     | 11%    |
| Total net investment income  | \$ 193   | \$ 192 | 1%     | \$ 598  | \$ 569 | 5%     |
| Interest Credited  | \$ 110   | \$ 110 | 0%     | \$ 326  | \$ 331 | -2%    |

(1) See “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” below for additional information.

(2) See “Consolidated Investments – Alternative Investments” below for additional information.

(3) Represents net investment income on the required statutory surplus for this segment and includes the effect of investment income on alternative investments for such assets that are held in the portfolios supporting statutory surplus versus the portfolios supporting product liabilities.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       |                          | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |                          |
|--|--|-------|--------------------------|---|-------|--------------------------|
|  |  |       | Basis<br>Point<br>Change |   |       | Basis<br>Point<br>Change |
| <b>Interest Rate Spread</b>  |  |       |                          |   |       |                          |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | 5.53%  | 5.71% | (18)                     | 5.57%   | 5.71% | (14)                     |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums                                   | 0.04%  | 0.04% | -                        | 0.20%   | 0.03% | 17                       |
| Alternative investments  | 0.00%  | 0.01% | (1)                      | 0.01%   | 0.02% | (1)                      |
| Net investment income yield on reserves  | 5.57%  | 5.76% | (19)                     | 5.78%   | 5.76% | 2                        |
| Interest rate credited to contract holders   | 3.31%  | 3.47% | (16)                     | 3.34%   | 3.52% | (18)                     |
| Interest rate spread   | 2.26%  | 2.29% | (3)                      | 2.44%   | 2.24% | 20                       |

Note: The yields, rates and spreads above are calculated using whole dollars instead of dollars rounded to millions.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |           |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |           |        |
|--|--|-----------|--------|---|-----------|--------|
|  |  |           | Change |   |           | Change |
| <b>Other Information</b>   |  |           |        |   |           |        |
| Average invested assets on reserves  | \$ 13,068  | \$ 12,462 | 5%     | \$ 12,848   | \$ 12,311 | 4%     |
| Average fixed account values, including<br>the fixed portion of variable   | 13,244   | 12,683    | 4%     | 13,048  | 12,515    | 4%     |
| Transfers to the fixed portion of variable<br>annuity products from the variable<br>portion of variable annuity products | 124  | 79        | 57%    | 214   | 148       | 45%    |
| Net flows for fixed annuities, including<br>the fixed portion of variable  | 22   | (106)     | 121%   | (87)  | (210)     | 59%    |

A portion of our investment income earned is credited to the contract holders of our fixed annuity products, including the fixed portion of variable annuity contracts. We expect to earn a spread between what we earn on the underlying general account investments supporting the fixed annuity product line, including the fixed portion of variable annuity contracts, and what we credit to our fixed annuity contract holders' accounts, including the fixed portion of variable annuity contracts. The interest rate spread for this segment represents the excess of the yield on invested assets on reserves over the average crediting rate. The yield on invested assets on reserves is calculated as net investment income, excluding the amounts attributable to our surplus investments, reverse repurchase agreement interest expense, inter-segment cash management program interest expense and interest on collateral, divided by average invested assets on reserves. The average invested assets on reserves are calculated based upon total invested assets, excluding hedge derivatives. The average crediting rate is calculated as interest credited before DSI amortization, divided by the average fixed account values, including the fixed portion of variable annuity contracts. Commercial mortgage loan prepayments and bond makewhole premiums, investment income on alternative investments and surplus investment income can vary significantly from period to period due to a number of factors and, therefore, may contribute to investment income results that are not indicative of the underlying trends.

#### Benefits

Benefits for this segment include changes in GDB and GLB benefit reserves and our expected costs associated with purchases of derivatives used to hedge our GDB benefit ratio unlocking.

## Underwriting, Acquisition, Insurance and Other Expenses

Details underlying underwriting, acquisition, insurance and other expenses (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |       |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|-------|--------|---|--------|--------|
|   | 2011   | 2010  | Change | 2011  | 2010   | Change |
| Underwriting, Acquisition, Insurance<br>and Other Expenses          |  |       |        |   |        |        |
| Commissions:  |  |       |        |   |        |        |
| Deferrable  | \$ 5   | \$ 6  | -17%   | \$ 17   | \$ 19  | -11%   |
| Non-deferrable  | 11   | 9     | 22%    | 33  | 28     | 18%    |
| General and administrative expenses                                 | 65   | 60    | 8%     | 200   | 171    | 17%    |
| Taxes, licenses and fees  | 3  | 3     | 0%     | 12  | 10     | 20%    |
| Total expenses incurred   | 84   | 78    | 8%     | 262   | 228    | 15%    |
| DAC deferrals   | (16)   | (15)  | -7%    | (51)  | (46)   | -11%   |
| Total expenses recognized before<br>amortization                    | 68   | 63    | 8%     | 211   | 182    | 16%    |
| DAC and VOBA amortization, net of<br>interest:                      |  |       |        |   |        |        |
| Prospective unlocking - assumption<br>changes                       | -  | (17)  | 100%   | -   | (17)   | 100%   |
| Prospective unlocking - model refinements                           | 3  | -     | NM     | 3   | -      | NM     |
| Retrospective unlocking   | (9)  | -     | NM     | (12)  | 5      | NM     |
| Amortization, net of interest,<br>excluding unlocking               | 19   | 20    | -5%    | 55  | 59     | -7%    |
| Total underwriting, acquisition,<br>insurance and other<br>expenses | \$ 81  | \$ 66 | 23%    | \$ 257  | \$ 229 | 12%    |
| DAC Deferrals   |  |       |        |   |        |        |
| As a percentage of annuity sales/deposits                           | 2.1%   | 2.1%  |        | 2.3%  | 2.1%   |        |

Commissions and other costs that vary with and are related primarily to the sale of annuity contracts are deferred to the extent recoverable and are amortized over the lives of the contracts in relation to EGPs. Certain of our commissions, such as trail commissions that are based on account values, are expensed as incurred rather than deferred and amortized. We do not pay commissions on sales of our mutual fund products, and distribution expenses associated with the sale of these mutual fund products are expensed as incurred.

## RESULTS OF INSURANCE SOLUTIONS

The Insurance Solutions business provides its products through two segments: Life Insurance and Group Protection. The Life Insurance segment offers wealth protection and transfer opportunities through term insurance, a linked-benefit product (which is a UL policy linked with riders that provide for long-term care costs) and both single (including corporate-owned UL and VUL (“COLI”) and bank-owned UL and VUL (“BOLI”)) and survivorship versions of UL and VUL insurance products. The Group Protection segment offers group life, disability and dental insurance to employers.

For factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language” above.

## Life Insurance

## Income (Loss) from Operations

Details underlying the results for Life Insurance (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Operating Revenues   |  |        |        |   |        |        |
| Insurance premiums   | \$ 104   | \$ 107 | -3%    | \$ 324  | \$ 327 | -1%    |
| Insurance fees   | 498  | 451    | 10%    | 1,473   | 1,404  | 5%     |
| Net investment income                                      | 569  | 543    | 5%     | 1,736   | 1,618  | 7%     |
| Other revenues and fees                                    | 5  | 7      | -29%   | 19  | 23     | -17%   |
| Total operating revenues                                   | 1,176  | 1,108  | 6%     | 3,552   | 3,372  | 5%     |
| Operating Expenses   |  |        |        |   |        |        |
| Interest credited  | 312  | 299    | 4%     | 922   | 896    | 3%     |
| Benefits   | 152  | 561    | -73%   | 1,209   | 1,333  | -9%    |
| Underwriting, acquisition, insurance and<br>other expenses | 527  | 168    | 214%   | 763   | 640    | 19%    |
| Total operating expenses                                   | 991  | 1,028  | -4%    | 2,894   | 2,869  | 1%     |
| Income (loss) from operations before<br>taxes              | 185  | 80     | 131%   | 658   | 503    | 31%    |
| Federal income tax expense (benefit)                       | 53   | 20     | 165%   | 208   | 155    | 34%    |
| Income (loss) from operations                              | \$ 132   | \$ 60  | 120%   | \$ 450  | \$ 348 | 29%    |

## Comparison of the Three Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- A \$16 million favorable prospective unlocking of DAC, VOBA, DFEL and reserves during the third quarter of 2011 compared to an \$82 million unfavorable prospective unlocking during the third quarter of 2010 (see “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” for more information):
  - § The favorable prospective unlocking during the third quarter of 2011 was due to a \$5 million favorable unlocking from assumption changes and an \$11 million favorable unlocking from model refinements;
  - § The prospective unlocking during the third quarter of 2011 created significant line item fluctuations as underwriting, acquisition, insurance and other expenses was increased by \$285 million, pre-tax, and benefits was decreased by \$322 million, pre-tax; and
  - § The unfavorable prospective unlocking during the third quarter of 2010 was due to an \$86 million unfavorable unlocking from assumption changes due primarily to lower investment margins attributable primarily to lowering our new money investment yield assumption to reflect the then current new money rates and to approximate the forward curve for interest rates relevant at such time, as this effect alone represented \$114 million unfavorable unlocking (see “Additional Information” below), as well as higher lapses than our model projections assumed, partially offset by lower surrenders and death claims than our model projections assumed, net of a \$4 million favorable unlocking from model refinements.

The increase in income from operations was partially offset by the following:

- An increase in benefits, excluding unlocking, attributable primarily to:
  - § Higher death claims; and
- § An increase in secondary guarantee life insurance product reserves from model refinements and continued growth in the business.

Comparison of the Nine Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- The effect of prospective unlocking discussed above and a \$20 million favorable prospective unlocking of DAC, VOBA, DFEL and reserves during the first six months of 2011 due to an \$18 million favorable unlocking from model refinements and a \$2 million favorable unlocking from assumption changes;
- Higher net investment income and relatively flat interest credited attributable primarily to:
  - § Growth in business in force;
- § More favorable investment income on alternative investments, including those within our surplus portfolio, and higher prepayment and bond makewhole premiums (see “Consolidated Investments – Alternative Investments” and “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” below for more information); and
  - § Reductions in crediting rates after the third quarter of 2010, discussed in “Additional Information” below; partially offset by:
    - § New money rates averaging below our portfolio yields; and
- An increase in insurance fees, excluding unlocking, attributable primarily to growth in insurance in force.

The increase in income from operations was partially offset by the following:

- An increase in benefits, excluding unlocking, attributable primarily to:
  - § Higher death claims; and
- § An increase in secondary guarantee life insurance product reserves from model refinements and continued growth in the business;
- An increase in underwriting, acquisition, insurance and other underwriting expenses, excluding amortization of DAC and VOBA, attributable primarily to:
  - § An increase in expenses associated with reserve financing supporting our secondary guarantee UL and term business due primarily to higher pricing that has occurred in reaction to the unfavorable market conditions experienced during the recession and our continued efforts to reduce the strain of these statutory reserves (see “Strategies to Address Statutory Reserve Strain” below for more information); and
  - § Higher incentive compensation accruals as a result of higher earnings and production performance relative to targets;
- An \$18 million unfavorable retrospective unlocking of DAC, VOBA and DFEL during the first nine months of 2011, compared to a \$4 million unfavorable retrospective unlocking during the first nine months of 2010:
  - § The unfavorable retrospective unlocking during the first nine months of 2011 was due primarily to lower premiums received and higher death claims than our model projections assumed; and
  - § The unfavorable retrospective unlocking during the first nine months of 2010 was due primarily to lower premiums received and higher death claims than our model projections assumed, partially offset by lower lapses and expenses than our model projections assumed; and
- A reduction in net investment income and an increase in underwriting, acquisition, insurance and other expenses as a result of the inter-company reinsurance agreement effective December 31, 2010.

Strategies to Address Statutory Reserve Strain

Our insurance subsidiaries have statutory surplus and RBC levels above current regulatory required levels. Products containing secondary guarantees require reserves calculated under AG38. Our insurance subsidiaries are employing strategies to reduce the strain of increasing AG38 and Valuation of Life Insurance Policies Model Regulation (“XXX”) statutory reserves associated with secondary guarantee UL and term products. As discussed further below, we have been successful in executing reinsurance solutions to release capital to Other Operations. We expect to regularly



execute transactions designed to release capital as we continue to sell products that are subject to these reserving requirements. We also plan to refinance prior transactions with long-term structured solutions.

Included in the letters of credit (“LOCs”) issued as of September 30, 2011, and reported in the credit facilities table in “Review of Consolidated Financial Condition – Liquidity and Capital Resources – Financing Activities,” was approximately \$1.4 billion of long-dated LOCs issued to support inter-company reinsurance arrangements, of which approximately \$200 million and \$400 million was issued for UL business with secondary guarantees through 2015 and 2031, respectively, and approximately \$800 million was issued for term business through 2023. LOCs and related capital market alternatives lower the capital effect of secondary guarantee UL products. An inability to obtain the necessary LOC capacity or other capital market alternatives could affect our returns on our in-force secondary guarantee UL business. However, we believe that our insurance subsidiaries have sufficient capital to support the increase in statutory reserves, based on our current reserve projections, if such structures are not available. See “Part II – Item 1A. Risk Factors – Changes to the calculation of reserves and attempts to mitigate the impact of Regulation XXX and Actuarial Guideline 38 may fail in whole or in part resulting in an adverse effect on our financial condition and results of

operations” herein for further information on XXX and AG38 reserves. See the table in “Underwriting, Acquisition, Insurance and Other Expenses” below for the presentation of our expenses associated with reserve financing. We expect these expenses will approximately double in 2011 as compared to the level we experienced in 2010 as a result of higher pricing that has occurred in reaction to the unfavorable market conditions experienced during the recession and our expectation to execute additional reserve financing arrangements.

#### Additional Information

We are in the process of completing a conversion of our actuarial valuation systems to a uniform valuation platform for a significant portion of this segment’s blocks of business. Although we expect some differences to emerge as a result of this exercise, based upon the current status of these efforts, we are not able to provide an estimate or range of the effects to our results of operations until completion of the conversion. See “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” in our 2010 Form 10-K for information on our actuarial system conversion.

We expect higher expenses for this segment during the fourth quarter of 2011 than what was experienced during the average of the first three quarters of 2011. The expected increase is attributable primarily to expected increases in investments in strategic initiatives.

We expect to manage the effects of spreads on near-term income from operations through portfolio management and, to a lesser extent, crediting rate actions, which assumes no significant changes in net flows into or out of our fixed accounts or other changes that may cause interest rate spreads to differ from our expectations. On January 1, 2011, we implemented a 65 basis point decrease in crediting rates on most interest-sensitive products not already at contractual guarantees, which reduced overall crediting rates by approximately 7 basis points. During the third quarter of 2010, we lowered our new money investment yield assumption to reflect the then current new money rates and to approximate the forward curve for interest rates relevant at such time. The result was a drop in the current new money investment rate followed by a gradual annual recovery over eight years to a rate of 6.31%, 54 basis points below our previous ultimate long-term assumption of 6.85%. This assumption revision had the effect of lowering the projected EGPs for this segment, thereby increasing our rate of amortization, which results in higher DAC, VOBA and DFEL amortization and lower earnings for this segment.

For information on interest rate spreads and the interest rate risk due to falling interest rates, see “Item 3. Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk – Interest Rate Risk on Fixed Insurance Businesses – Falling Rates” and “Part II – Item 1A. Risk Factors – Changes in interest rates and sustained low interest rates may cause interest rate spreads to decrease and changes in interest rates may also result in increased contract withdrawals” herein.

Sales are not recorded as a component of revenues (other than for traditional products) and do not have a significant effect on current quarter income from operations but are indicators of future profitability. Generally, we have higher sales during the second half of the year with the fourth quarter being our strongest. However, we face conditions in the marketplace as discussed in “Current Market Conditions” above that may challenge our sales volume for 2012.

We provide information about this segment’s operating revenue and operating expense line items, the period in which amounts are recognized, key drivers of changes and historical details underlying the line items and their associated drivers below.

#### Insurance Premiums

Insurance premiums relate to traditional products and are a function of the rates priced into the product and the level of insurance in force. Insurance in force, in turn, is driven by sales, persistency and mortality experience.



## Insurance Fees

Details underlying insurance fees, sales, net flows, account values and in-force face amount (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30,<br>2011 |        |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |          |        |
|---|--|--------|--------|---|----------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010     | Change |
| Insurance Fees  |  |        |        |   |          |        |
| Mortality assessments                                 | \$ 335   | \$ 320 | 5%     | \$ 986  | \$ 963   | 2%     |
| Expense assessments                                   | 230  | 208    | 11%    | 694   | 600      | 16%    |
| Surrender charges                                     | 21   | 22     | -5%    | 73  | 77       | -5%    |
| DFEL:   |  |        |        |   |          |        |
| Deferrals   | (119)  | (123)  | 3%     | (360)   | (355)    | -1%    |
| Amortization, net of interest:                        |  |        |        |   |          |        |
| Prospective unlocking - assumption<br>changes         | (17)   | 56     | NM     | -   | 56       | -100%  |
| Prospective unlocking - model<br>refinements          | 4  | (62)   | 106%   | (28)  | (62)     | 55%    |
| Retrospective unlocking                               | 2  | -      | NM     | (4)   | 15       | NM     |
| Amortization, net of interest,<br>excluding unlocking | 42   | 30     | 40%    | 112   | 110      | 2%     |
| Total insurance fees                                  | \$ 498   | \$ 451 | 10%    | \$ 1,473  | \$ 1,404 | 5%     |

|                       | For the Three<br>Months Ended<br>September 30,<br>2011 |        |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |        |        |
|-----------------------|--|--------|--------|---|--------|--------|
|                       | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Sales by Product      |  |        |        |   |        |        |
| UL:                   |  |        |        |   |        |        |
| Excluding MoneyGuard® | \$ 74  | \$ 76  | -3%    | \$ 242  | \$ 246 | -2%    |
| MoneyGuard®           | 48   | 27     | 78%    | 121   | 68     | 78%    |
| Total UL              | 122  | 103    | 18%    | 363   | 314    | 16%    |
| VUL                   | 13   | 11     | 18%    | 34  | 28     | 21%    |
| COLI and BOLI         | 8  | 18     | -56%   | 35  | 35     | 0%     |
| Term                  | 12   | 16     | -25%   | 39  | 54     | -28%   |
| Total sales           | \$ 155   | \$ 148 | 5%     | \$ 471  | \$ 431 | 9%     |

|                             |          |          |     |          |          |     |
|-----------------------------|----------|----------|-----|----------|----------|-----|
| Net Flows                   |          |          |     |          |          |     |
| Deposits                    | \$ 1,343 | \$ 1,230 | 9%  | \$ 3,887 | \$ 3,370 | 15% |
| Withdrawals and deaths      | (380)    | (505)    | 25% | (1,235)  | (1,393)  | 11% |
| Net flows                   | \$ 963   | \$ 725   | 33% | \$ 2,652 | \$ 1,977 | 34% |
| Contract holder assessments | \$ 819   | \$ 776   | 6%  | \$ 2,441 | \$ 2,292 | 7%  |

|                               | As of September 30, |            |        |
|-------------------------------|---------------------|------------|--------|
|                               | 2011                | 2010       | Change |
| Account Values                |                     |            |        |
| UL                            | \$ 27,485           | \$ 25,633  | 7%     |
| VUL                           | 4,658               | 4,759      | -2%    |
| Interest-sensitive whole life | 2,276               | 2,262      | 1%     |
| Total account values          | \$ 34,419           | \$ 32,654  | 5%     |
| In-Force Face Amount          |                     |            |        |
| UL and other                  | \$ 304,475          | \$ 294,171 | 4%     |
| Term insurance                | 269,969             | 262,583    | 3%     |
| Total in-force face amount    | \$ 574,444          | \$ 556,754 | 3%     |

Insurance fees relate only to interest-sensitive products and include mortality assessments, expense assessments (net of deferrals and amortization related to DFEL) and surrender charges. Mortality and expense assessments are deducted from our contract holders' account values. These amounts are a function of the rates priced into the product and premiums received, face amount in force and account values. Insurance in force, in turn, is driven by sales, persistency and mortality experience. In-force growth should be considered independently with respect to term products versus UL and other products, as term products have a lower profitability relative to face amount compared to interest-sensitive and other products.

Sales in the table above and as discussed above were reported as follows:

- UL (excluding linked-benefit products) and VUL (including COLI and BOLI) – first year commissionable premiums plus 5% of excess premiums received, including an adjustment for internal replacements of approximately 50% of commissionable premiums;
- MoneyGuard® (our linked-benefit product) – 15% of premium deposits; and
- Term – 100% of first year paid premiums.

UL and VUL products with secondary guarantees represented approximately 38% of interest-sensitive life insurance in force as of September 30, 2011, and approximately 46% and 49% of sales for the three and nine months ended September 30, 2011, respectively. Actuarial Guideline 37, or Variable Life Reserves for Guaranteed Minimum Death Benefits, and AG38 impose additional statutory reserve requirements for these products.

#### Net Investment Income and Interest Credited

Details underlying net investment income, interest credited (in millions) and our interest rate spread were as follows:

|  | For the Three Months Ended |        |        | For the Nine Months Ended |          |        |
|--|----------------------------|--------|--------|---------------------------|----------|--------|
|  | September 30,              |        |        | September 30,             |          |        |
|  | 2011                       | 2010   | Change | 2011                      | 2010     | Change |
| Net Investment Income  |                            |        |        |                           |          |        |
| Fixed maturity securities, mortgage loans on real estate and other, net of investment expenses | \$ 524                     | \$ 506 | 4%     | \$ 1,563                  | \$ 1,494 | 5%     |
| Commercial mortgage loan prepayment and bond makewhole premiums (1)                            | 5                          | 3      | 67%    | 21                        | 13       | 62%    |
| Alternative investments (2)  | 13                         | 8      | 63%    | 61                        | 35       | 74%    |

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|                             |  |        |        |    |          |          |     |
|-----------------------------|--|--------|--------|----|----------|----------|-----|
| Surplus investments (3)     |  | 27     | 26     | 4% | 91       | 76       | 20% |
| Total net investment income |  | \$ 569 | \$ 543 | 5% | \$ 1,736 | \$ 1,618 | 7%  |
| Interest Credited           |  | \$ 312 | \$ 299 | 4% | \$ 922   | \$ 896   | 3%  |

(1) See “Consolidated Investments – Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” below for additional information.

- (2) See “Consolidated Investments – Alternative Investments” below for additional information.  
(3) Represents net investment income on the required statutory surplus for this segment and includes the effect of investment income on alternative investments for such assets that are held in the portfolios supporting statutory surplus versus the portfolios supporting product liabilities.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       |                          | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |                          |
|--|--|-------|--------------------------|---|-------|--------------------------|
|  |  |       | Basis<br>Point<br>Change |   |       | Basis<br>Point<br>Change |
| <b>Interest Rate Yields and Spread</b>   |  |       |                          |   |       |                          |
| Attributable to interest-sensitive products:   |  |       |                          |   |       |                          |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | 5.74%  | 5.93% | (19)                     | 5.82%   | 5.89% | (7)                      |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums                                   | 0.06%  | 0.03% | 3                        | 0.08%   | 0.05% | 3                        |
| Alternative investments  | 0.16%  | 0.11% | 5                        | 0.26%   | 0.16% | 10                       |
| Net investment income yield on<br>reserves   | 5.96%  | 6.07% | (11)                     | 6.16%   | 6.10% | 6                        |
| Interest rate credited to contract holders   | 4.10%  | 4.15% | (5)                      | 4.09%   | 4.17% | (8)                      |
| Interest rate spread   | 1.86%  | 1.92% | (6)                      | 2.07%   | 1.93% | 14                       |
| Attributable to traditional products:  |  |       |                          |   |       |                          |
| Fixed maturity securities, mortgage loans<br>on real estate and other, net of<br>investment expenses | 5.90%  | 5.99% | (9)                      | 5.93%   | 6.12% | (19)                     |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums                                   | 0.03%  | 0.12% | (9)                      | 0.04%   | 0.05% | (1)                      |
| Alternative investments  | 0.00%  | 0.01% | (1)                      | 0.01%   | 0.01% | -                        |
| Net investment income yield on<br>reserves   | 5.93%  | 6.12% | (19)                     | 5.98%   | 6.18% | (20)                     |

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |           |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |           |        |
|--|--|-----------|--------|---|-----------|--------|
|  |  |           | Change |   |           | Change |
| <b>Averages</b>                              |  |           |        |   |           |        |
| Attributable to interest-sensitive products: |  |           |        |   |           |        |
| Invested assets on reserves                  | \$ 32,080  | \$ 29,510 | 9%     | \$ 31,454   | \$ 29,172 | 8%     |
| Account values - universal and whole life    | 30,237   | 28,545    | 6%     | 29,832  | 28,301    | 5%     |
| Attributable to traditional products:        |  |           |        |   |           |        |
| Invested assets on reserves                  | 4,311  | 4,493     | -4%    | 4,290   | 4,490     | -4%    |

A portion of the investment income earned for this segment is credited to contract holder accounts. Invested assets will typically grow at a faster rate than account values because of the AG38 reserve requirements, which cause statutory reserves to grow at a faster rate than account values. Invested assets are based upon the statutory reserve liabilities and are therefore affected by various reserve adjustments, including capital transactions providing relief from AG38 reserve requirements, which leads to a transfer of invested assets from this segment to Other Operations

for use in other corporate purposes. We expect to earn a spread between what we earn on the underlying general account investments and what we credit to our contract holders' accounts. The interest rate spread for this segment represents the excess of the yield on invested assets on reserves over the average crediting rate on interest-sensitive products. The yield on invested assets on reserves is calculated as net investment income, excluding amounts attributable to our surplus investments and reverse repurchase agreement interest expense, divided by average invested assets on reserves. In addition, we exclude the effect of earnings from affordable housing tax credit securities, which is reflected as a



reduction to federal income tax expense, from our spread calculations. We use our investment income to offset the earnings effect of the associated build of our policy reserves for traditional products. Commercial mortgage loan prepayments and bond makewhole premiums and investment income on alternative investments can vary significantly from period to period due to a number of factors, and, therefore, may contribute to investment income results that are not indicative of the underlying trends.

## Benefits

Details underlying benefits (dollars in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|---|--|--------|--------|---|----------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010     | Change |
| Benefits  |  |        |        |   |          |        |
| Death claims direct and assumed                                   | \$ 759   | \$ 605 | 25%    | \$ 2,179                                      | \$ 1,884 | 16%    |
| Death claims ceded  | (377)  | (258)  | -46%   | (1,047)                                       | (839)    | -25%   |
| Reserves released on death  | (108)  | (104)  | -4%    | (345)   | (328)    | -5%    |
| Net death benefits  | 274  | 243    | 13%    | 787   | 717      | 10%    |
| Change in secondary guarantee life<br>insurance product reserves: |  |        |        |   |          |        |
| Prospective unlocking - assumption<br>changes                     | (347)  | 60     | NM     | (317)   | 60       | NM     |
| Prospective unlocking - model<br>refinements                      | (8)  | 93     | NM     | 155   | 93       | 67%    |
| Change in reserves, excluding<br>unlocking                        | 128  | 89     | 44%    | 362   | 218      | 66%    |
| Other benefits:   |  |        |        |   |          |        |
| Prospective unlocking - assumption<br>changes                     | 33   | -      | NM     | 33  | -        | NM     |
| Other benefits, excluding unlocking (1)                           | 72   | 76     | -5%    | 189   | 245      | -23%   |
| Total benefits  | \$ 152   | \$ 561 | -73%   | \$ 1,209                                      | \$ 1,333 | -9%    |
| Death claims per \$1,000 of in-force                              | 1.91   | 1.75   | 9%     | 1.85  | 1.74     | 6%     |

(1) Includes primarily traditional product changes in reserves and dividends.

Benefits for this segment includes claims incurred during the period in excess of the associated reserves for its interest-sensitive and traditional products. In addition, benefits includes the change in secondary guarantee life insurance product reserves. The reserve for secondary guarantees is affected by changes in expected future trends of expense assessments causing unlocking adjustments to this liability similar to DAC, VOBA and DFEL.

## Underwriting, Acquisition, Insurance and Other Expenses

Details underlying underwriting, acquisition, insurance and other expenses (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|--------|--------|---|--------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Underwriting, Acquisition, Insurance<br>and Other Expenses          |  |        |        |   |        |        |
| Commissions   | \$ 161   | \$ 156 | 3%     | \$ 500  | \$ 474 | 5%     |
| General and administrative expenses                                 | 116  | 112    | 4%     | 343   | 319    | 8%     |
| Expenses associated with reserve<br>financing                       | 14   | 13     | 8%     | 42  | 25     | 68%    |
| Taxes, licenses and fees  | 40   | 31     | 29%    | 110   | 90     | 22%    |
| Total expenses incurred   | 331  | 312    | 6%     | 995   | 908    | 10%    |
| DAC and VOBA deferrals  | (223)  | (213)  | -5%    | (690)   | (644)  | -7%    |
| Total expenses recognized before<br>amortization                    | 108  | 99     | 9%     | 305   | 264    | 16%    |
| DAC and VOBA amortization, net of<br>interest:                      |  |        |        |   |        |        |
| Prospective unlocking - assumption<br>changes                       | 290  | 128    | 127%   | 276   | 128    | 116%   |
| Prospective unlocking - model<br>refinements                        | (5)  | (162)  | 97%    | (228)   | (162)  | -41%   |
| Retrospective unlocking   | 10   | 4      | 150%   | 24  | 21     | 14%    |
| Amortization, net of interest,<br>excluding unlocking               | 123  | 98     | 26%    | 383   | 386    | -1%    |
| Other intangible amortization                                       | 1  | 1      | 0%     | 3   | 3      | 0%     |
| Total underwriting, acquisition,<br>insurance and other<br>expenses | \$ 527   | \$ 168 | 214%   | \$ 763  | \$ 640 | 19%    |
| DAC and VOBA Deferrals  |  |        |        |   |        |        |
| As a percentage of sales  | 143.9%   | 143.9% |        | 146.5%  | 149.4% |        |

Commissions and other general and administrative expenses that vary with and are related primarily to the production of new business are deferred to the extent recoverable and for our interest-sensitive products are generally amortized over the lives of the contracts in relation to EGPs. For our traditional products, DAC and VOBA are amortized on either a straight-line basis or as a level percent of premium of the related contracts, depending on the block of business.

When comparing DAC and VOBA deferrals as a percentage of sales for the nine months ended September 30, 2011 and 2010, the decrease is primarily a result of incurred deferrable commissions declining at a rate higher than sales attributable primarily to changes in sales mix to products with lower commission rates.

## Group Protection

## Income (Loss) from Operations

Details underlying the results for Group Protection (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|--|--|--------|--------|---|----------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010     | Change |
| Operating Revenues   |  |        |        |   |          |        |
| Insurance premiums   | \$ 440   | \$ 414 | 6%     | \$ 1,336                                      | \$ 1,258 | 6%     |
| Net investment income                                      | 38   | 35     | 9%     | 115   | 103      | 12%    |
| Other revenues and fees                                    | 1  | 2      | -50%   | 7   | 6        | 17%    |
| Total operating revenues                                   | 479  | 451    | 6%     | 1,458   | 1,367    | 7%     |
| Operating Expenses   |  |        |        |   |          |        |
| Interest credited  | 1  | 1      | 0%     | 3   | 2        | 50%    |
| Benefits   | 319  | 330    | -3%    | 991   | 974      | 2%     |
| Underwriting, acquisition, insurance and<br>other expenses | 116  | 106    | 9%     | 344   | 309      | 11%    |
| Total operating expenses                                   | 436  | 437    | 0%     | 1,338   | 1,285    | 4%     |
| Income (loss) from operations before<br>taxes              | 43   | 14     | 207%   | 120   | 82       | 46%    |
| Federal income tax expense (benefit)                       | 15   | 5      | 200%   | 42  | 28       | 50%    |
| Income (loss) from operations                              | \$ 28  | \$ 9   | 211%   | \$ 78   | \$ 54    | 44%    |

|  | For the Three<br>Months<br>Ended<br>September 30, |      |        | For the Nine<br>Months Ended<br>September 30, |       |        |
|--|---|------|--------|---|-------|--------|
|  | 2011  | 2010 | Change | 2011  | 2010  | Change |
| Income (Loss) from Operations by<br>Product Line |   |      |        |   |       |        |
| Life   | \$ 12   | \$ 5 | 140%   | \$ 29   | \$ 24 | 21%    |
| Disability                                       | 15  | 4    | 275%   | 48  | 30    | 60%    |
| Dental   | -   | (1)  | 100%   | (3)   | (4)   | 25%    |
| Total non-medical                                | 27  | 8    | 238%   | 74  | 50    | 48%    |
| Medical  | 1   | 1    | 0%     | 4   | 4     | 0%     |
| Income (loss) from operations                    | \$ 28   | \$ 9 | 211%   | \$ 78   | \$ 54 | 44%    |

## Comparison of the Three and Nine Months Ended September 30, 2011 to 2010

Income from operations for this segment increased due primarily to the following:

- More favorable non-medical loss ratio experience;
- Growth in insurance premiums driven by normal, organic business growth in our non-medical products; and
- Higher net investment income driven by an increase in business and, for the nine months ended September 30, 2011, higher portfolio yields on surplus.

The increase in income from operations was partially offset by higher underwriting, acquisition, insurance and other expenses due primarily to higher costs of investments in strategic initiatives associated with enhancements to sales processes and improvements to technology platforms during the three and nine months ended September 30, 2011.

## Additional Information

During the three and nine months ended September 30, 2011, our non-medical loss ratios were 71.8% and 73.1%, respectively, below the 79.2% and 76.5% we experienced during the corresponding periods of 2010. Although we experienced improvement in our loss ratios for all non-medical product lines during 2011 as compared to unfavorable experience throughout 2010, loss ratios in general are likely to remain at the high end of our long-term expectation of 71% to 74% during the fourth quarter of 2011, as demonstrated by our disability claim incidence and short-term disability claim durations still being at elevated levels. However, we expect loss ratios to recover over time. For every one percent increase in the loss ratio above our expectation, we would expect an approximate annual \$10 million to \$12 million decrease to income from operations.

Management compares trends in actual loss ratios to pricing expectations because group-underwriting risks change over time. We expect normal fluctuations in our composite non-medical loss ratios of this segment, as claims experience is inherently uncertain. We are taking actions to manage the effects of our loss ratio results, such as implementing price adjustments on our product lines upon renewal to better reflect our experience going forward. In addition, we have been focusing on managing the higher volume of incidence through claims risk management, including contracting additional resources to help reduce caseloads and improve claim recovery experience so that incidence volumes do not detract from our claim recovery efforts. We are also employing tools to identify and support claimants who will return to work.

We expect expenses to remain elevated for this segment during the fourth quarter of 2011, attributable primarily to continued increases in investments in strategic initiatives.

We are evaluating the potential effects that health care reform may have on the value and profitability of this segment's products and income from operations, including, but not limited to, potential changes to traditional sources of income for our brokers who may seek additional portfolio options and/or modification to compensation structures.

During the second quarter of 2011, we reviewed the discount rate assumptions associated with reserves for long-term disability and life waiver claim incurrals. Due to the persistent decline in new money investment yields, we lowered the discount rate by 50 basis points to 4.25% on new incurrals, which decreased income from operations by \$3 million during the second quarter of 2011. For information on the effects of current interest rates on our long-term disability claim reserves, see "Item 3. Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk – Interest Rate Risk on Fixed Insurance Businesses – Falling Rates."

Sales relate to long-duration contracts sold to new contract holders and new programs sold to existing contract holders. We believe that the trend in sales is an important indicator of development of business in force over time. Our sales declined during the first nine months of 2011 as compared to the corresponding period of 2010 due to conditions in the marketplace.

We provide information about this segment's operating revenue and operating expense line items, the period in which amounts are recognized, key drivers of changes and historical details underlying the line items and their associated drivers below.

### Insurance Premiums

Details underlying insurance premiums (in millions) were as follows:

|  | For the Three<br>Months Ended | For the Nine<br>Months Ended |
|--|-------------------------------|------------------------------|
|--|-------------------------------|------------------------------|

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|                                    | September 30, |        |        | September 30, |          |        |
|------------------------------------|---------------|--------|--------|---------------|----------|--------|
|                                    | 2011          | 2010   | Change | 2011          | 2010     | Change |
| Insurance Premiums by Product Line |               |        |        |               |          |        |
| Life                               | \$ 174        | \$ 158 | 10%    | \$ 517        | \$ 476   | 9%     |
| Disability                         | 190           | 181    | 5%     | 567           | 542      | 5%     |
| Dental                             | 46            | 43     | 7%     | 137           | 123      | 11%    |
| Total non-medical                  | 410           | 382    | 7%     | 1,221         | 1,141    | 7%     |
| Medical                            | 30            | 32     | -6%    | 115           | 117      | -2%    |
| Total insurance premiums           | \$ 440        | \$ 414 | 6%     | \$ 1,336      | \$ 1,258 | 6%     |
| Sales                              | \$ 75         | \$ 68  | 10%    | \$ 187        | \$ 197   | -5%    |

Our cost of insurance and policy administration charges are embedded in the premiums charged to our customers. The premiums are a function of the rates priced into the product and our business in force. Business in force, in turn, is driven by sales and persistency experience. Sales in the table above are the combined annualized premiums for our life, disability and dental products.

#### Net Investment Income

We use our investment income to offset the earnings effect of the associated build of our policy reserves, which are a function of our insurance premiums and the yields on our invested assets.

#### Benefits and Interest Credited

Details underlying benefits and interest credited (in millions) and loss ratios by product line were as follows:

| Benefits and Interest Credited by<br>Product Line | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|--------|--------|---|--------|--------|
|   | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Life  | \$ 125   | \$ 125 | 0%     | \$ 386  | \$ 367 | 5%     |
| Disability  | 134  | 145    | -8%    | 396   | 404    | -2%    |
| Dental  | 35   | 34     | 3%     | 110   | 102    | 8%     |
| Total non-medical                                 | 294  | 304    | -3%    | 892   | 873    | 2%     |
| Medical   | 26   | 27     | -4%    | 102   | 103    | -1%    |
| Total benefits and interest credited              | \$ 320   | \$ 331 | -3%    | \$ 994  | \$ 976 | 2%     |
| <br>Loss Ratios by Product Line                   |  |        |        |   |        |        |
| Life  | 72.1%  | 79.2%  |        | 74.7%   | 77.1%  |        |
| Disability  | 70.4%  | 79.2%  |        | 70.0%   | 74.5%  |        |
| Dental  | 76.2%  | 79.3%  |        | 80.0%   | 83.2%  |        |
| Total non-medical                                 | 71.8%  | 79.2%  |        | 73.1%   | 76.5%  |        |
| Medical   | 86.9%  | 86.2%  |        | 87.8%   | 87.9%  |        |

Note: Loss ratios presented above are calculated using whole dollars instead of dollars rounded to millions.

## Underwriting, Acquisition, Insurance and Other Expenses

Details underlying underwriting, acquisition, insurance and other expenses (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30, |        |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--|--|--------|--------|---|--------|--------|
|  | 2011   | 2010   | Change | 2011  | 2010   | Change |
| Underwriting, Acquisition, Insurance<br>and Other Expenses       |  |        |        |   |        |        |
| Commissions  | \$ 50  | \$ 48  | 4%     | \$ 150  | \$ 142 | 6%     |
| General and administrative expenses                              | 60   | 51     | 18%    | 168   | 147    | 14%    |
| Taxes, licenses and fees   | 12   | 10     | 20%    | 32  | 29     | 10%    |
| Total expenses incurred  | 122  | 109    | 12%    | 350   | 318    | 10%    |
| DAC deferrals  | (16)   | (13)   | -23%   | (39)  | (41)   | 5%     |
| Total expenses recognized before<br>amortization                 | 106  | 96     | 10%    | 311   | 277    | 12%    |
| DAC and VOBA amortization, net of<br>interest                    | 10   | 10     | 0%     | 33  | 32     | 3%     |
| Total underwriting, acquisition,<br>insurance and other expenses | \$ 116   | \$ 106 | 9%     | \$ 344  | \$ 309 | 11%    |
| DAC Deferrals  |  |        |        |   |        |        |
| As a percentage of insurance premiums                            | 3.6%   | 3.1%   |        | 2.9%  | 3.3%   |        |

Expenses, excluding broker commissions, that vary with and are related primarily to the production of new business are deferred to the extent recoverable and are amortized on either a straight-line basis or as a level percent of premium of the related contracts depending on the block of business. Broker commissions, which vary with and are related to paid premiums, are expensed as incurred. The level of expenses is an important driver of profitability for this segment as group insurance contracts are offered within an environment that competes on the basis of price and service.

## RESULTS OF OTHER OPERATIONS

Other Operations includes investments related to the excess capital in our insurance subsidiaries; investments in media properties and other corporate investments; benefit plan net liability; the unamortized deferred gain on indemnity reinsurance related to the sale of reinsurance to Swiss Re in 2001; the results of certain disability income business; the Institutional Pension business, which is a closed-block of pension business, the majority of which was sold on a group annuity basis, and is currently in run-off; and debt costs. We are actively managing our remaining radio station clusters to maximize performance and future value.

For factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language” above.



## Income (Loss) from Operations

Details underlying the results for Other Operations (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |         |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|---|--|---------|--------|---|----------|--------|
|   | 2011   | 2010    | Change | 2011  | 2010     | Change |
| Operating Revenues  |  |         |        |   |          |        |
| Insurance premiums  | \$ 1   | \$ -    | NM     | \$ 1  | \$ -     | NM     |
| Net investment income   | 80   | 81      | -1%    | 236   | 244      | -3%    |
| Amortization of deferred gain on<br>business sold through reinsurance | 18   | 18      | 0%     | 54  | 55       | -2%    |
| Media revenues (net)  | 20   | 20      | 0%     | 56  | 53       | 6%     |
| Other revenues and fees   | 1  | 3       | -67%   | 4   | 15       | -73%   |
| Total operating revenues  | 120  | 122     | -2%    | 351   | 367      | -4%    |
| Operating Expenses  |  |         |        |   |          |        |
| Interest credited   | 27   | 29      | -7%    | 85  | 90       | -6%    |
| Benefits  | 34   | 35      | -3%    | 95  | 105      | -10%   |
| Media expenses  | 17   | 15      | 13%    | 51  | 43       | 19%    |
| Other expenses  | 33   | 31      | 6%     | 62  | 96       | -35%   |
| Interest and debt expense   | 71   | 74      | -4%    | 215   | 212      | 1%     |
| Total operating expenses  | 182  | 184     | -1%    | 508   | 546      | -7%    |
| Income (loss) from operations before<br>taxes                         | (62)   | (62)    | 0%     | (157)   | (179)    | 12%    |
| Federal income tax expense (benefit)                                  | (17)   | (22)    | 23%    | (53)  | (66)     | 20%    |
| Income (loss) from operations   | \$ (45)  | \$ (40) | -13%   | \$ (104)                                      | \$ (113) | 8%     |

## Comparison of the Three Months Ended September 30, 2011 to 2010

Loss from operations for this segment increased due primarily to the following:

- Less favorable tax items during the third quarter of 2011 that affected the federal income tax benefit; and
- Higher other expenses due primarily to:
  - § The recognition of a \$9 million estimated assessment during the third quarter of 2011 associated with the New York State Department of Financial Services' liquidation plan for Executive Life Insurance Company of New York; partially offset by:
    - § Legal and merger-related expenses in 2010; and
    - § Lower branding and non-brand marketing expenses in 2011 (see "Additional Information" below).

The increase in loss from operations was partially offset by lower interest and debt expense attributable to lower average balances of outstanding debt during the third quarter of 2011.

## Comparison of the Nine Months Ended September 30, 2011 to 2010

Loss from operations for this segment decreased due primarily to the following:

- Lower other expenses due primarily to:
  - § Higher legal and merger-related expenses in 2010;

- § Lower branding and non-brand marketing expenses in 2011 (see “Additional Information” below); and
  - § Higher reimbursement associated with reserve financing transactions in 2011;
- partially offset by:
- § The recognition of the estimated assessment discussed above; and
  - Lower benefits due to favorable mortality in our Institutional Pension business in 2011.

The decrease in loss from operations was partially offset by the following:

- Lower media earnings related primarily to the continued weakening of the U.S. economy, including poor consumer confidence;
- Lower net investment income, net of interest credited, due primarily to:
  - § Lower average invested assets driven primarily by repurchases of common stock, net cash used in operating activities primarily due to interest payments and transfers to other segments for OTTI, partially offset by distributable earnings received from our insurance segments; and
  - § The decline in new money rates and interest rates in general;
- Higher interest and debt expense attributable to higher average balances of outstanding debt in 2011; and
- Less favorable tax items during 2011 that affected the federal income tax benefit.

#### Additional Information

We expect higher expenses for Other Operations in the fourth quarter of 2011 than what was experienced during the average of the first three quarters of 2011. The expected increase includes increases in branding and non-brand marketing expenses.

See Note 10 for a discussion concerning audits and inquiries relating to our handling of unclaimed property. It is possible that these activities may result in additional payments to beneficiaries, additional escheatment of funds deemed abandoned under state laws and administrative penalties and interest. Currently, we are not able to estimate the reasonably possible costs associated with these matters.

The results of Other Operations include our thrift business. We are in the process of exiting this business, which will not have a significant effect on Other Operations' results.

We provide information about Other Operations' operating revenue and operating expense line items, the period in which amounts are recognized, key drivers of changes and historical details underlying the line items and their associated drivers below.

#### Net Investment Income and Interest Credited

We utilize an internal formula to determine the amount of capital that is allocated to our business segments. Investment income on capital in excess of the calculated amounts is reported in Other Operations. If regulations require increases in our insurance segments' statutory reserves and surplus, the amount of capital retained by Other Operations would decrease and net investment income would be negatively affected. In addition, as discussed below in "Review of Consolidated Financial Condition – Liquidity and Capital Resources – Sources of Liquidity and Cash Flow – Alternative Sources of Liquidity," we maintain an inter-segment cash management program where certain subsidiaries can borrow from or lend money to the holding company to meet short-term borrowing needs. The inter-segment cash management program affects net investment income for Other Operations, as all inter-segment eliminations are reported within Other Operations.

Write-downs for OTTI decrease the recorded value of our invested assets owned by our business segments. These write-downs are not included in the income from operations of our operating segments. When impairment occurs, assets are transferred to the business segments' portfolios and will reduce the future net investment income for Other Operations, but should not have an effect on a consolidated basis unless the impairments are related to defaulted securities. Statutory reserve adjustments for our business segments can also cause allocations of invested assets between the affected segments and Other Operations.

The majority of our interest credited relates to our reinsurance operations sold to Swiss Re in 2001. A substantial amount of the business was sold through indemnity reinsurance transactions, which is still recorded in our consolidated financial statements. The interest credited corresponds to investment income earnings on the assets we continue to hold for this business. There is no effect to income or loss in Other Operations or on a consolidated basis for these amounts because interest earned on the blocks that continue to be reinsured is passed through to Swiss Re in the form of interest credited.

#### Benefits

Benefits are recognized when incurred for Institutional Pension products and disability income business.

## Other Expenses

Details underlying other expenses (in millions) were as follows:

|  | For the Three Months Ended September 30, |       |        | For the Nine Months Ended September 30, |       |        |
|--|--|-------|--------|---|-------|--------|
|  | 2011                                     | 2010  | Change | 2011                                    | 2010  | Change |
| Other Expenses   |  |       |        |   |       |        |
| General and administrative expenses:   |  |       |        |   |       |        |
| Legal  | \$ -                                     | \$ 5  | -100%  | \$ 2                                    | \$ 18 | -89%   |
| Branding   | 9  | 10    | -10%   | 19                                      | 23    | -17%   |
| Non-brand marketing  | -  | 3     | -100%  | 2                                       | 8     | -75%   |
| Other (1)  | 12                                       | 12    | 0%     | 35                                      | 42    | -17%   |
| Total general and administrative expenses  | 21                                       | 30    | -30%   | 58                                      | 91    | -36%   |
| Merger-related expenses (2)  | -  | 2     | -100%  | -                                       | 7     | -100%  |
| Taxes, licenses and fees   | 14                                       | -     | NM     | 11                                      | (1)   | NM     |
| Inter-segment reimbursement associated with reserve financing and LOC expenses (3) | (2)                                      | (1)   | -100%  | (7)                                     | (1)   | NM     |
| Total other expenses   | \$ 33                                    | \$ 31 | 6%     | \$ 62                                   | \$ 96 | -35%   |

- (1) Includes expenses that are corporate in nature including charitable contributions, amortization of media intangible assets with a definite life, other expenses not allocated to our business segments and inter-segment expense eliminations.
- (2) Includes the result of actions undertaken by us to eliminate duplicate operations and functions as a result of the Jefferson-Pilot merger along with costs related to the implementation of our unified product portfolio and other initiatives. These actions were completed during 2010. Our cumulative integration expense was approximately \$225 million, pre-tax, which excluded amounts capitalized or recorded as goodwill.
- (3) Consists of reimbursements to Other Operations from the Life Insurance segment for the use of proceeds from certain issuances of senior notes that were used as long-term structured solutions, net of expenses incurred by Other Operations for its use of LOCs. The inter-segment amounts are not reported on our Consolidated Statements of Income.

## Interest and Debt Expense

Our current level of interest expense may not be indicative of the future due to, among other things, the timing of the use of cash, the availability of funds from our inter-company cash management program and the future cost of capital. For additional information on our financing activities, see "Review of Consolidated Financial Condition – Liquidity and Capital Resources – Sources of Liquidity and Cash Flow – Financing Activities" below.

## REALIZED GAIN (LOSS) AND BENEFIT RATIO UNLOCKING

Details underlying realized gain (loss), after-DAC (1) and benefit ratio unlocking (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |         |        | For the Nine<br>Months Ended<br>September 30, |         |        |
|---|--|---------|--------|---|---------|--------|
|   | 2011   | 2010    | Change | 2011  | 2010    | Change |
| Components of Realized Gain (Loss),<br>Pre-Tax  |  |         |        |   |         |        |
| Total operating realized gain (loss)  | \$ 22  | \$ 18   | 22%    | \$ 66   | \$ 49   | 35%    |
| Total excluded realized gain (loss)   | (185)  | 25      | NM     | (243)   | (27)    | NM     |
| Total realized gain (loss), pre-tax   | \$ (163)                                       | \$ 43   | NM     | \$ (177)                                      | \$ 22   | NM     |
| Reconciliation of Excluded Realized<br>Gain (Loss) Net of Benefit Ratio<br>Unlocking, After-Tax |  |         |        |   |         |        |
| Total excluded realized gain (loss)   | \$ (120)                                       | \$ 17   | NM     | \$ (158)                                      | \$ (17) | NM     |
| Benefit ratio unlocking   | (41)   | 25      | NM     | (37)  | -       | NM     |
| Excluded realized gain (loss) net of<br>benefit ratio unlocking, after-tax                      | \$ (161)                                       | \$ 42   | NM     | \$ (195)                                      | \$ (17) | NM     |
| Components of Excluded Realized<br>Gain (Loss) Net of Benefit Ratio<br>Unlocking, After-Tax     |  |         |        |   |         |        |
| Realized gain (loss) related to certain<br>investments  | \$ (28)  | \$ (17) | NM     | \$ (62)                                       | \$ (56) | NM     |
| Gain (loss) on the mark-to-market on<br>certain instruments                                     | (69)   | 69      | NM     | (62)  | 47      | NM     |
| Variable annuity net derivatives results:   |  |         |        |   |         |        |
| Hedge program performance   | (82)   | 20      | NM     | (111)   | (40)    | NM     |
| Unlocking for GLB reserves hedged   | (72)   | -       | NM     | (72)  | -       | NM     |
| GLB NPR component   | 92   | (30)    | NM     | 112   | 28      | 300%   |
| Total variable annuity net derivatives<br>results   | (62)   | (10)    | NM     | (71)  | (12)    | NM     |
| Indexed annuity forward-starting option   | (2)  | -       | NM     | -   | 4       | -100%  |
| Excluded realized gain (loss) net of<br>benefit ratio unlocking,<br>after-tax                   | \$ (161)                                       | \$ 42   | NM     | \$ (195)                                      | \$ (17) | NM     |

(1) DAC refers to the associated amortization of DAC, VOBA, DSI and DFEL and changes in other contract holder funds and funds withheld reinsurance liabilities.

For factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language” above.

For information on our counterparty exposure, see “Item 3. Quantitative and Qualitative Disclosures About Market Risk.”

Comparison of the Three and Nine Months Ended September 30, 2011 to 2010

We had realized losses during the three and nine months ended September 30, 2011, as compared to gains for the corresponding periods of 2010, due primarily to less favorable results on the mark-to-market on certain instruments and variable annuity net derivatives results.

Our hedge program performance during the three and nine months ended September 30, 2011, was unfavorably affected by volatile capital markets that were experienced during the third quarter of 2011 and prospective unlocking (see below for more information), partially offset by the NPR component of the liability being favorable during this same period attributable to an increase in the NPR factors related to 10-year CDS spreads. See “Variable Annuity Net Derivatives Results” below for a discussion of how our NPR adjustment is determined.

During 2011, we had unfavorable prospective unlocking, attributable primarily to changes in lapse assumptions, partially offset by changes in our assumptions for long-term volatility.

The unfavorable results related to the gain (loss) on the mark-to-market on certain instruments during the three and nine months ended September 30, 2011, as compared to the corresponding periods of 2010, were attributable primarily to widening spreads on corporate credit default swaps during 2011, whereas these spreads narrowed during 2010, which affect the derivative instruments related to our consolidated VIEs, partially offset by gains on our trading securities during 2011 due to the decline in interest rates during 2011.

For information regarding realized gains (losses) related to certain investments, see “Consolidated Investments – Realized Gain (Loss) Related to Certain Investments” below.

#### Operating Realized Gain (Loss)

Indexed annuity net derivatives results include the net difference between the change in the fair value of the S&P 500 call options that we hold and the change in the fair value of the embedded derivative liabilities of our indexed annuity products. The change in the fair value of the liability for the embedded derivative represents the amount that is credited to the indexed annuity contract.

Our GWB, guaranteed income benefit (“GIB”) and 4LATER® features have elements of both benefit reserves and embedded derivative reserves. We calculate the value of the embedded derivative reserve and the benefit reserve based on the specific characteristics of each GLB feature. For our GLBs that meet the definition of an embedded derivative under the Derivatives and Hedging Topic of the FASB ASC, we record them at fair value with changes in fair value recorded in realized gain (loss) on our Consolidated Statements of Income (Loss). In bifurcating the embedded derivative, we attribute to the embedded derivative the portion of total fees collected from the contract holder that relates to the GLB riders (the “attributed fees”). These attributed fees represent the present value of future claims expected to be paid for the GLB at the inception of the contract (the “net valuation premium”) plus a margin that a theoretical market participant would include for risk/profit (the “risk/profit margin”).

We include the risk/profit margin portion of the GLB attributed rider fees in operating realized gain (loss) and include the net valuation premium of the GLB attributed rider fees in excluded realized gain (loss). For our Annuities and Defined Contribution segments, the excess of total fees collected from the contract holders over the GLB attributed rider fees is reported in insurance fees.

#### Realized Gain (Loss) Related to Certain Investments

See “Consolidated Investments – Realized Gain (Loss) Related to Certain Investments” below.

#### Gain (Loss) on the Mark-to-Market on Certain Instruments

Gain (loss) on the mark-to-market on certain instruments, including those associated with our consolidated VIEs and trading securities represents changes in the fair values of certain derivative instruments (including the credit default swaps and contingent forwards associated with consolidated VIEs), total return swaps (embedded derivatives that are



theoretically included in our various modified coinsurance and coinsurance with funds withheld reinsurance arrangements that have contractual returns related to various assets and liabilities associated with these arrangements) and trading securities.

See Note 4 for information about our consolidated VIEs.

#### Variable Annuity Net Derivatives Results

Our variable annuity net derivatives results include the net valuation premium, the change in the GLB embedded derivative reserves and the change in the fair value of the derivative instruments we own to hedge them, including the cost of purchasing the hedging instruments. In addition, these results include the changes in reserves not accounted for at fair value and resulting benefit ratio unlocking on our GDB and GLB riders. It also includes the change in the fair value of the derivative instruments we own to hedge the change in our benefit ratio unlocking, excluding our expected cost of the hedging instruments and the associated benefit ratio unlocking. The benefit ratio unlocking represents changes in reserves on our GDB and GLB riders not accounted for at fair value.

Our GWB, GIB and 4LATER® features have elements of both benefit reserves and embedded derivative reserves. We calculate the value of the embedded derivative reserve and the benefit reserve based on the specific characteristics of each GLB feature. We record the embedded derivative reserve on our GLBs at fair value on our Consolidated Balance Sheets. We use derivative instruments to hedge our exposure to the risks and earnings volatility that result from changes in the GLB embedded derivatives reserves. The change in fair value of these derivative instruments is designed to generally offset the change in embedded derivative reserves. In the table above, we have presented the components of our GLB results, which can be volatile especially when sudden and significant changes in equity markets and/or interest rates occur. When we assess the effectiveness of our hedge program, we exclude the effect of the change in the component of the embedded derivative reserves related to the required NPR. We do not attempt to hedge the change in the NPR component of the liability. As of September 30, 2011, the net effect of the NPR resulted in a \$298 million decrease in the liability for our GLB embedded derivative reserves. The NPR factors affect the discount rate used in the calculation of the GLB embedded derivative reserve. Our methodology for calculating the NPR component of the embedded derivative reserve utilizes an extrapolated 30-year NPR spread curve applied to a series of expected cash flows over the expected life of the embedded derivative. Our cash flows consist of both expected fees to be received from contract holders and benefits to be paid, and these cash flows are different on a pre- and post- NPR basis. We utilize a model based on our holding company's credit default swap ("CDS") spreads adjusted for items, such as the liquidity of our holding company CDS. Because the guaranteed benefit liabilities are contained within our insurance subsidiaries, we apply items, such as the effect of our insurance subsidiaries' claims-paying ratings compared to holding company credit risk and the over-collateralization of insurance liabilities, in order to determine factors that are representative of a theoretical market participant's view of the NPR of the specific liability within our insurance subsidiaries.

Details underlying the NPR component and associated effect to our GLB embedded derivative reserves (dollars in millions) were as follows:

|  | As of<br>September<br>30,<br>2011 | As of<br>June 30,<br>2011 | As of<br>March 31,<br>2011 | As of<br>December<br>31,<br>2010 | As of<br>September<br>30,<br>2010 |
|--|-----------------------------------|---------------------------|----------------------------|----------------------------------|-----------------------------------|
| 10-year CDS spread                       | 4.42%                             | 2.02%                     | 1.78%                      | 1.98%                            | 2.55%                             |
| NPR factor related to 10-year CDS spread | 0.51%                             | 0.24%                     | 0.17%                      | 0.17%                            | 0.30%                             |
| Unadjusted embedded derivative liability | \$ 2,642                          | \$ 306                    | \$ 112                     | \$ 389                           | \$ 1,556                          |

Estimating what the absolute amount of the NPR effect will be period to period is difficult due to the utilization of all cash flows and the shape of the spread curve. Currently, we estimate that if the NPR factors as of September 30, 2011, were to have been zero along all points on the spread curve, then the NPR offset to the unadjusted liability would have resulted in an unfavorable effect to net income of approximately \$400 million, pre-DAC and tax. Alternatively, if the NPR factors were 20 basis points higher along all points on the spread curve as of September 30, 2011, then there would have been a favorable effect to net income of approximately \$120 million, pre-DAC and tax. In the preceding two sentences, "DAC" refers to the associated amortization of DAC, VOBA, DSI and DFEL. Changing market conditions could cause this relationship to deviate significantly in future periods. Sensitivity within this range is primarily a result of volatility in our CDS spreads and the slope of the CDS spread term structure.

For additional information on our guaranteed benefits, see "Critical Accounting Policies and Estimates – Derivatives – Guaranteed Living Benefits" above.

Indexed Annuity Forward-Starting Option

The liability for the forward-starting option reflects changes in the fair value of embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations applicable to future reset periods for our indexed annuity products accounted for under the Derivatives and Hedging and the Fair Value Measurements and Disclosures Topics of the FASB ASC. These fair values represent an estimate of the cost of the options we will purchase in the future, discounted back to the date of the balance sheet, using current market indications of volatility and interest rates, which can vary significantly from period to period due to a number of factors and therefore can provide results that are not indicative of the underlying trends.

## CONSOLIDATED INVESTMENTS

Details underlying our consolidated investment balances (in millions) were as follows:

|                               | Percentage of<br>Total Investments |                                  |                                   |                                  |
|-------------------------------|------------------------------------|----------------------------------|-----------------------------------|----------------------------------|
|                               | As of<br>September<br>30,<br>2011  | As of<br>December<br>31,<br>2010 | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
| Investments                   |                                    |                                  |                                   |                                  |
| AFS securities:               |                                    |                                  |                                   |                                  |
| Fixed maturity                | \$ 74,591                          | \$ 68,030                        | 80.9%                             | 81.6%                            |
| VIEs' fixed maturity          | 700                                | 584                              | 0.8%                              | 0.7%                             |
| Total fixed maturity          | 75,291                             | 68,614                           | 81.7%                             | 82.3%                            |
| Equity                        | 137                                | 197                              | 0.1%                              | 0.2%                             |
| Trading securities            | 2,726                              | 2,596                            | 3.0%                              | 3.1%                             |
| Mortgage loans on real estate | 6,893                              | 6,752                            | 7.5%                              | 8.1%                             |
| Real estate                   | 136                                | 202                              | 0.1%                              | 0.3%                             |
| Policy loans                  | 2,874                              | 2,865                            | 3.1%                              | 3.5%                             |
| Derivative investments        | 3,029                              | 1,076                            | 3.3%                              | 1.3%                             |
| Alternative investments       | 817                                | 750                              | 0.9%                              | 0.9%                             |
| Other investments             | 288                                | 288                              | 0.3%                              | 0.3%                             |
| Total investments             | \$ 92,191                          | \$ 83,340                        | 100.0%                            | 100.0%                           |

## Investment Objective

Invested assets are an integral part of our operations. We follow a balanced approach to investing for both current income and prudent risk management, with an emphasis on generating sufficient current income, net of income tax, to meet our obligations to customers, as well as other general liabilities. This balanced approach requires the evaluation of expected return and risk of each asset class utilized, while still meeting our income objectives. This approach is important to our asset-liability management because decisions can be made based upon both the economic and current investment income considerations affecting assets and liabilities. For a discussion on our risk management process, see "Part II – Item 7A. Quantitative and Qualitative Disclosures About Market Risk" in our 2010 Form 10-K.

## Investment Portfolio Composition and Diversification

Fundamental to our investment policy is diversification across asset classes. Our investment portfolio, excluding cash and invested cash, is composed of fixed maturity securities, mortgage loans on real estate, real estate (either wholly-owned or in joint ventures) and other long-term investments. We purchase investments for our segmented portfolios that have yield, duration and other characteristics that take into account the liabilities of the products being supported.

We have the ability to maintain our investment holdings throughout credit cycles because of our capital position, the long-term nature of our liabilities and the matching of our portfolios of investment assets with the liabilities of our various products.

## Fixed Maturity and Equity Securities Portfolios

Fixed maturity securities and equity securities consist of portfolios classified as AFS and trading. Mortgage-backed and private securities are included in both AFS and trading portfolios.

Details underlying our fixed maturity and equity securities portfolios by industry classification (in millions) are presented in the tables below. These tables agree in total with the presentation of AFS securities in Note 5; however, the categories below represent a more detailed breakout of the AFS portfolio; therefore, the investment classifications listed below do not agree to the investment categories provided in Note 5.

|   | As of September 30, 2011 |            |                       |           |               |
|---|--------------------------|------------|-----------------------|-----------|---------------|
|   | Amortized                | Unrealized | Unrealized            | Fair      | %             |
|   | Cost                     | Gains      | Losses<br>and<br>OTTI | Value     | Fair<br>Value |
| Fixed Maturity AFS Securities                           |                          |            |                       |           |               |
| Industry corporate bonds:                               |                          |            |                       |           |               |
| Financial services                                      | \$ 8,743                 | \$ 592     | \$ 149                | \$ 9,186  | 12.2%         |
| Basic industry  | 3,039                    | 276        | 38                    | 3,277     | 4.4%          |
| Capital goods   | 3,953                    | 447        | 16                    | 4,384     | 5.8%          |
| Communications  | 3,249                    | 317        | 38                    | 3,528     | 4.7%          |
| Consumer cyclical                                       | 3,094                    | 310        | 42                    | 3,362     | 4.5%          |
| Consumer non-cyclical                                   | 7,876                    | 1,224      | 1                     | 9,099     | 12.1%         |
| Energy  | 4,825                    | 633        | 3                     | 5,455     | 7.2%          |
| Technology  | 1,793                    | 195        | 4                     | 1,984     | 2.6%          |
| Transportation  | 1,434                    | 172        | 5                     | 1,601     | 2.1%          |
| Industrial other  | 906                      | 77         | 9                     | 974       | 1.3%          |
| Utilities   | 10,572                   | 1,379      | 36                    | 11,915    | 15.9%         |
| Corporate asset-backed securities ("ABS"):              |                          |            |                       |           |               |
| Collateralized debt obligations ("CDOs")                | 93                       | -          | 6                     | 87        | 0.1%          |
| Commercial real estate ("CRE") CDOs                     | 38                       | -          | 14                    | 24        | 0.0%          |
| Credit card   | 789                      | 47         | -                     | 836       | 1.1%          |
| Home equity   | 927                      | 3          | 273                   | 657       | 0.9%          |
| Manufactured housing                                    | 87                       | 5          | 1                     | 91        | 0.1%          |
| Auto loan   | 64                       | 1          | -                     | 65        | 0.1%          |
| Other   | 193                      | 30         | -                     | 223       | 0.3%          |
| CMBS:   |                          |            |                       |           |               |
| Non-agency backed                                       | 1,719                    | 70         | 119                   | 1,670     | 2.2%          |
| Collateralized mortgage and other obligations ("CMOs"): |                          |            |                       |           |               |
| Agency backed   | 3,467                    | 390        | -                     | 3,857     | 5.1%          |
| Non-agency backed                                       | 1,534                    | 14         | 197                   | 1,351     | 1.8%          |
| Mortgage pass through securities ("MPTS"):              |                          |            |                       |           |               |
| Agency backed   | 3,051                    | 188        | -                     | 3,239     | 4.3%          |
| Non-agency backed                                       | 1                        | -          | -                     | 1         | 0.0%          |
| Municipals:   |                          |            |                       |           |               |
| Taxable   | 3,395                    | 571        | 9                     | 3,957     | 5.3%          |
| Tax-exempt  | 12                       | -          | -                     | 12        | 0.0%          |
| Government and government agencies:                     |                          |            |                       |           |               |
| United States   | 1,240                    | 224        | -                     | 1,464     | 1.9%          |
| Foreign   | 1,643                    | 151        | 4                     | 1,790     | 2.4%          |
| Hybrid and redeemable preferred securities              | 1,317                    | 55         | 170                   | 1,202     | 1.6%          |
| Total fixed maturity AFS securities                     | 69,054                   | 7,371      | 1,134                 | 75,291    | 100.0%        |
| Equity AFS Securities                                   | 131                      | 16         | 10                    | 137       |               |
| Total AFS securities                                    | 69,185                   | 7,387      | 1,144                 | 75,428    |               |
| Trading Securities (1)                                  | 2,343                    | 416        | 33                    | 2,726     |               |
| Total AFS and trading securities                        | \$ 71,528                | \$ 7,803   | \$ 1,177              | \$ 78,154 |               |



|  | As of December 31, 2010 |            |                       |           |               |
|--|-------------------------|------------|-----------------------|-----------|---------------|
|  | Amortized               | Unrealized | Unrealized            | Fair      | %             |
|  | Cost                    | Gains      | Losses<br>and<br>OTTI | Value     | Fair<br>Value |
| Fixed Maturity AFS Securities              |                         |            |                       |           |               |
| Industry corporate bonds:                  |                         |            |                       |           |               |
| Financial services                         | \$ 8,377                | \$ 438     | \$ 148                | \$ 8,667  | 12.7%         |
| Basic industry                             | 2,478                   | 203        | 20                    | 2,661     | 3.9%          |
| Capital goods                              | 3,425                   | 243        | 45                    | 3,623     | 5.3%          |
| Communications                             | 3,050                   | 251        | 32                    | 3,269     | 4.8%          |
| Consumer cyclical                          | 2,772                   | 185        | 47                    | 2,910     | 4.2%          |
| Consumer non-cyclical                      | 7,259                   | 628        | 20                    | 7,867     | 11.5%         |
| Energy                                     | 4,533                   | 428        | 17                    | 4,944     | 7.2%          |
| Technology                                 | 1,414                   | 108        | 9                     | 1,513     | 2.2%          |
| Transportation                             | 1,379                   | 116        | 3                     | 1,492     | 2.2%          |
| Industrial other                           | 884                     | 53         | 10                    | 927       | 1.4%          |
| Utilities                                  | 9,800                   | 708        | 62                    | 10,446    | 15.2%         |
| ABS:                                       |                         |            |                       |           |               |
| CDOs                                       | 128                     | 22         | 8                     | 142       | 0.2%          |
| CRE CDOs                                   | 46                      | -          | 14                    | 32        | 0.0%          |
| Credit card                                | 831                     | 33         | 4                     | 860       | 1.3%          |
| Home equity                                | 1,002                   | 6          | 268                   | 740       | 1.1%          |
| Manufactured housing                       | 110                     | 3          | 4                     | 109       | 0.2%          |
| Auto loan                                  | 162                     | 2          | -                     | 164       | 0.2%          |
| Other                                      | 211                     | 21         | 1                     | 231       | 0.3%          |
| CMBS:                                      |                         |            |                       |           |               |
| Non-agency backed                          | 2,144                   | 95         | 186                   | 2,053     | 3.0%          |
| CMOs:                                      |                         |            |                       |           |               |
| Agency backed                              | 3,975                   | 308        | 1                     | 4,282     | 6.2%          |
| Non-agency backed                          | 1,718                   | 16         | 259                   | 1,475     | 2.1%          |
| MPTS:                                      |                         |            |                       |           |               |
| Agency backed                              | 2,978                   | 106        | 5                     | 3,079     | 4.5%          |
| Non-agency backed                          | 2                       | -          | -                     | 2         | 0.0%          |
| Municipals:                                |                         |            |                       |           |               |
| Taxable                                    | 3,219                   | 27         | 94                    | 3,152     | 4.6%          |
| Tax-exempt                                 | 3                       | -          | -                     | 3         | 0.0%          |
| Government and government agencies:        |                         |            |                       |           |               |
| United States                              | 931                     | 120        | 2                     | 1,049     | 1.5%          |
| Foreign                                    | 1,438                   | 94         | 7                     | 1,525     | 2.2%          |
| Hybrid and redeemable preferred securities | 1,476                   | 56         | 135                   | 1,397     | 2.0%          |
| Total fixed maturity AFS securities        | 65,745                  | 4,270      | 1,401                 | 68,614    | 100.0%        |
| Equity AFS Securities                      | 179                     | 25         | 7                     | 197       |               |
| Total AFS securities                       | 65,924                  | 4,295      | 1,408                 | 68,811    |               |
| Trading Securities (1)                     | 2,340                   | 297        | 41                    | 2,596     |               |
| Total AFS and trading securities           | \$ 68,264               | \$ 4,592   | \$ 1,449              | \$ 71,407 |               |

(1)



Certain of our trading securities support our modified coinsurance arrangements (“Modco”) and the investment results are passed directly to the reinsurers. Refer to the “Trading Securities” section of our 2010 Form 10-K for further details.

## AFS Securities

The general intent of the AFS accounting guidance is to reflect stockholders' equity as if unrealized gains and losses were actually recognized, and it is necessary that we consider all related accounting adjustments that would occur upon such a hypothetical recognition of unrealized gains and losses. Such related balance sheet effects include adjustments to the balances of DAC, VOBA, DFEL, other contract holder funds and deferred income taxes. Adjustments to each of these balances are charged or credited to accumulated OCI. For instance, DAC is adjusted upon the recognition of unrealized gains or losses because the amortization of DAC is based upon an assumed emergence of gross profits on certain insurance business. Deferred income tax balances are also adjusted because unrealized gains or losses do not affect actual taxes currently paid.

The quality of our AFS fixed maturity securities portfolio, as measured at estimated fair value and by the percentage of fixed maturity securities invested in various ratings categories, relative to the entire fixed maturity AFS security portfolio (in millions) was as follows:

| NAIC Designation(1)   | Rating Agency Equivalent Designation(1) | As of September 30, 2011 |                  |               | As of December 31, 2010 |                  |               |
|---|---|--------------------------|------------------|---------------|-------------------------|------------------|---------------|
|   |   | Amortized Cost           | Fair Value       | % of Total    | Amortized Cost          | Fair Value       | % of Total    |
| <b>Investment Grade Securities</b>  |   |                          |                  |               |                         |                  |               |
| 1   | Aaa / Aa / A                            | \$ 43,186                | \$ 48,117        | 63.9%         | \$ 40,573               | \$ 42,769        | 62.3%         |
| 2   | Baa                                     | 22,398                   | 24,219           | 32.2%         | 21,032                  | 22,286           | 32.5%         |
| <b>Total investment grade securities</b>  |   | <b>65,584</b>            | <b>72,336</b>    | <b>96.1%</b>  | <b>61,605</b>           | <b>65,055</b>    | <b>94.8%</b>  |
| <b>Below Investment Grade Securities</b>  |   |                          |                  |               |                         |                  |               |
| 3   | Ba                                      | 2,482                    | 2,225            | 3.0%          | 2,620                   | 2,403            | 3.5%          |
| 4   | B                                       | 555                      | 456              | 0.6%          | 796                     | 665              | 1.0%          |
| 5   | Caa and lower                           | 297                      | 182              | 0.2%          | 476                     | 325              | 0.5%          |
| 6   | In or near default                      | 136                      | 92               | 0.1%          | 248                     | 166              | 0.2%          |
| <b>Total below investment grade securities</b>  |   | <b>3,470</b>             | <b>2,955</b>     | <b>3.9%</b>   | <b>4,140</b>            | <b>3,559</b>     | <b>5.2%</b>   |
| <b>Total fixed maturity AFS securities</b>  |   | <b>\$ 69,054</b>         | <b>\$ 75,291</b> | <b>100.0%</b> | <b>\$ 65,745</b>        | <b>\$ 68,614</b> | <b>100.0%</b> |
| <b>Total securities below investment grade as a percentage of total fixed maturity AFS securities</b> |   | <b>5.0%</b>              | <b>3.9%</b>      |               | <b>6.3%</b>             | <b>5.2%</b>      |               |

(1) Based upon the rating designations determined and provided by the National Association of Insurance Commissioners ("NAIC") or the major credit rating agencies (Fitch, Moody's and S&P). For securities where the ratings assigned by the major credit agencies are not equivalent, the second highest rating assigned is used. For those securities where ratings by the major credit rating agencies are not available, which does not represent a significant amount of our total fixed maturity AFS securities, we base the ratings disclosed upon internal ratings.

Comparisons between the NAIC ratings and rating agency designations are published by the NAIC. The NAIC assigns securities quality ratings and uniform valuations, which are used by insurers when preparing their annual statements. The NAIC ratings are similar to the rating agency designations of the Nationally Recognized Statistical Rating Organizations for marketable bonds. NAIC ratings 1 and 2 include bonds generally considered investment grade (rated Baa3 or higher by Moody's, or rated BBB- or higher by S&P and Fitch), by such ratings

organizations. However, securities rated NAIC 1 and NAIC 2 could be below investment grade by the rating agencies, which is a result of the changes in the RBC rules for RMBS and CMBS for statutory reporting. NAIC ratings 3 through 6 include bonds generally considered below investment grade (rated Ba1 or lower by Moody's, or rated BB+ or lower by S&P and Fitch).

Greece, Ireland, Italy, Portugal and Spain are experiencing stress in the credit markets. As of September 30, 2011, we had direct sovereign exposure only to Italy, with an amortized cost of \$3 million and a fair value of \$2 million. We also had AFS securities in two large Spanish banks, where our investments were in subsidiaries located outside of Spain, with an amortized cost and a fair value of \$63 million as of September 30, 2011. Other banking exposure to these countries as of September 30, 2011, included a \$14 million notional CDS position where we have sold protection on a highly rated multi-national Spanish bank. As of September 30, 2011, we had no direct exposure to Greece.

Our total non-banking and non-sovereign AFS securities to Ireland, Italy, Portugal and Spain had an amortized cost of \$770 million and a fair value of \$785 million as of September 30, 2011, approximately 50% of which related to large multinational companies domiciled in those countries. The detailed breakout by country was as follows: Ireland – \$215 million amortized cost and \$211 million fair value; Italy – \$203 million amortized cost and \$216 million fair value; Portugal – \$40 million amortized cost and \$29 million fair value; and Spain – \$312 million amortized cost and \$329 million fair value.

As of September 30, 2011, and December 31, 2010, 69.7% and 79.8%, respectively, of the total publicly traded and private securities in an unrealized loss status were rated as investment grade. See Note 5 for maturity date information for our fixed maturity investment portfolio. Our gross unrealized losses on AFS securities as of September 30, 2011, decreased \$264 million. This change was attributable primarily to a decline in overall market yields, which was driven by market uncertainty and weakening economic activity. As more fully described in Note 1 of our 2010 Form 10-K, we regularly review our investment holdings for OTTI. We believe the unrealized loss position as of September 30, 2011, does not represent OTTI as we do not intend to sell these debt securities, it is not more likely than not that we will be required to sell the debt securities before recovery of their amortized cost basis, the estimated future cash flows are equal to or greater than the amortized cost basis of the debt securities, or we have the ability and intent to hold the equity securities for a period of time sufficient for recovery. For further information on our AFS securities unrealized losses, see “Additional Details on our Unrealized Losses on AFS Securities” below.

Selected information for certain AFS securities in a gross unrealized loss position (dollars in millions) was as follows:

|  | As of September 30, 2011 |                                  |  |  |                       |                   |
|--|--------------------------|----------------------------------|--|--|-----------------------|-------------------|
|  | Fair Value               | Gross Unrealized Losses and OTTI | Estimated Years until Call or Maturity | Estimated Average Years until Recovery | Subordination Current | Level Origination |
| CMBS                                       | \$ 376                   | \$ 119                           | 1 to 42                                | 28                                     | 22.7%                 | 15.3%             |
| Hybrid and redeemable preferred securities | 673                      | 170                              | 1 to 55                                | 32                                     | N/A                   | N/A               |

As provided in the table above, many of the securities in these categories are long-dated with some of the preferred securities being perpetual. This is purposeful as it matches the long-term nature of our liabilities associated with our life insurance and annuity products. See “Part II – Item 7A. Quantitative and Qualitative Disclosures About Market Risk” in our 2010 Form 10-K where we present information related to maturities of securities and the expected cash flows for rate sensitive liabilities and maturities of our holding company debt, which also demonstrates the long-term nature of the cash flows associated with these items. Because of this relationship, we do not believe it will be necessary to sell these securities before they recover or mature. For these securities, the estimated range and average period until recovery is the call or maturity period. It is difficult to predict or project when the securities will recover as it is dependent upon a number of factors including the overall economic climate. We do not believe it is necessary to impair these securities as long as the expected future cash flows are projected to be sufficient to recover the amortized cost of these securities.

The actual range and period until recovery could vary significantly depending on a variety of factors, many of which are out of our control. There are several items that could affect the length of the period until recovery, such as the pace of economic recovery, level of delinquencies, performance of the underlying collateral, changes in market interest rates, exposures to various industry or geographic conditions, market behavior and other market conditions.

We concluded that it is not more likely than not that we will be required to sell the fixed maturity AFS securities before recovery of their amortized cost basis, that the estimated future cash flows are equal to or greater than the amortized cost basis of the debt securities, and that we have the ability to hold the equity AFS securities for a period of time sufficient for recovery. This conclusion is consistent with our asset-liability management process. Management considers the following as part of the evaluation:

- The current economic environment and market conditions;
- Our business strategy and current business plans;
- The nature and type of security, including expected maturities and exposure to general credit, liquidity, market and interest rate risk;
- Our analysis of data from financial models and other internal and industry sources to evaluate the current effectiveness of our hedging and overall risk management strategies;
- The current and expected timing of contractual maturities of our assets and liabilities, expectations of prepayments on investments and expectations for surrenders and withdrawals of life insurance policies and annuity contracts;

- The capital risk limits approved by management; and
- Our current financial condition and liquidity demands.

To determine the recoverability of a debt security, we consider the facts and circumstances surrounding the underlying issuer including, but not limited to, the following:

- Historic and implied volatility of the security;
- Length of time and extent to which the fair value has been less than amortized cost;
- Adverse conditions specifically related to the security or to specific conditions in an industry or geographic area;
- Failure, if any, of the issuer of the security to make scheduled payments; and
- Recoveries or additional declines in fair value subsequent to the balance sheet date.

As reported on our Consolidated Balance Sheets, we had \$97.0 billion of investments and cash, which exceeded the liabilities for our future obligations under insurance policies and contracts, net of amounts recoverable from reinsurers, which totaled \$81.9 billion as of September 30, 2011. If it were necessary to liquidate securities prior to maturity or call to meet cash flow needs, we would first look to those securities that are in an unrealized gain position, which had a fair value of \$67.4 billion, excluding consolidated VIEs in the amount of \$700 million, as of September 30, 2011, rather than selling securities in an unrealized loss position. The amount of cash that we have on hand at any point of time takes into account our liquidity needs in the future, other sources of cash, such as the maturities of investments, interest and dividends we earn on our investments and the on-going cash flows from new and existing business.

See “AFS Securities – Evaluation for Recovery of Amortized Cost” in Note 1 in our 2010 Form 10-K and Note 5 for additional discussion.

As of September 30, 2011, and December 31, 2010, the estimated fair value for all private securities was \$9.2 billion and \$8.4 billion, both representing approximately 10% of total invested assets.

For information regarding our VIEs’ fixed maturity securities, see Note 4 in both this report and in our 2010 Form 10-K.

#### MBS (Included in AFS and Trading Securities)

Our fixed maturity securities include MBS. These securities are subject to risks associated with variable prepayments. This may result in differences between the actual cash flow and maturity of these securities than that expected at the time of purchase. Securities that have an amortized cost greater than par and are backed by mortgages that prepay faster than expected will incur a reduction in yield or a loss. Those securities with an amortized cost lower than par that prepay faster than expected will generate an increase in yield or a gain. In addition, we may incur reinvestment risks if market yields are lower than the book yields earned on the securities. Prepayments occurring slower than expected have the opposite effect. We may incur reinvestment risks if market yields are higher than the book yields earned on the securities and we are forced to sell the securities. The degree to which a security is susceptible to either gains or losses is influenced by: the difference between its amortized cost and par; the relative sensitivity of the underlying mortgages backing the assets to prepayment in a changing interest rate environment; and the repayment priority of the securities in the overall securitization structure.

We limit the extent of our risk on MBS by prudently limiting exposure to the asset class, by generally avoiding the purchase of securities with a cost that significantly exceeds par, by purchasing securities backed by stable collateral and by concentrating on securities with enhanced priority in their trust structure. Such securities with reduced risk typically have a lower yield (but higher liquidity) than higher-risk MBS. At selected times, higher-risk securities may

be purchased if they do not compromise the safety of the general portfolio. As of September 30, 2011, we did not have a significant amount of higher-risk, trust structured MBS. A significant amount of assets in our MBS portfolio are either guaranteed by U.S. government-sponsored enterprises or are supported in the securitization structure by junior securities enabling the assets to achieve high investment grade status.

Our exposure to subprime mortgage lending is limited to investments in banks and other financial institutions that may be affected by subprime lending and direct investments in ABS CDOs, ABS and RMBS. Mortgage-related ABS are backed by home equity loans and RMBS are backed by residential mortgages. These securities are backed by loans that are characterized by borrowers of differing levels of creditworthiness: prime; Alt-A; and subprime. Prime lending is the origination of residential mortgage loans to customers with excellent credit profiles. Alt-A lending is the origination of residential mortgage loans to customers who have prime credit profiles but lack documentation to substantiate income. Subprime lending is the origination of loans to customers with weak or impaired credit profiles.

Delinquency and loss rates on residential mortgages and home equity loans have been showing positive trends, and as long as the unemployment rate remains stable to improving, we expect these trends to continue. We continue to expect to receive payments in accordance with contractual terms for a significant amount of our securities, largely due to the seniority of the claims on the

collateral of the securities that we own. The tranches of the securities will experience losses according to their seniority level with the least senior (or most junior), typically the unrated residual tranche, taking the initial loss. The credit ratings of our securities reflect the seniority of the securities that we own. Our RMBS had a market value of \$8.7 billion and an unrealized gain of \$411 million, or 5%, as of September 30, 2011.

The market value of AFS securities and trading securities backed by subprime loans was \$454 million and represented less than 1% of our total investment portfolio as of September 30, 2011. AFS securities represented \$440 million, or 97%, and trading securities represented \$14 million, or 3%, of the subprime exposure as of September 30, 2011. AFS securities and trading securities rated A or above represented 45% of the subprime investments and \$228 million in market value of our subprime investments was backed by loans originating in 2005 and forward. The tables below summarize our investments in AFS securities backed by pools of residential mortgages (in millions):

| Type   | Fair Value as of September 30, 2011 |                  |        |          |           |
|--|-------------------------------------|------------------|--------|----------|-----------|
|  | Prime Agency                        | Prime/Non-Agency | Alt-A  | Subprime | Total     |
| CMOs and MPTS  | \$ 7,096                            | \$ 872           | \$ 480 | \$ -     | \$ 8,448  |
| ABS home equity  | 4                                   | -                | 213    | 440      | 657       |
| Total by type (1)  | \$ 7,100                            | \$ 872           | \$ 693 | \$ 440   | \$ 9,105  |
| Rating   |                                     |                  |        |          |           |
| AAA  | \$ 7,019                            | \$ 87            | \$ 34  | \$ 83    | \$ 7,223  |
| AA   | 65                                  | 50               | 6      | 45       | 166       |
| A  | 16                                  | 48               | 34     | 66       | 164       |
| BBB  | -                                   | 52               | 65     | 23       | 140       |
| BB and below   | -                                   | 635              | 554    | 223      | 1,412     |
| Total by rating (1)(2)   | \$ 7,100                            | \$ 872           | \$ 693 | \$ 440   | \$ 9,105  |
| Origination Year   |                                     |                  |        |          |           |
| 2004 and prior   | \$ 1,813                            | \$ 226           | \$ 235 | \$ 216   | \$ 2,490  |
| 2005   | 866                                 | 126              | 249    | 162      | 1,403     |
| 2006   | 250                                 | 171              | 170    | 61       | 652       |
| 2007   | 1,120                               | 349              | 39     | -        | 1,508     |
| 2008   | 254                                 | -                | -      | -        | 254       |
| 2009   | 1,291                               | -                | -      | 1        | 1,292     |
| 2010   | 1,172                               | -                | -      | -        | 1,172     |
| 2011   | 334                                 | -                | -      | -        | 334       |
| Total by origination year (1)  | \$ 7,100                            | \$ 872           | \$ 693 | \$ 440   | \$ 9,105  |
| Total AFS securities   |                                     |                  |        |          | \$ 75,428 |
| Total AFS RMBS as a percentage of total AFS securities                             |                                     |                  |        |          | 12.1%     |
| Total prime/non-agency, Alt-A and subprime as a percentage of total AFS securities |                                     |                  |        |          | 2.7%      |

(1)



Does not include the fair value of trading securities totaling \$278 million, certain of which support our Modco reinsurance agreements because investment results for these agreements are passed directly to the reinsurers. The \$278 million in trading securities consisted of \$253 million prime, \$11 million Alt-A and \$14 million subprime.

- (2) Based upon the rating designations determined and provided by the major credit rating agencies (Fitch, Moody's and S&P). For securities where the ratings assigned by the major credit agencies are not equivalent, the second highest rating assigned is used. For those securities where ratings by the major credit rating agencies are not available, which does not represent a significant amount of our total fixed maturity AFS securities, we base the ratings disclosed upon internal ratings.

| Type   | Amortized Cost as of September 30, 2011 |                  |        |          |           |
|--|---|------------------|--------|----------|-----------|
|  | Prime Agency                            | Prime/Non-Agency | Alt-A  | Subprime | Total     |
| CMOs and MPTS  | \$ 6,518                                | \$ 947           | \$ 584 | \$ 4     | \$ 8,053  |
| ABS home equity  | 4                                       | -                | 289    | 634      | 927       |
| Total by type (1)  | \$ 6,522                                | \$ 947           | \$ 873 | \$ 638   | \$ 8,980  |
| Rating   |   |                  |        |          |           |
| AAA  | \$ 6,449                                | \$ 85            | \$ 33  | \$ 86    | \$ 6,653  |
| AA   | 59                                      | 50               | 6      | 51       | 166       |
| A  | 14                                      | 51               | 36     | 70       | 171       |
| BBB  | -                                       | 56               | 67     | 24       | 147       |
| BB and below   | -                                       | 705              | 731    | 407      | 1,843     |
| Total by rating (1)(2)   | \$ 6,522                                | \$ 947           | \$ 873 | \$ 638   | \$ 8,980  |
| Origination Year   |   |                  |        |          |           |
| 2004 and prior   | \$ 1,674                                | \$ 235           | \$ 264 | \$ 274   | \$ 2,447  |
| 2005   | 775                                     | 148              | 306    | 233      | 1,462     |
| 2006   | 222                                     | 183              | 246    | 129      | 780       |
| 2007   | 980                                     | 381              | 57     | -        | 1,418     |
| 2008   | 229                                     | -                | -      | -        | 229       |
| 2009   | 1,211                                   | -                | -      | 2        | 1,213     |
| 2010   | 1,112                                   | -                | -      | -        | 1,112     |
| 2011   | 319                                     | -                | -      | -        | 319       |
| Total by origination year (1)  | \$ 6,522                                | \$ 947           | \$ 873 | \$ 638   | \$ 8,980  |
| Total AFS securities   |   |                  |        |          | \$ 69,185 |
| Total AFS RMBS as a percentage of total AFS securities                             |   |                  |        |          | 13.0%     |
| Total prime/non-agency, Alt-A and subprime as a percentage of total AFS securities |   |                  |        |          | 3.6%      |

- (1) Does not include the amortized cost of trading securities totaling \$267 million, certain of which support our Modco reinsurance agreements because investment results for these agreements are passed directly to the reinsurers. The \$267 million in trading securities consisted of \$236 million prime, \$14 million Alt-A and \$17 million subprime.
- (2) Based upon the rating designations determined and provided by the major credit rating agencies (Fitch, Moody's and S&P). For securities where the ratings assigned by the major credit agencies are not equivalent, the second highest rating assigned is used. For those securities where ratings by the major credit rating agencies are not available, which does not represent a significant amount of our total fixed maturity AFS securities, we base the ratings disclosed upon internal ratings.

None of these investments included any direct investments in subprime lenders or mortgages. We are not aware of material exposure to subprime loans in our alternative asset portfolio.



The following summarizes our investments in AFS securities backed by pools of consumer loan ABS (in millions):

| Rating  | As of September 30, 2011 |                |            |                |            |                |
|---|--------------------------|----------------|------------|----------------|------------|----------------|
|   | Credit Card              |                | Auto Loans |                | Total      |                |
|   | Fair Value               | Amortized Cost | Fair Value | Amortized Cost | Fair Value | Amortized Cost |
| AAA   | \$ 814                   | \$ 767         | \$ 57      | \$ 56          | \$ 871     | \$ 823         |
| BBB   | 22                       | 22             | 8          | 8              | 30         | 30             |
| Total by rating (1)(2)                                  | \$ 836                   | \$ 789         | \$ 65      | \$ 64          | \$ 901     | \$ 853         |
| Total AFS securities                                    |                          |                |            |                | \$ 75,428  | \$ 69,185      |
| Total by rating as a percentage of total AFS securities |                          |                |            |                | 1.2%       | 1.2%           |

- (1) Does not include the fair value of trading securities totaling \$5 million, certain of which support our Modco reinsurance agreements because investment results for these agreements are passed directly to the reinsurers. The \$5 million in trading securities consisted of \$3 million of credit card securities and \$2 million of auto loan securities.
- (2) Based upon the rating designations determined and provided by the major credit rating agencies (Fitch, Moody's and S&P). For securities where the ratings assigned by the major credit agencies are not equivalent, the second highest rating assigned is used. For those securities where ratings by the major credit rating agencies are not available, which does not represent a significant amount of our total fixed maturity AFS securities, we base the ratings disclosed upon internal ratings.

The following summarizes our investments in AFS securities backed by pools of commercial mortgages (in millions):

| Type                   | As of September 30, 2011 |                |                 |                |            |                |            |                |
|------------------------|--------------------------|----------------|-----------------|----------------|------------|----------------|------------|----------------|
|                        | Multiple Property        |                | Single Property |                | CRE CDOs   |                | Total      |                |
|                        | Fair Value               | Amortized Cost | Fair Value      | Amortized Cost | Fair Value | Amortized Cost | Fair Value | Amortized Cost |
| CMBS                   | \$ 1,621                 | \$ 1,627       | \$ 49           | \$ 92          | \$ -       | \$ -           | \$ 1,670   | \$ 1,719       |
| CRE CDOs               | -                        | -              | -               | -              | 24         | 38             | 24         | 38             |
| Total by type (1)      | \$ 1,621                 | \$ 1,627       | \$ 49           | \$ 92          | \$ 24      | \$ 38          | \$ 1,694   | \$ 1,757       |
| Rating                 |                          |                |                 |                |            |                |            |                |
| AAA                    | \$ 1,083                 | \$ 1,026       | \$ 14           | \$ 14          | \$ -       | \$ -           | \$ 1,097   | \$ 1,040       |
| AA                     | 236                      | 238            | 10              | 10             | -          | -              | 246        | 248            |
| A                      | 135                      | 138            | 5               | 6              | 1          | 2              | 141        | 146            |
| BBB                    | 103                      | 108            | 5               | 6              | 10         | 11             | 118        | 125            |
| BB and below           | 64                       | 117            | 15              | 56             | 13         | 25             | 92         | 198            |
| Total by rating (1)(2) | \$ 1,621                 | \$ 1,627       | \$ 49           | \$ 92          | \$ 24      | \$ 38          | \$ 1,694   | \$ 1,757       |
| Origination Year       |                          |                |                 |                |            |                |            |                |
| 2004 and prior         | \$ 959                   | \$ 954         | \$ 24           | \$ 24          | \$ 4       | \$ 5           | \$ 987     | \$ 983         |
| 2005                   | 331                      | 318            | 23              | 60             | 10         | 12             | 364        | 390            |

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|                               |          |          |       |       |       |       |          |          |
|-------------------------------|----------|----------|-------|-------|-------|-------|----------|----------|
| 2006                          | 137      | 154      | 2     | 8     | 10    | 21    | 149      | 183      |
| 2007                          | 138      | 147      | -     | -     | -     | -     | 138      | 147      |
| 2010                          | 56       | 54       | -     | -     | -     | -     | 56       | 54       |
| Total by origination year (1) | \$ 1,621 | \$ 1,627 | \$ 49 | \$ 92 | \$ 24 | \$ 38 | \$ 1,694 | \$ 1,757 |

Total AFS securities \$ 75,428 \$ 69,185

Total AFS securities backed

by pools of commercial  
mortgages as a percentage  
of total AFS securities

2.2% 2.5%

- (1) Does not include the fair value of trading securities totaling \$40 million, certain of which support our Modco reinsurance agreements because investment results for these agreements are passed directly to the reinsurers. The \$40 million in trading securities consisted of \$37 million CMBS and \$3 million CRE CDOs.
- (2) Based upon the rating designations determined and provided by the major credit rating agencies (Fitch, Moody's and S&P). For securities where the ratings assigned by the major credit agencies are not equivalent, the second highest rating assigned is used. For those securities where ratings by the major credit rating agencies are not available, which does not represent a significant amount of our total fixed maturity AFS securities, we base the ratings disclosed upon internal ratings.

Monoline insurers provide guarantees on debt for issuers, often in the form of credit wraps, which enhance the credit of the issuer. Monoline insurers guarantee the timely repayment of bond principal and interest when a bond issuer defaults and generally provide credit enhancement for bond issues such as municipal bonds and private placements as well as other types and structures of securities. Our direct exposure represents our bond holdings of the actual Monoline insurers. Our insured bonds represent our holdings in bonds of other issuers that are insured by Monoline insurers.

The following summarizes our exposure to Monoline insurers (in millions):

| Monoline Name   | As of September 30, 2011 |               |                      |                       |                                | Total Fair Value |
|---|--------------------------|---------------|----------------------|-----------------------|--------------------------------|------------------|
|   | Direct Exposure (1)      | Insured Bonds | Total Amortized Cost | Total Unrealized Gain | Total Unrealized Loss and OTTI |                  |
| AMBAC   | \$ -                     | \$ 219        | \$ 219               | \$ 10                 | \$ 39                          | \$ 190           |
| ASSURED GUARANTY LTD  | 30                       | -             | 30                   | -                     | 17                             | 13               |
| FGIC  | -                        | 72            | 72                   | 1                     | 16                             | 57               |
| FSA   | -                        | 30            | 30                   | 1                     | 1                              | 30               |
| MBIA  | 12                       | 125           | 137                  | 21                    | 18                             | 140              |
| XL CAPITAL LTD  | 54                       | 61            | 115                  | 2                     | 4                              | 113              |
| Total by Monoline insurer (2)                                     | \$ 96                    | \$ 507        | \$ 603               | \$ 35                 | \$ 95                          | \$ 543           |
| Total AFS securities  |                          |               | \$ 69,185            | \$ 7,387              | \$ 1,144                       | \$ 75,428        |
| Total by Monoline insurer as a percentage of total AFS securities |                          |               | 0.9%                 | 0.5%                  | 8.3%                           | 0.7%             |

(1) Additional indirect insured exposure through structured securities is excluded from this table.

(2) Does not include the fair value of trading securities totaling \$30 million, certain of which support our Modco reinsurance agreements because investment results for these agreements are passed directly to the reinsurers. The \$30 million in trading securities consisted of \$9 million of direct exposure and \$21 million of insured exposure. This table also excludes insured exposure totaling \$9 million for a guaranteed investment tax credit partnership.

#### Additional Details on our Unrealized Losses on AFS Securities

When considering unrealized gain and loss information, it is important to recognize that the information relates to the status of securities at a particular point in time and may not be indicative of the status of our investment portfolios subsequent to the balance sheet date. Further, because the timing of the recognition of realized investment gains and losses through the selection of which securities are sold is largely at management's discretion, it is important to consider the information provided below within the context of the overall unrealized gain or loss position of our investment portfolios. These are important considerations that should be included in any evaluation of the potential effect of unrealized loss securities on our future earnings.

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We have no concentrations of issuers or guarantors of fixed maturity and equity securities. We conduct enhanced analysis and monitoring for potential changes in unrealized loss status of securities that we believe are most at risk of impairment. The composition by industry categories of these securities was as follows (in millions):

|  | As of September 30, 2011 |        |           |        |               |               |
|--|--------------------------|--------|-----------|--------|---------------|---------------|
|  | Fair                     | %      | Amortized | %      | Unrealized    | Unrealized    |
|  | Value                    | Value  | Cost      | Cost   | Loss and OTTI | Loss and OTTI |
| CMOs   | \$ 423                   | 65.9%  | \$ 513    | 56.0%  | \$ 90         | 32.7%         |
| ABS  | 95                       | 14.8%  | 168       | 18.4%  | 73            | 26.6%         |
| CMBS   | 25                       | 3.9%   | 88        | 9.6%   | 63            | 22.9%         |
| Banking  | 35                       | 5.5%   | 67        | 7.3%   | 32            | 11.6%         |
| Diversified manufacturing  | 51                       | 8.0%   | 63        | 6.9%   | 12            | 4.4%          |
| Property and casualty insurers   | 9                        | 1.4%   | 12        | 1.3%   | 3             | 1.1%          |
| Paper  | 3                        | 0.5%   | 5         | 0.5%   | 2             | 0.7%          |
| Total securities subject to enhanced analysis and monitoring   | \$ 641                   | 100.0% | \$ 916    | 100.0% | \$ 275        | 100.0%        |
| Total AFS securities   | \$ 75,428                |        | \$ 69,185 |        | \$ 1,144      |               |
| Total securities subject to enhanced analysis and monitoring as a percentage of total AFS securities | 0.8%                     |        | 1.3%      |        | 24.0%         |               |

|  | As of December 31, 2010 |        |           |        |               |               |
|--|-------------------------|--------|-----------|--------|---------------|---------------|
|  | Fair                    | %      | Amortized | %      | Unrealized    | Unrealized    |
|  | Value                   | Value  | Cost      | Cost   | Loss and OTTI | Loss and OTTI |
| CMBS   | \$ 11                   | 3.2%   | \$ 83     | 15.6%  | \$ 72         | 37.7%         |
| CMOs   | 150                     | 43.8%  | 184       | 34.5%  | 34            | 17.8%         |
| Banking  | 67                      | 19.6%  | 98        | 18.4%  | 31            | 16.2%         |
| Diversified manufacturing                                    | 38                      | 11.1%  | 63        | 11.8%  | 25            | 13.1%         |
| ABS  | 17                      | 5.0%   | 34        | 6.4%   | 17            | 9.0%          |
| Property and casualty insurers                               | 42                      | 12.3%  | 52        | 9.8%   | 10            | 5.2%          |
| Gaming   | 12                      | 3.5%   | 13        | 2.4%   | 1             | 0.5%          |
| Industrial - other   | 5                       | 1.5%   | 6         | 1.1%   | 1             | 0.5%          |
| Total securities subject to enhanced analysis and monitoring | \$ 342                  | 100.0% | \$ 533    | 100.0% | \$ 191        | 100.0%        |
| Total AFS securities   | \$ 68,811               |        | \$ 65,924 |        | \$ 1,408      |               |
| Total securities subject to                                  |                         |        |           |        |               |               |

|  |      |      |       |
|--|------|------|-------|
| enhanced analysis and<br>monitoring as a percentage<br>of total AFS securities | 0.5% | 0.8% | 13.6% |
|--|------|------|-------|

In addition, as discussed in Note 1 in our 2010 Form 10-K, we perform detailed analysis of our AFS securities, including those presented above as well as other AFS securities. For selected information on these AFS securities in a gross unrealized loss position backed by pools of residential and commercial mortgages as of September 30, 2011, see Note 5.



The composition by industry categories of all securities in unrealized loss status (in millions), was as follows:

|   | As of September 30, 2011 |              |                |                  |                          |                            |
|---|--------------------------|--------------|----------------|------------------|--------------------------|----------------------------|
|   | Fair Value               | % Fair Value | Amortized Cost | % Amortized Cost | Unrealized Loss and OTTI | % Unrealized Loss and OTTI |
| ABS   | \$ 671                   | 9.1%         | \$ 965         | 11.3%            | \$ 294                   | 25.7%                      |
| Banking   | 1,512                    | 20.5%        | 1,775          | 20.9%            | 263                      | 23.0%                      |
| CMOs  | 995                      | 13.5%        | 1,187          | 14.0%            | 192                      | 16.8%                      |
| CMBS  | 375                      | 5.1%         | 494            | 5.8%             | 119                      | 10.4%                      |
| Media - non-cable   | 233                      | 3.2%         | 261            | 3.0%             | 28                       | 2.4%                       |
| Electric  | 247                      | 3.4%         | 275            | 3.2%             | 28                       | 2.4%                       |
| Property and casualty insurers                            | 117                      | 1.6%         | 144            | 1.7%             | 27                       | 2.4%                       |
| Paper   | 150                      | 2.1%         | 175            | 2.1%             | 25                       | 2.2%                       |
| Retailers   | 83                       | 1.1%         | 102            | 1.2%             | 19                       | 1.7%                       |
| Metals and mining   | 363                      | 4.9%         | 376            | 4.4%             | 13                       | 1.1%                       |
| Diversified Manufacturing                                 | 147                      | 2.0%         | 160            | 1.9%             | 13                       | 1.1%                       |
| Gaming  | 121                      | 1.6%         | 133            | 1.6%             | 12                       | 1.0%                       |
| Local authorities   | 36                       | 0.5%         | 47             | 0.6%             | 11                       | 1.0%                       |
| Life  | 182                      | 2.5%         | 192            | 2.2%             | 10                       | 0.9%                       |
| Industries with unrealized losses less than \$10 million  | 2,128                    | 28.9%        | 2,218          | 26.1%            | 90                       | 7.9%                       |
| Total by industry   | \$ 7,360                 | 100.0%       | \$ 8,504       | 100.0%           | \$ 1,144                 | 100.0%                     |
| Total AFS securities                                      | \$ 75,428                |              | \$ 69,185      |                  | \$ 1,144                 |                            |
| Total by industry as a percentage of total AFS securities |                          | 9.8%         |                | 12.3%            |                          | 100.0%                     |

As of December 31, 2010

|   | Fair Value | % Fair Value | Amortized Cost | % Amortized Cost | Unrealized Loss and OTTI | % Unrealized Loss and OTTI |
|---|------------|--------------|----------------|------------------|--------------------------|----------------------------|
| ABS   | \$ 843     | 7.0%         | \$ 1,142       | 8.5%             | \$ 299                   | 21.1%                      |
| CMOs  | 1,164      | 9.7%         | 1,419          | 10.6%            | 255                      | 18.1%                      |
| Banking   | 1,495      | 12.4%        | 1,693          | 12.6%            | 198                      | 14.1%                      |
| CMBS  | 379        | 3.2%         | 565            | 4.2%             | 186                      | 13.2%                      |
| Local authorities   | 1,933      | 16.1%        | 2,028          | 15.1%            | 95                       | 6.7%                       |
| Property and casualty insurers                            | 360        | 3.0%         | 409            | 3.0%             | 49                       | 3.5%                       |
| Electric  | 760        | 6.3%         | 806            | 6.0%             | 46                       | 3.3%                       |
| Diversified manufacturing                                 | 267        | 2.2%         | 301            | 2.2%             | 34                       | 2.4%                       |
| Media - non-cable   | 238        | 2.0%         | 263            | 2.0%             | 25                       | 1.8%                       |
| Life  | 287        | 2.4%         | 304            | 2.3%             | 17                       | 1.2%                       |
| Retailers   | 172        | 1.4%         | 187            | 1.4%             | 15                       | 1.1%                       |
| Gaming  | 153        | 1.3%         | 165            | 1.2%             | 12                       | 0.9%                       |
| Paper   | 130        | 1.1%         | 142            | 1.1%             | 12                       | 0.9%                       |
| Entertainment   | 193        | 1.6%         | 204            | 1.5%             | 11                       | 0.8%                       |
| Industries with unrealized losses less than \$10 million  | 3,641      | 30.3%        | 3,795          | 28.3%            | 154                      | 10.9%                      |
| Total by industry   | \$ 12,015  | 100.0%       | \$ 13,423      | 100.0%           | \$ 1,408                 | 100.0%                     |
| Total AFS securities                                      | \$ 68,811  |              | \$ 65,924      |                  | \$ 1,408                 |                            |
| Total by industry as a percentage of total AFS securities |            | 17.5%        |                | 20.4%            |                          | 100.0%                     |

#### Unrealized Loss on Below Investment Grade AFS Fixed Maturity Securities

Gross unrealized losses on below investment grade AFS fixed maturity securities represented 48.7% and 47.4% of total gross unrealized losses on all AFS securities as of September 30, 2011, and December 31, 2010, respectively. Generally, below investment grade fixed maturity securities are more likely than investment grade fixed maturity securities to develop credit concerns. The remaining 51.3% and 52.6% of the gross unrealized losses as of September 30, 2011, and December 31, 2010, respectively, related to investment grade AFS securities. The ratios of estimated fair value to amortized cost reflected in the table below were not necessarily indicative of the market value to amortized cost relationships for the securities throughout the entire time that the securities have been in an unrealized loss position nor are they necessarily indicative of these ratios subsequent to September 30, 2011.

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Details underlying fixed maturity securities below investment grade and in an unrealized loss position (in millions) were as follows:

| Aging Category  | Ratio of Amortized Cost to Fair Value Above | As of September 30, 2011 |                |                          |
|---|---|--------------------------|----------------|--------------------------|
|   |   | Fair Value               | Amortized Cost | Unrealized Loss and OTTI |
| 90 days or less   | 70%   | \$ 724                   | \$ 780         | \$ 56                    |
|   | 40% to 70%                                  | 90                       | 142            | 52                       |
|   | Below 40%                                   | 7                        | 21             | 14                       |
| Total 90 days or less   |   | 821                      | 943            | 122                      |
| 91 days to 180 days   | Above 70%                                   | 182                      | 199            | 17                       |
|   | 40% to 70%                                  | 1                        | 2              | 1                        |
| Total 91 to 180 days  |   | 183                      | 201            | 18                       |
| 181 days to 270 days  | Above 70%                                   | 11                       | 12             | 1                        |
|   | 40% to 70%                                  | 2                        | 3              | 1                        |
| Total 181 days to 270 days  |   | 13                       | 15             | 2                        |
| 271 days to 1 year  | Above 70%                                   | 94                       | 111            | 17                       |
| Total 271 days to 1 year  |   | 94                       | 111            | 17                       |
| Greater than 1 year   | Above 70%                                   | 825                      | 980            | 155                      |
|   | 40% to 70%                                  | 244                      | 425            | 181                      |
|   | Below 40%                                   | 22                       | 84             | 62                       |
| Total greater than 1 year   |   | 1,091                    | 1,489          | 398                      |
| Total below investment grade and in an unrealized loss position   |   | \$ 2,202                 | \$ 2,759       | \$ 557                   |
| Total AFS securities  |   | \$ 75,428                | \$ 69,185      | \$ 1,144                 |
| Total below investment grade and in an unrealized loss position as a percentage of total AFS securities |   | 2.9%                     | 4.0%           | 48.7%                    |



| Aging Category  | Ratio of<br>Amortized<br>Cost<br>to<br>Fair<br>Value<br>Above<br>70%<br>40% to<br>70%<br>Below<br>40% | As of December 31, 2010 |                   |                     |
|---|---|-------------------------|-------------------|---------------------|
|   |   | Fair<br>Value           | Amortized<br>Cost | Loss<br>and<br>OTTI |
| 90 days or less   |   | \$ 388                  | \$ 422            | \$ 34               |
|   |   | 78                      | 128               | 50                  |
|   |   | 2                       | 11                | 9                   |
| Total 90 days or less   |   | 468                     | 561               | 93                  |
| 91 days to 180 days   |   | 62                      | 77                | 15                  |
|   |   | 26                      | 42                | 16                  |
| Total 91 to 180 days  |   | 88                      | 119               | 31                  |
| 181 days to 270 days  |   | 57                      | 62                | 5                   |
|   |   | 1                       | 3                 | 2                   |
| Total 181 days to 270 days  |   | 58                      | 65                | 7                   |
| 271 days to 1 year  |   | 129                     | 160               | 31                  |
|   |   | 43                      | 72                | 29                  |
| Total 271 days to 1 year  |   | 172                     | 232               | 60                  |
| Greater than 1 year   |   | 1,307                   | 1,496             | 189                 |
|   |   | 258                     | 441               | 183                 |
|   |   | 21                      | 125               | 104                 |
| Total greater than 1 year   |   | 1,586                   | 2,062             | 476                 |
| Total below investment grade and in<br>an unrealized loss position  |   | \$ 2,372                | \$ 3,039          | \$ 667              |
| Total AFS securities  |   | \$ 68,811               | \$ 65,924         | \$ 1,408            |
| Total below investment grade and in an<br>unrealized loss position as a percentage<br>of total AFS securities |   | 3.4%                    | 4.6%              | 47.4%               |

## Mortgage Loans on Real Estate

The following tables summarize key information on mortgage loans on real estate (in millions):

| Credit Quality Indicator            | As of September<br>30, 2011 |        | As of December<br>31, 2010 |        |
|-------------------------------------|-----------------------------|--------|----------------------------|--------|
|                                     | Carrying<br>Value           | %      | Carrying<br>Value          | %      |
| Current                             | \$ 6,828                    | 99.1%  | \$ 6,699                   | 99.2%  |
| Delinquent and in foreclosure (1)   | 65                          | 0.9%   | 53                         | 0.8%   |
| Total mortgage loans on real estate | \$ 6,893                    | 100.0% | \$ 6,752                   | 100.0% |

(1) As of September 30, 2011, and December 31, 2010, there were 12 and 10 mortgage loans that were delinquent and in foreclosure, respectively.

|  | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|--|-----------------------------------|----------------------------------|
| By Segment                             |                                   |                                  |
| Retirement Solutions:                  |                                   |                                  |
| Annuities                              | \$ 1,297                          | \$ 1,172                         |
| Defined Contribution                   | 1,054                             | 920                              |
| Insurance Solutions:                   |                                   |                                  |
| Life Insurance                         | 3,763                             | 3,856                            |
| Group Protection                       | 284                               | 285                              |
| Other Operations                       | 495                               | 519                              |
| Total mortgage loans on<br>real estate | \$ 6,893                          | \$ 6,752                         |

| Property Type      | As of September<br>30, 2011 |        | State Exposure        | As of September<br>30, 2011 |        |
|--------------------|-----------------------------|--------|-----------------------|-----------------------------|--------|
|                    | Carrying<br>Value           | %      |                       | Carrying<br>Value           | %      |
| Office building    | \$ 2,212                    | 32.1%  | CA                    | \$ 1,612                    | 23.4%  |
| Industrial         | 1,796                       | 26.1%  | TX                    | 641                         | 9.2%   |
| Retail             | 1,550                       | 22.5%  | MD                    | 419                         | 6.1%   |
| Apartment          | 952                         | 13.8%  | VA                    | 349                         | 5.1%   |
| Mixed use          | 150                         | 2.2%   | FL                    | 293                         | 4.3%   |
| Hotel/Motel        | 134                         | 1.9%   | NC                    | 289                         | 4.2%   |
| Other commercial   | 99                          | 1.4%   | TN                    | 284                         | 4.1%   |
| Total              | \$ 6,893                    | 100.0% | WA                    | 271                         | 3.9%   |
|                    |                             |        | GA                    | 235                         | 3.4%   |
| Geographic Region  |                             |        | AZ                    | 222                         | 3.2%   |
| Pacific            | \$ 1,973                    | 28.5%  | IL                    | 192                         | 2.8%   |
| South Atlantic     | 1,720                       | 25.0%  | IN                    | 190                         | 2.8%   |
| West South Central | 662                         | 9.6%   | NV                    | 185                         | 2.7%   |
| East North Central | 646                         | 9.4%   | PA                    | 184                         | 2.7%   |
| Mountain           | 562                         | 8.2%   | OH                    | 177                         | 2.6%   |
| Middle Atlantic    | 427                         | 6.2%   | MN                    | 153                         | 2.2%   |
| East South Central | 402                         | 5.8%   | Other states under 2% | 1,197                       | 17.3%  |
| West North Central | 357                         | 5.2%   | Total                 | \$ 6,893                    | 100.0% |
| New England        | 144                         | 2.1%   |                       |                             |        |
| Total              | \$ 6,893                    | 100.0% |                       |                             |        |

| Origination Year | As of September<br>30, 2011 |        | Future Principal<br>Payments | As of September<br>30, 2011 |        |
|------------------|-----------------------------|--------|------------------------------|-----------------------------|--------|
|                  | Principal<br>Amount         | %      |                              | Principal<br>Amount         | %      |
| 2004 and prior   | \$ 2,618                    | 38.0%  | Remainder of 2011            | \$ 92                       | 1.3%   |
| 2005             | 790                         | 11.4%  | 2012                         | 298                         | 4.3%   |
| 2006             | 652                         | 9.4%   | 2013                         | 387                         | 5.6%   |
| 2007             | 921                         | 13.3%  | 2014                         | 410                         | 6.0%   |
| 2008             | 800                         | 11.6%  | 2015                         | 629                         | 9.1%   |
| 2009             | 149                         | 2.2%   | 2016 and thereafter          | 5,084                       | 73.7%  |
| 2010             | 281                         | 4.1%   | Total                        | \$ 6,900                    | 100.0% |
| 2011             | 689                         | 10.0%  |                              |                             |        |
| Total            | \$ 6,900                    | 100.0% |                              |                             |        |

As discussed in “Current Market Conditions” in our 2010 Form 10-K, the global financial markets and credit market conditions experienced a period of extreme volatility and disruption that began in the second half of 2007 and continued and substantially increased throughout 2008 that led to a decrease in the overall liquidity and availability of capital in the mortgage loan market, and in particular a decrease in activity by securitization lenders. These conditions and the overall economic downturn put pressure on the fundamentals of mortgage loans on real estate through rising vacancies, falling rents and falling property values.

See Note 5 for information regarding our loan-to-value and debt-service coverage ratios.

There were 10 and 9 impaired mortgage loans on real estate, or less than 1% of the total dollar amount of mortgage loans on real estate as of September 30, 2011, and December 31, 2010, respectively. The carrying value on the mortgage loans on real estate that were two or more payments delinquent as of September 30, 2011, was \$76 million, or 1% of total mortgage loans on real estate. The total principal and interest past due on the mortgage loans on real estate that were two or more payments delinquent as of September 30, 2011, was \$40 million. The carrying value on the mortgage loans on real estate that were two or more payments delinquent as of December 31, 2010, was \$48 million, or 1% of total mortgage loans on real estate. The total principal and interest past due on the mortgage loans on real estate that were two or more payments delinquent as of December 31, 2010, was \$5 million. See Note 1 in our 2010 Form 10-K for more information regarding our accounting policy relating to the impairment of mortgage loans on real estate.

#### Alternative Investments

The carrying value of our consolidated alternative investments by business segment (in millions), which consisted primarily of investments in limited partnerships, was as follows:

|                       | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|-----------------------|-----------------------------------|----------------------------------|
| Retirement Solutions: |                                   |                                  |
| Annuities             | \$ 118                            | \$ 95                            |
| Defined Contribution  | 73                                | 71                               |
| Insurance Solutions:  |                                   |                                  |



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|                               |        |        |
|-------------------------------|--------|--------|
| Life Insurance                | 594    | 546    |
| Group Protection              | 35     | 30     |
| Other Operations              | (3)    | 8      |
| Total alternative investments | \$ 817 | \$ 750 |

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Income (loss) derived from our consolidated alternative investments by business segment (in millions) was as follows:

|                                   | For the Three<br>Months<br>Ended<br>September 30, |       |        | For the Nine<br>Months<br>Ended<br>September 30, |       |        |
|-----------------------------------|---|-------|--------|--|-------|--------|
|                                   | 2011  | 2010  | Change | 2011   | 2010  | Change |
| Retirement Solutions:             |   |       |        |  |       |        |
| Annuities                         | \$ 1  | \$ 2  | -50%   | \$ 11  | \$ 8  | 38%    |
| Defined Contribution              | 1   | 2     | -50%   | 6  | 6     | 0%     |
| Insurance Solutions:              |   |       |        |  |       |        |
| Life Insurance                    | 15  | 10    | 50%    | 72   | 42    | 71%    |
| Group Protection                  | -   | 1     | -100%  | 3  | 3     | 0%     |
| Total alternative investments (1) | \$ 17   | \$ 15 | 13%    | \$ 92  | \$ 59 | 56%    |

(1) Includes net investment income on the alternative investments supporting the required statutory surplus of our insurance businesses.

The increase in our investment income on alternative investments presented in the table above when comparing the first nine months of 2011 to the same period in 2010 was due primarily to the improvement in the market specifically benefiting our energy limited partnership holdings.

As of September 30, 2011, and December 31, 2010, alternative investments included investments in approximately 97 and 95 different partnerships, respectively, and the portfolio represented less than 1% of our overall invested assets. The partnerships do not represent off-balance sheet financing and generally involve several third-party partners. Some of our partnerships contain capital calls, which require us to contribute capital upon notification by the general partner. These capital calls are contemplated during the initial investment decision and are planned for well in advance of the call date. The capital calls are not material in size and are not material to our liquidity. Alternative investments are accounted for using the equity method of accounting and are included in other investments on our Consolidated Balance Sheets.

As discussed in “Critical Accounting Policies and Estimates – Investments – Valuation of Alternative Investments” in our 2010 Form 10-K, we update the carrying value of our alternative investment portfolio whenever audited financial statements of the investees for the preceding year become available. Net investment income (loss) derived from our consolidated alternative investments by segment (in millions) related to the effect of preceding year audit adjustments recorded during the indicated year at the investee was as follows:

|                       | For the Three<br>Months<br>Ended<br>September<br>30, |      |        | For the Nine<br>Months Ended<br>September 30, |      |        |
|-----------------------|--|------|--------|---|------|--------|
|                       | 2011   | 2010 | Change | 2011  | 2010 | Change |
| Retirement Solutions: |  |      |        |   |      |        |
| Annuities             | \$ -   | \$ - | NM     | \$ 4  | \$ 3 | 33%    |
| Defined Contribution  | -  | -    | NM     | 2   | 1    | 100%   |
| Insurance Solutions:  |  |      |        |   |      |        |
| Life Insurance        | (1)  | -    | NM     | 29  | 14   | 107%   |
| Group Protection      | -  | -    | NM     | 2   | 1    | 100%   |

Total \$ (1) \$ - NM \$ 37 \$ 19 95%

Income (loss), after-tax, derived from our consolidated alternative investments by class (in millions) related to the effect of preceding year audit adjustments recorded during the indicated year at the investee was as follows:

|  | For the Three<br>Months<br>Ended<br>September<br>30, |      |        | For the Nine<br>Months Ended<br>September 30, |       |        |
|--|--|------|--------|---|-------|--------|
|  | 2011   | 2010 | Change | 2011  | 2010  | Change |
| Venture capital  | \$   | \$ - | NM     | \$ 20   | \$ 14 | 43%    |
| Real estate  | (1)  | -    | NM     | (2)   | (2)   | 0%     |
| Oil and gas  | -  | -    | NM     | 19  | 7     | 171%   |
| Associated amortization of DAC,<br>VOBA, DSI, and DFEL | 1  | -    | NM     | (12)  | (6)   | -100%  |
| Federal income tax expense (benefit)                   | -  | -    | NM     | (9)   | (5)   | -80%   |
| Total  | \$ -   | \$ - | NM     | \$ 16   | \$ 8  | 100%   |

#### Non-Income Producing Investments

As of September 30, 2011, and December 31, 2010, the carrying amount of fixed maturity securities, mortgage loans on real estate and real estate that were non-income producing was \$13 million and \$17 million, respectively.

#### Net Investment Income

Details underlying net investment income (in millions) and our investment yield were as follows:

|  | For the Three<br>Months Ended<br>September 30, |          |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|--|--|----------|--------|---|----------|--------|
|  | 2011   | 2010     | Change | 2011  | 2010     | Change |
| Net Investment Income  |  |          |        |   |          |        |
| Fixed maturity AFS securities  | \$ 964   | \$ 935   | 3%     | \$ 2,878                                      | \$ 2,750 | 5%     |
| VIEs' fixed maturity AFS securities                                    | 4  | 4        | 0%     | 10  | 11       | -9%    |
| Equity AFS securities  | 1  | 1        | 0%     | 4   | 4        | 0%     |
| Trading securities   | 38   | 39       | -3%    | 116   | 118      | -2%    |
| Mortgage loans on real estate  | 102  | 105      | -3%    | 306   | 321      | -5%    |
| Real estate  | 5  | 6        | -17%   | 17  | 17       | 0%     |
| Standby real estate equity commitments                                 | -  | -        | NM     | 1   | 1        | 0%     |
| Policy loans   | 42   | 41       | 2%     | 125   | 127      | -2%    |
| Invested cash  | 1  | 2        | -50%   | 3   | 6        | -50%   |
| Commercial mortgage loan prepayment<br>and bond makewhole premiums (1) | 14   | 12       | 17%    | 73  | 29       | 152%   |
| Alternative investments (2)  | 17   | 15       | 13%    | 92  | 59       | 56%    |
| Consent fees   | -  | 3        | -100%  | 2   | 4        | -50%   |
| Other investments  | (7)  | (1)      | NM     | (19)  | 2        | NM     |
| Investment income  | 1,181  | 1,162    | 2%     | 3,608   | 3,449    | 5%     |
| Investment expense   | (30)   | (30)     | 0%     | (86)  | (91)     | 5%     |
| Net investment income  | \$ 1,151                                       | \$ 1,132 | 2%     | \$ 3,522                                      | \$ 3,358 | 5%     |

- (1) See “Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums” below for additional information.
- (2) See “Alternative Investments” above for additional information.

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |       |                          | For the Nine<br>Months Ended<br>September 30,<br>2010 |       |                          |
|--|--|-------|--------------------------|---|-------|--------------------------|
|  |  |       | Basis<br>Point<br>Change |   |       | Basis<br>Point<br>Change |
| Interest Rate Yield  |  |       |                          |   |       |                          |
| Fixed maturity securities, mortgage<br>loans on real estate and other,<br>net of investment expenses | 5.45%  | 5.61% | (16)                     | 5.52%   | 5.66% | (14)                     |
| Commercial mortgage loan<br>prepayment and bond<br>makewhole premiums                                | 0.07%  | 0.06% | 1                        | 0.12%   | 0.05% | 7                        |
| Alternative investments  | 0.08%  | 0.08% | -                        | 0.15%   | 0.10% | 5                        |
| Consent fees   | 0.00%  | 0.02% | (2)                      | 0.00%   | 0.01% | (1)                      |
| Net investment income yield<br>on invested assets  | 5.60%  | 5.77% | (17)                     | 5.79%   | 5.82% | (3)                      |

|   | For the Three<br>Months Ended<br>September 30,<br>2011 |           |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |           |        |
|---|--|-----------|--------|---|-----------|--------|
|   |  |           | Change |   |           | Change |
| Average invested assets at amortized cost | \$ 82,254  | \$ 78,517 | 5%     | \$ 81,117   | \$ 76,985 | 5%     |

We earn investment income on our general account assets supporting fixed annuity, term life, whole life, UL, interest-sensitive whole life and fixed portion of defined contribution and VUL products. The profitability of our fixed annuity and life insurance products is affected by our ability to achieve target spreads, or margins, between the interest income earned on the general account assets and the interest credited to the contract holder on our average fixed account values, including the fixed portion of variable. Net investment income and the interest rate yield table each include commercial mortgage loan prepayments and bond makewhole premiums, alternative investments and contingent interest and standby real estate equity commitments. These items can vary significantly from period to period due to a number of factors and therefore can provide results that are not indicative of the underlying trends.

The increase in net investment income when comparing nine months ended September 30, 2011, to the same period of 2010 was attributable to higher prepayment and bond makewhole premiums, more favorable investment income on alternative investments (see "Alternative Investments" above and "Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums" below for more information) and higher invested assets driven primarily by favorable net flows on fixed account values, including the fixed portion of variable and to a lesser extent issuances of common stock and debt, partially offset by new money rates averaging below our portfolio yields.

#### Standby Real Estate Equity Commitments

Historically, we have entered into standby commitments, which obligated us to purchase real estate at a specified cost if a third-party sale does not occur within approximately one year after construction is completed. These commitments were used by a developer to obtain a construction loan from an outside lender on favorable terms. In return for issuing the commitment, we received an annual fee and a percentage of the profit when the property is sold. During 2009, we suspended the practice of entering into new standby real estate commitments.

As of September 30, 2011, we did not have any standby real estate equity commitments. During the first nine months of 2011, we funded commitments of \$19 million and recorded a gain of \$6 million due to our funding being less than our estimated allowance for loss related to these commitments.

### Commercial Mortgage Loan Prepayment and Bond Makewhole Premiums

Prepayment and makewhole premiums are collected when borrowers elect to call or prepay their debt prior to the stated maturity. A prepayment or makewhole premium allows investors to attain the same yield as if the borrower made all scheduled interest payments until maturity. These premiums are designed to make investors indifferent to prepayment.

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The increase in prepayment and makewhole premiums when comparing 2011 to 2010 was attributable primarily to a decline in interest rates coupled with improvements in the capital markets and real estate financing environment, which resulted in more refinancing activity and more prepayment income.

#### Realized Gain (Loss) Related to Certain Investments

The detail of the realized gain (loss) related to certain investments (in millions) was as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |         |       | For the Nine<br>Months Ended<br>September 30,<br>2010 |         |      | Change |
|--|--|---------|-------|---|---------|------|--------|
| Fixed maturity AFS securities:   |  |         |       |   |         |      |        |
| Gross gains  | \$ 17  | \$ 12   | 42%   | \$ 84   | \$ 96   | -13% |        |
| Gross losses   | (63)   | (61)    | -3%   | (177)   | (174)   | -2%  |        |
| Equity AFS securities:   |  |         |       |   |         |      |        |
| Gross gains  | -  | 3       | -100% | 10  | 9       | 11%  |        |
| Gross losses   | -  | -       | NM    | -   | (4)     | 100% |        |
| Gain (loss) on other investments   | (3)  | (2)     | -50%  | 1   | (33)    | 103% |        |
| Associated amortization of DAC, VOBA,<br>DSI, and DFEL and changes in other<br>contract holder funds | 5  | 22      | -77%  | (13)  | 20      | NM   |        |
| Total realized gain (loss) related to<br>certain investments   | \$ (44)  | \$ (26) | -69%  | \$ (95)   | \$ (86) | -10% |        |

Amortization of DAC, VOBA, DSI, DFEL and changes in other contract holder funds reflect an assumption for an expected level of credit-related investment losses. When actual credit-related investment losses are realized, we recognize a true-up to our DAC, VOBA, DSI and DFEL amortization and changes in other contract holder funds within realized loss reflecting the incremental effect of actual versus expected credit-related investment losses. These actual to expected amortization adjustments could create volatility in net realized gains and losses. The write-down for impairments includes both credit-related and interest-rate related impairments.

Realized gains and losses generally originate from asset sales to reposition the portfolio or to respond to product experience. During the first nine months of 2011 and 2010, we sold securities for gains and losses. In the process of evaluating whether a security with an unrealized loss reflects declines that are other-than-temporary, we consider our ability and intent to sell the security prior to a recovery of value. However, subsequent decisions on securities sales are made within the context of overall risk monitoring, assessing value relative to other comparable securities and overall portfolio maintenance. Although our portfolio managers may, at a given point in time, believe that the preferred course of action is to hold securities with unrealized losses that are considered temporary until such losses are recovered, the dynamic nature of portfolio management may result in a subsequent decision to sell. These subsequent decisions are consistent with the classification of our investment portfolio as AFS. We expect to continue to manage all non-trading invested assets within our portfolios in a manner that is consistent with the AFS classification.

We consider economic factors and circumstances within countries and industries where recent write-downs have occurred in our assessment of the status of securities we own of similarly situated issuers. While it is possible for realized or unrealized losses on a particular investment to affect other investments, our risk management has been designed to identify correlation risks and other risks inherent in managing an investment portfolio. Once identified, strategies and procedures are developed to effectively monitor and manage these risks. The areas of risk correlation



that we pay particular attention to are risks that may be correlated within specific financial and business markets, risks within specific industries and risks associated with related parties.

When the detailed analysis by our credit analysts and investment portfolio managers leads us to the conclusion that a security's decline in fair value is other-than-temporary, the security is written down to estimated recovery value. In instances where declines are considered temporary, the security will continue to be carefully monitored. See "Critical Accounting Policies and Estimates" in our 2010 Form 10-K for additional information on our portfolio management strategy.

Details underlying write-downs taken as a result of OTTI (in millions) were as follows:

|  | For the Three<br>Months Ended<br>September 30,<br>2011 |         |        | For the Nine<br>Months Ended<br>September 30,<br>2010 |          |        |
|--|--|---------|--------|---|----------|--------|
|  | 2011   | 2010    | Change | 2011  | 2010     | Change |
| Fixed Maturity Securities                          |  |         |        |   |          |        |
| Corporate bonds                                    | \$ (3)   | \$ (34) | 91%    | \$ (9)  | \$ (80)  | 89%    |
| MBS:   |  |         |        |   |          |        |
| CMOs   | (22)   | (16)    | -38%   | (65)  | (52)     | -25%   |
| CMBS   | (8)  | (4)     | -100%  | (47)  | (4)      | NM     |
| ABS CDOs   | -  | -       | NM     | (1)   | (1)      | 0%     |
| Hybrid and redeemable preferred securities         | -  | -       | NM     | (2)   | (5)      | 60%    |
| Total fixed maturity securities                    | (33)   | (54)    | 39%    | (124)   | (142)    | 13%    |
| Equity Securities                                  |  |         |        |   |          |        |
| Other financial services securities                | -  | -       | NM     | -   | (3)      | 100%   |
| Total equity securities                            | -  | -       | NM     | -   | (3)      | 100%   |
| Gross OTTI recognized in net income (loss)         | (33)   | (54)    | 39%    | (124)   | (145)    | 14%    |
| Associated amortization of DAC, VOBA, DSI and DFEL | 8  | 8       | 0%     | 30  | 35       | -14%   |
| Net OTTI recognized in net income (loss), pre-tax  | \$ (25)  | \$ (46) | 46%    | \$ (94)   | \$ (110) | 15%    |
| Portion of OTTI Recognized in OCI                  |  |         |        |   |          |        |
| Gross OTTI recognized in OCI                       | \$ 21  | \$ 62   | -66%   | \$ 48   | \$ 84    | -43%   |
| Change in DAC, VOBA, DSI and DFEL                  | (4)  | (9)     | 56%    | (9)   | (7)      | -29%   |
| Net portion of OTTI recognized in OCI, pre-tax     | \$ 17  | \$ 53   | -68%   | \$ 39   | \$ 77    | -49%   |

The decrease in write-downs for OTTI when comparing the first nine months of 2011 to the same period in 2010 was primarily due to an improvement in the credit markets, partially offset by an increase in write-downs for OTTI on our AFS MBS attributable primarily to continued weakness within the commercial and residential real estate market that affected select RMBS and CMBS holdings.

The \$172 million of impairments taken during the first nine months of 2011 were split between \$124 million of credit related impairments and \$48 million of non-credit related impairments. The credit related impairments were largely attributable to our RMBS and CMBS holdings primarily as a result of continued weakness within the commercial and residential real estate market that affected select RMBS and CMBS holdings. The non-credit related impairments were incurred due to declines in values of securities for which we do not have an intent to sell or it is not more likely than not that we will be required to sell the securities before recovery.

## REVIEW OF CONSOLIDATED FINANCIAL CONDITION

### Liquidity and Capital Resources

#### Sources of Liquidity and Cash Flow

Liquidity refers to the ability of an enterprise to generate adequate amounts of cash from its normal operations to meet cash requirements with a prudent margin of safety. Our principal sources of cash flow from operating activities are insurance premiums and fees and investment income, while sources of cash flows from investing activities result from maturities and sales of invested assets. Our operating activities provided cash of \$934 million and \$1.1 billion for the first nine months of 2011 and 2010, respectively. When considering our liquidity and cash flow, it is important to distinguish between the needs of our insurance

subsidiaries and the needs of the holding company, LNC. As a holding company with no operations of its own, LNC derives its cash primarily from its operating subsidiaries.

The sources of liquidity of the holding company are principally comprised of dividends and interest payments from subsidiaries, augmented by holding company short-term investments, bank lines of credit and the ongoing availability of long-term public financing under an SEC-filed shelf registration statement. These sources of liquidity and cash flow support the general corporate needs of the holding company, including its common and preferred stock dividends, interest and debt service, funding of callable securities, securities repurchases, acquisitions and investment in core businesses. Our cash flows associated with collateral received from and posted with counterparties change as the market value of the underlying derivative contract changes. As the value of a derivative asset declines (or increases), the collateral required to be posted by our counterparties would also decline (or increase). Likewise, when the value of a derivative liability declines (or increases), the collateral we are required to post for our counterparties' benefit would also decline (or increase). During the first nine months of 2011, our payables for collateral on derivative investments increased by \$1.8 billion as declines in the equity and credit markets and interest rates increased the fair values of the associated derivative investments. For additional information, see "Credit Risk" in Note 6.

Details underlying the primary sources of our holding company cash flows (in millions) were as follows:

|   | For the Three<br>Months Ended<br>September 30, |       |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|---|--|-------|--------|---|--------|--------|
|   | 2011   | 2010  | Change | 2011  | 2010   | Change |
| Dividends from Subsidiaries   |  |       |        |   |        |        |
| The Lincoln National Life Insurance<br>Company ("LNL")  | \$ 250   | \$ -  | NM     | \$ 550  | \$ 275 | 100%   |
| Delaware Investments (1)  | -  | -     | NM     | -   | 390    | -100%  |
| Other   | 7  | 1     | NM     | 19  | 23     | -17%   |
| Loan Repayments and Interest from<br>Subsidiaries   |  |       |        |   |        |        |
| Interest on inter-company notes   | 31   | 27    | 15%    | 93  | 71     | 31%    |
|   | \$ 288   | \$ 28 | NM     | \$ 662  | \$ 759 | -13%   |
| Other Cash Flow and Liquidity Items   |  |       |        |   |        |        |
| Net proceeds on common stock issuance   | \$ -   | \$ -  | NM     | \$ -  | \$ 368 | -100%  |
| Lincoln UK sale proceeds  | -  | -     | NM     | -   | 18     | -100%  |
| Increase (decrease) in commercial paper,<br>net   | -  | -     | NM     | (100)   | -      | NM     |
| Net capital received from (paid for taxes<br>on) stock option exercises and restricted<br>stock | -  | -     | NM     | (1)   | -      | NM     |
|   | \$ -   | \$ -  | NM     | \$ (101)                                      | \$ 386 | NM     |

(1) For 2010, amount includes proceeds on the sale of Delaware. For more information, see Note 3.

The table above focuses on significant and recurring cash flow items and excludes the effects of certain financing activities, namely the periodic issuance and retirement of debt and cash flows related to our inter-company cash management program (discussed below). Taxes have been eliminated from the analysis due to a tax sharing agreement among our primary subsidiaries resulting in a modest effect on net cash flows at the holding company. Also excluded from this analysis is the modest amount of investment income on short-term investments of

the holding company.

#### Subsidiaries' Statutory Reserving and Surplus

For discussion of our strategies to lessen the burden of increased AG38 and XXX statutory reserves associated with certain UL products and other products with secondary guarantees on our insurance subsidiaries, see “Results of Insurance Solutions – Life Insurance – Income (Loss) from Operations – Strategies to Address Statutory Reserve Strain.”

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## Financing Activities

Although our subsidiaries currently generate adequate cash flow to meet the needs of our normal operations, periodically we may issue debt or equity securities to maintain ratings and increase liquidity, as well as to fund internal growth, acquisitions and the retirement of our debt and equity securities.

We currently have an effective shelf registration statement, which allows us to issue, in unlimited amounts, securities, including debt securities, preferred stock, common stock, warrants, stock purchase contracts, stock purchase units, depository shares and trust preferred securities of our affiliated trusts.

Details underlying debt and financing activities (in millions) were as follows:

|   | For the Nine Months Ended September 30, 2011 |          |                                 |                                      |                         |                   |
|---|--|----------|---------------------------------|--------------------------------------|-------------------------|-------------------|
|   | Beginning<br>Balance                         | Issuance | Maturities<br>and<br>Repayments | Change<br>in Fair<br>Value<br>Hedges | Other<br>Changes<br>(1) | Ending<br>Balance |
| <b>Short-Term Debt</b>                                      |  |          |                                 |                                      |                         |                   |
| Commercial paper (2)  | \$ 100                                       | \$ -     | \$ -                            | \$ -                                 | \$ (100)                | \$ -              |
| Current maturities of long-term debt (3)                    | 250  | -        | -                               | -                                    | 300                     | 550               |
| Other short-term debt (4)                                   | 1  | -        | (1)                             | -                                    | -                       | -                 |
| Total short-term debt                                       | \$ 351                                       | \$ -     | \$ (1)                          | \$ -                                 | \$ 200                  | \$ 550            |
| <b>Long-Term Debt</b>                                       |  |          |                                 |                                      |                         |                   |
| Senior notes  | \$ 3,464                                     | \$ 300   | \$ -                            | \$ 222                               | \$ (299)                | \$ 3,687          |
| Bank borrowing  | 200  | -        | -                               | -                                    | -                       | 200               |
| Federal Home Loan Bank of<br>Indianapolis ("FHLBI") advance | 250  | -        | -                               | -                                    | -                       | 250               |
| Capital securities  | 1,485  | -        | (275)                           | -                                    | 1                       | 1,211             |
| Total long-term debt  | \$ 5,399                                     | \$ 300   | \$ (275)                        | \$ 222                               | \$ (298)                | \$ 5,348          |

- (1) Includes the net increase (decrease) in commercial paper, non-cash reclassification of long-term debt to current maturities of long-term debt, accretion of discounts and (amortization) of premiums, as applicable.
- (2) During the nine months ended September 30, 2011, we had an average of \$47 million outstanding, a maximum amount outstanding of \$103 million at any time and a weighted average interest rate of 0.27%.
- (3) Consisted of a \$250 million 6.20% fixed rate senior note and a \$300 million 5.65% fixed rate senior note that both mature in less than one year.
- (4) Consisted of advances from the FHLBI with a maturity of less than one year when made. We repaid these advances effective September 8, 2011.

On June 24, 2011, we completed the issuance and sale of \$300 million aggregate principal amount of our 4.85% senior notes due 2021. We used the net proceeds from this offering primarily to redeem \$275 million aggregate principal amount of our 6.75% capital securities due 2066 on July 7, 2011, and recorded a loss of \$5 million, after-tax, on the early extinguishment of debt.

Within the next two years, we have a \$250 million 6.20% fixed rate senior note maturing on December 15, 2011, a \$300 million 5.65% fixed rate senior note maturing on August 27, 2012, and a \$200 million floating rate senior note maturing on July 18, 2013. The specific resources or combination of resources that we will use to meet these

maturities will depend upon, among other things, the financial market conditions present at the time of maturity. As of September 30, 2011, the holding company had approximately \$800 million in cash and cash equivalents and \$25 million invested in fixed maturity corporate bonds; however, as discussed below, it had a \$51 million payable under the inter-company cash management program.

We have not accounted for repurchase agreements, securities lending transactions, or other transactions involving the transfer of financial assets with an obligation to repurchase the transferred assets as sales and do have any other transactions involving the transfer of financial assets with an obligation to repurchase the transferred assets. For information about our collateralized financing transactions on our investments, see "Payables for Collateral on Investments" in Note 5.

Details underlying our credit facilities with a group of domestic and foreign banks (in millions) were as follows:

|                                     | Expiration Date | As of September 30, 2011 |                        |             |
|-------------------------------------|-----------------|--------------------------|------------------------|-------------|
|                                     |                 | Maximum Available        | Borrowings Outstanding | LOCs Issued |
| Credit Facilities                   |                 |                          |                        |             |
| Credit facility with the FHLBI (1)  | N/A             | \$ 850                   | \$ 850                 | N/A         |
| Four-year revolving credit facility | Jun-2015        | 2,000                    | -                      | 210         |
| LOC facility                        | Mar-2023        | 828                      | -                      | 828         |
| LOC facility                        | Aug-2031        | 428                      | -                      | 428         |
| Total                               |                 | \$ 4,106                 | \$ 850                 | \$ 1,466    |

- (1) We are allowed to borrow up to 20 times the amount of our common stock investment in the FHLBI. All borrowings from the FHLBI are required to be secured by certain investments owned by LNL. Our borrowing capacity under this credit facility does not have an expiration date and continues while our investment in the FHLBI common stock remains outstanding as long as LNL maintains a satisfactory level of creditworthiness and does not incur a material adverse change in its financial, business, regulatory or other areas that would materially affect its operations and viability. As of September 30, 2011, we had a \$250 million floating-rate term loan outstanding under the facility (classified within long-term debt on our Consolidated Balance Sheets) due June 20, 2017, which may be prepaid on four specified reset dates. We also borrowed \$100 million under the facility at a rate of 0.28% that is due May 16, 2012, and \$500 million under the facility at a rate of 0.27% that is due November 28, 2011 (both of which are classified within payables for collateral on investments on our Consolidated Balance Sheets).

Effective as of June 10, 2011, we entered into a credit agreement with a syndicate of banks. This agreement (the “credit facility”) allows for any combination of issuance of LOCs and borrowing of up to \$2.0 billion; however, only \$1.0 billion of the borrowing is available to reimburse the banks for drawn LOCs. The credit facility is unsecured and has a commitment termination date of June 10, 2015. LOCs issued under the credit facility may remain outstanding for one year following the applicable commitment termination date of the agreement. The LOCs support inter-company reinsurance transactions and specific treaties associated with our business sold through reinsurance. LOCs are used primarily to satisfy the U.S. regulatory requirements of our domestic insurance companies for which reserve credit is provided by our affiliated reinsurance companies, as discussed above in “Results of Insurance Solutions – Life Insurance – Income (Loss) from Operations – Strategies to Address Statutory Reserve Strain,” and our domestic clients of the business sold through reinsurance.

The credit facility contains customary terms and conditions, including covenants restricting our ability to incur liens, merge or consolidate with another entity where we are not the surviving entity and dispose of all or substantially all of our assets. The credit facility also includes financial covenants including: maintenance of a minimum consolidated net worth (as defined in the facility) equal to the sum of \$9.2 billion plus fifty percent (50%) of the aggregate net proceeds of equity issuances received by us in accordance with the terms of the credit facility; and a debt-to-capital ratio as defined in accordance with the credit facility not to exceed 0.35 to 1.00. Further, the credit facility contains customary events of default, subject to certain materiality thresholds and grace periods for certain of those events of default. The events of default include payment defaults, covenant defaults, material inaccuracies in representations and warranties, certain cross-defaults, bankruptcy and liquidation proceedings and other customary defaults. Upon an event of default, the credit facility provides that, among other things, the commitments may be terminated and the loans then outstanding may be declared due and payable. As of September 30, 2011, we were in compliance with all such covenants.



This credit facility replaced our existing four-year credit facility dated as of June 9, 2010, and set to expire June 9, 2014, and the commitments under the existing credit facility have been terminated. Our 364-day credit facility expired June 8, 2011, prior to entering into the new credit agreement.

On August 26, 2011, one of our wholly-owned subsidiaries entered into a credit facility agreement with a third-party lender. Under the agreement, the lender issued an irrevocable LOC effective August 26, 2011, with a maximum scheduled LOC amount of up to approximately \$520 million. The LOC supports an inter-company reinsurance agreement and expires August 26, 2031. The credit facility agreement contains customary terms and conditions, including covenants restricting the ability of the subsidiary to incur liens, merge or consolidate with another entity and dispose of all or substantially all of its assets. Further, the credit facility agreement contains customary events of default, subject to certain materiality thresholds and grace periods for certain of those events of default. The events of default include payment defaults, covenant defaults, material inaccuracies in representations and warranties, bankruptcy and liquidation proceedings and other customary defaults. Upon an event of default, the credit facility agreement provides that, among other things, obligations to issue, amend or increase the amount of any LOC shall be terminated

and any obligations shall become immediately due and payable. As of September 30, 2011, we were in compliance with all such covenants.

On April 28, 2011, certain of our wholly-owned subsidiaries amended and restated the reimbursement agreement (the “reimbursement agreement”) entered into on December 31, 2009, with a third-party lender. Under the amended agreement, the lender issued an irrevocable LOC effective April 1, 2011, with a maximum scheduled LOC amount of up to approximately \$925 million. The LOC supports an inter-company reinsurance agreement and expires March 31, 2023. The reimbursement agreement contains customary terms and conditions, including covenants restricting the ability of those subsidiaries to incur liens, merge or consolidate with another entity and dispose of all or substantially all of their assets. Further, the reimbursement agreement contains customary events of default, subject to certain materiality thresholds and grace periods for certain of those events of default. The events of default include payment defaults, covenant defaults, material inaccuracies in representations and warranties, bankruptcy and liquidation proceedings and other customary defaults. Upon an event of default, the reimbursement agreement provides that, among other things, obligations to issue, amend or increase the amount of any LOC shall be terminated and any obligations shall become immediately due and payable. As of September 30, 2011, we were in compliance with all such covenants.

See “Part II – Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Review of Consolidated Financial Condition – Liquidity and Capital Resources – Financing Activities” in our 2010 Form 10-K for additional information on our credit facilities.

If current debt ratings and claims-paying ratings were downgraded in the future, terms in our derivative agreements may be triggered, which could negatively affect overall liquidity. For the majority of our counterparties, there is a termination event should the long-term senior debt ratings of LNC drop below BBB-/Baa3 (S&P/Moody’s). Our long-term senior debt held a rating of A-/Baa2 (S&P/Moody’s) as of September 30, 2011. In addition, contractual selling agreements with intermediaries could be negatively affected, which could have an adverse effect on overall sales of annuities, life insurance and investment products. See “Part I – Item 1A. Risk Factors – A decrease in the capital and surplus of our insurance subsidiaries may result in a downgrade to our credit and insurer financial strength ratings” and “Part I – Item 1A. Risk Factors – A downgrade in our financial strength or credit ratings could limit our ability to market products, increase the number or value of policies being surrendered and/or hurt our relationships with creditors” in our 2010 Form 10-K for more information. See “Part I – Item 1. Business – Ratings” in our 2010 Form 10-K for additional information on our current bond ratings.

#### Alternative Sources of Liquidity

In order to manage our capital more efficiently, we have an inter-company cash management program where certain subsidiaries can lend to or borrow from the holding company to meet short-term borrowing needs. The cash management program is essentially a series of demand loans, which are permitted under applicable insurance laws, among LNC and its affiliates that reduces overall borrowing costs by allowing LNC and its subsidiaries to access internal resources instead of incurring third-party transaction costs. For our Indiana-domiciled insurance subsidiaries, the borrowing and lending limit is currently the lesser of 3% of the insurance company’s admitted assets and 25% of its surplus, in both cases, as of its most recent year end.

The holding company did not borrow from the cash management program during the third quarter of 2011. There was no balance as of September 30, 2011. In addition, the holding company had an outstanding payable of \$51 million to certain subsidiaries resulting from amounts placed by the subsidiaries in the inter-company cash management account in excess of funds borrowed by those subsidiaries as of September 30, 2011. Any increase (decrease) in either of these holding company cash management program payable balances results in an immediate and equal increase (decrease) to holding company cash and cash equivalents.

Our insurance subsidiaries, by virtue of their general account fixed income investment holdings, can access liquidity through securities lending programs and repurchase agreements. As of September 30, 2011, our insurance subsidiaries had securities with a carrying value of \$198 million out on loan under the securities lending program and \$280 million carrying value subject to reverse-repurchase agreements. The cash received in our securities lending program is typically invested in cash equivalents, short-term investments or fixed maturity securities.

For factors that could cause actual results to differ materially from those set forth in this section, see “Part I – Item 1A. Risk Factors” in our 2010 Form 10-K, as updated in “Part II – Item 1A. Risk Factors” below, and “Forward-Looking Statements – Cautionary Language” above.

#### Divestitures

For a discussion of our divestitures, see Note 3.

## Uses of Capital

Our principal uses of cash are to pay policy claims and benefits, operating expenses, commissions and taxes, to purchase new investments, to purchase reinsurance, to fund policy surrenders and withdrawals, to pay dividends to our stockholders and to repurchase our stock and debt securities.

## Return of Capital to Common Stockholders

One of the Company's primary goals is to provide a return to our common stockholders through share price accretion, dividends and stock repurchases. We expect to repurchase additional shares of common stock over the remainder of 2011 depending on market conditions and alternative uses of capital. The amount and timing of share repurchase depends on key capital ratios, rating agency expectations, the generation of free cash flow and an evaluation of the costs and benefits associated with alternative uses of capital. In determining dividends, the Board takes into consideration items such as current and expected earnings, capital needs, rating agency considerations and requirements for financial flexibility.

Details underlying this activity (in millions, except per share data), were as follows:

|   | For the Three<br>Months Ended<br>September 30, |       |        | For the Nine<br>Months Ended<br>September 30, |          |        |
|---|--|-------|--------|---|----------|--------|
|   | 2011   | 2010  | Change | 2011  | 2010     | Change |
| Common dividends to stockholders                        | \$ 15  | \$ 3  | NM     | \$ 47   | \$ 9     | NM     |
| Repurchase and cancellation of common<br>stock warrants | -  | 48    | -100%  | -   | 48       | -100%  |
| Repurchase of common stock                              | 150  | -     | NM     | 375   | -        | NM     |
| Total cash returned to stockholders                     | \$ 165   | \$ 51 | 224%   | \$ 422  | \$ 57    | NM     |
| Number of shares issued                                 | -  | -     | NM     | -   | 14.138   | -100%  |
| Average price per share                                 | \$ -   | \$ -  | NM     | \$ -  | \$ 26.09 | -100%  |
| Number of shares repurchased                            | 6.713  | -     | NM     | 14.276  | -        | NM     |
| Average price per share                                 | \$ 22.36                                       | \$ -  | NM     | \$ 26.29                                      | \$ -     | NM     |

Note: Average price per share is calculated using whole dollars instead of dollars rounded to millions.

## Other Uses of Capital

In addition to the amounts in the table above in "Return of Capital to Common Stockholders," other uses of holding company cash flow (in millions) were as follows:

|                                      | For the Three<br>Months Ended<br>September 30, |       |        | For the Nine<br>Months Ended<br>September 30, |        |        |
|--------------------------------------|--|-------|--------|---|--------|--------|
|                                      | 2011   | 2010  | Change | 2011  | 2010   | Change |
| Debt service (interest paid)         | \$ 62  | \$ 69 | -10%   | \$ 204  | \$ 199 | 3%     |
| Capital contribution to subsidiaries | -  | 8     | -100%  | 16  | 25     | -36%   |
| Total                                | \$ 62  | \$ 77 | -19%   | \$ 220  | \$ 224 | -2%    |

The above table focuses on significant and recurring cash flow items and excludes the effects of certain financing activities, namely the periodic retirement of debt and cash flows related to our inter-company cash management account. Taxes have been eliminated from the analysis due to a tax sharing agreement among our primary subsidiaries resulting in a modest effect on net cash flows at the holding company.

#### Significant Trends in Sources and Uses of Cash Flow

As stated above, LNC's cash flow, as a holding company, is largely dependent upon the dividend capacity of its insurance company subsidiaries as well as their ability to advance funds to it through inter-company borrowing arrangements, which may be affected by factors influencing the insurance subsidiaries' RBC and statutory earnings performance. We currently expect to be able to meet

the holding company's ongoing cash needs and to have sufficient capital to offer downside protection in the event that the capital and credit markets experience another period of extreme volatility and disruption. A decline in capital market conditions, which reduces our insurance subsidiaries' statutory surplus and RBC, may require them to retain more capital and may pressure our subsidiaries' dividends to the holding company, which may lead us to take steps to preserve or raise additional capital. For factors that could affect our expectations for liquidity and capital, see "Part I – Item 1A. Risk Factors" in our 2010 Form 10-K, as updated in "Part II – Item 1A. Risk Factors" below.

## OTHER MATTERS

### Other Factors Affecting Our Business

In general, our businesses are subject to a changing social, economic, legal, legislative and regulatory environment. Some of the changes include initiatives to require more reserves to be carried by our insurance subsidiaries. Although the eventual effect on us of the changing environment in which we operate remains uncertain, these factors and others could have a material effect on our results of operations, liquidity and capital resources. For factors that could cause actual results to differ materially from those set forth in this section, see "Part I – Item 1A. Risk Factors" in our 2010 Form 10-K, as updated in "Part II – Item 1A. Risk Factors" below, and "Forward-Looking Statements – Cautionary Language" above.

### Recent Accounting Pronouncements

See Note 2 for a discussion of recent accounting pronouncements that have been implemented during the periods presented or that have been issued and are to be implemented in the future.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

We analyze and manage the risks arising from market exposures of financial instruments, as well as other risks, in an integrated asset-liability management process that takes diversification into account. By aggregating the potential effect of market and other risks on the entire enterprise, we estimate, review and in some cases manage the risk to our earnings and shareholder value. We have exposures to several market risks including interest rate risk, foreign currency exchange risk, equity market risk, default risk, basis risk and credit risk. The exposures of financial instruments to market risks, and the related risk management process, are most important to our Retirement Solutions and Insurance Solutions businesses, where most of the invested assets support accumulation and investment-oriented insurance products. As an important element of our integrated asset-liability management process, we use derivatives to minimize the effects of changes in interest levels, the shape of the yield curve, currency movements and volatility. In this context, derivatives are designated as a hedge and serve to minimize interest rate risk by mitigating the effect of significant increases in interest rates on our earnings. Additional market exposures exist in our other general account insurance products and in our debt structure and derivatives positions. Our primary sources of market risk are: substantial, relatively rapid and sustained increases or decreases in interest rates; fluctuations in currency exchange rates; or a sharp drop in equity market values. These market risks are discussed in detail in the following pages and should be read in conjunction with our consolidated financial statements and the accompanying notes to the consolidated financial statements ("Notes") presented in "Item 1. Financial Statements," as well as "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A")."

### Interest Rate Risk

#### Interest Rate Risk on Fixed Insurance Businesses – Falling Rates

In periods of declining interest rates, we have to reinvest the cash we receive as interest or return of principal on our investments in lower yielding instruments. Moreover, borrowers may prepay fixed income securities, commercial mortgages and mortgage-backed securities in our general accounts in order to borrow at lower market rates, which exacerbate this risk. Because we are entitled to reset the interest rates on our fixed rate annuities only at limited, pre-established intervals, and because many of our contracts have guaranteed minimum interest or crediting rates, our spreads could decrease and potentially become negative.

Prolonged historically low rates are not healthy for our business fundamentals. However, we have recognized this threat and have been proactive in our investment strategies, product designs, crediting rate strategies and overall asset-liability practices to mitigate the risk of unfavorable consequences in this type of environment. For some time now, new products have been sold with low minimum crediting floors, and we apply disciplined asset-liability management standards, such as locking in spreads on these products at the time of issue.

The following summarizes solely a hypothetical significant unfavorable stress scenario to earnings if new money rates, currently averaging approximately 125 to 150 basis points below our portfolio yields, remain in place through 2013 to illustrate the sensitivity to our earnings if such a scenario were to happen:

- **Life Insurance** – The stress on earnings has been mitigated by proactive strategies to lock in long-dated and high-yielding assets to manage this risk. We executed on strategies which allowed us to effectively pre-buy assets in anticipation of future flows and maturing securities. We have also taken actions on crediting rates. We estimate that this scenario would have an approximate unfavorable earnings effect in a range of \$0 to \$5 million during the remainder of 2011, \$15 million to \$20 million during 2012 and \$35 million to \$40 million during 2013. Our deferred acquisition costs (“DAC”), value of business acquired (“VOBA”), and deferred front-end loads (“DFEL”) methodology assumes that new money rates grade from current levels to a long-term yield assumption over time. During the third quarter of 2010, we lowered our long-term new money investment yield assumption to reflect the then current new money rates and to approximate the forward curve for interest rates relevant at such time. The result was a drop in the current new money investment rate followed by a gradual annual recovery over eight years to a rate of 6.31%, 54 basis points below our previous ultimate long-term assumption of 6.85%. During the third quarter of 2011, we lowered our initial new money investment yield assumption to reflect the current environment. As a result, we recorded an unfavorable prospective unlocking of \$114 million, after tax, as discussed in “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” and “Results of Insurance Solutions – Life Insurance” in the MD&A.
- **Retirement Solutions** – The earnings drag from spread compression is modest and largely concentrated in our Defined Contribution segment, which is a function of this segment having higher guaranteed crediting rates and recurring premiums. We estimate that this scenario would have an approximate unfavorable earnings effect in a range of \$0 to \$5 million during the remainder of 2011, \$15 million to \$20 million during 2012 and \$20 million to \$25 million during 2013. Since we currently have the ability to manage spread compression through crediting rate actions, our Annuities segment is not currently sensitive to spread compression so there is very little effect estimated. The risk for our Annuities segment is sensitivity to sharp rising rates and we manage this risk by selling market value adjusted product and through purchase of derivative protection.
- **Group Protection** – We reviewed the discount rate assumptions associated with our long-term disability claim reserves and life waiver claim incurrals during the third quarter of 2011, which resulted in no change to the discount rate. Spread compression would unfavorably affect annualized earnings by up to \$5 million during 2012 and \$7 million during 2013.
- **Other Operations** – We may also be affected by sensitivity to our exposures in our institutional pension and disability run-off blocks of business that are sensitive to interest rates and could contribute to an effect.

We believe that applying this same hypothetical scenario to statutory earnings would produce similar percentage changes to earnings effects to those disclosed above.

In isolation, we believe the effects to our balance sheet from sustained low interest rates under this scenario would be modest assuming no changes to our long-term yield assumption and also excluding the effects of the new DAC methodology discussed in “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Introduction – Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL – New DAC Methodology.” With regard to our goodwill balance, low interest rates generally support a lower discount rate and therefore a higher goodwill implied fair value.

The estimates above are based upon a hypothetical scenario and are only representative of the effects of new money rates remaining in place through 2013 keeping all else equal and does not give consideration to the aggregate effect of other factors, including but not limited to: contract holder activity; hedge positions; changing equity markets; shifts in implied volatilities; and changes in other capital markets. In addition, the scenario only illustrated the effect to spreads and certain unlocking and reserve changes. Minimum guaranteed rates on annuity and universal life (“UL”)



policies generally range from 0.6% to 5.0%. Other potential effects of the scenario were not considered in the analysis. See “Part II – Item 1A. Risk Factors – Changes in interest rates and sustained low interest rates may cause interest rate spreads to decrease and changes in interest rates may also result in increased contract withdrawals” herein for additional information on interest rates.

The following provides detail on the percentage differences between the September 30, 2011, interest rates being credited to contract holders based on the third quarter of 2011 declared rates and the respective minimum guaranteed policy rate (dollars in millions), broken out by contract holder account values reported within the Retirement Solutions and Insurance Solutions businesses:

|   | Account Values                    |   |                                       | Total     | % Account Values |
|---|-----------------------------------|---|---------------------------------------|-----------|------------------|
|   | Retirement Solutions<br>Annuities | Retirement Solutions<br>Defined Contribution(1) | Insurance Solutions<br>Life Insurance |           |                  |
| Excess of Crediting Rates over Contract Minimums  |                                   |   |                                       |           |                  |
| Discretionary rate setting products (2)(3)  |                                   |   |                                       |           |                  |
| No difference   | \$ 6,055                          | \$ 9,365  | \$ 25,463                             | \$ 40,883 | 64.4%            |
| Up to 0.10%   | 34                                | 200   | 569                                   | 803       | 1.3%             |
| 0.11% to 0.20%  | 64                                | 1   | 87                                    | 152       | 0.2%             |
| 0.21% to 0.30%  | 107                               | 69  | 223                                   | 399       | 0.6%             |
| 0.31% to 0.40%  | 66                                | 1   | 55                                    | 122       | 0.2%             |
| 0.41% to 0.50%  | 85                                | 53  | 648                                   | 786       | 1.2%             |
| 0.51% to 0.60%  | 132                               | -   | 187                                   | 319       | 0.5%             |
| 0.61% to 0.70%  | 140                               | 22  | 362                                   | 524       | 0.8%             |
| 0.71% to 0.80%  | 130                               | -   | 520                                   | 650       | 1.0%             |
| 0.81% to 0.90%  | 98                                | -   | 295                                   | 393       | 0.6%             |
| 0.91% to 1.00%  | 64                                | 86  | 97                                    | 247       | 0.4%             |
| 1.01% to 1.50%  | 296                               | 83  | 172                                   | 551       | 0.9%             |
| 1.51% to 2.00%  | 40                                | 157   | 20                                    | 217       | 0.3%             |
| 2.01% to 2.50%  | 5                                 | 45  | -                                     | 50        | 0.1%             |
| 2.51% to 3.00%  | 10                                | -   | 98                                    | 108       | 0.2%             |
| 3.01% and above   | 3                                 | 1   | -                                     | 4         | 0.0%             |
| Total discretionary rate setting products   | 7,329                             | 10,083  | 28,796                                | 46,208    | 72.7%            |
| Other contracts (4)   | 14,046                            | 3,312   | -                                     | 17,358    | 27.3%            |
| Total account values  | \$ 21,375                         | \$ 13,395                                       | \$ 28,796                             | \$ 63,566 | 100.0%           |
| Percentage of discretionary rate setting product account values at minimum guaranteed rates | 82.6%                             | 92.9%   | 88.4%                                 | 88.5%     |                  |

- (1) Excludes policy loans.
- (2) Contracts currently within new money rate bands are grouped according to the corresponding portfolio rate band in which they will fall upon their first anniversary.
- (3) The average crediting rates in excess of average minimum guaranteed rates for our Annuities, Defined Contribution and Life Insurance segments were 13 basis points, 6 basis points and 8 basis points, respectively.
- (4) Includes multi-year guarantee annuities, indexed annuities, modified guarantee annuities, single premium immediate annuities, dollar cost averaging contracts and indexed-based rate setting products for our Defined Contribution segment. The average crediting rates in excess of average minimum guaranteed rates for indexed-based rate setting products within our Defined Contribution segment was 11 basis points, and 75% of account values were already at their minimum guaranteed rates.

The maturity structure and call provisions of the related portfolios are structured to afford protection against erosion of investment portfolio yields during periods of declining interest rates. We devote extensive effort to evaluating the risks associated with falling interest rates by simulating asset and liability cash flows for a wide range of interest rate scenarios. We seek to manage these exposures by maintaining a suitable maturity structure and by limiting our exposure to call risk in each respective investment portfolio.

#### Derivatives

We have entered into derivative transactions to hedge our exposure to rapid changes in interest rates. The derivative programs are used to help us achieve somewhat stable margins while providing competitive crediting rates to contract holders during periods when interest rates are changing. Such derivatives include interest rate swap agreements, interest rate futures, interest rate cap

agreements, forward-starting interest rate swaps, consumer price index swaps, interest rate cap corridors and treasury locks. See Note 6 for additional information on our derivatives used to hedge our exposure to changes in interest rates.

In addition to continuing existing programs, we may use derivative instruments in other strategies to limit risk and enhance returns, particularly in the management of investment spread businesses. We have established policies, guidelines and internal control procedures for the use of derivatives as tools to enhance management of the overall portfolio of risks assumed in our operations. Annually, our Board of Directors reviews our derivatives policy.

## Equity Market Risk

### Effect of Equity Market Sensitivity

Due to the use of our reversion to the mean (“RTM”) process and our hedging strategies as described in “Critical Accounting Policies and Estimates” in the MD&A, we expect that, in general, short-term fluctuations in the equity markets should not have a significant effect on our quarterly earnings from unlocking of assumptions for DAC, VOBA, deferred sales inducements (“DSI”) and DFEL, as we do not unlock our long-term equity market assumptions based upon short-term fluctuations in the equity markets. However, there is an effect to earnings from the effects of equity market movements on account values and assets under management and the related asset-based fees we earn on those assets net of related expenses we incur based upon the level of assets.

The following presents our estimate of the effect on income (loss) from operations (in millions), from the change in asset-based fees and related expenses, if the level of the Standard & Poor’s (“S&P”) 500 Index® (“S&P 500”), which ended at 1131 as of September 30, 2011, were to decrease to 905 over six months after September 30, 2011, and remain at that level through the next six months or increase to 1355 over six months after September 30, 2011, and remain at that level through the next six months, excluding any effect related to sales, prospective unlocking, persistency, hedge program performance or customer behavior caused by the equity market change:

|                      | S&P<br>500<br>at 905<br>(1) | S&P<br>500<br>at 1355<br>(1) |
|----------------------|-----------------------------|------------------------------|
| Segment              |                             |                              |
| Annuities            | \$ (67)                     | \$ 36                        |
| Defined Contribution | (7)                         | 4                            |

- (1) The baseline for these effects assumes an 8% to 9% annual equity market growth rate, depending on the block of business, beginning on October 1, 2011. The baseline is then compared to scenarios of S&P 500 at the 905 and 1355 levels, which assume the index moves to those levels over six months, remains at those levels through the next six months and grows at 8% to 9% annually, depending on the block of business, thereafter. The difference between the baseline and S&P 500 at the 905 and 1355 level scenarios is presented in the table.

Refer to “Critical Accounting Policies and Estimates – DAC, VOBA, DSI and DFEL” in the MD&A for discussion on the effects of equity markets on our RTM.

The effect on earnings summarized above is an expected effect for the next twelve months. The effect of quarterly equity market changes upon fee revenues and asset-based expenses will not be fully recognized in the current quarter because fee revenues are earned and related expenses are incurred based upon daily variable account values. The difference between the current period average daily variable account values compared to the end of period variable

account values affects fee revenues in subsequent periods. Additionally, the effect on earnings may not necessarily be symmetrical with comparable increases in the equity markets. This discussion concerning the estimated effects of ongoing equity market volatility on the fees we earn from account values and assets under management is intended to be illustrative. Actual effects may vary depending on a variety of factors, many of which are outside of our control, such as changing customer behaviors that might result in changes in the mix of our business between variable and fixed annuity contracts, switching among investment alternatives available within variable products, changes in sales production levels or changes in policy persistency. For purposes of this guidance, the change in account values is assumed to correlate with the change in the relevant index.

#### Credit-Related Derivatives

We use credit-related derivatives to minimize our exposure to credit-related events and we also sell credit default swaps to offer credit protection to our contract holders and investors. See Note 6 for additional information.

## Credit Risk

Through the use of derivative instruments, we are exposed to both credit risk (our counterparty fails to make payment) and market risk (the value of the instrument falls). When the fair value of a derivative contract is positive, this generally indicates that the counterparty owes us and, therefore, creates a credit risk for us equal to the extent of the fair value gain in the derivative. When the fair value of a derivative contract is negative, this generally indicates we owe the counterparty and therefore we have no credit risk, but have been affected by market risk. We minimize the credit risk in derivative instruments by entering into transactions with high quality counterparties with minimum credit ratings that are reviewed regularly by us, by limiting the amount of credit exposure to any one counterparty and by requiring certain counterparties to post collateral if our credit risk exceeds certain limits. We also maintain a policy of requiring all derivative contracts to be governed by an International Swaps and Derivatives Association (“ISDA”) Master Agreement. We do not believe that the credit or market risks associated with derivative instruments are material to any insurance subsidiary or to us. See Note 6 for additional information on our credit risk.

We have derivative positions with counterparties. Assuming zero recovery value, our exposure is the positive market value of the derivative positions with a counterparty, less collateral, that would be lost if the counterparty were to default. As of September 30, 2011, and December 31, 2010, our counterparty risk exposure, net of collateral, was \$110 million and \$184 million, respectively. As of September 30, 2011, we had exposure to 21 counterparties, with a maximum exposure of \$58 million, net of collateral, to a single counterparty. The credit risk associated with such agreements is minimized by purchasing such agreements from financial institutions with long-standing, superior performance records. For the majority of our counterparties, there is a termination event should the long-term senior debt ratings of Lincoln National Corporation drop below BBB-/Baa3 (S&P/Moody’s Investors Service). Additionally, we maintain a policy of requiring all derivative contracts to be governed by an ISDA Master Agreement.

Our fair value of counterparty exposure (in millions) was as follows:

|        | As of<br>September<br>30,<br>2011 | As of<br>December<br>31,<br>2010 |
|--------|-----------------------------------|----------------------------------|
| Rating |                                   |                                  |
| AAA    | \$ 2                              | \$ 7                             |
| AA     | 22                                | 26                               |
| A      | 85                                | 146                              |
| BBB    | 1                                 | 5                                |
| Total  | \$ 110                            | \$ 184                           |

## Item 4. Controls and Procedures

### Conclusions Regarding Disclosure Controls and Procedures

We maintain disclosure controls and procedures, which are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to the Company’s management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. As of the end of the period required by this report, we, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act). Based on

that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us and our consolidated subsidiaries required to be disclosed in our periodic reports under the Exchange Act.

#### Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2011, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

A control system, no matter how well designed and operated, can provide only reasonable assurance that the control system's objectives will be met. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the company have been detected. Projections of any evaluation of controls effectiveness to future periods are subject to

risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

## PART II – OTHER INFORMATION

### Item 1. Legal Proceedings

Information regarding reportable legal proceedings is contained in Note 10 to the consolidated financial statements in “Part I – Item 1.”

### Item 1A. Risk Factors

The risk factors set forth below updates those set forth in Lincoln National Corporation and its majority-owned subsidiaries’ (“LNC” or the “Company,” which also may be referred to as “we,” “our” or “us”) Form 10-K for the year ended December 31, 2010. You should carefully consider the risks described in our Form 10-K and those described below, as well as other information contained in the Form 10-K and this Form 10-Q, including our financial statements and the notes thereto, before making an investment decision. The risks and uncertainties described in our Form 10-K and below are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations. If any of these risks actually occur, our business, financial condition and results of operations could be materially affected. In that case, the value of our securities could decline substantially.

Difficult conditions in the global capital markets and the economy generally may materially adversely affect our business and results of operations.

Our results of operations are materially affected by conditions in the global capital markets and the economy generally, both in the U.S. and elsewhere around the world. Concerns over the viability of the European Union and its ability to resolve the European debt crisis, the ability of the U.S. government to reign in the U.S. deficit, continued high unemployment and a stagnant real estate market in the U.S. have contributed to increased volatility and diminished expectations for the economy and the markets going forward. These events may have an adverse effect on us given our credit and equity market exposure. Our revenues are likely to decline in such circumstances and our profit margins could erode. In addition, in the event of extreme prolonged market events, such as the global credit crisis and recession that occurred during 2008 and 2009, we could incur significant losses. Even in the absence of a market downturn, we are exposed to substantial risk of loss due to market volatility.

Factors such as consumer spending, business investment, domestic and foreign government spending, the volatility and strength of the capital markets, the potential for inflation or deflation and uncertainty over domestic and foreign government actions all affect the business and economic environment and, ultimately, the amount and profitability of our business. In an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and lower consumer spending, the demand for our financial and insurance products could be adversely affected. In addition, we may experience an elevated incidence of claims and lapses or surrenders of policies. Our contract holders may choose to defer paying insurance premiums or stop paying insurance premiums altogether. Adverse changes in the economy could affect earnings negatively and could have a material adverse effect on our business, results of operations and financial condition.

Changes in interest rates and sustained low interest rates may cause interest rate spreads to decrease and changes in interest rates may also result in increased contract withdrawals.



Interest rate fluctuations and/or a sustained period of low interest rates could negatively affect our profitability. Some of our products, principally fixed annuities, interest-sensitive whole life, UL and the fixed portion of VUL, have interest rate guarantees that expose us to the risk that changes in interest rates will reduce our spread, or the difference between the amounts that we are required to pay under the contracts and the amounts we are able to earn on our general account investments intended to support our obligations under the contracts. Spreads are an important component of our net income. Declines in our spread or instances where the returns on our general account investments are not enough to support the interest rate guarantees on these products could have a material adverse effect on our businesses or results of operations.

In periods when interest rates are declining or remain at low levels, we may have to reinvest the cash we receive as interest or return of principal on our investments in lower yielding instruments reducing our spread. Moreover, borrowers may prepay fixed-income securities, commercial mortgages and mortgage-backed securities in our general account in order to borrow at lower market rates, which exacerbates this risk. Lowering interest crediting rates helps to mitigate the effect of spread compression on some of our products. However, because we are entitled to reset the interest rates on our fixed rate annuities only at limited, pre-established intervals, and since many of our contracts have guaranteed minimum interest or crediting rates, our spreads could still decrease and potentially become negative.

Our expectation for future spreads is an important component in the amortization of deferred acquisition costs (“DAC”) and value of business acquired (“VOBA”) as it affects the future profitability of the business. Currently, new money rates continue to be at historically low levels. If interest rates were to remain low over a sustained period of time, and based on recent pronouncements by the Federal Reserve Board that rates are likely to remain low at least through 2013, this would put additional pressure on our spreads, potentially resulting in unlocking of our DAC and VOBA assets, thereby reducing net income in the affected reporting period. We would expect the effect to be most pronounced in our Life Insurance segment. For additional information on interest rate risks, see “Part I – Item 3. Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk.”

A decline in market interest rates could also reduce our return on investments that do not support particular policy obligations. During periods of sustained lower interest rates, policy liabilities may not be sufficient to meet future policy obligations and may need to be strengthened, thereby reducing net income in the affected reporting period. Accordingly, declining interest rates may materially affect our results of operations, financial position and cash flows and significantly reduce our profitability.

Increases in market interest rates may also negatively affect our profitability. In periods of rapidly increasing interest rates, we may not be able to replace the assets in our general account with higher yielding assets needed to fund the higher crediting rates necessary to keep our interest-sensitive products competitive. We therefore may have to accept a lower spread and thus lower profitability or face a decline in sales and greater loss of existing contracts and related assets. Increases in interest rates may cause increased surrenders and withdrawals of insurance products. In periods of increasing interest rates, policy loans and surrenders and withdrawals of life insurance policies and annuity contracts may increase as contract holders seek to buy products with perceived higher returns. This process may lead to a flow of cash out of our businesses. These outflows may require investment assets to be sold at a time when the prices of those assets are lower because of the increase in market interest rates, which may result in realized investment losses. A sudden demand among consumers to change product types or withdraw funds could lead us to sell assets at a loss to meet the demand for funds. Furthermore, unanticipated increases in withdrawals and termination may cause us to unlock our DAC and VOBA assets, which reduce net income. An increase in market interest rates could also have a material adverse effect on the value of our investment portfolio, for example, by decreasing the estimated fair values of the fixed income securities that comprise a substantial portion of our investment portfolio. An increase in interest rates could also result in decreased fee income associated with a decline in the value of variable annuity account balances invested in fixed income funds.

Changes to the calculation of reserves and attempts to mitigate the impact of Regulation XXX and Actuarial Guideline 38 may fail in whole or in part resulting in an adverse effect on our financial condition and results of operations.

The Valuation of Life Insurance Policies Model Regulation (“XXX”) requires insurers to establish additional statutory reserves for term life insurance policies with long-term premium guarantees and UL policies with secondary guarantees. In addition, Actuarial Guideline 38 (“AG 38”) clarifies the application of XXX with respect to certain UL insurance policies with secondary guarantees, commonly known as “AXXX.” Virtually all of our newly issued term and the great majority of our newly issued UL insurance products are now affected by XXX and AG 38. The application of both AG 38 and XXX involve numerous interpretations. Recently, the Life Actuarial Task Force, an advisory group to the Life Insurance and Annuities (A) Committee of the National Association of Insurance Commissioners (“NAIC”) submitted a draft statement on the application of AG 38 (the “Statement”) to the Committee. The Statement indicates that its release is the first phase of a multi-step deliberative process within the NAIC and is not intended as a final determination on the issue at this time. In addition, after the NAIC process, any final Statement must also be approved by individual states insurance departments before it is effective. Therefore, the final status of the Statement is currently unknown. We believe that the Statement attempts to impose an interpretation of AG 38 that runs counter to long-standing and valid interpretations of AG 38, and do not expect it to be adopted in its current form. In its current form, the Statement is ambiguous in defining the manner in which AXXX reserves should be calculated

making its impact unclear. However, any change to the method for calculating reserves may require us to significantly increase our statutory reserves for UL policies with secondary guarantees. Further, changes in the method of calculating reserves may also impact the future profitability and sales of our UL insurance policies with secondary guarantees.

We have implemented reinsurance and capital management actions to mitigate the capital impact of XXX and AG 38, including the use of letters of credit to support the reinsurance provided by captive reinsurance subsidiaries. Although formal details have not been provided, we anticipate the rating agencies may require a portion of these letters of credit to be included in our leverage calculations, which would pressure our leverage ratios and potentially our ratings. Therefore, we cannot provide assurance that there will not be regulatory, rating agency or other challenges to the actions we have taken to date. The result of those potential challenges could require us to increase statutory reserves or incur higher operating and/or tax costs.

We also cannot provide assurance that we will be able to continue to implement actions to mitigate the impact of XXX or AG 38 on future sales of term and UL insurance products. If we are unable to continue to implement those actions, we may have lower returns on such products sold than we currently anticipate or reduce our sales of these products.

Changes in accounting standards issued by the Financial Accounting Standards Board or other standard-setting bodies may adversely affect our financial statements.

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) as identified in the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification™ (“ASC”). From time to time, we are required to adopt new or revised accounting standards or guidance that are incorporated into the FASB ASC. It is possible that future accounting standards we are required to adopt could change the current accounting treatment that we apply to our consolidated financial statements and that such changes could have a material adverse effect on our financial condition and results of operations.

For example, the FASB issued Accounting Standards Update (“ASU”) No. 2010-26, “Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts” (“ASU 2010-26”), which clarifies the types of costs that insurance companies may capitalize and amortize over the life of the business. ASU 2010-26 significantly reduces the amount of acquisition cost that we will be able to defer in connection with sales of our insurance products. Although this will not affect the ultimate profitability of our products, we expect it could materially alter the pattern of our earnings. In addition, the final guidance permits companies to apply the guidance retrospectively with a cumulative effect adjustment to the balance sheet. This guidance is effective for fiscal years and interim periods beginning after January 1, 2012, and have elected to adopt the guidance retrospectively. Therefore, all prior periods presented in the financials will be restated. We currently estimate that retrospective adoption will result in a cumulative effect adjustment to the opening balance of retained earnings as of January 1, 2012, of approximately \$950 million to \$1.15 billion. We expect the implementation of the guidance will result in a reduction of future net income. For further information, see “Part I – Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies – DAC, VOBA, DSI and DFEL.”

In addition, the FASB is working on several projects with the International Accounting Standards Board, which could result in significant changes as GAAP converges with International Financial Reporting Standards (“IFRS”), including how we account for our insurance contracts and financial instruments and how our financial statements are presented. Furthermore, the SEC is considering whether and how to incorporate IFRS into the U.S. financial reporting system. The accounting changes being proposed by the FASB will be a complete change to how we account for and report significant areas of our business, such as insurance contracts and DAC. The effective dates and transition methods are not known; however, issuers may be required to or may choose to adopt the new standards retrospectively. In this case, the issuer will report results under the new accounting method as of the effective date, as well as for all periods presented. The changes to GAAP and ultimate conversion to IFRS will impose special demands on issuers in the areas of governance, employee training, internal controls, contract fulfillment and disclosure and will likely affect how we manage our business, as it will likely affect other business processes such as design of compensation plans, product design, etc.

Legal and regulatory actions are inherent in our businesses and could result in financial losses or harm our businesses.

We are, and in the future may be, subject to legal and regulatory actions in the ordinary course of our insurance and retirement operations. Pending legal actions include proceedings relating to aspects of our businesses and operations that are specific to us and proceedings that are typical of the businesses in which we operate. Some of these proceedings have been brought on behalf of various alleged classes of complainants. In certain of these matters, the plaintiffs are seeking large and/or indeterminate amounts, including punitive or exemplary damages. Substantial legal liability in these or future legal or regulatory actions could have a material financial effect or cause significant harm to our reputation, which in turn could materially harm our business prospects.

Our life insurance subsidiaries are currently being audited on behalf of multiple states’ treasury and controllers’ offices for compliance with laws and regulations concerning the identification, reporting and escheatment of unclaimed

contract benefits or abandoned funds. The audits focus on insurance company processes and procedures for identifying unreported death claims, and their use of the Social Security Master Death File to identify deceased policy and contract holders. In addition, our life insurance subsidiaries are the subject of multiple state Insurance Department inquiries and market conduct examinations with a similar focus on the handling of unreported claims and abandoned property. The audits and related examination activity may result in additional payments to beneficiaries, escheatment of funds deemed abandoned under state laws, administrative penalties, and changes in the our procedures for the identification of unreported claims and handling of escheatable property. We are not currently able to estimate the amount of benefits which may become payable as a result of any such unreported claims or the potential increase in the cost of implementing related changes in procedures.

Our information systems may experience interruptions or breaches in security.

Our information systems are critical to the operation of our business. Any failure, interruption or breach in security could result in disruptions to our critical systems and adversely affect our customer relationships. While we employ a robust and tested information security program, there can be no assurance that any such failure, interruption or security breach will not occur or, if any does occur, that it can be sufficiently remediated. The occurrence of any such failure, interruption or security breach of our systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and financial liability.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) The following table summarizes purchases of equity securities by the issuer during the quarter ended September 30, 2011 (dollars in millions, except per share data):

| Period              | (a) Total<br>Number<br>of Shares<br>(or Units)<br>Purchased (1) | (b)<br>Average<br>Price Paid<br>per Share<br>(or Unit) | (c) Total<br>Number<br>of Shares (or<br>Units)<br>Purchased as<br>Part of<br>Publicly<br>Announced<br>Plans or<br>Programs (2) | (d)<br>Approximate<br>Dollar<br>Value of<br>Shares (or<br>Units) that<br>May Yet Be<br>Purchased<br>Under the<br>Plans or<br>Programs (3) |
|---------------------|---|--|--|---|
| 7/1/11 -<br>7/31/11 | 612   | \$ 27.06   | -  | \$ 890  |
| 8/1/11 -<br>8/31/11 | 6,720,249   | 22.37  | 6,712,700  | 740   |
| 9/1/11 -<br>9/30/11 | 839   | 20.18  | -  | 740   |

(1) Of the total number of shares purchased, no shares were received in connection with the exercise of stock options and related taxes and 9,000 shares were withheld for taxes on the vesting of restricted stock. For the quarter ended September 30, 2011, there were 6,712,700 shares purchased as part of publicly announced plans or programs.

(2) On February 23, 2007, our Board approved a \$2.0 billion increase to our securities repurchase authorization, bringing the total authorization at that time to \$2.6 billion. As of September 30, 2011, our remaining security repurchase authorization was \$740 million. The security repurchase authorization does not have an expiration date. The amount and timing of share repurchase depends on key capital ratios, rating agency expectations, the generation of free cash flow and an evaluation of the costs and benefits associated with alternative uses of capital. The shares repurchased in connection with the awards described in Note 20 to the consolidated financial statements of our 2010 Form 10-K are not included in our security repurchase.

(3) As of the last day of the applicable month.

## Item 6. Exhibits

The Exhibits included in this report are listed in the Exhibit Index beginning on page E-1, which is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LINCOLN NATIONAL  
CORPORATION

By: /s/ RANDAL J.  
FREITAG  
Randal J. Freitag  
Executive Vice President  
and Chief Financial  
Officer

By: /s/ DOUGLAS N.  
MILLER  
Douglas N. Miller  
Senior Vice President and  
Chief Accounting Officer

Dated: November 3, 2011

LINCOLN NATIONAL CORPORATION  
Exhibit Index for the Report on Form 10-Q  
For the Quarter Ended September 30, 2011

- 12 Historical Ratio of Earnings to Fixed Charges.
- 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101 Attached as Exhibit 101 to this report are the following Interactive Data Files formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets as of September 30, 2011, and December 31, 2010; (ii) Consolidated Statements of Income for the three and nine months ended September 30, 2011 and 2010; (iii) Consolidated Statements of Stockholders' Equity for the nine months ended September 30, 2011 and 2010; (iv) Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 and 2010; and (v) Notes to the Consolidated Financial Statements. Users of this data are advised pursuant to Rule 401 of Regulation S-T that the information contained in the XBRL documents is unaudited and these are not the official publicly filed financial statements of Lincoln National Corporation.

In accordance with Rule 402 of Regulation S-T, the XBRL related information in this report shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as shall be expressly set forth by specific reference in such filing.