LINCOLN NATIONAL CORP
Form 10-K/A
March 11, 2004

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-K/A

AMENDMENT NO. 1

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2003

Commission File Number 1-6028

LINCOLN NATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

Indiana	**35-1140070**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

1500 Market Street, Suite 3900, Philadelphia, Pennsylvania 19102-2112

(Address of principal executive offices)

Registrant s telephone number (215) 448-1400

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Exchanges on which registered
Common Stock	New York, Chicago and Pacific
Common Share Purchase Rights	New York, Chicago and Pacific
$3.00 Cumulative Convertible Preferred Stock, Series A	New York and Chicago
7.65% Trust Preferred Securities, Series E*	New York
6.75% Trust Preferred Securities, Series F*	New York

* Issued by Lincoln National Capital V and Lincoln National Capital VI, respectively. Payments of distributions and payments on liquidation or redemption are guaranteed by Lincoln National Corporation.

Securities registered pursuant to Section 12(g) of the Act: None

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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 such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes x No ¨

The aggregate market value of the shares of the registrant s common stock held by non-affiliates (based upon the closing price of these shares on the New York Stock Exchange) as of the last business day of the registrant s most recently completed second fiscal quarter, was $6,330,107,000.

As of March 3, 2004, 178,680,105 shares of common stock of the registrant were outstanding.

Select materials from the Proxy Statement for the Annual Meeting of Shareholders, scheduled for May 13, 2004 have been incorporated by reference into Part III of this Form 10-K.

Explanatory Note

This Amendment Number 1 to our annual report on Form 10-K for the year ended December 31, 2003 is being filed solely due to the inadvertent omission of the report of our independent auditors on our consolidated financial statements for the year ended December 31, 2003. This amendment speaks as of the original filing date of our annual report of Form 10-K. Except for the inclusion of the foregoing report of our independent auditors, no other information contained in our Form 10-K for the year ended December 31, 2003 has been updated or amended.

SIGNATURE PAGE

LINCOLN NATIONAL CORPORATION

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, LNC has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

By /s/ Casey J. Trumble Casey J. Trumble	(Senior Vice President and Chief Accounting Officer)	March 11, 2004

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Lincoln National Corporation

Listing of Exhibits

23	Consent of Ernst & Young LLP, Independent Auditors.
31	Certifications of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2003.
32	Certifications of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2003.

LINCOLN NATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

	December 31	
	2003	**2002**
	(000s omitted)	
ASSETS		
Investments:		
Securities available-for-sale, at fair value:		
Fixed maturity (cost: 2003 - $30,959,445; 2002 - $31,103,146)	$ 32,769,479	$ 32,767,465
Equity (cost: 2003 - $173,519; 2002 - $334,493)	199,078	337,216
Trading securities	3,120,127	
Mortgage loans on real estate	4,195,028	4,205,470
Real estate	112,881	279,702
Policy loans	1,924,391	1,945,626
Derivative investments	82,475	86,236
Other investments	374,180	378,136
Total Investments	42,777,639	39,999,851
Cash and invested cash	1,711,196	1,690,534
Property and equipment	235,181	242,135
Deferred acquisition costs	3,192,349	2,970,866
Premiums and fees receivable	352,116	212,942
Accrued investment income	522,720	536,720
Assets held in separate accounts	46,565,156	36,178,336
Federal income taxes	45,900	317,726
Amounts recoverable from reinsurers	7,839,196	7,280,014
Goodwill	1,234,693	1,233,232
Other intangible assets	1,230,424	1,291,973
Other assets	1,038,298	1,230,316
Total Assets	$ 106,744,868	$ 93,184,645
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Insurance and Investment Contract Liabilities:		
Insurance policy and claim reserves	$ 24,712,732	$ 23,558,874
Contractholder funds	22,605,333	21,286,396
Liabilities related to separate accounts	46,565,156	36,178,336
Total Insurance and Investment Contract Liabilities	93,883,221	81,023,606
Short-term debt	43,976	153,045
Long-term debt	1,117,540	1,119,245
Junior subordinated debentures issued to affiliated trusts	341,295	392,658
Reinsurance related derivative liability	352,258	
Funds withheld reinsurance liabilities	1,817,905	1,762,026
Other liabilities	2,452,201	2,409,426
Deferred gain on indemnity reinsurance	924,847	977,149
Total Liabilities	100,933,243	87,837,155
Shareholders Equity:		
	593	666

Series A preferred stock - 10,000,000 shares authorized (2003 liquidation value - $1,420)		
Common stock - 800,000,000 shares authorized	1,528,701	1,467,439
Retained earnings	3,413,302	3,144,831
Accumulated Other Comprehensive Income:		
Foreign currency translation adjustment	108,993	50,780
Net unrealized gain on securities available-for-sale	793,054	753,272
Net unrealized gain on derivative instruments	22,094	28,349
Minimum pension liability adjustment	(55,112)	(97,847)
Total Accumulated Other Comprehensive Income	869,029	734,554
Total Shareholders Equity	5,811,625	5,347,490
Total Liabilities and Shareholders Equity	$ 106,744,868	$ 93,184,645

See notes to the consolidated financial statements on pages 96 through 158.

LINCOLN NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

	Year ended December 31		
	2003	**2002**	**2001**
	(000s omitted except for per share amounts)		
Revenue:			
Insurance premiums	$ 280,951	$ 315,943	$ 1,704,002
Insurance fees	1,417,488	1,410,831	1,514,926
Investment advisory fees	205,018	183,317	197,150
Net investment income	2,638,526	2,631,910	2,708,732
Equity in earnings (losses) of unconsolidated affiliates		(647)	5,672
Realized loss on investments and derivative instruments (net of amounts restored against balance sheet accounts)	(19,191)	(271,526)	(114,457)
Gain on transfer of securities from available-for-sale to trading	371,461		
Amortization of deferred gain on indemnity reinsurance	75,842	74,381	20,387
Gain on reinsurance embedded derivative/trading securities	4,119		
Other revenue and fees	309,667	291,253	341,592
Total Revenue	5,283,881	4,635,462	6,378,004
Benefits and Expenses:			
Benefits	2,428,523	2,859,505	3,409,740
Underwriting, acquisition, insurance and other expenses	1,712,694	1,733,185	2,141,313
Interest and debt expense	95,101	96,613	121,019
Total Benefits and Expenses	4,236,318	4,689,303	5,672,072
Income (loss) before Federal Income Taxes and Cumulative Effect of Accounting Changes	1,047,563	(53,841)	705,932
Federal income taxes (benefit)	280,408	(102,646)	144,712
Income before Cumulative Effect of Accounting Changes	767,155	48,805	561,220
Cumulative Effect of Accounting Changes (net of Federal Income Taxes)	(255,219)		(15,566)
Net Income	$ 511,936	$ 48,805	$ 545,654
Earnings Per Common Share-Basic			
Income before Cumulative Effect of Accounting Changes	$ 4.33	$ 0.27	$ 2.97
Cumulative Effect of Accounting Changes (net of Federal Income Taxes)	(1.44)		(0.08)
Net Income	$ 2.89	$ 0.27	$ 2.89
Earnings Per Common Share-Diluted:			
Income before Cumulative Effect of Accounting Changes	$ 4.27	$ 0.26	$ 2.93
Cumulative Effect of Accounting Changes (net of Federal Income Taxes)	(1.42)		(0.08)

Net Income	$ 2.85	$ 0.26	$ 2.85

See notes to the consolidated financial statements on pages 96 through 158.

LINCOLN NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	Year Ended December 31		
	2003	2002	2001
	(000s omitted except for per share amounts)		
Series A Preferred Stock:			
Balance at beginning-of-year	$ 666	$ 762	$ 857
Conversion into common stock	(73)	(96)	(95)
Balance at End-of-Year	593	666	762
Common Stock:			
Balance at beginning-of-year	1,467,439	1,376,098	1,066,260
Conversion of series A preferred stock	73	96	95
Stock compensation/issued for benefit plans	61,189	142,783	148,636
Cancelled / issued for acquisition of subsidiaries		(474)	(4,740)
Retirement of common stock		(51,064)	(64,147)
FELINE PRIDES conversion			229,994
Balance at End-of-Year	1,528,701	1,467,439	1,376,098
Retained Earnings:			
Balance at beginning-of-year	3,144,831	3,753,774	3,879,502
Comprehensive income	646,411	610,176	684,859
Less other comprehensive income (loss) (net of federal income tax):			
Foreign currency translation adjustment	58,213	58,842	(29,992)
Net unrealized gain on securities available-for-sale, net of reclassification adjustment	39,782	557,591	183,633
Net unrealized gain (loss) on derivative instruments	(6,255)	6,826	21,523
Minimum pension liability adjustment	42,735	(61,888)	(35,959)
Net Income	511,936	48,805	545,654
Retirement of common stock		(423,422)	(439,603)
Dividends declared:			
Series A preferred ($3.00 per share)	(58)	(60)	(71)
Common (2003-$1.355; 2002-$1.295; 2001-$1.235)	(243,407)	(234,266)	(231,708)
Balance at End-of-Year	3,413,302	3,144,831	3,753,774
Foreign Currency Translation Adjustment:			
Balance at beginning-of-year	50,780	(8,062)	21,930
Change during the year	58,213	58,842	(29,992)
Balance at End-of-Year	108,993	50,780	(8,062)
Net Unrealized Gain on Securities Available-for-Sale:			
Balance at beginning-of-year	753,272	195,681	12,048
Change during the year	39,782	557,591	183,633

Balance at End-of-Year	793,054	753,272	195,681
Net Unrealized Gain on Derivative Instruments:			
Balance at beginning-of-year	28,349	21,523	
Cumulative effect of accounting change			17,583
Change during the year	(6,255)	6,826	3,940
Balance at End-of-Year	22,094	28,349	21,523
Minimum Pension Liability Adjustment:			
Balance at beginning-of-year	(97,847)	(35,959)	
Change during the year	42,735	(61,888)	(35,959)
Balance at End-of-Year	(55,112)	(97,847)	(35,959)
Total Shareholders Equity at End-of-Year	$ 5,811,625	$ 5,347,490	$ 5,303,817

LINCOLN NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

-CONTINUED-

	Year Ended December 31		
	2003	**2002**	**2001**
		(Number of Shares)	
Series A Preferred Stock:			
Balance at beginning-of-year	20,118	23,034	25,980
Conversion into common stock	(2,372)	(2,916)	(2,946)
Balance at End-of-Year	17,746	20,118	23,034
Common Stock:			
Balance at beginning-of-year	177,307,999	186,943,738	190,748,050
Conversion of series A preferred stock	37,952	46,656	47,136
Stock compensation/issued for benefit plans	866,504	2,416,951	2,904,250
Cancelled/issued for acquisition of subsidiaries		(11,246)	(107,994)
Retirement of common stock		(12,088,100)	(11,278,022)
FELINE PRIDES conversion			4,630,318
Balance Issued and Outstanding at End-of-Year	178,212,455	177,307,999	186,943,738
Common Stock at End-of-Year:			
Assuming conversion of preferred stock	178,496,391	177,629,887	187,312,282
Diluted basis	180,695,189	178,544,446	189,291,491

See notes to the consolidated financial statements on pages 96 through 158.

LINCOLN NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31		
	2003	**2002**	**2001**
		(000s omitted)	
Cash Flows from Operating Activities:			
Net income	$ 511,936	$ 48,805	$ 545,654
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Deferred acquisition costs	(335,651)	(280,587)	(346,397)
Premiums and fees receivable	(139,173)	187,134	63,931
Accrued investment income	14,000	26,770	(47,860)
Policy liabilities and accruals	16,054	(361,432)	(491,417)
Net trading securities purchases, sales and maturities	(467,098)		
Gain on reinsurance embedded derivative/trading securities	(4,118)		
Cumulative effect of accounting change Modco embedded derivative	392,541		
Contractholder funds	1,120,520	852,098	1,119,013
Amounts recoverable from reinsurers	(527,082)	222,771	(81,461)
Federal income taxes	222,617	(53,504)	110,298
Federal income taxes paid on proceeds from disposition		(516,152)	
Stock-based compensation expense	59,313	60,163	63,626
Provisions for depreciation	65,627	36,266	30,765
Amortization of goodwill			43,385
Amortization of other intangible assets	88,153	144,717	125,168
Realized loss on investments and derivative instruments	19,191	271,526	114,457
Gain on sale of subsidiaries		8,258	(12,848)
Amortization of deferred gain	(75,842)	(74,381)	(20,387)
Other	(82,965)	(76,399)	52,656
Net Adjustments	532,017	447,248	722,929
Net Cash Provided by Operating Activities	1,043,953	496,053	1,268,583
Cash Flows from Investing Activities:			
Securities-available-for-sale:			
Purchases	(13,791,838)	(14,232,238)	(11,113,886)
Sales	8,425,329	8,389,010	5,989,074
Maturities	3,071,282	2,539,219	2,520,373
Purchase of other investments	(1,523,384)	(1,281,117)	(1,832,593)
Sale or maturity of other investments	1,768,833	1,776,515	1,865,438
Proceeds from disposition of business		(195,000)	2,036,238
Increase (decrease) in cash collateral on loaned securities	112,236	(95,341)	78,259
Other	(117,198)	(165,288)	(158,007)
Net Cash Provided by (Used in) Investing Activities	(2,054,740)	(3,264,240)	(615,104)
Cash Flows from Financing Activities:			
Long-term debt			
Decrease (includes payments and transfers to short-term debt)			(99,968)
Issuance		248,990	249,220
Junior subordinated debentures issued to affiliated trusts			
Retirement / call	(204,987)	(81,998)	(440,038)
Issuance	145,275		169,694
Net increase (decrease) in short-term debt	(109,069)	(197,158)	48,031
Universal life and investment contract deposits	4,935,740	5,305,499	4,897,828
Universal life and investment contract withdrawals	(2,746,914)	(3,262,194)	(3,288,290)
Investment contract transfers	(816,826)	108,479	(373,000)
Increase in funds withheld liability	55,879		

Common stock issued for benefit plans	12,699	82,620	85,008
Retirement of common stock		(474,486)	(503,750)
Other liabilities retirement of common stock		(131,890)	
Dividends paid to shareholders	(240,348)	(234,621)	(230,127)
Net Cash Provided by (Used in) Financing Activities	1,031,449	1,363,241	514,608
Net Increase (Decrease) in Cash and Invested Cash	20,662	(1,404,946)	1,168,087
Cash and Invested Cash at Beginning-of-Year	1,690,534	3,095,480	1,927,393
Cash and Invested Cash at End-of-Year	$ 1,711,196	$ 1,690,534	$ 3,095,480

See notes to the consolidated financial statements on pages 96 through 158.

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Basis of Presentation. The accompanying consolidated financial statements include Lincoln National Corporation (LNC) and its majority-owned subsidiaries. Through subsidiary companies, LNC operates multiple insurance and investment management businesses divided into four business segments (see Note 9). The collective group of companies uses Lincoln Financial Group as its marketing identity. Less than majority-owned entities in which LNC has at least a 20% interest are reported on the equity basis. These consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States.

Use of Estimates. The nature of the insurance and investment management businesses requires management to make numerous estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results will differ from those estimates.

Investments. Securities available-for-sale consist of fixed maturity and equity securities, which are carried at fair value. The cost of available-for-sale fixed maturity securities is adjusted for amortization of premiums and discounts. The cost of available-for-sale fixed maturity and equity securities is reduced to fair value with a corresponding charge to realized loss on investments for declines in value that are other than temporary.

Trading securities consist of fixed maturity and equity securities in designated portfolios, which support modified coinsurance (Modco) and coinsurance with funds withheld (CFW) reinsurance arrangements. Investment results for these portfolios, including gains and losses from sales, are passed directly to the reinsurers through the contractual terms of the reinsurance arrangements. Trading securities are carried at fair value and changes in fair value are recorded in net income as they occur. Offsetting these amounts are corresponding changes in the fair value of embedded derivative liabilities associated with the underlying reinsurance arrangements.

For the mortgage-backed securities portion of the trading and available-for-sale fixed maturity securities portfolios, LNC recognizes investment income using a constant effective yield based on anticipated prepayments and the estimated economic life of the securities. When estimates of prepayments change, the effective yield is recalculated to reflect actual payments to date and anticipated future payments. When the effective yield changes, the carrying value of the security is adjusted prospectively. This adjustment is reflected in net investment income.

Mortgage loans on real estate, which are primarily held in the Life Insurance and Lincoln Retirement segments, are carried at the outstanding principal balances adjusted for amortization of premiums and discounts and are net of valuation allowances. Valuation allowances are established for the excess carrying value of the mortgage loan over its estimated fair value when it is probable that, based upon current information and events, LNC will be unable to collect all amounts due under the contractual terms of the loan agreement. When LNC determines that a loan is impaired, the cost is adjusted or a provision for loss is established equal to the difference between the amortized cost of the mortgage loan and the estimated value. Estimated value is based on: 1) the present value of expected future cash flows discounted at the loan s effective interest rate; 2) the loan s observable market price; 3) the fair value of the collateral. The provision for losses is reported as realized gain (loss) on investments. Mortgage loans deemed to be uncollectible are charged against the allowance for losses and subsequent recoveries, if any, are credited to the allowance for losses. Interest income on mortgage loans includes interest collected, the change in accrued interest, and amortization of premiums and discounts. Mortgage loan fees and costs are recorded in net investment income as they are incurred.

Investment real estate is carried at cost less accumulated depreciation. Depreciation is provided on a straight-line basis over the estimated useful life of the asset. Cost is adjusted for impairment when the projected

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

undiscounted cash flow from the investment is less than the carrying value. Impaired real estate is written down to the estimated fair value of the real estate, which is generally computed using the present value of expected future cash flows from the real estate discounted at a rate commensurate with the underlying risks. Also, valuation allowances for losses are established, as appropriate, for real estate holdings that are in the process of being sold. Real estate acquired through foreclosure proceedings is reclassified on the balance sheet from mortgage loans on real estate to real estate and is recorded at fair value at the settlement date, which establishes a new cost basis. If a subsequent periodic review of a foreclosed property indicates the fair value, less estimated costs to sell, is lower than the carrying value at settlement date, the carrying value is adjusted to the lower amount. Write-downs to real estate and any changes to the reserves on real estate are reported as realized gain (loss) on investments.

Policy loans are carried at aggregate unpaid balances.

Cash and invested cash are carried at cost and include all highly liquid debt instruments purchased with a maturity of three months or less.

Realized gain (loss) on investments is recognized in net income, net of associated amortization of deferred acquisition costs and investment expenses, using the specific identification method. Changes in the fair values of available-for-sale securities carried at fair value are reflected directly in shareholders equity, after deductions for related adjustments for deferred acquisition costs and amounts required to satisfy policyholder commitments that would have been recorded had these securities been sold at their fair value, and after deferred taxes or credits to the extent deemed recoverable.

Realized gain (loss) on sale of subsidiaries, net of taxes, is recognized in net income.

Derivative Instruments. LNC hedges certain portions of its exposure to interest rate fluctuations, the widening of bond yield spreads over comparable maturity U.S. Government obligations, credit risk, foreign exchange risk and equity risk fluctuations by entering into derivative transactions. A description of LNC s accounting for its hedging of such risks is discussed in the following paragraphs.

LNC recognizes all derivative instruments as either assets or liabilities in the consolidated balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, LNC must designate the hedging instrument based upon the exposure being hedged as a cash flow hedge, fair value hedge or a hedge of a net investment in a foreign operation. As of December 31, 2003 and 2002, LNC had derivative instruments that were designated and qualified as cash flow hedges, fair value hedges and hedges of a net investment in a foreign operation. In addition, LNC had derivative instruments that were economic hedges, but were not designated as hedging instruments under Financial Accounting Standards No. 133 (FAS 133).

For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income (OCI) and reclassified into net income in the same period or periods during which the hedged transaction affects net income. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of designated future cash flows of the hedged item (hedge ineffectiveness), if any, is recognized in current income during the period of change. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current income during the period of change in fair values. For derivative instruments that are designated and qualify as a hedge of a net investment in a foreign operation, the

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

gain or loss is reported in OCI as part of the cumulative translation adjustment to the extent it is effective. For derivative instruments not designated as hedging instruments, the gain or loss is recognized in current income during the period of change.

LNC s has certain Modco and CFW reinsurance arrangements with embedded derivatives related to the funds withheld assets. 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 fair value of these derivatives are recorded in net income as they occur. Offsetting these amounts are corresponding changes in the fair value of trading securities in portfolios that support these arrangements.

See Note 7 for further discussion of LNC s accounting policy for derivative instruments.

Loaned Securities. Securities loaned are treated as collateralized financing transactions and a liability is recorded equal to the cash collateral received which is typically greater than the market value of the related securities loaned. This liability is included within Other Liabilities within LNC s consolidated balance sheet. In other instances, LNC will hold as collateral securities with a market value at least equal to the securities loaned. Securities held as collateral are not recorded in LNC s consolidated balance sheet in accordance with accounting guidance for secured borrowings and collateral. LNC s agreements with third parties generally contain contractual provisions to allow for additional collateral to be obtained when necessary. LNC values collateral daily and obtains additional collateral when deemed appropriate.

Property and Equipment. Property and equipment owned for company use is carried at cost less allowances for depreciation. Provisions for depreciation of investment real estate and property and equipment owned for company use are computed principally on the straight-line method over the estimated useful lives of the assets.

Premiums and Fees on Investment Products and Universal Life and Traditional Life Insurance Products.

Investment Products and Universal Life Insurance Products: Investment products consist primarily of individual and group variable and fixed deferred annuities. Universal life insurance products include universal life insurance, variable universal life insurance, corporate-owned life insurance, bank-owned life insurance and other interest-sensitive life insurance policies. Revenues for investment products and universal life insurance products consist of net investment income, asset based fees, cost of insurance charges, percent of premium charges, policy administration charges and surrender charges that have been assessed and earned against policy account balances and premiums received during the period. The timing of revenue recognition as it relates to fees assessed on investment contracts is determined based on the nature of such fees. Asset based fees, cost of insurance and policy administration charges are assessed on a daily or monthly basis and recognized as revenue when assessed and earned. Percent of premium charges are assessed at the time of premium payment and recognized as revenue when assessed and earned. Certain amounts assessed that represent compensation for services to be provided in future periods are reported as unearned revenue and recognized in income over the periods benefited. Surrender charges are recognized upon surrender of a contract in accordance with contractual terms.

Traditional Life Insurance Products: Traditional life insurance products include those products with fixed and guaranteed premiums and benefits and consist primarily of whole life insurance, limited-payment life insurance, term life insurance and certain annuities with life contingencies. Premiums for traditional life insurance products are recognized as revenue when due from the policyholder.

Investment Advisory Fees. As specified in the investment advisory agreements with the mutual funds, fees are determined and recognized as revenues monthly, based on the average daily net assets of the mutual funds

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

managed. Investment advisory contracts generally provide for the determination and payment of advisory fees based on market values of managed portfolios at the end of a calendar month or quarter. Investment management and advisory contracts typically are renewable annually with cancellation clauses ranging up to 90 days.

Other Revenues and Fees. Other revenue and fees principally consists of amounts earned by LNC s retail distribution arm, Lincoln Financial Advisors (LFA) from sales of third party insurance and investment products. Such revenue is recorded as earned at the time of sale.

Assets Held in Separate Accounts/Liabilities Related to Separate Accounts. These assets and liabilities represent segregated funds administered and invested by LNC s insurance subsidiaries for the exclusive benefit of pension and variable life and annuity contractholders. Both the assets and liabilities are carried at fair value. The fees earned by LNC s insurance subsidiaries for administrative and contractholder maintenance services performed for these separate accounts are included in insurance fee revenue.

Deferred Acquisition Costs. Commissions and other costs of acquiring universal life insurance, variable universal life insurance, unit-linked products, traditional life insurance, annuities and other investment contracts, which vary with and are primarily related to the production of new business, have been deferred to the extent recoverable. The methodology for determining the amortization of acquisition costs varies by product type based on two different accounting pronouncements: Statement of Financial Accounting Standards No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments (FAS 97) and Statement of Financial Accounting Standards No. 60, Accounting and Reporting by Insurance Enterprises (FAS 60). Under FAS 97, acquisition costs for universal life and variable universal life insurance and investment-type products, which include unit-linked products and fixed and variable deferred annuities, are amortized over the lives of the policies in relation to the incidence of estimated gross profits from surrender charges, investment, mortality net of reinsurance ceded and expense margins, and actual realized gain (loss) on investments. Past amortization amounts are adjusted when revisions are made to the estimates of current or future gross profits expected from a group of products. Policy lives for universal and variable universal life policies are estimated to be 30 years, based on the expected lives of the policies and are variable based on the inception of each policy for unit-linked policies. Policy lives for fixed and variable deferred annuities are 14 to 18 years for the traditional, long surrender charge period products and 8 to 10 years for the more recent short-term, or no surrender charge products. The front-end load annuity product has an assumed life of 25 years. Longer lives are assigned to those blocks that have demonstrated favorable experience.

Under FAS 60, acquisition costs for traditional life insurance products, which include whole life and term life insurance contracts are amortized over periods of 10 to 30 years on either a straight-line basis or as a level percent of premium of the related policies depending on the block of business. There are currently no deferred acquisition costs being amortized under FAS 60 for fixed and variable payout annuities.

For all FAS 97 and FAS 60 policies, amortization is based on assumptions consistent with those used in the development of the underlying policy form adjusted for emerging experience and expected trends.

Policy sales charges that are collected in the early years of an insurance policy have been deferred (referred to as deferred front-end loads) and are amortized into income over the life of the policy in a manner consistent with that used for DAC. (See above for discussion of amortization methodologies.)

Benefits and Expenses. Benefits and expenses for universal life-type and other interest-sensitive life insurance products include interest credited to policy account balances and benefit claims incurred during the period in excess of policy account balances. Interest crediting rates associated with funds invested in the general

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

account of LNC s insurance subsidiaries during 2001 through 2003 ranged from 4.00% to 7.00%. For traditional life, group health and disability income products, benefits and expenses, other than deferred acquisition costs, are recognized when incurred in a manner consistent with the related premium recognition policies.

Interest and debt expense includes interest on junior subordinated debentures issued to affiliated trusts.

Goodwill and Other Intangible Assets. Prior to January 1, 2002, goodwill, as measured by the excess of the cost of acquired subsidiaries or businesses over the fair value of net assets acquired, was amortized using the straight-line method over periods of 20 to 40 years in accordance with the benefits expected to be derived from the acquisitions. Effective January 1, 2002, goodwill is not amortized, but is subject to impairment tests conducted at least annually.

Other intangible assets for acquired insurance businesses consist of the value of existing blocks of business (referred to as the present value of in-force). The present value of in-force is amortized over the expected lives of the block of insurance business in relation to the incidence of estimated profits expected to be generated on universal life, variable universal life and investment-type products acquired, (i.e., unit-linked products and variable deferred annuities) and over the premium paying period for insurance products acquired, (i.e., traditional life insurance products). Amortization is based upon assumptions used in pricing the acquisition of the block of business and is adjusted for emerging experience. Accordingly, amortization periods and methods of amortization for present value of in-force vary depending upon the particular characteristics of the underlying blocks of acquired insurance business.

Other intangible assets for acquired Investment Management subsidiaries include institutional customer relationships, covenants not to compete and mutual fund customer relationships. These assets are still required to be amortized on a straight-line basis over their useful life for periods ranging from 6 to 15 years depending upon the characteristics of the particular underlying relationships for the intangible asset.

Prior to January 1, 2002, the carrying values of goodwill and other intangible assets were reviewed periodically for indicators of impairment in value that are other than temporary, including unexpected or adverse changes in the following: (1) the economic or competitive environments in which the company operates, (2) profitability analyses, (3) cash flow analyses, and (4) the fair value of the relevant subsidiary. If there was an indication of impairment then the cash flow method would be used to measure the impairment and the carrying value would be adjusted as necessary. However, effective January 1, 2002, goodwill is subject to impairment tests conducted at least annually. Other intangible assets will continue to be reviewed periodically for indicators of impairment consistent with the policy that was in place prior to January 1, 2002.

Insurance and Investment Contract Liabilities. The liabilities for future policy benefits and claim reserves for universal and variable universal life insurance policies consist of policy account balances that accrue to the benefit of the policyholders, excluding surrender charges. The liabilities for future insurance policy benefits and claim reserves for traditional life policies are computed using assumptions for investment yields, mortality and withdrawals based principally on generally accepted actuarial methods and assumptions at the time of policy issue. Interest assumptions for traditional direct individual life reserves for all policies range from 2.25% to 6.75% depending on the time of policy issue. The interest assumptions for immediate and deferred paid-up annuities range from 0.75% to 13.55%.

The liabilities for future claim reserves for the guaranteed minimum death benefit (GMDB) feature on certain variable annuity contracts are a function of the net amount at risk (NAR), mortality, persistency and incremental death benefit mortality and expense assessments (M&E) expected to be incurred over the period of time for which the NAR is positive. At any point in time, the NAR is the difference between the potential death

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

benefit payable and the total variable annuity account values subject to the GMDB. At each quarterly valuation date, the GMDB reserves are calculated for every variable annuity contract with a GMDB feature based on projections of account values and NAR followed by the computation of the present value of expected NAR death claims using product pricing mortality assumptions less expected GMDB M&E revenue during the period for which the death benefit options are assumed to be in the money.

With respect to its insurance and investment contract liabilities, LNC continually reviews its: 1) overall reserve position; 2) reserving techniques and 3) reinsurance arrangements. As experience develops and new information becomes known, liabilities are adjusted as deemed necessary. The effects of changes in estimates are included in the operating results for the period in which such changes occur.

Reinsurance. LNC s insurance companies enter into reinsurance agreements with other companies in the normal course of their business. Prior to the acquisition of LNC s reinsurance operations by Swiss Re in 2001, LNC s insurance subsidiaries assumed reinsurance from unaffiliated companies. The transaction with Swiss Re involved a series of indemnity reinsurance transactions combined with the sale of certain stock companies that comprised LNC s reinsurance operations. All reinsurance agreements, excluding Modco agreements, are reported on a gross basis since there is a right of offset.

Postretirement Medical and Life Insurance Benefits. LNC accounts for its postretirement medical and life insurance benefits using the full accrual method.

Stock Based Compensation. Effective January 1, 2003 LNC implemented the provisions of Statement of Financial Accounting Standard No. 123, Accounting for Stock-Based Compensation, (FAS 123) to expense the fair value of stock options granted to employees. On December 31, 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation- Transition and Disclosure (FAS 148), which provides alternative methods of transition for entities that change to the fair value method of accounting for stock-based employee compensation.

LNC adopted the retroactive restatement method under FAS148 and restated all periods presented to reflect stock-based employee compensation cost under the fair value accounting method in FAS 123 for all employee awards granted, modified or settled in fiscal years beginning after December 15, 1994.

Foreign Currency Translation. LNC s foreign subsidiaries balance sheet accounts and income statement items are translated at the current and average exchange rates for the year, respectively. Resulting translation adjustments are reported as a component of shareholders equity. Other translation adjustments for foreign currency transactions that affect cash flows are reported in comprehensive income.

Earnings per Share. Basic earnings per share is computed by dividing earnings available to common shareholders by the average common shares outstanding. Diluted earnings per share is computed assuming the conversion or exercise of dilutive convertible preferred securities, non-vested stock, stock options, performance share units and deferred compensation shares outstanding during the year.

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Changes in Accounting Principles and Changes in Estimates

Accounting for Variable Interest Entities. In January 2003, the Financial Accounting Standards Board (FASB) issued initial guidance under Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46), which requires the consolidation of variable interest entities (VIE) by an enterprise if that enterprise has a variable interest that will absorb a majority of the VIE s expected losses if they occur, receive a majority of the entity s expected residual returns if they occur, or both. If one enterprise will absorb a majority of a VIE s expected losses and another enterprise will receive a majority of that VIE s expected residual returns, the enterprise absorbing a majority of the losses shall consolidate the VIE. A VIE is an entity in which no equity investors have the characteristics of a controlling financial interest or have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. In response to concerns raised by LNC and others in the Insurance and Investment industries with respect to the initial guidance, the FASB significantly modified several key aspects of the rules in a revised interpretation issued in December 2003. LNC adopted the final FIN 46 rules on December 31, 2003.

LNC currently manages seven Collateralized Debt Obligation pools (CDOs), and of these, there are five where the asset management fees paid to LNC no longer contain performance based incentives. As a result, LNC is not considered the primary beneficiary of these VIE s. LNC s maximum exposure to loss in these five CDOs is an investment in a small portion of the senior debt issued by one of these CDO pools, which had a carrying and estimated fair value of approximately $3 million, at December 31, 2003.

For the other two CDOs, LNC still has the right to earn performance-based fees above the base asset management fees. These performance-based fees are considered variable fees for purposes of performing the analysis of expected residual returns. In addition, LNC also holds investment interests in these CDOs. However, in these two CDOs, LNC has determined that the expected variability in its fees and the level of other LNC interests in the CDO, are currently below the level that would result in LNC being treated as the primary beneficiary. Future changes in the interest held by the third party investors in these two CDO pools, relative to LNC s interest, will require retesting of LNC s potential status as primary beneficiary. LNC will continue to disclose its variable interests in these two CDO pools. LNC s maximum exposure to loss is its investment in these two CDO pools, which had a carrying value of approximately $14.5 million, and an estimated fair value of approximately $13.9 million, at December 31, 2003.

LNC identified certain partnership investments that required consolidation under the requirements of FIN 46. LNC consolidated these partnerships at December 31, 2003 with no material effect to either financial condition or results of operations.

FIN 46 also affected LNC s accounting for the junior subordinated debentures issued to affiliated trusts. Previously, LNC consolidated the affiliated trusts which resulted in LNC carrying a liability equal to the trusts liability to the preferred shareholders. These trusts are variable interests as defined by FIN 46, and LNC will not receive a majority of expected residual returns. LNC deconsolidated its $10.0 million investment in the trusts as of December 31, 2003. The effect was a $10.0 million increase to other invested assets and a corresponding increase in the liability for junior subordinated debentures payable to affiliated trusts.

Accounting for Modified Coinsurance. FASB s Derivative Implementation Group Statement 133 Implementation Issue No. B36 (DIG B36). DIG B36 provides that the embedded derivatives included within Modco and CFW reinsurance agreements must be accounted for separately from the underlying reinsurance agreements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The effective date for implementation of DIG B36 for LNC was the October 1, 2003 start date of the fourth quarter. The following table summarizes the various effects on shareholders equity from the implementation of DIG B36 (in millions):

Initial Adoption Shareholder Equity Effect on October 1, 2003

Notes		Pre-tax	After-tax
	Recording of Embedded Derivative		
1A	Cumulative effect of accounting change	$ (392.5)	$ (255.2)
1B	Release of liability for unrealized investment gains	376.3	244.6
	Total	(16.2)	(10.6)
2A	Reclassification of available-for-sale securities to trading securities	371.5	241.5
2B	Release of unrealized available-for-sale security gains in Other Comprehensive Income	(371.5)	(241.5)
	Total available for sale to trading adjustment		
	Total effect on Shareholders Equity from DIG B36 Implementation on October 1, 2003	$ (16.2)	$ (10.6)

1A. At the time of adoption, LNC recorded a charge to net income as a cumulative effect of a change in accounting, representing the fair value of the embedded derivatives included in various Modco and CFW reinsurance agreements.

1B. In conjunction with recording the above charge in 1A. LNC also recorded an increase in Other Comprehensive Income relating to the fact that prior to the adoption of DIG B36 the net unrealized gains on the underlying available-for-sale securities supporting these reinsurance agreements had been accounted for as gains benefiting the reinsurance companies assuming the risks under these Modco and CFW reinsurance agreements.

2A. Concurrent with the initial recording of the embedded derivative associated with these reinsurance arrangements, LNC reclassified related available-for-sale securities to trading account classification.

2B. The previously recorded increases to shareholder s equity reported in Other Comprehensive Income as a result of the available-for-sale classification of these securities were reversed as part of the reclassification accounting.

During the fourth quarter of 2003 and going forward, changes in the fair value of the embedded derivative flow through net income, as do changes in the fair value of the trading account securities, as represented by adjustments 3A and 3B in the table below. For the quarter ended December 31, 2003, the effect of the two new mark-to-market adjustments on net income was $4.2 million pre-tax ($2.7 million after-tax). The table below combines the trading account and embedded derivative mark-to-mark accounting with the implementation effects discussed above to demonstrate the effects on the income statement for the quarter ended December 31, 2003 (in millions).

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net Income Effect for the Quarter Ended December 31, 2003

Notes		Pre-tax	After-tax
	Revenues Realized Investment Results		
3A	Trading account securities Change during fourth quarter	$ (35.9)	$ (23.4)
3B	Embedded derivative Change during fourth quarter	40.1	26.1
	Net gain on Modco and CFW in fourth quarter	4.2	2.7
	Reclassification of available-for-sale securities to trading account securities	371.5	241.5
	Income before accounting changes	375.7	244.2
	Cumulative effect of accounting change	(392.5)	(255.2)
	Net Income	$ (16.8)	$ (11.0)

As indicated in the above tables, the implementation of DIG B36 resulted in an initial decrease to shareholders equity and the ongoing accounting of DIG B36 will continue to give rise to ongoing gains and losses flowing through net income as the embedded derivative and trading account securities are continuously marked to market.

These adjustments do not net to zero in any one particular accounting period due to the fact that not all of the invested assets supporting these Modco and CFW reinsurance agreements were available-for-sale securities that could be reclassified to trading account securities, and not all Modco and CFW reinsurance agreements have segregated portfolios of securities that can be classified as trading account securities. However, it is important to note that these differences in net income will reverse over the term of the underlying Modco and CFW reinsurance agreements, reflecting the fact that the new accounting for the embedded derivatives prescribed in DIG B36 changes the timing of the recognition of income under these Modco and CFW reinsurance agreements but does not change the total amount of earnings that will ultimately be reported over the life of these agreements.

Statement of Accounting Position 03-1. In July 2003, the Accounting Standards Executive Committee (AcSEC) of the American Institute of Certified Public Accountants issued Statement of Position 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (the SOP). LNC will adopt the SOP as of January 1, 2004.

The SOP provides guidance related to the reporting and disclosure of certain insurance contracts and separate accounts, including guidance for computing reserves for products with guaranteed benefits, such as guaranteed minimum death benefits (GMDB), and for products with annuitization benefits such as guaranteed minimum income benefits. In addition, the SOP addresses the presentation and reporting of separate accounts, the capitalization and amortization of sales inducements, and secondary guarantees on universal-life type contracts.

GMDB Reserves. Although there was no method prescribed under generally accepted accounting principles for GMDB reserving until the issuance of the SOP, LNC s Retirement segment has been recording a reserve for GMDB s. At December 31, 2003 LNC s GMDB reserve was $46.4 million. Based upon a comparison of the requirements of the SOP to LNC s established practice of reserving for GMDB, the adoption of the GMDB reserving methodology under the SOP is not expected to have a material effect on LNC s financial statements.

Sales Inducements. LNC s Retirement segment variable annuity product offerings include contracts that offer a bonus credit, typically ranging from 2% to 5% of each deposit. LNC also offers enhanced interest rates to variable annuity contracts that are under dollar cost averaging (DCA) funding arrangements. Bonus credits and

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

excess DCA interest are considered sales inducements under the SOP and, as such, are to be deferred as a sales inducement asset and amortized as a benefit expense over the expected life of the contract. Amortization will be computed using the same methodology and assumptions used in amortizing DAC.

LNC currently defers bonus credits as part of the DAC asset and reports the amortization of bonus credits as part of DAC amortization. Upon adoption of the SOP, LNC will reclassify bonus credits from DAC to deferred sales inducements on its balance sheet and report deferred sales inducement amortization as part of benefit expense. Prior period balance sheet and income statement line item presentation will be reclassified to conform to the new basis of presentation.

LNC currently reports excess DCA interest as benefit expense when the excess interest is earned under the contract. Upon adoption of the SOP, LNC will begin deferring excess DCA interest as deferred sales inducements and amortizing these deferred sales inducements as benefit expense over the expected life of the contract. Amortization will be calculated using the same methodology and assumptions used in amortizing DAC. While over the long run the same amount of excess DCA interest expense will emerge under the SOP as under LNC s current accounting method, because of the prospective treatment of new deferred sales inducements, LNC expects earnings to be slightly higher under the SOP, relative to LNC s current approach, for near term financial reporting periods. For instance, had the rules for excess DCA interest expense under the SOP been in effect for 2003, LNC estimates that Lincoln Retirement would have reported increased earnings of about $6 million. The actual effect on LNC s results in future periods will depend upon the volume of business written with excess DCA interest.

Separate Accounts. LNC s current accounting is consistent with the provisions of the SOP relating to the reporting and measuring of separate account product assets and liabilities as general account assets and liabilities when specific criteria are not met, as well as for the reporting and measuring seed money in separate accounts as general account assets, and for recognizing contract holder liabilities. The adoption of these provisions of the SOP are expected to have no effect on LNC s financial statements.

Universal Life Contracts. LNC s Life Insurance segment offers individual and survivor-life universal life insurance products that provide a secondary guarantee to the contract holder, commonly referred to as a no-lapse guarantee. This feature permits a policy that would normally terminate, if the net cash value were to fall below zero, to remain in force as long as the conditions of the no-lapse provision are met. LNC s analysis of this benefit indicates that this feature should be considered insignificant, as newly defined by the SOP. In general, LNC does not expect to record an additional liability for its current secondary guarantee offerings. However, in the event that an additional liability is required under the SOP for certain of LNC s current secondary guarantee features, LNC would not expect the adoption of the SOP to have a material effect on its financial statements.

LNC understands that throughout the life insurance industry a wide variety of interpretations and approaches to the application of the SOP to fixed and variable universal life contracts have recently begun to emerge. Industry-wide concern over this inconsistency in interpretation has become so great that on February 18, 2004 the American Council of Life Insurers (ACLI) submitted a letter on behalf of the industry to the Chairman of AcSEC, requesting a delay of the effective date for the SOP, as it applies to universal life insurance, until such time that guidance for these implementation matters can be made available. If AcSEC decides to address these industry-wide concerns and issue new guidance, LNC s current estimates of the expected effects of the adoption of the SOP could change.

Other Products and Riders. LNC continues to review the features and characteristics of other products and riders offered within its Retirement, Life Insurance, and Lincoln UK segments, and to evaluate the potential applicability of the SOP to these other products and riders. With respect to the other products and riders that are the subject of this ongoing review, LNC does not currently expect that the adoption of the SOP should have a material effect on LNC s financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

FASB Financial Staff Position No. FAS - 106-1 Medicare Prescription Drug Improvement and Modernization Act of 2003. In December 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Medicare Act) became law. Beginning in 2006, the Medicare Act provides various alternatives that could result in an offset to some portion of the costs of prescription drug benefits provided to retirees. In January 2004, the staff of the FASB issued Financial Staff Position No. FAS 106-1 (FSP 106-1), which permits a sponsor of a post-retirement health care plan that provides retiree prescription drug benefits to make a one-time election to defer accounting for the effects of the Medicare Act.

There are several uncertainties that exist as to the eventual effects of the Medicare Act on the cost of the prescription drug benefits currently included in LNC s retiree medical benefit plan. These uncertainties include various administrative components related to the Medicare Act that have yet to be developed, the potential for significant legislative changes to the Medicare Act prior to its implementation in 2006, and the interrelated effects that the existence of various cost containment measures currently included within LNC s retiree medical benefit plans may have under the new legislation. However, regardless of the outcome of these various uncertainties, LNC does not currently expect that the Medicare Act would have a material affect on future net income due to the cost containment measures already in place under LNC s retiree medical benefit plans.

Due to these uncertainties and expected immaterial impact, LNC has elected to defer accounting for the effects of the Medicare Act. Having made this deferral election, FSP 106-1 prohibits LNC from accounting for the effects of the Medicare Act until such time as either final FASB guidance is issued or a significant event occurs that would require a remeasurement of plan assets and obligations. Accordingly, the measures of accumulated post-retirement benefit obligation and periodic post-retirement benefit cost in LNC s financial statements for the year ended December 31, 2003 do not reflect the effects of the Medicare Act.

Change in Estimate for Disability Income and Personal Accident Reinsurance Reserves. As a result of developments and information received in the third quarter of 2003 relating to personal accident matters, LNC increased reserves on this exited business by $20.9 million after-tax ($32.1 million pre-tax) with a corresponding increase in reinsurance recoverable from Swiss Re and in the deferred gain. As a result of developments and information obtained during 2002 relating to personal accident and disability income matters, LNC increased these exited business reserves by $198.5 million after-tax or $1.07 per fully diluted share ($305.4 million pre-tax). After giving effect to LNC s $100 million indemnification obligation to Swiss Re, LNC recorded a $133.5 after-tax ($205.4 million pre-tax) increase in reinsurance recoverable from Swiss Re with a corresponding increase in the deferred gain. (See Note 11 for further explanation of LNC s Reinsurance transaction with Swiss Re.)

Accounting for Stock-Based Compensation - Transition and Disclosure. On December 31, 2002, the FASB issued Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation- Transition and Disclosure (FAS 148), which provides alternative methods of transition for entities that change to the fair value method of accounting for stock-based employee compensation. LNC adopted the fair value method of accounting under FAS 123 with the retroactive restatement method, as amended by FAS 148, as of January 1, 2003 and restated its financial statements for the years 2002, 2001, and 2000.

Accounting for Costs Associated with Exit or Disposal Activities. In June 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 146, Accounting for Costs Associated with Exit or Disposal Activities (FAS 146), which addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Action (including Certain Costs Incurred in a

Restructuring) (Issue 94-3). The principal difference between FAS 146 and Issue 94-3 is that FAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

liability is incurred, rather than at the date of an entity s commitment to an exit plan. FAS 146 is effective for exit or disposal activities after December 31, 2002. LNC adopted FAS 146 on January 1, 2003, and the adoption affects the timing of when expense is recognized for restructuring activities after December 31, 2002. See Note 12 for information on Restructuring charges.

Accounting for the Impairment or Disposal of Long-lived Assets. LNC adopted Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets on January 1, 2002. The effect of adoption was immaterial.

Accounting for Business Combinations and Goodwill and Other Intangible Assets. LNC adopted Statements of Financial Accounting Standards No. 141, Business Combinations (FAS 141), and No. 142, Goodwill and Other Intangible Assets (FAS 142) on January 1, 2002. Afte consideration of the provisions of the new standards regarding proper classification of goodwill and other intangible assets on the consolidated balance sheet, LNC did not reclassify any goodwill or other intangible balances held as of January 1, 2002.

In compliance with the transition provision of FAS 142, LNC completed the first step of the transitional goodwill impairment test during the second quarter of 2002. The valuation techniques used by LNC to estimate the fair value of the group of assets comprising the different reporting units varied based on the characteristics of each reporting unit s business and operations. A discounted cash flow model was used to assess the goodwill of the reporting units within LNC s Lincoln Retirement, Life Insurance and Lincoln UK segments. A valuation technique combining multiples of revenues, earnings before interest, taxes, depreciation and amortization (EBITDA) and assets under management was used to assess the goodwill in LNC s Investment Management segment. The results of the first step of the tests indicate that LNC does not have impaired goodwill. In accordance with FAS 142, LNC has chosen October 1 as its annual review date. As such, LNC performed annual valuation reviews during the fourth quarter of 2003 and 2002. The results of the tests performed as of October 1, 2003 and 2002 indicate that LNC does not have impaired goodwill.

As a result of the application of the non-amortization provisions of the new standards, LNC had an increase in net income of $41.7 million ($0.22 per common share on a fully diluted basis) for the year ended December 31, 2002.

The reconciliation of reported net income to adjusted net income is as follows:

(in millions except per share amounts)	**Year Ended December 31, 2001**
Reported Net Income	$ 545.6
Add back: Goodwill Amortization (after-tax)	43.4
Adjusted Net Income	$ 589.0

Earnings Per Common Share Basic:	
Reported Net Income	$ 2.89
Add back: Goodwill Amortization (after-tax)	0.23
Adjusted Net Income	$ 3.12
Earnings Per Common Share Diluted:	
Reported Net Income	$ 2.85
Add-back: Goodwill Amortization (after-tax)	0.23
Adjusted Net Income	$ 3.08

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The consolidated carrying value of goodwill changes as a result of acquisitions and changes in foreign currency exchange rates. The Lincoln UK segment s carrying value changes as a result of the translation of the Lincoln UK balance from British pounds to U.S. dollars based on prevailing exchange rates as of the balance sheet date. During the 2002, goodwill for the Retirement segment increased as a result of the acquisition of The Administrative Management Group, Inc. (AMG). Total purchased goodwill in 2002 from the acquisition was $20.2 million. (see Note 11).

Change in Estimate of Premium Receivables on Certain Client-Administered Individual Life Reinsurance. During the first quarter of 2001, LNC s former Reinsurance segment refined its estimate of due and unpaid premiums on its client-administered individual life reinsurance business. As a result of the significant growth in the individual life reinsurance business generated in recent years, the Reinsurance segment initiated a review of the block of business in the last half of 2000. An outgrowth of that analysis resulted in a review of the estimation of premiums receivable for due and unpaid premiums on client-administered business. During the first quarter of 2001, the Reinsurance segment completed the review of this matter, and concluded that enhanced information flows and refined actuarial techniques provided a basis for a more precise estimate of premium receivables on this business. As a result, the Reinsurance segment recorded income of $25.5 million or $0.13 per share ($39.3 million pre-tax) related to periods prior to 2001.

Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets. On April 1, 2001, LNC adopted Emerging Issues Task Force Issue No. 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets (EITF 99-20). EITF 99-20 was effective for fiscal quarters beginning after March 15, 2001. EITF 99-20 changed the manner in which LNC determined impairment of certain investments including collateralized bond obligations. Upon the adoption of EITF 99-20, LNC recognized a net realized loss on investments of $11.3 million after-tax or $0.06 per share ($17.3 million pre-tax) reported as a cumulative effect of change in accounting principle. In arriving at this amount, deferred acquisition costs of $12.2 million were restored and netted against net realized loss on investments.

Accounting for Derivative Instruments and Hedging Activities. Effective January 1, 2001, LNC adopted Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133) on a prospective basis. The transition adjustments that LNC recorded upon adoption of FAS 133 on January 1, 2001 resulted in a net loss of $4.3 million after-tax or $0.02 per share ($6.6 million pre-tax) recorded in net income, and a net gain of $17.6 million after-tax or $0.09 per share ($27.1 million pre-tax) recorded as a component of Other Comprehensive Income (OCI) in equity. Deferred acquisition costs of $4.8 million were restored and netted against the transition loss on derivatives recorded in net income and deferred acquisition costs of $18.3 million were amortized and netted against the transition gain recorded in OCI. A portion of the transition adjustment ($3.5 million after-tax) recorded in net income upon adoption of FAS 133 was reclassified from the OCI account, Net Unrealized Gain on Securities Available-for-Sale. These transition adjustments were reported in the financial statements as a cumulative effect of a change in accounting principle.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Investments

The amortized cost, gross unrealized gains and losses, and fair value of securities available-for-sale are as follows:

December 31 (in millions)	Amortized Cost	Gains	Losses	Fair Value
2003:				
Corporate bonds	$ 24,305.0	$ 1,736.6	$ (173.1)	$ 25,868.5
U.S. Government bonds	219.0	9.3	(2.5)	225.8
Foreign government bonds	1,153.2	58.0	(16.6)	1,194.6
Asset and mortgage-backed securities:				
Mortgage pass-through securities	469.9	15.3	(1.5)	483.7
Collateralized mortgage obligations	2,434.4	66.9	(9.2)	2,492.1
Commercial Mortgage Backed Securities	1,956.0	119.2	(13.1)	2,062.1
Other asset-backed securities	152.3	5.9	(0.5)	157.7
State and municipal bonds	147.9	5.4	(0.5)	152.8
Redeemable preferred stocks	121.8	10.5	(0.1)	132.2
Total fixed maturity securities	30,959.5	2,027.1	(217.1)	32,769.5
Equity securities	173.5	27.3	(1.7)	199.1
Total	$ 31,133.0	$ 2,054.4	$ (218.8)	$ 32,968.6
2002:				
Corporate bonds	$ 24,703.8	$ 1,876.8	$ (645.9)	$ 25,934.7
U.S. Government bonds	410.8	105.0	(2.3)	513.5
Foreign government bonds	1,063.8	73.2	(26.7)	1,110.3
Asset and mortgage-backed securities:				
Mortgage pass-through securities	711.2	26.5	(1.8)	735.9
Collateralized mortgage obligations	2,100.7	114.7	(0.4)	2,215.0
Commercial Mortgage Backed Securities	1,712.1	139.7	(11.9)	1,839.9
Other asset-backed securities	212.6	12.6	(0.5)	224.7
State and municipal bonds	109.4	5.1	(0.1)	114.4
Redeemable preferred stocks	78.7	1.7	(1.3)	79.1
Total fixed maturity securities	31,103.1	2,355.3	(690.9)	32,767.5
Equity securities	334.5	47.2	(44.5)	337.2
Total	$ 31,437.6	$ 2,402.5	$ (735.4)	$ 33,104.7

Future maturities of fixed maturity securities available-for-sale are as follows:

December 31, 2003 (in millions)	Amortized Cost	Fair Value
Due in one year or less	$ 695.7	706.1
Due after one year through five years	6,924.7	7,324.1
Due after five years through ten years	9,302.7	9,921.3
Due after ten years	9,023.8	9,622.4
Subtotal	25,946.9	27,573.9
Asset and mortgage-backed securities	5,012.6	5,195.6
Total	$ 30,959.5	32,769.5

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The foregoing data is based on stated maturities. Actual maturities will differ in some cases because borrowers may have the right to call or pre-pay obligations.

Par value, amortized cost and estimated fair value of investments in asset and mortgage-backed securities available-for-sale summarized by interest rates of the underlying collateral are as follows:

December 31, 2003 (in millions)	**Par Value**	**Amortized Cost**	**Fair Value**
Below 6%	$ 2,247.0	$ 1,598.8	$ 1,607.2
6%-7%	1,324.9	1,331.1	1,375.9
7% - 8%	1,525.0	1,539.6	1,636.6
Above 8%	550.3	543.1	575.9
Total	$ 5,647.2	$ 5,012.6	$ 5,195.6

The quality ratings for fixed maturity securities available-for-sale are as follows:

December 31, 2003 (in millions except %)	**Fair Value**	**% of Total**
Treasuries and AAA	$ 7,414.3	22.6
AA	2,057.3	6.3
A	9,833.8	30.0
BBB	11,164.0	34.1
BB	1,448.2	4.4
Less than BB	851.9	2.6
Total	$ 32,769.5	100

The major categories of net investment income are as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Fixed maturity securities available-for-sale	$ 2,113.2	$ 2,117.0	$ 2,121.0

Equity securities available-for-sale	12.3	15.4	17.6
Trading securities	46.5		
Mortgage loans on real estate	338.3	356.8	374.5
Real estate	43.9	47.4	49.5
Policy loans	123.2	134.5	125.3
Invested cash	7.8	37.6	68.4
Other investments	48.7	16.3	69.6
Investment revenue	2,733.9	2,725.0	2,825.9
Investment expense	95.4	93.1	117.1
Net investment income	$ 2,638.5	$ 2,631.9	$ 2,708.8

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Trading securities at fair value retained in connection with Modco and CFW reinsurance arrangements, consisted of the following:

December 31 (in millions)	**2003**
Corporate bonds	$ 2,479.2
U.S. Government bonds	287.4
Foreign government bonds	49.1
Asset and mortgage-backed securities:	
Mortgage pass-through securities	18.9
Collateralized mortgage obligations	112.0
Commercial Mortgage Backed Securities	139.7
Other asset-backed securities	9.7
State and municipal bonds	20.2
Redeemable preferred stocks	1.7
Total fixed maturity securities	3,117.9
Equity securities	2.2
Total	$ 3,120.1

The detail of the realized loss on investments and derivative instruments is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Fixed maturity securities available-for-sale			
Gross gain	$ 336.7	$ 171.4	$ 193.0
Gross loss	(356.8)	(586.3)	(435.3)
Equity securities available-for-sale			
Gross gain	27.8	9.8	30.2
Gross loss	(40.1)	(23.6)	(24.4)
Other investments	28.1	23.4	33.7
Associated (amortization)/restoration of deferred acquisition costs and provision for policyholder commitments	(2.4)	145.0	106.8
Investment expenses	(10.0)	(12.4)	(9.2)
Total Investments	(16.7)	(272.7)	(105.2)
Derivative instruments net of associated (amortization)/restoration of deferred acquisition costs	(2.5)	1.2	(9.3)
Total Investments and Derivative Instruments	$ (19.2)	$ (271.5)	$ (114.5)

Provisions (credits) for write-downs and net changes in allowances for loss, which are included in the realized gain (loss) on investments and derivative instruments shown above, are as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Fixed maturity securities available-for-sale	$ 249.4	$ 300.1	$ 237.2
Equity securities available-for-sale	3.4	21.4	15.7
Mortgage loans on real estate	5.6	9.7	(2.7)
Real estate	4.1		0.7
Other long-term investments		6.4	0.9
Guarantees	(0.3)	0.1	
Total	$ 262.2	$ 337.7	$ 251.8

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The portion of market adjustment for trading securities and the corresponding market adjustment for the reinsurance embedded derivative related to trading securities at December 31, 2003 was $334.7 million.

The change in net unrealized gains (losses) on investments in fixed maturity and equity securities available-for-sale is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Fixed maturity securities	$ 145.6	$ 1,274.7	$ 317.0
Equity securities	22.9	(23.4)	(60.8)
Total	$ 168.5	$ 1,251.3	$ 256.2

For total traded and private securities held by LNC at December 31, 2003 that are in unrealized loss status, the fair value, amortized cost, unrealized loss and total time period that the security has been in an unrealized loss position are presented in the table below.

(000s omitted)	**Fair Value**	**% Fair Value**	**Amortized Cost**	**% Amortized Cost**	**Unrealized Loss**	**% Unrealized Loss**
2003						
≤ 90 days	$ 1,975,203	39.8%	$ 1,995,639	38.5%	$ (20,436)	9.3%
> 90 days but ≤ 180 days	1,342,624	27.1%	1,382,841	26.7%	(40,217)	18.4%
> 180 days but ≤ 270 days	536,887	10.8%	565,322	10.9%	(28,435)	13.0%
> 270 days but ≤ 1 year	148,057	3.0%	153,286	3.0%	(5,229)	2.4%
> 1 year	957,206	19.3%	1,081,730	20.9%	(124,524)	56.9%
Total	$ 4,959,977	100.0%	$ 5,178,818	100.0%	$ (218,841)	100.0%

Securities available-for-sale that were deemed to have declines in fair value that were other than temporary were written down to fair value. The fixed maturity securities to which these write-downs apply were generally of investment grade at the time of purchase, but were subsequently downgraded by rating agencies to below-investment grade. Factors considered by LNC in determining whether declines in the fair value of fixed maturity securities are other than temporary include 1) the significance of the decline, 2) LNC s ability and intent to retain the investment for a sufficient period of time for it to recover, 3) the time period during which there has been a significant decline in value, and 4) fundamental analysis of the liquidity, business prospects and overall financial condition of the issuer. Based upon these factors, securities that have indications of potential impairment are subject to intensive review. Where such analysis results in a conclusion that declines in fair values are other than temporary, the security is written down to fair value. See Note 8 (Fair Value of Financial Instruments) to the consolidated financial statements for a general discussion of the methodologies and assumptions used to determine estimated fair values.

The balance sheet captions, Real Estate and Property and Equipment, include allowances for depreciation as follows:

December 31 (in millions)	2003	2002
Real estate	$ 22.0	$ 41.0
Property and equipment	166.9	175.6

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Impaired mortgage loans along with the related allowance for losses are as follows:

December 31 (in millions)	**2003**	**2002**
Impaired loans with allowance for losses	$ 120.2	$ 72.3
Allowance for losses	(17.5)	(11.9)
Impaired loans with no allowance for losses		
Net impaired loans	$ 102.7	$ 60.4

The allowance for losses is maintained at a level believed adequate by LNC to absorb estimated probable credit losses. LNC s periodic evaluation of the adequacy of the allowance for losses is based on LNC s past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay (including the timing of future payments), the estimated value of the underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective, as it requires estimating the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change.

A reconciliation of the mortgage loan allowance for losses for these impaired mortgage loans is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Balance at beginning-of-year	$ 11.9	$ 2.2	$ 4.9
Provisions for losses	16.4	12.7	0.7
Releases due to principal paydowns	(10.8)	(3.0)	(3.4)
Releases due to foreclosures			
Balance at end-of-year	$ 17.5	$ 11.9	$ 2.2

The average recorded investment in impaired mortgage loans and the interest income recognized on impaired mortgage loans were as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Average recorded investment in impaired loans	$ 72.6	$ 54.0	$ 25.0
Interest income recognized on impaired loans	8.1	5.6	3.0

All interest income on impaired mortgage loans was recognized on the cash basis of income recognition.

As of December 31, 2003, LNC had no mortgage loans on non-accrual status compared with $1.8 million at December 31, 2002. As of December 31, 2003 and 2002, LNC had no mortgage loans past due 90 days and still accruing.

As of December 31, 2003 and 2002, LNC had restructured mortgage loans of $63.6 million and $4.6 million, respectively. LNC recorded $4.7 million and $0.4 million of interest income on these restructured mortgage loans in 2003 and 2002, respectively. Interest income in the amount of $5.8 million and $0.4 million would have been recorded on these mortgage loans according to their original terms in 2003 and 2002, respectively. As of December 31, 2003 and 2002, LNC had no outstanding commitments to lend funds on restructured mortgage loans.

As of December 31, 2003, LNC s investment commitments for fixed maturity securities (primarily private placements), mortgage loans on real estate and real estate were $578.2 million. This includes $205.8 million of standby commitments to purchase real estate upon completion and leasing.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The carrying value of fixed maturity securities available-for-sale, mortgage loans on real estate and real estate investments which were non-income producing totaled $133.0 million and $37.3 million at December 31, 2003 and 2002, respectively.

During the fourth quarter of 2001, LNC completed a securitization of commercial mortgage loans. In the aggregate, the loans had a fair value of $209.7 million and a carrying value of $198.1 million. LNC received $209.7 million from the trust for the sale of the loans. A recourse liability was not recorded since LNC is not obligated to repurchase any loans from the trust that may later become delinquent. Servicing fees of $0.2 million and $0.2 million were received in 2003 and 2002, respectively. The transaction was hedged with total return swaps to lock in the value of the loans. LNC recorded a loss on the hedge of $10.1 million pre-tax and a realized gain on the sale of $11.6 million pre-tax resulting in a net gain of $1.5 million pre-tax. Upon securitization, LNC did not retain an interest in the securitized assets; however, LNC later invested $14.3 million of its general account assets in the certificates issued by the trust. This investment is included in fixed maturity securities on the balance sheet.

During the third quarter of 2003, LNC completed a securitization of commercial mortgage loans. In the aggregate, the loans had a fair value of $182.2 million and a carrying value of $167.3 million. LNC received $182.2 million from the trust for the sale of the loans. A recourse liability was not recorded since LNC is not obligated to repurchase any loans from the trust that may later become delinquent. Servicing fees of $0.03 million were received in 2003. The transaction was hedged with interest rate swaps to lock in the value of the loans. LNC recorded a gain on the hedge of $7.8 million pre-tax and realized a gain on the sale of $14.9 million pre-tax resulting in a total net gain of $22.7 million pre-tax. LNC did not retain an interest in the securitized assets.

4. Federal Income Taxes

The Federal income tax expense (benefit) is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Current	$ 30.7	$ (159.2)	$ 495.0
Deferred	249.7	56.5	(350.3)
Total tax expense	$ 280.4	$ (102.7)	$ 144.7

The effective tax rate on pre-tax income from continuing operations is lower than the prevailing corporate Federal income tax rate. A reconciliation of this difference is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**

Tax rate times pre-tax income	$ 366.6	$ (18.8)	$ 247.1
Effect of:			
Tax-preferred investment income	(56.3)	(52.6)	(68.6)
UK taxes	(10.1)	(16.1)	(28.5)
Tax credits	(15.5)	(17.7)	(17.1)
Goodwill			13.2
Other items	(4.3)	2.5	(1.4)
Provision for income taxes	$ 280.4	$ (102.7)	$ 144.7
Effective tax rate	27%	N/M	21%

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The effective tax rate is a ratio of tax expense over pre-tax income. Since the pre-tax income of $(53.8) million resulted in a tax benefit of $102.7 million in 2002, the effective tax rate was not meaningful.

The Federal income tax recoverable asset (liability) is as follows:

December 31 (in millions)	**2003**	**2002**
Current	$ (27.4)	$ 70.0
Deferred	73.3	247.7
Total Federal income tax asset	$ 45.9	$ 317.7

Significant components of LNC s deferred tax assets and liabilities are as follows:

December 31 (in millions)	**2003**	**2002**
Deferred tax assets:		
Insurance and investment contract liabilities	$ 1,188.0	$ 1,268.8
Reinsurance deferred gain	321.6	397.5
Net operating and capital loss carryforwards	150.7	197.2
Modco embedded derivative	124.0	
Postretirement benefits other than pensions	15.5	33.0
Compensation related	114.1	138.5
Ceding commission asset	14.8	16.7
Other	176.3	221.4
Total deferred tax assets	2,105.0	2,273.1
Valuation allowance for deferred tax assets	51.2	51.2
Net deferred tax assets	2,053.8	2,221.9
Deferred tax liabilities:		
Deferred acquisition costs	616.0	540.6
Investment related	256.4	206.0
Net unrealized gain on securities available-for-sale	644.1	602.2
Trading security gains	117.2	
Present value of business in-force	322.6	354.5
Other	24.2	270.9
Total deferred tax liabilities	1,980.5	1,974.2

Net deferred tax asset	$ 73.3	$ 247.7

Net cash received for Federal income taxes in 2003 was $65.0 million due to the carry back of 2002 tax losses. Cash paid for Federal income taxes in 2002 and 2001 was $382.9 million and $57.6 million, respectively.

LNC is required to establish a valuation allowance for any gross deferred tax assets that are unlikely to reduce taxes payable in future years tax returns. At December 31, 2003, LNC believes that it is more likely than not that all gross deferred tax assets will reduce taxes payable in future years except for the amount of the valuation allowance established in 2001. In 2001, LNC established a valuation allowance of $51.2 million for the gross deferred tax asset relating to net operating losses of its foreign life reinsurance subsidiary. The net operating losses of this subsidiary are subject to Federal income tax limitations that only allow the net operating losses to be used to offset future taxable income of the subsidiary. Due to the disposition of its reinsurance operations, LNC believes that it is more likely than not that LNC will not realize all of the tax benefits associated

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

with this subsidiary s net operating losses. Because LNC has been required to defer recognition of the gain on the portion of the disposition of its reinsurance operation that was structured as indemnity reinsurance, the establishment of this valuation allowance was recorded as a decrease in the after-tax amount of the reinsurance deferred gain carried on LNC s consolidated balance sheet.

At December 31, 2003, LNC had net operating loss carryforwards for Federal income tax purposes of $282.6 million for its foreign life reinsurance company, Lincoln National Reinsurance Company (Barbados) (LNR Barbados) that expire in 2014 and 2018. LNC also had net capital loss carryforwards of $147.9 million that will expire in 2007. In contrast to the net operating losses of LNR Barbados, the net capital losses can be used to offset capital gains of any affiliate in future LNC consolidated U.S. tax returns. Accordingly, LNC believes that it is more likely than not that the capital losses will be fully utilized within the allowable carryforward period.

LNC has made the decision not to permanently reinvest earnings in Lincoln National (UK) plc and Investment Management s UK operating subsidiary Delaware Investment Advisers, Ltd. Full U.S. deferred taxes applicable to any un-repatriated earnings have been recorded.

Under prior Federal income tax law, one-half of the excess of a life insurance company s income from operations over its taxable investment income was not taxed, but was set aside in a special tax account designated as Policyholders Surplus. At December 31, 2003, LNC has approximately $196.0 million of untaxed Policyholders Surplus on which no payment of Federal income taxes will be required unless it is distributed as a dividend, or under other specified conditions. Barring the passage of unfavorable tax legislation, LNC does not believe that any significant portion of the account will be taxed in the foreseeable future. Accordingly, no deferred tax liability has been recognized relating to LNC s Policyholders Surplus balance. If the entire Policyholders Surplus balance became taxable at the current Federal rate, the tax would be approximately $68.6 million.

LNC has been identified by the Internal Revenue Service (IRS) as a coordinated industry taxpayer requiring annual audits. The audits from tax years through 1995 have been completed and these years are closed. LNC is currently under audit by IRS for years 1996-2002. LNC does not anticipate that any adjustments that might result from such audits would be material to LNC s consolidated results of operations or financial condition.

5. Supplemental Financial Data

Reinsurance transactions included in the income statement captions, Insurance Premiums and Insurance Fees , are as follows:

Year Ended December 31 (in millions)	**2003***	**2002***	**2001***
Insurance assumed	$ 1.0	$ 1.1	$ 1,425.4
Insurance ceded	250.9	233.1	993.9

Net reinsurance premiums and fees	$ (249.9)	$ 232.0	$ 431.5

* The reinsurance activity for the year ended December 31, 2001 includes the activity of the former Reinsurance segment for the eleven months ended November 30, 2001 and the activity related to the indemnity reinsurance transaction with Swiss Re for the one month ended December 31, 2001. The reinsurance activity for 2003 and 2002 excludes activity related to the indemnity reinsurance transaction with Swiss Re.

The income statement caption, Benefits, is net of reinsurance recoveries of $0.6 billion in each of the years ended December 31, 2003, 2002 and 2001.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A roll forward of the balance sheet account, Deferred Acquisition Costs, is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**
Balance at beginning-of-year	$ 2,970.9	$ 2,885.3
Deferral	658.7	627.3
Amortization	(323.1)	(346.7)
Adjustment related to realized gains (losses) on securities available-for-sale	(50.2)	115.0
Adjustment related to unrealized gains on securities available-for-sale	(126.0)	(338.5)
Foreign currency translation adjustment	62.0	56.9
Other		(28.4)
Balance at end-of-year	$ 3,192.3	$ 2,970.9

Realized gains and losses on investments and derivative instruments on the Statements of Income for the year ended December 31, 2003, 2002 and 2001 are net of amounts restored or (amortized) against deferred acquisition costs of $(50.2) million, $115.0 million and $112.9 million, respectively. In addition, realized gains and losses for the year ended December 31, 2003, 2002 and 2001 are net of adjustments made to policyholder reserves of $48.4 million, $27.3 million and $10.5 million, respectively. LNC has either a contractual obligation or has a consistent historical practice of making allocations of investment gains or losses to certain policyholders and to certain reinsurance arrangements.

Details underlying the income statement caption, Underwriting, Acquisition, Insurance and Other Expenses, are as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Commissions	$ 576.1	$ 579.4	$ 860.3
Other volume related expenses	328.4	256.8	184.8
Operating and administrative expenses	894.4	928.0	1,114.5
Deferred acquisition costs net of amortization	(335.7)	(280.6)	(346.4)
Restructuring charges	53.8	(2.2)	38.0
Goodwill amortization			43.4
Other intangibles amortization	88.2	144.7	125.2
Other	107.1	107.1	121.5
Total	$ 1,712.7	$ 1,733.2	$ 2,141.3

The carrying amount of goodwill by reportable segment as of December 31, is as follows:

(in millions)	2003	2002
Life Insurance Segment	$ 855.1	$ 855.1
Investment Management Segment	300.7	300.7
Lincoln Retirement Segment	64.1	64.1
Lincoln UK Segment	14.8	13.3
Total	$ 1,234.7	$ 1,233.2

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For intangible assets subject to amortization, the total gross carrying amount and accumulated amortization in total and for each major intangible asset class by segment are as follows:

	As of December 31, 2003		As of December 31, 2002	
(in millions)	**Gross Carrying Amount**	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Amortized Intangible Assets:				
Present value of in-force				
Lincoln Retirement Segment	$ 225.0	$ 111.9	$ 225.0	$ 102.3
Life Insurance Segment	1,254.2	445.5	1,254.2	364.1
Lincoln UK Segment**	381.8	107.1	344.2	106.8
Client lists				
Investment Management Segment	103.6	69.7	103.6	61.8
Total	$ 1,964.6	$ 734.2	$ 1,927.0	$ 635.0

** The gross carrying amount and accumulated amortization of the present value of in-force for the Lincoln UK segment changed from December 31, 2002 to December 31, 2003 due to the translation of the balances from British pounds to U.S. dollars based on the prevailing exchange rate as of the balance sheet dates.

The aggregate amortization expense for other intangible assets for the years ended December 31, 2003, 2002 and 2001 was $88.1 million, $144.7 million and $125.2 million, respectively.

Future estimated amortization of other intangible assets is as follows (in millions):

2004 - $81.4	2005 - $79.4	2006 - $76.6
2007 - 78.8	2008 - 77.4	Thereafter 834.0

A reconciliation of the present value of insurance business acquired included in other intangible assets is as follows:

December 31 (in millions)	**2003**	**2002**	**2001**
Balance at beginning of year	$ 1,250.2	$ 1,362.5	$ 1,483.3
Adjustments to balance			(0.7)

Interest accrued on unamortized balance	73.9	81.4	84.5
(Interest rates range from 5% to 7%)			
Amortization	(154.1)	(217.8)	(197.6)
Foreign exchange adjustment	26.5	24.1	(7.0)
Balance at end-of-year	1,196.5	1,250.2	1,362.5
Other intangible assets (non-insurance)	33.9	41.8	50.1
Total other intangible assets at end-of-year	$ 1,230.4	$ 1,292.0	$ 1,412.6

Details underlying the balance sheet caption, Contractholder Funds, are as follows:

December 31 (in millions)	**2003**	**2002**
Premium deposit funds	$ 21,769.3	$ 20,518.8
Undistributed earnings on participating business	155.1	156.7
Other	680.9	610.9
Total	$ 22,605.3	$ 21,286.4

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Details underlying the balance sheet captions related to total debt are as follows:

December 31 (in millions)	**2003**	**2002**
Short-term debt:		
Commercial paper	$ 44.0	$ 141.1
Other short-term notes		11.9
Total short-term debt	44.0	153.0
Long-term debt less current portion:		
7.250% notes payable, due 2005	192.7	192.5
5.25% notes payable, due 2007	255.2	257.2
6.5% notes payable, due 2008	100.1	100.1
6.20% notes payable, due 2011	249.4	249.3
7% notes payable, due 2018	200.2	200.2
9.125% notes payable, due 2024	119.9	119.9
Total long-term debt	1,117.5	1,119.2
Junior subordinated debentures issued to affiliated trusts:		
7.40% (redeemed July 2003)		200.0
5.67% (matured August 2003)		5.0
7.65% due 2050	186.7	187.7
6.75% due 2052	154.6	
Total	341.3	392.7
Total Debt	$ 1,502.8	$ 1,664.9

The U.S. commercial paper outstanding at December 31, 2003 had a weighted average interest rate of 1.2%.

Future maturities of long-term debt are as follows (in millions):

2004	$	2006	$	2008	$ 100
2005	$ 193	2007	$ 250	Thereafter	$ 570.3

LNC also has access to capital from junior subordinated debentures issued to affiliated trusts. Hybrid securities currently outstanding, which combine debt and equity characteristics, were offered through a series of trusts (Lincoln National Capital V and VI). These trusts were formed solely for the purpose of issuing preferred securities and lending the proceeds to LNC. The common securities of these trusts are owned by LNC. The only assets of Lincoln National Capital V and VI are the junior subordinated debentures issued by LNC. Distributions are paid by these trusts to the preferred security holders on a quarterly basis. The principal obligations of these trusts are irrevocably guaranteed by LNC. Upon liquidation of these trusts, the holders of the preferred securities would be entitled to a fixed amount per share plus accumulated and unpaid distributions. LNC reserves the right to: 1) redeem the preferred securities at a fixed price plus accumulated and unpaid distributions and; 2) extend the stated redemption date up to 19 years if certain conditions are met. LNC has determined that the trusts are variable interest entities as defined by FIN 46. Prior to the implementation of FIN 46, LNC consolidated the trusts, which resulted in the elimination of the junior subordinated debentures issued to the affiliated trusts. Upon implementation of FIN 46, LNC no longer consolidates these trusts. The effect of the deconsolidation was not material.

In July 2003 LNC redeemed the $200 million 7.40% Trust Originated Preferred Securities (TOPrS) issued by Lincoln Capital III and guaranteed by LNC. A loss of $3.7 million ($5.6 million pre-tax) related to unamortized issuance costs was reported in 2003 related to the redemption. This expense is included in the income statement caption Interest and debt expense. In September, Lincoln Capital VI, a wholly-owned

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affiliated trust of LNC, issued $150 million of 6.75% Trust Preferred Securities, Series F guaranteed by LNC. The debentures mature September 11, 2052 and can be redeemed for principal plus accrued interest beginning September 11, 2008.

In January 2002, LNC redeemed $100 million 8.35% TOPrS which were issued by Lincoln Capital II in August 1996. In June 2002, LNC issued $250 million 5.25% five-year senior notes. In conjunction with the $250 million debt issue, LNC executed an interest rate swap in the amount of $100 million notional that effectively converted the 5.25% fixed rate coupon on that portion of the bond into LIBOR-based floating rate debt.

In April 2002, a new shelf registration statement was declared effective by the Securities and Exchange Commission. The new shelf registration totaled $1.2 billion (including $402.5 million of registered but unissued securities from previous registration statements). After giving consideration to the $250 million 5.25% five-year senior notes issued in June 2002 and the $150 million retail trust preferred securities issued in September 2003 by Lincoln Capital V, LNC had at December 31, 2003 $800 million remaining under the shelf registration to issue debt securities, preferred stock, common stock, warrants, stock purchase contracts and stock purchase units of LNC and trust preferred securities of two affiliated trusts. The net proceeds from the sale of the securities offered by this shelf registration and the applicable prospectus supplement(s) are expected to be used by LNC for general corporate purposes, including repurchases of outstanding common stock, repayment or redemption of outstanding debt or preferred stock, the possible acquisition of financial services businesses or assets thereof, investment in portfolio assets and working capital needs. See Subsequent Event footnote on page 158.

LNC maintains three revolving credit agreements with a group of domestic and foreign banks totaling $536 million. One agreement, in the amount of $300 million, expires in December 2005 and the second agreement, in the amount of $200 million, expires in February 2007. The Lincoln UK agreement was renewed in January 2004 for $18 million maturing in January 2005. All three agreements provide for interest on borrowings based on various money market indices. Under all three agreements, LNC must maintain senior unsecured long-term debt ratings of at least S&P A- and Moody s A3 or be restricted by an adjusted debt to capitalization ratio. At December 31, 2003, LNC had no outstanding borrowings under the agreements. During 2003, 2002 and 2001, fees paid for maintaining revolving credit agreements amounted to $0.5 million, $0.6 million and $0.7 million, respectively.

Cash paid for interest related to LNC s debt and junior subordinated debentures of affiliated subsidiary trusts for 2003, 2002 and 2001 was $93.5 million, $96.6 million and $123.1 million, respectively.

6. Employee Benefit Plans

Pension and Other Post-retirement Benefit Plans U.S. LNC maintains funded defined benefit pension plans for most of its U.S. employees and, prior to January 1, 1995, most full-time agents. Effective January 1, 2002, the employees pension plan has a cash balance formula. Employees retiring before 2012 will have their benefits calculated under both the old and new formulas and will receive the greater of the two calculations. Employees retiring in 2012 or after will receive benefits under the amended plan. Benefits under the old employees plan are based on total years of service and the highest 60 months of compensations during the last 10 years of employment. Under the amended plan, employees have guaranteed account balances that grow with pay and interest credits each year. The amendment to the employees pension plan resulted in a $27.8 million pre-tax negative unrecognized prior service cost in 2001 that will be evenly recognized over future periods. All benefits applicable to the defined benefit plan for agents were frozen as of December 31, 1994. The plans are funded by contributions to tax-exempt trusts. LNC s funding policy is consistent with the funding requirements of Federal law and regulations. Contributions are intended to provide not only the benefits attributed to service to date, but also those expected to be earned in the future.

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

LNC sponsors three types of unfunded, nonqualified, defined benefit plans for certain U.S. employees and agents: supplemental retirement plans, a salary continuation plan, and supplemental executive retirement plans.

The supplemental retirement plans provide defined benefit pension benefits in excess of limits imposed by Federal tax law.

The salary continuation plan provides certain officers of LNC defined pension benefits based on years of service and final monthly salary upon death or retirement.

The supplemental executive retirement plan provides defined pension benefits for certain executives who became employees of LNC as a result of the acquisition of a block of individual life insurance and annuity business from CIGNA Corporation (CIGNA). Effective January 1, 2000, this plan was amended to freeze benefits payable under this plan. Effective January 1, 2000, a second supplemental executive retirement plan was established for this same group of executives to guarantee that the total benefit payable under the LNC employees defined benefit pension plan benefit formula will be determined using an average compensation not less than the minimum three-year average compensation as of December 31, 1999. All benefits payable from this plan are reduced by benefits payable from the LNC employees defined benefit pension plan.

LNC also sponsors unfunded plans that provide post-retirement medical, dental and life insurance benefits to full-time U.S. employees and agents who, depending on the plan, have worked for LNC 10 years and attained age 55 (60 for agents). Medical and dental benefits are also available to spouses and other dependents of employees and agents. For medical and dental benefits, limited contributions are required from individuals who retired prior to November 1, 1988. Contributions for later retirees, which can be adjusted annually, are based on such items as years of service at retirement and age at retirement. Effective April 1, 2004, the employees post-retirement plan was changed such that employees and agents not attaining age 50 by that date will not be eligible to receive life insurance benefits when they retire. This amendment to the plan resulted in the immediate recognition at the end of 2003 of a one-time curtailment gain of $2.4 million pre-tax. Life insurance benefits for retirees are noncontributory for employees and agents that attain the age of 50 by April 1, 2004 and meet the eligibility requirements at the time they retire; however, these participants can elect supplemental contributory life benefits up to age 70. Effective July 1, 1999, the agents post-retirement plan was changed to require agents retiring on or after that date to pay the full medical and dental premium costs. Beginning January 1, 2002, the employees post-retirement plan was changed to require employees not yet age 50 with five years of service by the end of 2001 to pay the full medical and dental premium cost when they retire. This change in the plan resulted in the immediate recognition at the end of 2001 of a one-time curtailment gain of $11.3 million pre-tax.

On December 1, 2001, Swiss Re acquired LNC s reinsurance business. This transaction resulted in the immediate recognition of a one-time curtailment gain on post-retirement benefits of $6 million pre-tax and additional expense of $1.4 million pre-tax related to pension benefits for a net curtailment gain of $4.6 million pre-tax. This net curtailment gain was included in the realized gain on sale of subsidiaries for the year ended December 31, 2001. Due to the release of the pension obligations on these former LNC employees, there was a $16 million gain in the pension plan that was used to offset prior plan losses.

As discussed in Note 2, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Medicare Act) became law. Beginning in 2006, the Medicare Act provides various alternatives that could result in an offset to some portion of the costs of prescription drug benefits provided to retirees. In January 2004, the staff of the FASB issued Financial Staff Position No. FAS 106-1 (FSP 106-1), which permits a sponsor of a post-retirement health care plan that provides retiree prescription drug benefits to make a one-time election to defer accounting for the effects of the Medicare Act.

LNC has elected to defer accounting for the effects of the Medicare Act. Accordingly, the measures of accumulated post-retirement benefit obligation and periodic post-retirement benefit cost in LNC s financial statements for the year ended December 31, 2003 do not reflect the effects of the Medicare Act.

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Obligations, Funded Status and Assumptions U.S. Plans

Information with respect to U.S. defined benefit plan asset activity and defined benefit plan obligations is as follows:

	Pension Benefits		Other Post-retirement Benefits	
Year Ended December 31 (in millions)	**2003**	**2002**	**2003**	**2002**
Change in plan assets:				
Fair value of plan assets at beginning-of-year	$ 391.8	$ 389.7	$	$
Actual return on plan assets	94.3	(36.2)		
Company contributions	56.6	66.5	5.7	8.0
Administrative expenses	(2.0)	(1.7)		
Benefits paid	(30.2)	(26.5)	(5.7)	(8.0)
Fair value of plan assets at end-of-year	$ 510.5	$ 391.8	$	$
Change in benefit obligation:				
Benefit obligation at beginning-of-year	$ 520.6	$ 474.7	$ 106.5	$ 96.8
Plan amendments				
Service cost	19.5	18.5	1.6	1.5
Interest cost	32.1	31.8	6.0	6.1
Plan participants contributions			1.3	1.4
Special termination benefits	1.4			
Plan curtailment gain			(2.4)	
Actuarial (gains) losses	(14.7)	22.1	(11.1)	8.7
Benefits paid	(30.2)	(26.5)	(5.7)	(8.0)
Benefit obligation at end-of-year	$ 528.7	$ 520.6	$ 96.2	$ 106.5
Underfunded status of the plans	$ (18.2)	$ (128.8)	$ (96.2)	$ (106.5)
Unrecognized net actuarial (gains) losses	48.2	132.0	(1.7)	9.2
Unrecognized prior negative service cost	(17.1)	(20.1)		
Prepaid (accrued) benefit cost	$ 12.9	$ (16.9)	$ (97.9)	$ (97.3)
Weighted-average assumptions as of December 31:				
Weighted-average discount rate	6.50%	6.50%	6.50%	6.50%
Expected return on plan assets	8.25%	8.25%		
Rate of increase in compensation:				
Salary continuation plan	4.00%	5.00%		
All other plans	4.00%	4.00%	4.00%	4.00%

LNC uses a December 31 measurement date for its U. S. pension and post-retirement plans.

The expected return on plan assets for 2003 and 2002 was 8.25%. This rate is initially established at the beginning of the plan year based on the historical rates of return and is reevaluated based on the actual return through an interim date during the current plan year. As there was not a significant variance between the projected actual return for both 2002 and 2003 and the expected return of 8.25%, LNC maintained the expected return at 8.25% for the actuarial valuation calculated at the end of each year.

The calculation of the accumulated post-retirement benefits obligation assumes a weighted-average annual rate of increase in the per capita cost of covered benefits (i.e. health care cost trend rate) of 10.0% for 2003. It further

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

assumes the rate will gradually decrease to 5.0% by 2015 and remain at that level in future periods. The health care cost trend rate assumption has a significant effect on the amounts reported. For example, increasing the assumed health care cost trend rates by one percentage point each year would increase the accumulated post-retirement benefits obligation as of December 31, 2003 and 2002 by $4.8 million and $7.5 million, respectively. The aggregate of the estimated service and interest cost components of net periodic postretirement benefits cost for the year ended December 31, 2003 and 2002 would increase by $0.4 million and $0.6 million, respectively.

Information for U.S. pension plans with accumulated benefit obligations in excess of plan assets is as follows:

	December 31	
(in millions)	**2003**	**2002***
Accumulated benefit obligation	$ 142.9	$ 507.2
Projected benefit obligation	145.2	520.6
Fair value of plan assets	78.2	391.8

* In 2002, all plans had accumulated benefit obligations in excess of plan assets.

Minimum Pension Liability Adjustment

	For the year ended December 31,	
(in millions)	**2003**	**2002**
Increase/(decrease) in minimum pension liability adjustment included in other comprehensive income (after-tax):		
U.S. plans	$ (55.5)	$ 64.8
Non-U.S. plan	12.8	(3.0)
Total	$ (42.7)	$ 61.8

	As of December 31	
	2003	**2002**
Minimum pension liability adjustment included in accumulated other comprehensive income (after-tax)		

U.S. plans	$ 9.3	$ 64.8
Non-U.S. plan	45.8	33.0
Total	$ 55.1	$ 97.8

Components of Net Periodic Pension Cost U.S. Plans

The components of net defined benefit pension plan and post-retirement benefit plan expense are as follows:

	Pension Benefits			Other Postretirement Benefits		
Year Ended December 31 (in millions)	**2003**	**2002**	**2001**	**2003**	**2002**	**2001**
Service cost	$ 20.8	$ 19.0	$ 14.8	$ 1.6	$ 1.5	$ 2.7
Interest cost	32.1	31.8	34.0	6.0	6.1	7.2
Expected return on plan assets	(32.0)	(31.1)	(34.0)			
Amortization of prior service cost	(2.2)	(2.5)	0.4			
Recognized net actuarial (gains) losses	6.7	0.3	0.3	(0.2)	(0.5)	(0.5)
Net periodic benefit expense	$ 25.4	$ 17.5	$ 15.5	$ 7.4	$ 7.1	$ 9.4

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

LNC maintains a defined contribution plan for its U.S. insurance agents. Contributions to this plan are based on a percentage of the agents annual compensation as defined in the plan. Effective January 1, 1998, LNC assumed the liabilities for a non-contributory defined contribution plan covering certain highly compensated former CIGNA agents and employees. Contributions for this plan are made annually based upon varying percentages of annual eligible earnings as defined in the plan. Contributions to this plan are in lieu of any contributions to the qualified agent defined contribution plan. Effective January 1, 2000, this plan was expanded to include certain highly compensated LNC agents. The combined pre-tax expenses for these plans amounted to $3.7 million, $1.0 million and $2.8 million in 2003, 2002 and 2001, respectively. These expenses reflect both LNC s contribution as well as changes in the measurement of LNC s liabilities under these plans.

U.S. Plan Assets

LNC s U.S. pension plan asset allocations at December 31, 2003 and 2002, by asset category are as follows:

Asset Category	2003	2002
Equity securities	61.9%	59.6%
Fixed income securities	30.7	31.9
Real estate	5.6	5.0
Cash and cash equivalents	1.8	3.5
Total	100.0%	100.0%

The primary investment objective of LNC s U.S. defined benefit pension plan is for capital appreciation and income growth, with an emphasis on avoiding undue risk. A secondary objective is for current income. Investments can be made using the following asset classes: both domestic and international equity and fixed income securities, real estate, guaranteed products, venture capital, oil and gas and other asset classes the investment managers deem prudent. A five-year time horizon is utilized, as there are inevitably short-run fluctuations, which will cause variations in investment performance.

Each managed fund is expected to rank in the upper 50% of similar funds over the three and/or five year periods. Managers not meeting criteria will be subject to additional due diligence review and possible termination. The following short-term ranges have been established for weightings in the various asset categories:

Asset Category	Weighting Range

Cash		0-20%
Guaranteed Products		0-20%
Fixed Income		20-80%
Long-term	0-10%	
High-Yield	0-10%	
International/Emerging Markets*	0-10%	
Real Estate		0-20%
Equities		20-80%
Small-cap	0-20%	
International*	0-20%	
Emerging Markets*	0-10%	
Other		0-20%
Total International**		0-25%

The total of domestic cash, domestic fixed income, and domestic equities shall not be less than 50%.

*   Currency exposure can be hedged up to 100%
**   International/Emerging Markets-Fixed Income and Equities

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Within the broad ranges provided above, LNC currently targets asset weightings as follows: 64% equities, 35% fixed income, including real estate, and 1% cash. The performance of the plan and the managed funds are monitored on a quarterly basis to relative to the plan s objectives. The performance of the managed fund is measured against the following indices: S&P 500, EAFE, Russell 2000, NAREIT, Lehman US Universal and Salomon (Citigroup) 90-day T-Bill. LNC reviews this investment policy on an annual basis.

LNC s plan assets are principally managed by LNC s Investment Management segment.

U.S. Plan Cash Flows

LNC expects to contribute between $0 million and $18 million to its qualified U.S. defined benefit pension plans in 2004. In addition, LNC expects to fund approximately $9 million and $6 million in 2004 for benefit payments for its unfunded non-qualified U.S. defined benefit plan and U.S. post-retirement benefit plans, respectively.

Pension Plan Non-U.S. The employees of LNC s primary foreign subsidiary are covered by a defined benefit pension plan. The plan provides death and pension benefits based on final pensionable salary. At December 31, 2003 and 2002, plan assets were under the projected benefit obligations by $79.0 million and $62.7 million, respectively, and were included in other liabilities in LNC s balance sheet. Net pension costs for the foreign plan were $6.8 million, $10.0 million and $7.4 million for 2003, 2002 and 2001, respectively. See above (U.S. plans) for discussion of the minimum pension liability adjustment for the non-U.S. defined benefit pension plan.

401(k), Money Purchase and Profit Sharing Plans. LNC also sponsors contributory defined contribution plans for eligible U.S. employees and agents. These plans include 401(k) plans and effective April 1, 2001, a defined contribution money purchase plan for eligible employees of Delaware Management Holdings, Inc. (Delaware). Prior to April 1, 2001, the defined contribution money purchase plan was structured as a profit sharing plan. LNC s contributions to the 401(k) plans are equal to participant s pre-tax contribution, not to exceed 6% of base pay, multiplied by a percentage, ranging from 50% to 150%, which varies according to certain incentive criteria as determined by LNC s Board of Directors.

LNC s contribution to the defined contribution money purchase plan is equal to 7.5% per annum of a participant s eligible compensation, while its contribution to the previous profit sharing plan of Delaware was equal to an amount, if any, determined in accordance with a resolution of the Board of Directors. Each plan year s contribution is allocated in the proportion that the plan compensation of each eligible participant bears to the total plan compensation of all eligible participants for such plan year. Compensation is defined as all of an eligible participant s plan year earnings and is subject to the limitation of Section 401(a) of the Internal Revenue Code of 1986, as amended. For 2003, 2002, and 2001 the contribution to the defined contribution money purchase plan was based on 7.5% of the eligible compensation for the years ended December 31, 2003 and December 31, 2002 and for the nine-month period ended December 31, 2001, respectively. For the profit sharing plan s fiscal year ended March 31, 2001, the Board issued a resolution authorizing a 15% per annum contribution to the plan. Expense for the 401(k) and profit sharing plans amounted to $36.1 million, $22.6 million and $27.0 million in 2003, 2002 and 2001, respectively.

Deferred Compensation Plans. LNC sponsors contributory deferred compensation plans for certain U.S. employees and agents. Plan participants may elect to defer payment of a portion of their compensation, as defined by the plans. At this point, LNC has not chosen to fund these plans. Plan participants may select from a variety of alternative measures for purposes of calculating the investment return considered attributable to their deferral. Under the terms of these plans, LNC agrees to pay out amounts based upon the alternative measure selected by the participant. Plan participants who are also participants in an LNC 401(k) plan and who have reached the contribution limit for that plan may also elect to defer the additional amounts into the deferred

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

compensation plan. LNC makes matching contributions to these plans based upon amounts placed into the deferred compensation plans by individuals who have reached the contribution limit under the 401(k) plan. The amount of LNC s contribution is calculated in a manner similar to the employer match calculation described in the 401(k) plans section above. Expense for these plans amounted to $28.7 million, $1.7 million and $0.6 million in 2003, 2002 and 2001, respectively. These expenses reflect both LNC s employer matching contributions of $6.4 million, $9.4 million and $6.3 million, as well as increases (decreases) in the measurement of LNC s liabilities under these plans of $22.3 million, $(7.7) million and $(5.7) million for 2003, 2002 and 2001, respectively.

In the fourth quarter of 2001, LNC began investing in a variable annuity contract with investment options that are similar to the investment options within the deferred compensation plan, with the objective of partially mitigating the earnings effects created by changes in the value of LNC s deferred compensation plan liabilities. At December 31, 2001, $50 million had been invested with an additional $10 million invested in June of 2002. The value of the deferred compensation liability and the variable annuity are both marked to market through net income. There is a direct correlation of the movement in value of the variable annuity contract with the movement in value of the equity portion of the deferred compensation liability. Income (expense) for the change in value of the variable annuity contract was $14.7 million, $(12.8) million and $2.8 million in 2003, 2002 and 2001. The value of the variable annuity contract at December 31, 2003, 2002 and 2001 was $64.7 million, $50 million and $52.8 million, respectively.

In the fourth quarter of 1999, LNC modified the terms of the deferred compensation plans to provide that plan participants who selected LNC stock as the measure for their investment return would receive shares of LNC stock in satisfaction of this portion of their deferral. In addition, participants were precluded from diversifying any portion of their deferred compensation plan account that is measured by LNC s stock performance. As a result of these modifications to the plans, ongoing changes in value of LNC s stock no longer affect the expenses associated with this portion of the deferred compensation plans.

In connection with the acquisition of the block of individual life insurance and annuity business from CIGNA, LNC assumed the liability for an unfunded contributory deferred compensation plan covering certain former CIGNA employees and agents. These participants became immediately eligible for the LNC contributory deferred compensation plans, and therefore this plan was frozen as to future deferrals as of January 1, 1998. Effective January 1, 2001, this frozen plan was merged into the LNC contributory deferred compensation plans and the associated expenses for 2003, 2002 and 2001 are included in those plan expenses disclosed above.

The total liabilities associated with these plans were $197.8 million and $161.3 million at December 31, 2003 and 2002, respectively.

Stock-Based Incentive Compensation Plans. LNC has various incentive plans for employees, agents and directors of LNC and its subsidiaries that provide for the issuance of stock options, stock incentive awards, stock appreciation rights, and restricted stock awards. Prior to 2003, these plans were comprised primarily of stock option incentive plans.

Effective January 1, 2003, LNC s stock-based employee compensation plan was revised to provide for performance vesting, and to provide for awards that may be paid out in a combination of stock options, performance shares of LNC stock and cash. This plan replaced the LNC stock option plan; however, the separate stock option incentive plans established by Delaware Investments U.S., Inc. (DIUS) and DIAL Holding Company, Inc. (DIAL) as described below, will continue. Awards under this plan for 2003 consisted of 322,827 10-year LNC stock options, 781,376 performance share units that could result in the issuance of LNC shares, and cash awards. As of December 31, 2003, 204,316 stock options and 708,063 performance share units

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

of these 2003 awards were outstanding. The performance measures that must be met for vesting to occur are established at the beginning of the three year performance period. Certain participants in the plan will select from seven different combinations of stock options, performance shares and or cash in determining the form of their award. Other participants will have their award paid in performance shares.

Total compensation expense for LNC incentive plans involving performance vesting for 2003 was $0.4 million relating to stock options, $6.1 million relating to performance shares, and $0.8 million relating to cash awards. The amount of stock option expense for the performance vesting awards is included in the total LNC stock option expense as discussed below. All expense calculations for performance vesting stock options, performance shares, and performance vesting cash awards that were granted in 2003 have been based upon the current assumption that the actual performance achievement over the three-year performance measurement period will result in target levels of long-term incentive compensation payouts. As the three-year performance period progresses, LNC will continue to refine its estimate of the expense associated with these awards so that by the end of the three-year performance period, LNC s cumulative expense will reflect the actual level of awards that vest.

Stock options awarded under the stock option incentive plans in effect prior to 2003 were granted with an exercise price equal to the market value of LNC stock at the date of grant and, subject to termination of employment, expire 10 years from the date of grant. Such options are transferable only upon death. Options become exercisable in 25% increments over the four-year period following the option grant anniversary date. A reload option feature was added on May 14, 1997. In most cases, persons exercising an option after that date have been granted new options in an amount equal to the number of matured shares tendered to exercise the original option award. The reload options are granted for the remaining term of the related original option and have an exercise price equal to the market value of LNC stock at the date of the reload award. Reload options can be exercised two years after the grant date if the value of the new option has appreciated by at least 25%. The reload feature is not available for options granted after 2002.

Effective January 1, 2003, LNC adopted the fair value recognition method of accounting for its stock option incentive plans under Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (FAS 123), which is considered the preferable accounting method for stock-based compensation. Previously, LNC accounted for its stock option incentive plans using the intrinsic value method of accounting under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25), and related interpretations. For more information, see Note 1.

Information with respect to LNC stock options outstanding at December 31, 2003 is as follows:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding at December 31, 2003	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number Exercisable at December 31, 2003	Weighted-Average Exercise Price

$10 - $20	75,642	0.41	$	19.76	75,642	$ 19.76
21 - 30	4,823,118	4.52		25.19	3,557,646	25.33
31 - 40	2,744,607	5.74		34.40	1,950,085	34.78
41 - 50	7,652,072	4.66		46.86	6,847,477	47.23
51 - 60	1,837,050	8.09		52.11	607,487	52.15
$10 - $60	17,132,489				13,038,337	

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The option price assumptions used for the LNC stock option incentive plans were as follows:

	2003	2002	2001
Dividend yield	4.8%	2.5%	2.8%
Expected volatility	39.4%	39.6%	40.0%
Risk-free interest rate	2.3%	4.5%	4.6%
Expected life (in years)	3.2	4.2	4.2
Weighted-average fair value per option granted	$ 5.88	$ 16.03	$ 13.39

Information with respect to the LNC incentive plans involving stock options is as follows:

	Options Outstanding		Options Exercisable	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Balance at January 1, 2001	20,947,238	$ 34.69	6,715,434	$ 35.05
Granted-original	2,561,883	43.74		
Granted-reloads	130,129	48.19		
Exercised (includes shares tendered)	(3,096,146)	27.24		
Forfeited	(619,596)	44.63		
Balance at December 31, 2001	19,923,508	36.74	9,437,881	37.91
Granted-original	2,154,709	51.67		
Granted-reloads	40,609	49.67		
Exercised (includes shares tendered)	(2,554,776)	31.89		
Forfeited	(956,041)	42.20		
Balance at December 31, 2002	18,608,009	38.89	10,883,053	38.87
Granted-original	417,408	25.57		
Granted-reloads	130,481	33.19		
Exercised (includes shares tendered)	(1,061,447)	25.50		
Forfeited	(961,962)	41.41		
Balance at December 31, 2003	17,132,489	39.21	13,038,337	39.46

Total compensation expense for LNC incentive plans involving stock options, including the Delaware stock option incentive plans discussed below, for 2003, 2002, and 2001 was $51.5 million, $59.9 million, and $63.6 million, respectively.

Delaware Stock Option Incentive Plans: In 2001, Delaware Management Holdings, Inc. (Holdings), through its wholly-owned subsidiaries DIUS and DIAL, established separate stock option incentive plans for its domestic and international personnel, respectively. Stock options awarded under the plans are granted with an exercise price equal to the estimated fair market value per share at the date of the grant, as determined by an outside appraiser, and expire 10 years from the date of the grant, subject to conditions of the plan agreements. Options granted under the DIUS plan become exercisable and vest in 25% increments over the four-year period following the option grant anniversary date. Options granted under the DIAL plan also vest in 25% increments over the four-year period following the option grant anniversary date, however, such options are exercisable immediately. In the event DIAL options are exercised prior to vesting, such stock acquired is restricted from resale until vested under the option terms.

Shares acquired upon exercise, provided they have been held for more than six months and are vested, may be put to Holdings at the most recent determined fair market value per share, subject to the specific terms of

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the plan agreements. Fair market value is determined on a semi-annual basis by the outside appraiser. Additionally, shares acquired upon exercise, provided they have been held for more than six months and are vested, may be called by Holdings, DIUS or DIAL, as applicable, at the most recent determined fair market value per share.

The option price assumptions used for the DIUS and DIAL stock option incentive plans were as follows:

	2003 DIUS	2002 DIUS	2001 DIUS	2003 DIAL	2002 DIAL	2001 DIAL
Dividend yield	2.23%	2.42%	1.95%	5.22%	3.76%	6.01%
Expected volatility	45.0%	50.0%	50.0%	45.0%	50.0%	50.0%
Risk-free interest rate	2.6%	4.1%	4.2%	2.6%	4.3%	4.2%
Expected life (in years)	4.6	4.6	4.6	4.6	4.6	4.6
Weighted-average fair value per option granted	$ 33.37	$ 41.24	$ 41.25	$ 6.92	$ 9.22	$ 7.28

At December 31, 2003, DIUS had 10,000,000 shares of common stock outstanding. Information with respect to the DIUS incentive plan involving stock options is as follows:

	Options Outstanding		Options Exercisable	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Balance at December 31, 2000		$		$
Granted-original	810,796	103.23		
Exercised (includes shares tendered)				
Forfeited				
Balance at December 31, 2001	810,796	103.23		
Granted-original	277,200	107.45		
Exercised (includes shares tendered)				
Forfeited				
Balance at December 31, 2002	1,087,996	104.31	280,877	103.61
Granted-original	277,200	98.71		
Exercised (includes shares tendered)				
Forfeited	(161,256)	104.68		

Balance at December 31, 2003	1,203,940	$ 102.97	427,880	$ 103.75

At December 31, 2003, the range of exercise prices for options outstanding under the DIUS incentive plan involving stock options was $98.71 to $107.45, with a weighted-average remaining contractual life of 8.1 years.

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At December 31, 2003, DIAL had 10,000,000 shares of common stock outstanding. Information with respect to the DIAL incentive plan involving stock options is as follows:

	Options Outstanding		Options Exercisable	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Balance at December 31, 2000		$		$
Granted-original	810,810	25.47		
Exercised (includes shares tendered)				
Forfeited				
Balance at December 31, 2001	810,810	25.47		
Granted-original	277,200	26.62		
Exercised (includes shares tendered)				
Forfeited				
Balance at December 31, 2002	1,088,010	25.76	202,703	25.47
Granted-original	583,579	26.79		
Exercised (includes shares tendered)				
Forfeited	(48,686)	25.82		
Balance at December 31, 2003	1,622,903	$ 26.13	454,750	$ 25.64

At December 31, 2003, the range of exercise prices for options outstanding under the DIAL incentive plan involving stock options was $25.47 to $26.79, with a weighted-average remaining contractual life of 8.3 years.

Stock Appreciation Rights Incentive Plan. LNC has in place a stock appreciation right (SAR) incentive program for agents that do not meet the stringent definition of a common law employee. The SARs under this program are rights on LNC stock that are cash settled and become exercisable in 25% increments over the four year period following the SAR grant date. SARs are granted with an exercise price equal to the market value of LNC stock at the date of grant and, subject to termination of employment, expire five years from the date of grant. Such SARs are transferable only upon death.

LNC recognizes compensation expense for the SAR program based on the fair value method using an option-pricing model. Compensation expense and the related liability are recognized on a straight-line basis over the vesting period of the SARs. The SAR liability is marked-to-market through net income. This accounting treatment causes volatility in net income as a result of changes in the market value of

LNC stock. LNC hedges this volatility by purchasing call options on LNC stock. Call options hedging vested SARs are also marked-to-market through net income. Total compensation expense (income) recognized for the SAR program for 2003, 2002 and 2001 was $6.8 million, $(0.7) million and $4.8 million, respectively. The mark-to-market gain (loss) recognized through net income on the call options on LNC stock for 2003, 2002 and 2001 was $0.3 million, $(6.7) million and $0.8 million, respectively. The SAR liability at December 31, 2003 and 2002 was $9.8 million and $3.7 million, respectively.

Information with respect to the LNC SARs incentive plan at December 31, 2003 is as follows:

	SARs Outstanding			SARs Exercisable	
Range of Exercise Prices	Number Outstanding at December 31, 2003	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number Exercisable at Dec. 31, 2003	Weighted-Average Exercise Price
$20 - $30	731,011	2.50	$ 24.89	266,263	$ 24.72
31 - 40	9,750	3.46	34.41	2,332	36.74
41 - 50	495,288	2.20	43.57	238,384	43.58
51 - 60	363,475	3.20	52.10	90,913	52.10
$20 - $60	1,599,524			597,892	

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The option price assumptions used for the LNC SAR plan were as follows:

	2003	2002	2001
Dividend yield	4.6%	2.7%	2.7%
Expected volatility	35.0%	29.5%	42.0%
Risk-free interest rate	3.3%	5.0%	5.5%
Expected life (in years)	5.0	5.0	5.0
Weighted-average fair value per SAR granted	$ 9.05	$ 10.86	$ 18.84

Information with respect to the LNC incentive plan involving SARs is as follows:

	SARs Outstanding		SARs Exercisable	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Balance at January 1, 2001	751,052	$ 24.94	82,421	$ 24.72
Granted-original	544,205	43.51		
Exercised (includes shares tendered)	(142,785)	24.74		
Forfeited	(27,381)	28.92		
Balance at December 31, 2001	1,125,091	33.85	102,710	25.02
Granted-original	383,675	51.95		
Exercised (includes shares tendered)	(90,818)	28.57		
Forfeited	(35,700)	34.95		
Balance at December 31, 2002	1,382,248	39.20	301,108	32.06
Granted-original	326,650	25.28		
Exercised (includes shares tendered)	(63,224)	24.72		
Forfeited	(46,150)	39.57		
Balance at December 31, 2003	1,599,524	$ 36.92	597,892	$ 36.45

In addition to the stock-based incentives discussed above, LNC has awarded restricted shares of LNC stock, generally subject to a three-year vesting period. Information with respect to LNC Restricted stock (non-vested stock) awarded from 2001 through 2003 was as follows:

	2003	2002	2001
Restricted stock (number of shares)	35,851	71,079	72,155
Weighted-average price per share at time of grant	$ 34.03	$ 35.67	$ 46.60

7. Restrictions, Commitments and Contingencies

Statutory Information and Restrictions

Net income (loss) as determined in accordance with statutory accounting practices for LNC s insurance subsidiaries excluding the insurance subsidiaries sold to Swiss Re in 2001 was $0.237 billion, $(0.159) billion and $0.268 billion for 2003, 2002 and 2001, respectively. On December 7, 2001, Swiss Re acquired LNC s reinsurance operations. The transaction structure involved a series of indemnity reinsurance transactions combined with the sale of certain stock companies that comprised LNC s reinsurance operation. See Note 11 for further discussion of Swiss Re s acquisition of LNC s reinsurance operations. All of LNC s foreign life reinsurance companies were sold to Swiss Re on December 7, 2001 except Lincoln National Reinsurance Company (Barbados) and Lincoln Re (Ireland) Limited. In the second quarter of 2002, LNC exercised a contractual right to put its interest in Lincoln Re (Ireland) Limited to Swiss Re.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Shareholders equity as determined in accordance with statutory accounting practices for LNC s insurance subsidiaries was $3.1 billion and $3.0 billion for December 31, 2003 and 2002, respectively.

LNC s primary insurance subsidiary, The Lincoln National Life Insurance Company (LNL) acquired a block of individual life insurance and annuity business from CIGNA in January 1998 and a block of individual life insurance from Aetna Inc. in October 1998. These acquisitions were structured as indemnity reinsurance transactions. The statutory accounting regulations do not allow goodwill to be recognized on indemnity reinsurance transactions and therefore, the related statutory ceding commission flows through the statement of operations as an expense resulting in a reduction of statutory earned surplus. As a result of these acquisitions, LNL s statutory earned surplus was negative.

LNC s insurance subsidiaries are subject to certain insurance department regulatory restrictions as to the transfer of funds and payment of dividends to the holding company. Generally, these restrictions pose no short-term liquidity concerns for the holding company. As a result of negative statutory earned surplus, LNL was required to obtain the prior approval of the Indiana Insurance Commissioner (Commissioner) before paying any dividends to LNC until its statutory earned surplus became positive. During the first quarter of 2002, LNL received approval from the Commissioner to reclassify total dividends of $495 million paid to LNC in 2001 from LNL s earned surplus to paid-in-capital. This change plus the increase in statutory earned surplus from the disposition of LNC s reinsurance operations through an indemnity reinsurance transaction with Swiss Re resulted in positive statutory earned surplus for LNL at December 31, 2001.

In general, a dividend is not subject to prior approval from the Commissioner provided LNL s statutory earned surplus is positive and the proposed dividend, plus all other dividends made within the twelve consecutive months prior to the date of the proposed dividend, does not exceed the standard limitation of the greater of 10% of total statutory earned surplus or the amount of statutory earnings in the prior calendar year. Dividends of $710 million were paid by LNL to LNC in the second quarter of 2002. These distributions were made in two installments. The first installment of $60 million was paid in April. The second installment of $650 million was paid in June. As both installments exceeded the standard limitation noted above, a special request was made for each payment and each was approved by the Commissioner. Both distributions represented a portion of the proceeds received from the indemnity reinsurance transaction with Swiss Re. As a result of the payment of dividends plus earnings in 2002, LNL s statutory earned surplus was negative as of December 31, 2002. Due to the negative statutory earned surplus as of December 31, 2002, any dividend(s) paid by LNL in 2003 were subject to prior approval from the Commissioner.

Dividends of $200 million were paid by LNL to LNC in three quarterly installments during 2003. A special request was made for each payment and each was approved by the Commissioner. As occurred in 2001, $164.2 million of dividends approved and paid while statutory earned surplus is negative were classified as a reduction to paid-in-capital. Due to statutory earnings and favorable credit markets, LNL expects to be able to pay dividends in 2004 without prior approval.

LNL is recognized as an accredited reinsurer in the state of New York, which effectively enables it to conduct reinsurance business with unrelated insurance companies that are domiciled within the state of New York. As a result, in addition to regulatory restrictions imposed by the state of Indiana, LNL is also subject to the regulatory requirements that the State of New York imposes upon accredited reinsurers.

Reinsurance Contingencies

See Note 11, Acquisitions and Divestitures, for discussion of contingencies surrounding Swiss Re s acquisition of LNC s reinsurance operations on December 7, 2001.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

United Kingdom Selling Practices

Various selling practices of the Lincoln UK segment have come under scrutiny by the U.K. regulators in the last 10 years. These selling practices include the sale and administration of individual pension products, mortgage endowments and the selling practices of City Financial Partners Limited (CFPL), a subsidiary company purchased in December 1997. Regarding the sale and administration of pension products to individuals, regulatory agencies have raised questions as to what constitutes appropriate advice to individuals who bought pension products as an alternative to participation in an employer-sponsored plan. In cases of inappropriate advice, an extensive investigation may have to be done and the individual put in a position similar to what would have been attained if the individual had remained in the employer-sponsored plan.

With regard to mortgage endowments, an agreed upon resolution with regulatory authorities in connection with a subsidiary company resulted in redress payments of about $1.8 million during 2003. Regulatory reviews of other subsidiary companies marketing mortgage endowments are currently in abeyance.

Following allegations made by the U.K. Consumers Association (an organization which acts on behalf of consumers of goods and services provided in the U.K.) concerning various selling practices of CFPL, LNC conducted an internal sample review of ten-year savings plans sold by CFPL during the period September 1, 1998 to August 31, 2000 and, following discussions with the U.K. regulator, it was agreed that LNC would write to all customers with a ten-year savings plan sold by CFPL to determine whether the sales of those policies were appropriate. The agreed upon redress process was concluded in September of 2003, with offers of redress to approximately 5,400 contractholders, and payment of a $762,600 fine for the mis-selling of ten-year savings plans by CFPL covering the period between September 1, 1998 and August 31, 2000.

At December 31, 2003 and 2002, the aggregate liability associated with Lincoln UK selling practices was $25.0 million and $82.2 million, respectively. The decrease in the aggregate liability was a result of redress payments and expenditures partially offset by exchange rate fluctuation. These reserves are based on various assumptions, in particular, the expected level of future complaints. Accordingly, the aggregate liability may prove to be deficient or excessive. However, it is management s opinion that future developments regarding Lincoln UK selling practices will not materially affect the consolidated financial position of LNC.

Marketing and Compliance Issues

Recently, there has been a significant increase in federal and state regulatory activity in the industry relating to numerous issues including market timing and late trading of mutual fund and variable insurance products and broker-dealer access arrangements. LNC, like many others in the industry, has received requests for information from the SEC and a subpoena from the New York Attorney General s Office seeking documentation and other information relating to these issues. LNC is in the process of responding to these requests and continues to cooperate fully with the regulators.

Regulators also continue to focus on replacement and exchange issues. Under certain circumstances companies have been held responsible for replacing existing policies with policies that were less advantageous to the policyholder. LNC s management continues to monitor compliance procedures to minimize any potential liability. Due to the uncertainty surrounding all of these matters, it is not possible to provide a meaningful estimate of the range of potential outcomes; however it is management s opinion that future developments will not materially affect the consolidated financial position of LNC.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Leases

Certain of LNC s subsidiaries lease their home office properties through sale-leaseback agreements. The agreements provide for a 25-year lease period with options to renew for six additional terms of five years each. The agreements also provide LNC with the right of the first refusal to purchase the properties during the terms of the lease, including renewal periods, at a price defined in the agreements. LNC also has the option to purchase the leased properties at fair market value as defined in the agreements on the last day of the initial 25-year lease period ending in 2009 or the last day of any of the renewal periods.

Total rental expense on operating leases in 2003, 2002 and 2001 was $67.1 million, $67.0 million and $79.4 million, respectively. Future minimum rental commitments are as follows (in millions):

2004	$ 61.4	2006	$ 53.0	2008	$ 41.2
2005	58.7	2007	49.8	Thereafter	65.3

Information Technology Commitment

In February 1998, LNL signed a seven-year contract with IBM Global Services for information technology services for the Fort Wayne operations. In February 2004, LNL completed renegotiations and extended the contract through February 2010. Annual costs are dependent on usage but are expected to range from $55.0 million to $60.0 million.

Lincoln UK Outsourcing Agreement

Lincoln UK agreed to outsource its customer and policy administration functions to the Capita Group Plc on August 1, 2002. The contract was originally for a term of 10 years. During 2003, this agreement was converted to an evergreen contract. The annual cost is based on a per policy charge plus an amount for other services provided. The total costs over the next 10 years of the contract are estimated to be $307.5 million and annual costs over the next five years are estimated to decline from $35.2 million to $30.0 million. The amounts quoted are estimates as the actual cost will depend on the number of policies in force and the applicable inflation rate for the period concerned. Lincoln UK or Capita may terminate the contract, subject to the necessary conditions being satisfied, by serving six and 12 months notice, respectively.

Football Stadium Naming Rights Commitment

On June 3, 2002, LNC announced an agreement with the Philadelphia Eagles to name the Eagles new stadium Lincoln Financial Field. In exchange for the naming rights, LNC agreed to pay $139.6 million over a 20-year period, through annual payments to the Eagles which average approximately $6.7 million per year. The total amount includes a maximum annual increase related to the Consumer Price Index (CPI). This future commitment has not been recorded as a liability on LNC s balance sheet as it is being accounted for in a manner consistent with the accounting for operating leases under Statement of Financial Accounting Standards No. 13, Accounting for Leases.

Human Resources Outsourcing Agreement

LNC agreed to outsource its human resources administration functions, including payroll, to IBM on September 29, 2003. The contract is for a term of 10 years and the annual cost is based on per check and per employee charge. The total costs over the life of the contract are estimated to be $46 million and annual costs over the next five years are estimated to decline from $5.3 million to $4.5 million. The actual cost will depend on the number of active employees and the applicable inflation rate for the period concerned.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Insurance Ceded and Assumed

LNC s insurance companies cede insurance to other companies. The portion of risks exceeding each company s retention limit is reinsured with other insurers. LNC seeks reinsurance coverage within the businesses that sell life insurance to limit its liabilities. As of December 31, 2002, LNC s retention policy is to retain no more than $10 million on a single insured life. For 2003, the retention policy was changed to limit retention on new sales to $5 million. Portions of LNC s deferred annuity business have been reinsured on a Modco basis with other companies to limit LNC s exposure to interest rate risks. At December 31, 2003, the reserves associated with these reinsurance arrangements totaled $2.4 billion. To cover products other than life insurance, LNC acquires other insurance coverages with retentions and limits that management believes are appropriate for the circumstances. The accompanying financial statements reflect premiums, benefits and deferred acquisition costs, net of insurance ceded (see Note 5). LNC s insurance companies remain liable if their reinsurers are unable to meet contractual obligations under applicable reinsurance agreements.

Certain LNC insurance companies assume insurance from other companies. At December 31, 2003, LNC s insurance companies provided $84.5 million of statutory surplus relief to other insurance companies under reinsurance transactions. Generally, such amounts are offset by corresponding receivables from the ceding company, which are secured by future profits on the reinsured business. However, LNC s insurance companies are subject to the risk that the ceding company may become insolvent and the right of offset would not be permitted. LNC s reinsurance operations were acquired by Swiss Re on December 7, 2001. The transaction structure involved a series of indemnity reinsurance transactions combined with the sale of certain stock companies that comprised LNC s reinsurance operation. Under the indemnity reinsurance agreements, Swiss Re reinsured certain liabilities and obligations of LNC. Because LNC is not relieved of its legal liability to the ceding companies, the liabilities and obligations associated with the reinsured contracts remain on the balance sheets of LNC with a corresponding reinsurance receivable from Swiss Re.

Letters of Credit

LNC maintains $550 million in bank agreements to issue standby letters of credit on behalf of subsidiaries of LNC and for the benefit of third parties. These letters of credit support LNL s reinsurance needs and specific treaties associated with LNC s reinsurance business, which was acquired by Swiss Re on December 7, 2001 (see Note 11 for further discussion of this transaction). Letters of credit are primarily used to satisfy the U.S. regulatory requirements of domestic clients of the former Reinsurance segment who have contracted with the Reinsurance subsidiaries not domiciled in the United States. The letter of credit allows the cedents to take credit for reinsured reserves on their statutory balance sheets. At December 31, 2003, there was a total of $455.7 million in outstanding bank letters of credit supporting six separate reinsurance treaties.

Vulnerability from Concentrations

LNC s amounts recoverable from reinsurers represents receivables from and reserves ceded to reinsurers. LNC obtains reinsurance from a diverse group of reinsurers and monitors concentration as well as financial strength ratings of LNC s principal reinsurers. LNC s principal reinsurers are strongly rated companies, with Swiss Re representing the largest exposure. As discussed above, LNC sold its reinsurance business to Swiss Re through an indemnity reinsurance arrangement in 2001. Because LNC is not relieved of its liability to the ceding companies for this business, the liabilities and obligations associated with the reinsured contracts remain on the consolidated balance sheet of LNC with a corresponding reinsurance receivable from the business sold to Swiss Re, which totaled $5.1 billion at December 31, 2003, and is included in amounts recoverable from reinsurers. In addition to various remedies that LNC would have in the event of a default by Swiss Re, LNC continues to hold assets in support of certain of the transferred reserves. These assets consist of those reported as trading securities

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and certain mortgage loans. LNC s funds withheld and embedded derivative liabilities include $1.8 billion and $0.3 billion, respectively, related to the business reinsured by Swiss Re.

At December 31, 2003, LNC did not have a material concentration of financial instruments in a single investee or industry. LNC s investments in mortgage loans principally involve commercial real estate. At December 31, 2003, 28.6% of such mortgages, or $1.2 billion, involved properties located in California and Texas. Such investments consist of first mortgage liens on completed income-producing properties and the mortgage outstanding on any individual property does not exceed $37.6 million. Also at December 31, 2003, LNC did not have a concentration of: 1) business transactions with a particular customer or lender; 2) sources of supply of labor or services used in the business or; 3) a market or geographic area in which business is conducted that makes it vulnerable to an event that is at least reasonably possible to occur in the near term and which could cause a severe impact to LNC s financial position.

Although LNC does not have any significant concentration of customers, LNC s Retirement segment has had a long-standing distribution relationship with American Funds Distributors (AFD) that is significant to this segment. Prior to 2003, AFD used wholesalers who focus on both American Funds mutual funds as well as the American Legacy Variable Annuity products. In 2002, LNC and AFD agreed to transition the wholesaling of American Legacy to LFD, which was completed in 2003. The American Legacy Variable Annuity product line sold through LFD accounted for about 17% of LNC s total gross annuity deposits in 2003, compared with about 15% sold through AFD in 2002. In addition, the American Legacy Variable Annuity product line represents approximately 35% and 31% of LNC s total gross annuity account values at December 31, 2003 and 2002, respectively.

Other Contingency Matters

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 ultimately will be resolved without materially affecting the consolidated financial position of LNC.

In 2001, LNL concluded the settlement of all class action lawsuits alleging fraud in the sale of LNL non-variable universal life and participating whole life policies issued between January 1, 1981 and December 31, 1998. Since 2001, LNL has reached settlements with a substantial number of the owners of policies that opted out of the class action settlement. LNL continues to defend a small number of opt out claims and lawsuits. While there is continuing uncertainty about the ultimate costs of settling the remaining opt out cases, it is management s opinion that established reserves are adequate and future developments will not materially affect the consolidated financial position of LNC.

LNC and LNL have pursued claims with their liability insurance carriers for reimbursement of certain costs incurred in connection with the class action settlement and the settlement of claims and litigation brought by owners that opted out of the class action settlement. During the fourth quarter of 2002, LNC and LNL settled their claims against three liability carriers on a favorable basis. LNC and LNL continue to pursue similar claims against a fourth liability insurance carrier.

For discussion of the resolution of legal proceedings related to LNC s sale of its former reinsurance business to Swiss Re, refer to the discussion of Reinsurance Contingencies above.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

State guaranty funds assess insurance companies to cover losses to policyholders of insolvent or rehabilitated companies. Mandatory assessments may be partially recovered through a reduction in future premium taxes in some states. LNC has accrued for expected assessments net of estimated future premium tax deductions.

Guarantees

LNC has guarantees with off-balance-sheet risks whose contractual amounts represent credit exposure. Guarantees with off-balance sheet risks having contractual values of $14.2 million and $22.4 million were outstanding at December 31, 2003 and 2002, respectively.

Certain subsidiaries of LNC have invested in real estate partnerships that use industrial revenue bonds to finance their projects. LNC has guaranteed the repayment of principal and interest on these bonds. Certain subsidiaries of LNC are also involved in other real estate partnerships that use conventional mortgage loans. In case of default by the partnerships, LNC has recourse to the underlying real estate. In some cases, the terms of these arrangements involve guarantees by each of the partners to indemnify the mortgagor in the event a partner is unable to pay its principal and interest payments. These guarantees expire in 2005 through 2008.

In addition, certain subsidiaries of LNC have sold commercial mortgage loans through grantor trusts, which issued pass-through certificates. These subsidiaries have agreed to repurchase any mortgage loans which remain delinquent for 90 days at a repurchase price substantially equal to the outstanding principal balance plus accrued interest thereon to the date of repurchase. In case of default by the partnerships, LNC has recourse to the underlying real estate. It is management s opinion that the value of the properties underlying these commitments is sufficient that in the event of default, the impact would not be material to LNC. These guarantees expire in 2004 through 2009.

Derivative Instruments

LNC maintains 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 risk, equity risk, and credit risk. LNC assesses these risks by continually identifying and monitoring changes in interest rate exposure, foreign currency exposure, equity market exposure, and credit exposure that may adversely impact expected future cash flows and by evaluating hedging opportunities. Derivative instruments that are currently used as part of LNC s interest rate risk management strategy include interest rate swaps and interest rate caps. Derivative instruments that are used as part of LNC s foreign currency risk management strategy include foreign currency swaps and foreign exchange forwards. Call options on LNC stock and financial futures are used as part of LNC s equity market risk management strategy. LNC also uses credit default swaps as part of its credit risk management strategy.

By using derivative instruments, LNC is exposed to credit and market risk. If the counterparty fails to perform, credit risk is equal to the extent of the fair value gain in the derivative. When the fair value of a derivative contract is positive, this generally indicates that the counterparty owes LNC and, therefore, creates a payment risk for LNC. When the fair value of a derivative contract is negative, LNC owes the counterparty and therefore LNC has no payment risk. LNC minimizes the credit (or payment) risk in derivative instruments by entering into transactions with high quality counterparties that are reviewed periodically by LNC. LNC also maintains a policy of requiring that all derivative contracts be governed by an International Swaps and Derivatives Association (ISDA) Master Agreement.

LNC and LNL are required to maintain minimum ratings as a matter of routine practice in negotiating ISDA agreements. Under the majority of ISDA agreements and as a matter of policy, LNL has agreed to maintain

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

financial strength or claims-paying ratings above S&P BBB and Moody s Baa2. A downgrade below these levels would result in termination of the derivatives contract at which time any amounts payable by LNC would be dependent on the market value of the underlying derivative contract. In certain transactions, LNC and the counterparty have entered into a collateral support agreement requiring LNC to post collateral upon significant downgrade. LNC is required to maintain long-term senior debt ratings of S&P BBB- and Moody s Baa3. LNC also requires for its own protection minimum rating standards for counterparty credit protection. LNL is required to maintain financial strength or claims-paying ratings above S&P A- and Moody s A3 under certain ISDA agreements, which collectively do not represent material notional exposure. LNC does not believe the inclusion of termination or collateralization events pose any material threat to its liquidity position.

Market risk is the adverse effect that a change in interest rates, currency rates, implied volatility rates, or a change in certain equity indexes or instruments has on the value of a financial instrument. LNC manages the market risk by establishing and monitoring limits as to the types and degree of risk that may be undertaken.

LNC s derivative instruments are monitored by its risk management committee as part of that committee s oversight of LNC s derivative activities. LNC s derivative instruments committee is responsible for implementing various hedging strategies that are developed through its analysis of financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into LNC s overall risk management strategies.

LNC has derivative instruments with off-balance-sheet risks whose notional or contract amounts exceed the credit exposure. Outstanding derivative instruments with off-balance-sheet risks, shown in notional or contract amounts along with their carrying value and estimated fair values, are as follows:

			Assets (Liabilities)	
	Notional or Contract Amounts		Carrying Value/ Fair Value	Carrying Value/ Fair Value
December 31 (in millions)	**2003**	**2002**	**2003**	**2002**
Interest rate derivative instruments				
Interest rate cap agreements	2,550.0	1,276.8	$ 13.2	$ 4.7
Swaptions		180.0		
Interest rate swap agreements	694.8	701.6	55.4	75.1
Total interest rate derivative instruments	3,244.8	2,158.4	68.6	79.8
Foreign currency derivative instruments				
Foreign exchange forward contracts	15.1	43.0	(0.9)	(1.8)
Foreign currency swaps	17.9	61.5	(1.5)	(2.4)

Total foreign currency derivative instruments	33.0	104.5	(2.4)	(4.2)
Credit derivative instruments				
Credit default swaps	8.0	26.0	0.3	0.9
Equity indexed derivative instruments				
Financial futures	9.0			
Call options (based on LNC stock)	1.5	1.3	16.0	7.4
Total equity indexed derivative instruments	10.5	1.3	16.0	7.4
Embedded derivatives per FAS 133			(352.3)	2.3
Total derivative instruments*	3,296.3	2,290.2	$ (269.8)	$ 86.2

* Total derivative instruments for 2003 are composed of $82.5 million and $(352.3) million on the consolidated balance sheet in Derivative Instruments and Reinsurance Related Derivative Liability, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A reconciliation of the notional or contract amounts for the significant programs using derivative agreements and contracts is as follows:

	Interest Rate Cap Agreements		Swaptions		Interest Rate Swap Agreements	
December 31 (in millions)	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**
Balance at beginning-of-year	1,276.8	1,258.8	180.0	1,752.0	701.6	507.6
New contracts	1,500.0	800.0			260.0	246.6
Terminations and maturities	(226.8)	(782.0)	(180.0)	(1,572.0)	(266.8)	(52.6)
Balance at end-of-year	2,550.0	1,276.8		180.0	694.8	701.6

	Financial Futures		Foreign Exchange Forward Contracts		Foreign Currency Swap Agreements	
December 31 (in millions)	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**
Balance at beginning-of-year		N/A	43.0	67.0	61.5	94.6
New contracts	72.7		64.8	138.6	0.0	
Terminations and maturities	(63.7)		(92.7)	(162.7)	(43.6)	(33.1)
Foreign exchange adjustment				0.1		
Balance at end-of-year	9.0		15.1	43.0	17.9	61.5

	Credit Default Swaps		Call Options (Based on LNC Stock)		Treasury Locks	
December 31 (in millions)	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**
Balance at beginning-of-year	26.0	29.0	1.3	1.1	N/A	
New contracts			0.3	0.3		100.0
Terminations and maturities	(18.0)	(3.0)	(0.1)	(0.1)		(100.0)
Balance at end-of-year	8.0	26.0	1.5	1.3		

Accounting for Derivative Instruments and Hedging Activities

As of December 31, 2003 and 2002, LNC had derivative instruments that were designated and qualified as cash flow hedges, fair value hedges, hedges of a net investment in a foreign operation and derivative instruments that were not designated as hedging instruments. See Note 1 to the consolidated financial statements for detailed discussion of the accounting treatment for derivative instruments. For the year ended December 31, 2003 and 2002, LNC recognized a net loss of $2.0 million after-tax and a net gain of $2.5 million after-tax, respectively, in net income as a component of realized gains and losses on investments and derivative instruments. These gains (losses) relate to the ineffective portion of cash flow hedges, the change in market value for derivative instruments not designated as hedging instruments, and the gain (loss) on swap terminations. For the year ended December 31, 2003 and 2002, LNC recognized a loss of $6.3 million after-tax and a gain of $6.8 million after-tax, respectively, in OCI related to the change in market value on derivative instruments that are designated and qualify as cash flow hedges. In addition, for the year ended December 31, 2001, $3.5 million after-tax was reclassified from unrealized gain (loss) on securities available-for-sale to unrealized gain (loss) on derivative instruments, both in OCI. This reclassification relates to derivative instruments that were marked to market through unrealized gain (loss) on securities available-for-sale prior to the adoption of FAS 133.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivative Instruments Designated in Cash Flow Hedges

Interest Rate Swap Agreements. LNC uses interest rate swap agreements to hedge its 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. LNC is required to pay the counterparty the stream of variable interest payments based on the coupon payments from the hedged bonds, and in turn, receives a fixed payment from the counterparty, at a predetermined interest rate. The net receipts/payments from these interest rate swaps are recorded in net investment income. Gains (losses) on interest rate swaps hedging interest rate exposure on floating rate bond coupon payments are reclassified from accumulated OCI to net income as bond interest is accrued.

LNC also uses interest rate swap agreements to hedge its exposure to interest rate fluctuations related to the forecasted purchase of assets for certain investment portfolios. The gains (losses) resulting from the swap agreements are recorded in OCI. The gains (losses) are reclassified from accumulated OCI to earnings over the life of the assets once the assets are purchased. As of December 31, 2003, there were no interest rate swaps hedging forecasted asset purchases.

Foreign Currency Swaps. LNC uses 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. Gains (losses) on foreign currency swaps hedging foreign exchange risk exposure on foreign currency bond coupon payments are reclassified from accumulated OCI to net income as bond interest is accrued. The foreign currency swaps expire in 2005 through 2006.

Call Options on LNC Stock. LNC uses call options on LNC stock to hedge the expected increase in liabilities arising from stock appreciation rights (SARs) granted on LNC stock. Upon option expiration, the payment, if any, is the increase in LNC s stock price over the strike price of the option applied to the number of contracts. Call options hedging vested SARs are not eligible for hedge accounting and both are marked to market through net income. Call options hedging nonvested SARs are eligible for hedge accounting and are accounted for as cash flow hedges of the forecasted vesting of SAR liabilities. To the extent that the cash flow hedges are effective, changes in the fair value of the call options are recorded in accumulated OCI. Amounts recorded in OCI are reclassified to net income upon vesting of SARs. LNC s call option positions will be maintained until such time the SARs are either exercised or expire and LNC s SAR liabilities are extinguished. The SARs expire five years from the date of grant.

Treasury Lock. LNC used treasury lock agreements to hedge its exposure to variability in future semi-annual interest payments, attributable to changes in the benchmark interest rate, related to the issuance of its 10-year $250 million senior debt in 2001 and its 5-year $250 million senior debt in 2002. A treasury lock is an agreement that allows the holder to lock in a benchmark interest rate, so that if the benchmark interest rate increases, the holder is entitled to receive a payment from the counterparty to the agreement equal to the present value of the difference in the benchmark interest rate at the determination date and the locked-in benchmark interest rate. If the benchmark interest rate decreases, the holder must pay the counterparty to the agreement an amount equal to the present value of the difference in the benchmark interest rate at the determination date and the locked-in benchmark interest rate. The receipt (payment) from the termination of a treasury lock is recorded in OCI and is reclassified from accumulated OCI to interest expense over the coupon-paying period of the related senior debt.

Total Return Swaps. LNC used total return swaps to hedge its exposure to interest rate and spread risk resulting from the forecasted sale of assets in a securitization of certain LNC mortgage loans in 2001. A total return swap is an agreement that allows the holder to protect itself against loss of value by effectively transferring

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the economic risk of asset ownership to the counterparty. The holder pays (receives) the total return equal to interest plus capital gains or losses on a referenced asset and receives a floating rate of interest. As of December 31, 2003, LNC did not have any open total return swaps.

Gains and losses on derivative contracts are reclassified from accumulated OCI to current period earnings. As of December 31, 2003, $19.3 million of the deferred net gains on derivative instruments accumulated in OCI are expected to be reclassified as earnings during the next twelve months. This reclassification is primarily due to the receipt of interest payments associated with variable rate securities and forecasted purchases, payment of interest on LNC s senior debt, the receipt of interest payments associated with foreign currency securities, and the periodic vesting of SARs.

Derivative Instruments Designated in Fair Value Hedges

Interest Rate Swap Agreements. LNC uses interest rate swap agreements to hedge the risk of paying a higher fixed rate interest on junior subordinated debentures issued to affiliated trusts and on senior debt than would be paid on long-term debt based on current interest rates in the marketplace. LNC is required to pay the counterparty a stream of variable interest payments based on the referenced index, and in turn, receives a fixed payment from the counterparty, at a predetermined interest rate. The net receipts/payments from these interest rate swaps are recorded as an adjustment to the interest expense related to the debt being hedged. The changes in fair value of the interest rate swap are reported in the consolidated statement of income in the period of change along with the offsetting changes in fair value of the debt being hedged.

Derivative Instruments Designated in Net Investment in a Foreign Operation

Foreign Currency Forward Contract. LNC uses foreign currency forward contracts to hedge a portion of its net investment in its foreign subsidiary, Lincoln UK. The foreign currency forward contracts obligate LNC to deliver a specified amount of currency at a future date at a specified exchange rate. All gains or losses on the foreign currency forward contracts are recorded in OCI and remain in accumulated OCI until such time that Lincoln UK is sold or liquidated. The foreign currency forward contracts outstanding at December 31, 2003 terminate in 2004.

All Other Derivative Instruments

LNC uses various other derivative instruments for risk management purposes that either do not qualify for hedge accounting treatment or have not currently been qualified by LNC for hedge accounting treatment. The gain or loss related to the change in market value for these derivative instruments is recognized in current income during the period of change (reported as realized gain (loss) on investments in the consolidated statements of income except where otherwise noted below).

Financial Futures. LNC uses financial futures contracts to hedge the liability exposure on certain options in variable annuity products. These contracts obligate LNC to buy or sell a financial instrument at a specified future date for a specified price. They may be settled in cash or through delivery of the financial instrument. Cash settlements on the change in market value of financial futures contracts along with the resulting gains and losses are recorded daily in net income. The open positions at December 31, 2003, all expire in 2004.

Interest Rate Swap Agreements. LNC used a forward starting interest rate swap agreement to hedge its exposure to the forecasted sale of mortgage loans. LNC was required to pay the counterparty a predetermined fixed stream of payments, and in turn, received payments based on a floating rate from the counterparty. The net receipts/payments from these interest rate swaps were recorded in realized gain (loss) on investments and derivative instruments. As of December 31, 2003, there were no forward starting interest rate swap agreements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Interest Rate Cap Agreements. The interest rate cap agreements, which expire in 2006 through 2008, entitle LNC 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. The purpose of LNC s interest rate cap agreement program is to provide a level of protection for its annuity line of business from the effect of rising interest rates. The interest rate cap agreements provide an economic hedge of the annuity line of business. However, the interest rate cap agreements are not linked to assets and liabilities on the balance sheet that meet the significantly increased level of specificity required under FAS 133. Therefore, the interest rate cap agreements do not qualify for hedge accounting under FAS 133.

Swaptions. Swaptions entitled LNC to receive settlement payments from the counterparties on specified expiration dates, contingent on future interest rates. For each swaption, the amount of such settlement payments, if any, were determined by the present value of the difference between the fixed rate on a market rate swap and the strike rate multiplied by the notional amount. The purpose of LNC s swaption program was to provide a level of protection for its annuity line of business from the effect of rising interest rates. The swaptions provided an economic hedge of the annuity line of business. However, the swaptions were not linked to specific assets and liabilities on the balance sheet that met the significantly increased level of specificity required under FAS 133. Therefore, the swaptions did not qualify for hedge accounting under FAS 133. At December 31, 2003, there were no outstanding swaptions.

Foreign Exchange Forwards. LNC s foreign affiliate, Lincoln UK, used foreign exchange forward contracts, which are traded over-the-counter, to hedge short-term debt issuance in currencies other than the British Pound until Lincoln UK terminated their commercial paper program in the second quarter of 2002. The foreign currency forward contracts obligate LNC to deliver a specified amount of currency at a future date at a specified exchange rate. The foreign exchange forward contracts were marked to market through interest and debt expense within the income statement.

Credit Default Swaps. LNC uses credit default swaps which expire in 2006 to hedge against a drop in bond prices due to credit concerns of certain bond issuers. A credit swap allows LNC to put the bond back to the counterparty at par upon a credit event by the bond issuer. A credit event is defined as bankruptcy, failure to pay, or obligation acceleration. LNC has not currently qualified credit default swaps for hedge accounting under FAS 133 as amounts are insignificant.

Call Options on LNC Stock. As discussed previously in the Cash Flow Hedges section, LNC uses call options on LNC stock to hedge the expected increase in liabilities arising from SARs granted on LNC stock. Call options hedging vested SARs are not eligible for hedge accounting treatment under FAS 133. Mark to market changes are recorded in net income.

Derivative Instrument Embedded in Deferred Compensation Plan. LNC has 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. This derivative instrument is not eligible for hedge accounting treatment under FAS 133.

Call Options on Bifurcated Remarketable Put Bonds. LNC owns various debt securities that contain call options attached by an investment banker before the sale to the investor. These freestanding call options are exercisable by a party other than the issuer of the debt security to which they are attached and are accounted for separately from the debt security. LNC has not currently qualified call options bifurcated from remarketable put bonds for hedge accounting treatment as amounts are insignificant.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivative Instrument Embedded in Modified Coinsurance and Coinsurance with Funds Withheld Arrangements. LNC is involved in various Modco and CFW reinsurance arrangements that have embedded derivatives. The change in fair value of the embedded derivative, as well as the gains or losses on trading supporting these arrangements, flows through net income. This embedded derivative is not eligible for hedge accounting treatment under FAS 133.

LNC has used certain other derivative instruments in the past for hedging purposes. Although other derivative instruments may have been used in the past, any derivative type that was not outstanding from January 1, 2002 through December 31, 2003 is not discussed in this disclosure. Other derivative instruments LNC has used include spread-lock agreements and put options. At December 31, 2003, there are no outstanding positions in these derivative instruments.

Additional Derivative Information. Income and (expenses) for the agreements and contracts described above amounted to $28.6 million, $23.0 million and $3.5 million in 2003, 2002 and 2001, respectively. The increase in income for 2002 and 2003 was primarily because of payments received on interest rate swaps.

LNC is exposed to credit loss in the event of nonperformance by counterparties on various derivative contracts. However, LNC does not anticipate nonperformance by any of the counterparties. The credit risk associated with such agreements is minimized by purchasing such agreements from financial institutions with long-standing, superior performance records. 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 LNC s favor. At December 31, 2003, the exposure was $85.3 million.

8. Fair Value of Financial Instruments

The following discussion outlines the methodologies and assumptions used to determine the estimated fair value of LNC s financial instruments. Considerable judgment is required to develop these fair values. 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 LNC s financial instruments.

Fixed Maturity and Equity Securities Available-for-Sale and Trading Securities. Fair values for fixed maturity securities are based on quoted market prices, where available. For fixed maturity securities not actively traded, fair values are estimated using values obtained from independent pricing services. In the case of private placements, fair values are estimated by discounting expected future cash flows using a current market rate applicable to the coupon rate, credit quality and maturity of the investments. The fair values for equity securities are based on quoted market prices.

Mortgage Loans on Real Estate. The estimated fair value of mortgage loans on real estate was 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, caliber of tenancy, borrower and payment record. Fair values for impaired mortgage loans are based on: 1) the present value of expected future cash flows discounted at the loan s effective interest rate; 2) the loan s market price or; 3) the fair value of the collateral if the loan is collateral dependent.

Policy Loans. The estimated fair value of investments in policy loans was calculated on a composite discounted cash flow basis using Treasury interest rates consistent with the maturity durations assumed. These durations were based on historical experience.

Derivative Instruments. LNC employs several different methods for determining the fair value of its derivative instruments. Fair values for these contracts are based on current settlement values. These values are

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

based on: 1) quoted market prices for foreign currency exchange contracts and financial futures contracts; 2) industry standard models that are commercially available for interest rate cap agreements, swaptions, spread-lock agreements, interest rate swaps, commodity swaps, credit default swaps, total return swaps and put options; 3) Monte Carlo techniques for the equity call options on LNC stock. These techniques project cash flows of the derivatives using current and implied future market conditions. The cash flows are then present valued to arrive at the derivatives current fair market values; and 4) Black-Scholes pricing methodology for standard European equity call options.

Other Investments, and Cash and Invested Cash. The carrying value for assets classified as other investments, and cash and invested cash in the accompanying balance sheets approximates their fair value. Other investments include limited partnership investments which are accounted for using the equity method of accounting.

Investment Type Insurance Contracts. The balance sheet captions, Insurance Policy and Claims Reserves and Contractholder Funds, include investment type insurance contracts (i.e., deposit contracts and certain guaranteed interest contracts). The fair values for the deposit contracts and certain guaranteed interest contracts are based on their approximate surrender values. The fair values for the remaining guaranteed interest and similar contracts are estimated using discounted cash flow calculations. 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.

The remainder of the balance sheet captions, Insurance Policy and Claims Reserves and Contractholder Funds that do not fit the definition of investment type insurance contracts are considered insurance contracts. Fair value disclosures are not required for these insurance contracts and have not been determined by LNC. It is LNC s position that the disclosure of the fair value of these insurance contracts is important because readers of these financial statements could draw inappropriate conclusions about LNC s shareholders equity determined on a fair value basis. It could be misleading if only the fair value of assets and liabilities defined as financial instruments are disclosed. LNC and other companies in the insurance industry are monitoring the related actions of the various rule-making bodies and attempting to determine an appropriate methodology for estimating and disclosing the fair value of their insurance contract liabilities.

Short-term and Long-term Debt. Fair values for long-term debt issues are based on quoted market prices or estimated using discounted cash flow analysis based on LNC s current incremental borrowing rate for similar types of borrowing arrangements where quoted prices are not available. For short-term debt, the carrying value approximates fair value.

Junior Subordinated Debentures Issued to Affiliated Trusts. Fair values for junior subordinated debentures issued to affiliated trusts are based on quoted market prices.

Guarantees. LNC s guarantees include guarantees related to industrial revenue bonds, real estate partnerships and mortgage loan pass-through certificates. Based on historical performance where repurchases have been negligible and the current status of the debt, none of the loans are delinquent and the fair value liability for the guarantees related to the industrial revenue bonds, real estate partnerships and mortgage loan pass-through certificates is insignificant.

Investment Commitments. Fair values for commitments to make investments in fixed maturity securities (primarily private placements), mortgage loans on real estate and real estate are based on the difference between the value of the committed investments as of the date of the accompanying balance sheets and the commitment date. These estimates take into account changes in interest rates, the counterparties credit standing and the remaining terms of the commitments.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Separate Accounts. Assets held in separate accounts are reported in the accompanying consolidated balance sheets at fair value. The related liabilities are also reported at fair value in amounts equal to the separate account assets.

The carrying values and estimated fair values of LNC s financial instruments are as follows:

	2003		2002	
December 31 (in millions)	**Carrying Value**	**Fair Value**	**Carrying Value**	**Fair Value**
Assets (liabilities):				
Securities available-for-sale				
Fixed maturities	$ 32,769.5	$ 32,769.5	$ 32,767.5	$ 32,767.5
Equity	199.1	199.1	337.2	337.2
Trading securities	3,120.1	3,120.1		
Mortgage loans on real estate	4,195.0	4,556.0	4,205.5	4,678.8
Policy loans	1,924.4	2,029.9	1,945.6	2,117.3
Derivatives Instruments*	(269.9)	(269.9)	86.2	86.2
Other investments	374.2	374.2	378.1	378.1
Cash and invested cash	1,711.2	1,711.2	1,690.5	1,690.5
Investment type insurance contracts:				
Deposit contracts and certain guaranteed interest contracts	(21,204.4)	(21,295.9)	(20,016.7)	(20,250.1)
Remaining guaranteed interest and similar contracts	(86.7)	(91.2)	(120.5)	(128.2)
Short-term debt	(44.0)	(44.0)	(153.0)	(153.0)
Long-term debt	(1,117.5)	(1,210.9)	(1,119.2)	(1,186.7)
Junior subordinated debentures issued to affiliated trusts	(341.3)	(342.2)	(392.7)	(387.9)
Guarantees	(0.1)		(0.4)	
Investment commitments		0.2		0.9

* Total derivative instruments for 2003 are composed of $82.5 million and $352.3 million on the consolidated balance sheet in Derivative Instruments and Reinsurance Related Embedded Derivative, respectively.

As of December 31, 2003 and 2002, the carrying value of the deposit contracts and certain guaranteed contracts is net of deferred acquisition costs of $448.6 million and $486.0 million, respectively, excluding adjustments for deferred acquisition costs applicable to changes in fair value of securities. The carrying values of these contracts are stated net of deferred acquisition costs so that they are comparable with the fair value basis.

9. Segment Information

LNC has four business segments: Lincoln Retirement, Life Insurance, Investment Management and Lincoln UK. Prior to the fourth quarter of 2001, LNC had a Reinsurance segment. LNC s reinsurance business was acquired by Swiss Re in December 2001. As the majority of the business acquired by Swiss Re was via indemnity reinsurance agreements, LNC is not relieved of its legal liability to the ceding companies for this business. This means that the liabilities and obligations associated with the reinsured contracts remain on the balance sheets of LNC with a corresponding reinsurance receivable from Swiss Re. In addition, the gain resulting from the indemnity reinsurance portion of the transaction was deferred and is being amortized into earnings at the rate that earnings on the reinsured business are expected to emerge, over a period of 15 years. The ongoing management of the indemnity reinsurance contracts and the reporting of the deferred gain are within LNC s

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Other Operations. Given the lengthy period of time over which LNC will continue to amortize the deferred gain, and the fact that related assets and liabilities will continue to be reported on LNC s financial statements, the historical results for the Reinsurance segment prior to the close of the transaction with Swiss Re are not reflected in discontinued operations, but as a separate line in Other Operations. The results for 2001 related to the former Reinsurance segment are for the eleven months ended November 30, 2001.

The Lincoln Retirement segment, with principal operations in Fort Wayne, Indiana, provides tax-deferred investment growth and lifetime income opportunities for its clients through the manufacture and sale of fixed and variable annuities. Through a broad-based distribution network, Lincoln Retirement provides an array of annuity products to individuals and employer-sponsored groups in all 50 states of the United States. Lincoln Retirement distributes some of its products through LNC s wholesaling unit, Lincoln Financial Distributors (LFD), as well as LNC s retail unit, Lincoln Financial Advisors (LFA). In addition, Lincoln Retirement has alliances with a variety of unrelated companies where LNC provides the manufacturing platform for annuity products and the alliance company provides investment management, marketing and distribution.

The Life Insurance segment, with principal operations in Hartford, Connecticut, focuses on the creation and protection of wealth for its clients through the manufacture and sale of life insurance products throughout the United States. The Life Insurance segment offers, through its Hartford operations, universal life, variable universal life, interest-sensitive whole life, corporate owned life insurance and linked-benefit life (a universal life product with a long-term care benefit). In addition, it offers term life insurance through its Schaumburg, Illinois operations. The Life Insurance segment s products are primarily distributed through LFD and LFA.

The Investment Management segment, with principal operations in Philadelphia, Pennsylvania, offers a variety of asset management services to retail and institutional clients throughout the United States and certain foreign countries. Its product offerings include mutual funds and managed accounts. It also provides investment management and account administration services for variable annuity products, 401(k), 529 college savings plans, pension, endowment, trust, and other institutional accounts. Retail products are primarily marketed by LFD through financial intermediaries including LFA. Institutional products, asset management products, are marketed by a separate sales force within Delaware, which works closely with pension consultants.

Lincoln UK s principal operations are in Barnwood, Gloucester, England, and it is licensed to do business throughout the United Kingdom (UK). Lincoln UK manages, administers and accepts new deposits on its current block of business and accepts new business for certain products. Lincoln UK s product portfolio principally consists of unit-linked life and pension products, which are similar to U.S. produced variable life and annuity products.

LNC reports operations of LFA and LFD and the operations not directly related to the business segments and unallocated corporate items (i.e., corporate investment income, interest expense on corporate debt, unallocated overhead expenses, and the amortization of the gain on the sale of reinsurance business) in Other Operations. As noted above, the financial results of the former Reinsurance segment were moved to Other Operations upon the close of the transaction with Swiss Re in December 2001.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Financial data by segment for 2001 through 2003 is as follows:

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Revenue, Excluding Net Investment Income and Certain Other Items*:			
Lincoln Retirement	$ 501.4	$ 528.1	$ 634.0
Life Insurance	995.0	982.6	987.3
Investment Management (1)	424.1	368.0	401.4
Lincoln UK	210.4	213.2	213.4
Other Operations	538.7	526.7	1,874.7
Consolidating adjustments	(380.5)	(335.1)	(339.9)
Total	2,289.1	2,283.5	3,770.9
Net Investment Income:			
Lincoln Retirement	1,483.7	1,457.5	1,399.1
Life Insurance	911.1	899.1	910.2
Investment Management	49.9	50.5	53.6
Lincoln UK	64.1	62.1	64.8
Other Operations	133.2	168.6	292.1
Consolidating adjustments	(3.5)	(6.0)	(11.1)
Total	2,638.5	2,631.8	2,708.7
Other Items*:			
Lincoln Retirement	69.7	(197.8)	(64.8)
Life Insurance	(0.6)	(96.7)	(56.9)
Investment Management	0.4	(5.4)	(3.7)
Lincoln UK	(1.1)	1.9	12.4
Other Operations	287.9	15.0	9.8
Consolidating adjustments		3.2	1.6
Total	356.3	(279.8)	(101.6)
Income (Loss) before Federal Income Taxes and Cumulative Effect of Accounting Changes:			
Lincoln Retirement	463.0	(5.5)	306.5
Life Insurance	365.4	294.3	364.0
Investment Management	34.6	(0.9)	(3.2)
Lincoln UK	64.5	34.3	59.2
Other Operations	120.0	(379.2)	(22.2)
Consolidating adjustments		3.2	1.6
Total	1,047.5	(53.8)	705.9

* Other Items include Realized Gain (Loss) on Investments and Derivative Instruments, Sale of Subsidiaries, Market Adjustment on Trading Securities, and Market Adjustment for Reinsurance Embedded Derivative/Trading Securities

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Year Ended December 31 (in millions)	**2003**	**2002**	**2001**
Income Tax Expense (Benefit):			
Lincoln Retirement	$ 98.9	$ (59.2)	$ 34.1
Life Insurance	113.9	88.1	129.2
Investment Management	4.5	0.5	5.6
Lincoln UK	21.6	(3.4)	(7.6)
Other Operations	41.5	(129.7)	(17.2)
Consolidating adjustments		1.1	0.6
Total	280.4	(102.6)	144.7
Cumulative Effect of Accounting Changes:			
Lincoln Retirement	(63.6)		(7.3)
Life Insurance	0.6		(5.5)
Investment Management			(0.1)
Lincoln UK			
Other Operations	(192.2)		(2.7)
Consolidating adjustments			
Total	(255.2)		(15.6)
Net Income (Loss):			
Lincoln Retirement	300.5	53.7	265.1
Life Insurance	252.1	206.1	229.3
Investment Management	30.2	(1.4)	(8.9)
Lincoln UK	42.9	37.7	66.8
Other Operations	(113.8)	(249.4)	(7.8)
Consolidating adjustments		2.1	1.1
Total	$ 511.9	$ 48.8	$ 545.6

December 31 (in millions)	**2003**	**2002**	**2001**
Assets:			
Lincoln Retirement	$ 61,657.9	$ 52,896.4	$ 56,888.2
Life Insurance	21,239.8	19,591.6	18,409.7
Investment Management	1,561.1	1,461.4	1,460.5
Lincoln UK	8,684.7	7,327.1	7,788.8
Other Operations	15,090.1	13,951.5	15,582.7
Consolidating adjustments	(1,488.7)	(2,043.4)	(2,088.3)
Total	$ 106,744.9	$ 93,184.6	$ 98,041.6

(1) Revenues for the Investment Management segment include inter-segment revenues for asset management services provided to the other segments of LNC. These inter-segment revenues totaled $101.2 million, $97.7 million and $105.0 million for 2003, 2002 and 2001, respectively.

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Most of LNC s foreign operations are conducted by Lincoln UK. The data for this company is shown above under the Lincoln UK segment heading. The other segments, except for the Lincoln Retirement segment, have non-U.S. operations. Foreign intracompany revenues are not significant. Financial data for Lincoln UK and the other non-U.S. units* is as follows:

Year Ended December 31 (in millions)	2003	2002	2001
Revenue	$ 335.0	$ 326.8	$ 392.7
Net Income before Federal Income Taxes	78.7	39.1	101.4
Income Tax Expense (Benefit)	18.9	(14.6)	(19.2)
Net Income	$ 59.8	$ 53.7	$ 120.6
Assets (at end of year)	$ 8,745.4	$ 7,394.9	$ 7,890.5

* The financial data for other non-U.S. units includes the activity of several former reinsurance subsidiaries for the eleven months ended November 30, 2001. These entities were sold to Swiss Re in December 2001.

10. Shareholders Equity

LNC s common and series A preferred stocks are without par value.

All of the issued and outstanding series A preferred stock is $3 cumulative convertible and is convertible at any time into shares of common stock. The conversion rate is sixteen shares of common stock for each share of series A preferred stock, subject to adjustment for certain events. The series A preferred stock is redeemable at the option of LNC at $80 per share plus accrued and unpaid dividends. Outstanding series A preferred stock has full voting rights, subject to adjustment if LNC is in default as to the payment of dividends. If LNC is liquidated or dissolved, holders of series A preferred stock will be entitled to payments of $80 per share. The difference between the aggregate preference on liquidation value and the financial statement balance for the series A preferred stock was $0.8 million at December 31, 2003.

LNC has outstanding one common share purchase (Right) on each outstanding share of LNC s common stock. A Right will also be issued with each share of LNC s common stock that is issued before the Rights become exercisable or expire. If a person or group announces an offer that would result in beneficial ownership of 15% or more of LNC s common stock, the Rights will become exercisable and each Right will entitle its holder to purchase one share of LNC s common stock for $100. Upon the acquisition of 15% or more of LNC s common stock, each holder of a Right (other than the person acquiring the 15% or more) will have the right to acquire the number of shares of LNC common stock that have a market value of two times the exercise price of the Right. If LNC is acquired in a business combination transaction in which LNC does not survive, each holder of a Right (other than the acquiring person) will have the right to acquire common stock of the acquiring person having a market value of two times the exercise price of the Right. LNC can redeem each Right for one cent at any time prior to the tenth day after a person or group has acquired 15% or more of LNC s common stock. The Rights expire on November 14, 2006. As of December 31, 2003, there were 178,212,455 Rights outstanding.

During 2002 and 2001, LNC purchased and retired 12,088,100 and 11,278,022 shares, respectively, of its common stock at a total cost of $474.5 million and $503.7 million, respectively. There were no repurchases in 2003. The common stock account was reduced for these purchases in proportion to the percentage of shares acquired. The remainder of the purchase price was charged to retained earnings.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Per share amounts for net income before cumulative effect of accounting change and net income from continuing operations are shown on the income statement using 1) an earnings per common share basic calculation and 2) an earnings per common share-assuming dilution calculation. A reconciliation of the factors used in the two calculations are as follows:

Year Ended December 31	2003	2002	2001
Numerator: [millions]			
Net income before cumulative effect of accounting changes as used in basic calculation	$ 767.1	$ 48.8	$ 561.2
Cumulative effect of accounting changes as used in basic calculation	(255.2)		(15.6)
	511.9	48.8	545.6
Dividends on convertible preferred stock	0.1	0.1	0.1
	$ 512.0	$ 48.9	$ 545.7
Denominator: [number of shares]			
Weighted-average shares, as used in basic calculation	177,368,137	182,664,850	188,624,613
Shares to cover conversion of preferred stock	302,974	336,734	389,024
Shares to cover non-vested stock	148,713	70,697	31,160
Average stock options outstanding during the period	7,261,850	11,895,565	16,624,905
Assumed acquisition of shares with assumed proceeds and benefits from exercising stock options (at average market price for the year).	(6,159,250)	(10,230,935)	(13,163,012)
Shares repurchaseable from measured but unrecognized stock option expense	(437,062)	(1,011,586)	(1,826,828)
Average deferred compensation shares	956,405	859,402	796,575
Weighted-average shares, as used in diluted calculation	179,441,767	184,584,727	191,476,437

LNC has stock options outstanding which were issued at prices that are above the current average market price of LNC common stock. In the event the average market price of LNC s common stock exceeds the issue price of stock options, such options would be dilutive to LNC s earnings per share and will be shown in the table above. Participants in LNC s deferred compensation plans that select LNC stock for measuring the investment return attributable to their deferral amounts will be paid out in LNC stock. The obligation to satisfy these deferred compensation plan liabilities is dilutive and is shown in the table above.

Details underlying the balance sheet caption Net Unrealized Gain on Securities Available-for-Sale, are as follows:

December 31 (in millions)	2003	2002

Fair value of securities available-for-sale	$ 32,968.6	$ 33,104.7
Cost of securities available-for-sale	31,133.0	31,437.6
Unrealized gain	1,835.6	1,667.1
Adjustments to deferred acquisition costs	(549.0)	(418.4)
Amounts required to satisfy policyholder commitments	(61.9)	(76.4)
Foreign currency exchange rate adjustment	12.5	9.8
Deferred income taxes	(444.1)	(428.8)
Net unrealized gain on securities available-for-sale	$ 793.1	$ 753.3

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Adjustments to deferred acquisition costs and amounts required to satisfy policyholder commitments are netted against the Deferred Acquisition Costs asset line and included within the Insurance Policy and Claim Reserves line on the balance sheet, respectively.

Details underlying the change in Net Unrealized Gain on Securities Available-for-Sale, Net of Reclassification Adjustment shown on the Consolidated Statements of Shareholder s Equity are as follows:

Year Ended December 31	**2003**	**2002**	**2001**
Unrealized gains on securities available-for-sale arising during the year	$ 762.9	$ 802.2	$ 345.4
Less: Reclassification adjustment for gains (losses) on disposals of prior year inventory included in net income (1)	206.4	(72.1)	43.8
Less: Federal income tax expense on reclassification	15.3	316.7	117.9
Less: Transfer from available-for-sale to trading securities	371.5		
Less: Federal income tax expense on transfer	129.9		
Net unrealized gain on securities available-for-sale, net of reclassifications and federal income tax expense	$ 39.8	$ 557.6	$ 183.7

(1) The reclassification adjustment for gains (losses) does not include the impact of associated adjustments to deferred acquisition costs and amounts required to satisfy policyholder commitments.

The Net Unrealized Gain on Derivative Instruments component of other comprehensive income shown on the Consolidated Statements of Shareholders Equity is net of Federal income tax expense (benefit) of $(3.9) million, $1.2 million, and $12.6 million for 2003, 2002 and 2001, respectively, and net of adjustments to deferred acquisition costs of $(4.5) million, $1.6 million and $23.8 million for 2003, 2002 and 2001, respectively. The 2001 amounts for tax expense and deferred acquisition cost adjustment include $9.5 million and $18.3 million, respectively, related to the transition adjustment recorded for the adoption of FAS 133

The Foreign Currency Translation component of other comprehensive income shown on the Consolidated Statements of Shareholders Equity is net of Federal income tax expense (benefit) of $31.3 million, $31.7 million and $(16.1) million for 2003, 2002 and 2001, respectively.

11. Acquisitions and Divestitures

On August 30, 2002, LNC acquired The Administrative Management Group, Inc. (AMG), an employee benefits record keeping firm for $21.6 million in cash. Contingent payments up to an additional $14 million will be paid over a period of 4 years (2003-2006) if certain criteria are met. Lincoln Retirement recorded an expense of $1.2 million after-tax ($1.8 million pre-tax) for 2003 relating to such contingent payments. AMG, a strategic partner of LNC s Retirement segment for several years, provides record keeping services for the Lincoln Alliance Program along with approximately 200 other clients nationwide. The application of purchase accounting to this acquisition resulted in goodwill of $20.2 million.

On December 7, 2001, Swiss Re acquired LNC s reinsurance operation for $2.0 billion. In addition, LNC retained the capital supporting the reinsurance operation. After giving effect to the increased levels of capital needed within the Life Insurance and Lincoln Retirement segments that result from the change in the ongoing mix of business under LNC s internal capital allocation models, the disposition of LNC s reinsurance operation freed-up approximately $100 million of retained capital.

The transaction structure involved a series of indemnity reinsurance transactions combined with the sale of certain stock companies that comprised LNC s reinsurance operation. At closing, an immediate gain of $15.0 million after-tax

LINCOLN NATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

was recognized on the sale of the stock companies. A gain of $723.1 million after-tax ($1.1 billion pre-tax) relating to the indemnity reinsurance agreements was reported at the time of closing. This gain was recorded as a deferred gain on LNC s consolidated balance sheet, in accordance with the requirements of FAS 113, and is being amortized into earnings at the rate that earnings on the reinsured business are expected to emerge, over a period of 15 years.

Effective with the closing of the transaction, the former Reinsurance segment s historical results were moved into Other Operations. During December 2001 LNC recognized in Other Operations $5.0 million ($7.9 million pre-tax) of deferred gain amortization. In addition, in December 2001, LNC recognized $7.9 million ($12.5 million pre-tax) of accelerated deferred gain amortization relating to the fact that certain Canadian indemnity reinsurance contracts were novated after the sale, but prior to December 31, 2001.

On October 29, 2002 LNC and Swiss Re settled disputed matters totaling about $770 million that had arisen in connection with the final closing balance sheets associated with Swiss Re s acquisition of LNC s reinsurance operations. The settlement provided for a payment by LNC of $195 million to Swiss Re, which was recorded by LNC as a reduction in deferred gain. As a result of additional information made available to LNC following the settlement with Swiss Re in the fourth quarter of 2002, LNC recorded a further reduction in the deferred gain of $51.6 million after-tax ($79.4 million pre-tax), as well as a $9.4 million after-tax ($8.3 million pre-tax) reduction in the gain on the sale of subsidiaries.

As part of the dispute settlement, LNC also paid $100 million to Swiss Re in satisfaction of LNC s $100 million indemnification obligation with respect to personal accident business. As a result of this payment, LNC has no further underwriting risk with respect to the reinsurance business sold. However, because LNC has not been relieved of it legal liabilities to the underlying ceding companies with respect to the portion of the business indemnity reinsured by Swiss Re, under FAS 113 the reserves for the underlying reinsurance contracts as well as a corresponding reinsurance recoverable from Swiss Re will continue to be carried on LNC s balance sheet during the run-off period of the underlying reinsurance business. This is particularly relevant in the case of the exited personal accident and disability income reinsurance lines of business where the underlying reserves are based upon various estimates that are subject to considerable uncertainty.

As a result of developments and information obtained during 2002 relating to personal accident and disability income matters, LNC increased these exited business reserves by $198.5 million after-tax ($305.4 million pre-tax). After giving effect to LNC s $100 million indemnification obligation, LNC recorded a $133.5 after-tax ($205.4 million pre-tax) increase in reinsurance recoverable from Swiss Re with a corresponding increase in the deferred gain. As a result of developments and information received in the third quarter of 2003 relating to personal accident matters, LNC increased reserves on this exited business by $20.9 million after-tax ($32.1 million pre-tax) with a corresponding increase in reinsurance recoverable from Swiss Re and in the deferred gain.

The combined effects of the 2002 settlement of disputed matters and exited business reserve increases reduced the $723.1 million after-tax ($1.1 billion pre-tax) deferred gain reported at closing by $44.9 million after-tax ($69 million pre-tax). An additional $1.3 million after-tax ($2 million pre-tax) of deferred gain was recognized in net income, due to a novation of certain Canadian business during 2002. During 2003, LNC amortized into net income $49.3 million after-tax ($75.8 million pre-tax) of the deferred gain.

Also during 2002, LNC exercised a contractual right to put its interest in a subsidiary company containing LNC s disability income reinsurance business to Swiss Re for $10 million. The $10 million sale price was approximately equal to LNC s book basis in the subsidiary.

Through December 31, 2003, of the original $2 billion in proceeds received by LNC, approximately $560 million was paid for taxes and deal expenses and approximately $1.0 billion was used to repurchase stock, reduce

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

debt, and support holding company cash flow needs. LNC also paid $195 million to Swiss Re to settle the closing balance sheet disputed matters and $100 million to satisfy LNC s personal accident business indemnification obligations. The remaining proceeds have been dedicated to the ongoing capital needs of The Lincoln National Life Insurance Company.

Because of ongoing uncertainty related to personal accident and disability income businesses, the reserves related to these exited business lines carried on LNC s balance sheet at December 31, 2003 may ultimately prove to be either excessive or deficient. For instance, in the event that future developments indicate that these reserves should be increased, under FAS 113 LNC would record a current period non-cash charge to record the increase in reserves. Because Swiss Re is responsible for paying the underlying claims to the ceding companies, LNC would record a corresponding increase in reinsurance recoverable from Swiss Re. However, FAS 113 does not permit LNC to take the full benefit in earnings for the recording of the increase in the reinsurance recoverable in the period of the change. Rather, LNC would increase the deferred gain recognized upon the closing of the indemnity reinsurance transaction with Swiss Re and would report a cumulative amortization catch-up adjustment to the deferred gain balance as increased earnings recognized in the period of change. Any amount of additional increase to the deferred gain above the cumulative amortization catch-up adjustment must continue to be deferred and will be amortized into income in future periods over the remaining period of expected run-off of the underlying business. No cash would be transferred between LNC and Swiss Re as a result of these developments.

Accordingly, even though LNC has no continuing underwriting risk, and no cash would be transferred between LNC and Swiss Re, in the event that future developments indicate LNC s December 31, 2003 personal accident or disability income reserves are deficient or redundant, FAS 113 requires LNC to adjust earnings in the period of change, with only a partial offset to earnings for the cumulative deferred gain amortization adjustment in the period of change. The remaining amount of increased gain would be amortized into earnings over the remaining run-off period of the underlying business.

As noted above, effective with the closing of the transaction, the Reinsurance segment s results for the eleven months ended November 30, 2001 and the year ended December 31, 2000 were moved into Other Operations.

Earnings from LNC s reinsurance operations were as follows:

(in millions)	**Eleven Months Ended November 30, 2001**
Revenue	$ 1,681.3
Benefits and Expenses	1,505.3
Income before Federal Income Taxes and Cumulative Effect of Accounting Changes	176.0
Federal Income Taxes	59.0
Income before Cumulative Effect of Accounting Changes	117.0

Cumulative Effect of Accounting Changes (after-tax)		(2.4)
Net Income	$	114.6

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Restructuring Charges

The following provides details on LNC s restructuring charges.

1998 Restructuring Plan

During 1998, LNC implemented two restructuring plans, with only the plan relating to downsizing LNC s corporate center operations not completed as of December 31, 2000. The aggregate charges associated with the restructuring plan totaled $14.3 million after-tax ($22.0 million pre-tax) for the year ended December 31, 1998. These charges were included in Underwriting, Acquisition, Insurance and Other Expenses on the Consolidated Statement of Income in the year the restructuring were incurred. These aggregate pre-tax costs include $8.9 million for employee severance and termination benefits, $9.9 million for asset impairments and $3.2 million for rents on abandoned facilities. During the fourth quarter of 2000, $0.5 million (pre-tax) of the original charge to downsize LNC s corporate center operations was reversed. This plan was completed in the third quarter of 2002 due to the termination of the lease, which resulted from LNC s purchase and ultimate sale of the abandoned building. The remaining $0.2 million related to the terminated lease was reversed as a reduction in restructuring costs during the third quarter of 2002. Total pre-tax costs of $21.3 million were expended or written-off under this restructuring plan.

1999 Restructuring Plan

In 1999, LNC implemented three different restructuring plans, with those plans relating to the discontinuance of HMO excess-of-loss reinsurance programs (HMO Reinsurance), and the streamlining of Lincoln UK s operations not completed as of December 31, 2000. The aggregate charges associated with these two unrelated restructuring plans totaled $9.7 million after-tax ($14.9 million pre-tax) and were included in Underwriting, Acquisition, Insurance and Other Expenses on the Consolidated Statement of Income for the year ended December 31, 1999. These aggregate pre-tax costs include $6.3 million for employee severance and termination benefits and $8.6 million for other costs relating to exiting business activities. Through December 31, 2001, actual pre-tax costs of $3.7 million were expended or written-off for the HMO Reinsurance restructuring plan. During the fourth quarter of 2000, $1.0 million (pre-tax) of the original charge for the discontinuance of HMO excess-of-loss restructuring plan was reversed. During the fourth quarter of 2001, the remaining restructuring reserve of $0.2 million relating to the HMO excess-of-loss reinsurance programs was transferred to Swiss Re as part of its acquisition of LNC s reinsurance operations.

Included in the 1999 restructuring charge is $6.5 million after-tax ($10.0 million pre-tax) recorded in the Lincoln UK segment. The objective of this restructuring plan is to reduce operating costs by consolidating and eliminating redundant staff functions and facilities. Expenditures and write-offs under the restructuring plan began in the fourth quarter of 1999 and were completed in the 3rd quarter of 2001 except for lease payments on closed facilities, which will continue until 2016. Through December 31, 2003, $8.3 million (pre-tax) has been expended or written-off under this restructuring plan and 112 positions have been eliminated.

2000 Restructuring Plan

During 2000, LNC implemented restructuring plans relating to 1) the downsizing and consolidation of the operations of Vantage Global Advisors, Inc. (Vantage); 2) the exit of all direct sales and sales support operations of Lincoln UK and the consolidation of its Uxbridge home office with its Barnwood home office; and 3) the downsizing and consolidation of the investment management operations of Lincoln Investment Management (LIM). The Vantage restructuring charge was recorded in the second quarter, the Lincoln UK restructuring was recorded in the third and fourth quarters, and the LIM restructuring charge was recorded in the

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

fourth quarter of 2000. The Vantage plan was completed in the fourth quarter of 2001 and the LIM plan was completed in the third quarter of 2002. All expenditures and write-offs for the LIM restructuring plan were completed in the third quarter of 2002 and $0.4 million of the original reserve was released. The release of the reserve was primarily due to LNC s purchase and ultimate sale of the vacant office space on terms, which were favorable to what was included in the original restructuring plan for rent on this office space. The remaining restructuring reserve for the Lincoln UK plan is for lease payments on closed sales offices. The following table provides information about the 2000 restructuring plans.

(in millions)	Vantage Plan	Lincoln UK Plan	LIM Plan	Total
Employee severance and termination benefits	$ 2.3	$ 29.8	$ 1.7	$ 33.8
Write-off of impaired assets	1.4	39.2	0.3	40.9
Other costs	0.4	30.4	1.9	32.7
2000 Restructuring Charge (pre-tax)	4.1	99.4	3.9	107.4
Amounts expended and written-off in 2001	3.5	85.4	1.7	90.6
Amounts reversed through in 2001	0.6			0.6
Restructuring reserve at December 31, 2001		14.0	2.2	16.2
Amounts expended in 2002		2.6	1.8	4.4
Amounts reversed in 2002		1.7	0.4	2.1
Restructuring reserve at December 31, 2002		9.7		9.7
Amounts expended in 2003		1.3		1.3
Amounts reversed in 2003				
Restructuring reserve at December 31, 2003	$	$ 8.4	$	$ 8.4
Positions to be eliminated under original plan	15	671	19	
Actual positions eliminated through December 31, 2003	13	671	19	
Expected completion date	Completed 4th Quarter 2001	2015	Completed 3rd Quarter 2002	

2001 Restructuring Plan

During 2001, LNC implemented restructuring plans relating to 1) the consolidation of the Syracuse operations of Lincoln Life & Annuity Company of New York into the Lincoln Retirement segment operations in Fort Wayne, Indiana and Portland, Maine; 2) the elimination of duplicative functions in the Schaumburg, Illinois operations of First Penn-Pacific, and the absorption of these functions into the Lincoln Retirement and Life Insurance segment operations in Fort Wayne, Indiana and Hartford, Connecticut; 3) the reorganization of the life wholesaling function within the independent planner distribution channel, consolidation of retirement wholesaling territories, and streamlining of the marketing and communications functions in LFD; 4) the reorganization and consolidation of the life insurance operations in Hartford, Connecticut related to the streamlining of underwriting and new business processes and the completion of outsourcing of administration of certain closed blocks of business 5) the planned consolidation of the Boston, Massachusetts investment and marketing office with the Philadelphia, Pennsylvania investment and marketing operations in order to eliminate redundant facilities and functions within the Investment Management segment 6) the combination of LFD channel oversight, positioning of LFD to take better advantage of ongoing marketplace consolidation and expansion of the customer base of wholesalers in certain non-productive territories and 7) the consolidation of operations and space in LNC s Fort Wayne, Indiana operations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Syracuse restructuring charge was recorded in the first quarter of 2001 and was completed in the first quarter of 2002. The Schaumburg, Illinois restructuring charge was recorded in the second quarter of 2001, the LFD restructuring charges were recorded in the second and fourth quarters of 2001, and the remaining restructuring charges were all recorded in the fourth quarter of 2001. The LFD restructuring plan that was initiated in the second quarter of 2001 was completed in the fourth quarter of 2002. The Life Insurance segment restructuring plan that was initiated in the fourth quarter of 2001 was completed in the fourth quarter of 2002.

The aggregate charges associated with all restructuring plans entered into during 2001 totaled $24.6 million after-tax ($38.0 million pre-tax) for the year ended December 31, 2001. The component elements of these aggregate pre-tax costs include employee severance and termination benefits of $12.2 million, write-off of impaired assets of $3.3 million and other exit costs of $22.5 million primarily related to the termination of equipment leases ($1.4 million) and rent on abandoned office space ($20.0 million). Actual pre-tax costs totaling $1.3 million were expended or written-off and 30 positions were eliminated under the Syracuse restructuring plan. The total amount expended for this plan exceeded the original restructuring reserve by $0.3 million. Actual pre-tax costs totaling $1.8 million were expended or written-off and 26 positions were eliminated under the second quarter of 2001 LFD restructuring plan. The amount expended for this plan was equal to the original reserve. Actual pre-tax costs totaling $2.3 million were expended or written-off and 36 positions were eliminated under the fourth quarter of 2001 Life Insurance segment restructuring plan. The amount expended for this plan was in excess of the original reserve by less than $0.1 million. In addition, $0.1 million of excess reserve on the Schaumburg, Illinois restructuring plan was released during the second quarter of 2002 and $1.5 million of excess reserve on the Fort Wayne restructuring plan was released during the third quarter of 2002. The release of the reserve on the Fort Wayne restructuring plan was due to LNC s purchase and ultimate sale of the vacant building on terms that were favorable to what was included in the original restructuring plan for rent on this abandoned office space. The following table provides information about the remaining 2001 restructuring plans.

(in millions)	Schaumburg Plan	Boston Office Consolidation	LFD Plan-4th Quarter	Fort Wayne Operations	Total
Employee severance and termination benefits	$ 3.2	$	$ 3.8	$ 0.3	$ 7.3
Write-off of impaired assets		0.1		3.2	3.3
Other costs:					
Termination of equipment leases				1.4	1.4
Rent on abandoned office space	0.9	0.5		19.5	20.9
Total 2001 Restructuring Charges (pre-tax)	$ 4.1	$ 0.6	$ 3.8	$ 24.4	$ 32.9
Amounts expended and written-off through 2001	2.4		1.2		3.6
Restructuring reserve at December 31, 2001	1.7	0.6	2.6	24.4	29.3
Amounts expended in 2002	1.3	0.2	2.6	22.3	26.4
Amounts reversed in 2002	0.1			1.5	1.6
Restructuring reserve at December 31, 2002	0.3	0.4	*	0.6	1.3
Amounts expended in 2003	0.1	*	*	0.5	0.6
Restructuring reserve at December 31, 2003	$ 0.2	$ 0.4	$	$ 0.1	$ 0.7

Positions to be eliminated under original plan	27		63	9	99
Actual positions eliminated through December 31, 2003	26		62	19	107
Expected completion date	1st Quarter 2004	4th Quarter 2005	Completed 1st Quarter 2003	2nd Quarter 2004	

* Amount is less than $0.1 million.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2002 Restructuring Plan

During the second quarter of 2002, Lincoln Retirement completed a review of its entire internal information technology organization. As a result of that review, Lincoln Retirement decided in the second quarter of 2002 to reorganize its IT organization in order to better align the activities and functions conducted within its own organization and its IT service providers. This change was made in order to focus Lincoln Retirement on its goal of achieving a common administrative platform for its annuities products, to better position the organization and its service providers to respond to changing market conditions, and to reduce overall costs in response to increased competitive pressures. The following table provides information about this restructuring plan.

(in millions)	**Lincoln Retirement**
Employee severance and termination benefits	$ 1.6
2002 Restructuring Charge (pre-tax)	1.6
Amounts expended in 2002	0.9
Restructuring reserve at December 31, 2002	0.7
Amounts expended in 2003	0.7
Restructuring reserve at December 31, 2003	$
Positions to be eliminated under original plan	49
Actual positions eliminated through December 31, 2003	49
Completion date	Completed in 3rd Quarter 2003

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2003 Restructuring Plan

In January 2003, the Life Insurance segment announced that it was realigning its operations in Hartford, Connecticut and Schaumburg, Illinois to enhance productivity, efficiency and scalability while positioning the segment for future growth. In February 2003, Lincoln Retirement announced plans to consolidate its fixed annuity operations in Schaumburg, Illinois into Fort Wayne, Indiana. In June 2003, LNC announced that it was combining its retirement and life insurance businesses into a single operating unit focused on providing wealth accumulation and protection, income distribution and wealth transfer products. The realigned organization is expected to significantly reduce operating expenses while positioning LNC for future growth and to take advantage of the recent market recovery. In August 2003, LNC announced additional realignment activities, which impact all of LNC s domestic operations. The following table provides information about the 2003 restructuring plans.

(in millions)	Life Insurance Realignment Jan 2003	Fixed Annuity Consolidation Feb 2003	Realignment June/August 2003	Total
Total expected charges as of December 31, 2003	$ 21.0	$ 5.0	$ 101.0	$ 127.0
Amounts incurred through December 31				
Employee severance and termination benefits	$ 7.0	$ 1.8	$ 27.4	$ 36.2
Write-off of impaired assets	1.9		3.0	4.9
Other Costs:				
Rent on abandoned office space	6.0	2.2		8.2
Other	2.8	0.2	1.5	4.5
Total 2003 Restructuring Charges (pre-tax)	17.7	4.2	31.9	53.8
Amounts expended through December 31, 2003	16.3	3.6	18.8	38.7
Amounts reversed through December 31, 2003				
Restructuring reserve at December 31, 2003	$ 1.4	$ 0.6	$ 13.1	$ 15.1
Additional amounts expended that do not qualify as restructuring charges	$ 2.0	$ 0.5	$ 6.8	$ 9.3
Expense savings realized in 2003 (pre-tax)	$ 20.0	$ 3.0	$ 6.7	$ 29.7
Total expected annual expense savings (pre-tax)	$ 20.0	$ 6.4	$ 96.6	$ 123.0
Expected completion date	2nd Quarter 2006	2nd Quarter 2006	1st Quarter 2006	

Pre-tax restructuring charges for the June/August realignment activities for the year ended December 31, 2003 were reported in the following segments: Retirement ($15.9 million), Life Insurance ($1.7 million), Investment Management ($7.1 million), and Other Operations ($7.2 million).

13. Subsequent Events

In February 2004 LNC issued of $200 million 4.75% Notes due 2014 with semi-annual interest payments in February and August. The notes were priced at 99.297% and net proceeds to the company were $197.3 million, which will be used for general corporate purposes. Until the funds are needed for such purposes, the net proceeds will be used to invest in short-term investment grade securities and to pay down short-term debt. LNC used a treasury lock to reduce exposure to interest rate changes prior to closing. The treasury lock was closed prior to the issuance of the Notes with a gain of approximately $1 million. This gain, along with the costs of issuance, will be amortized over the life of the Notes.

Board of Directors

Lincoln National Corporation

We have audited the accompanying consolidated balance sheets of Lincoln National Corporation as of December 31, 2003 and 2002, and the related consolidated statements of income, shareholders equity and cash flows for each of the three years in the period ended December 31, 2003. Our audits also included the financial statement schedules listed in the Index at Item 15(a)(2). These financial statements and schedules are the responsibility of the Corporation s management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lincoln National Corporation at December 31, 2003 and 2002, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

As discussed in Notes 1 and 2 to the consolidated financial statements, in 2003 the Corporation changed its method of accounting for stock compensation costs, certain reinsurance arrangements and costs associated with exit or disposal activities. Also, as discussed in Note 2 to the consolidated financial statements, in 2002 the Corporation changed its method of accounting for goodwill and its related amortization, and in 2001 the Corporation changed its method of accounting for derivative instruments and hedging activities as well as its method of accounting for impairment of certain investments.

/s/ ERNST & YOUNG LLP

Philadelphia, Pennsylvania

February 6, 2004