

STATEMENT OF ADDITIONAL INFORMATION (SAI)

**Dated May 1, 2009
Relating to Prospectus Dated May 1, 2009 for**

Lincoln SVUL-IV product

Lincoln Life Flexible Premium Variable Life Account R, Registrant

The Lincoln National Life Insurance Company, Depositor

The SAI is not a prospectus. The SAI provides you with additional information about Lincoln Life, the Separate Account and your policy. It should be read in conjunction with the product prospectus.

A copy of the product prospectus may be obtained without charge by writing to our Administrative Office:

Customer Service Center
One Granite Place
Concord, NH 03301

or by telephoning (800) 444-2363, and requesting a copy of the Lincoln SVUL-IV product prospectus.

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GENERAL INFORMATION

Lincoln Life

The Lincoln National Life Insurance Company (“Lincoln Life”, “the Company”, “we”, “us”, “our”) (EIN 35-0472300), organized in 1905, is an Indiana-domiciled insurance company, engaged primarily in the direct issuance of life insurance contracts and annuities. Lincoln Life is wholly owned by Lincoln National Corporation (LNC), a publicly held insurance and financial services holding company incorporated in Indiana. Lincoln Life is obligated to pay all amounts promised to policy owners under the policies. Death benefit proceeds and rider benefits, to the extent those proceeds and benefits exceed the then current Accumulation Value of your policy, are backed by the claims-paying ability of Lincoln Life.

Lincoln Financial Group is the marketing name for Lincoln National Corporation (NYSE:LNC) and its affiliates. Lincoln Financial Group sells a wide variety of financial products and solutions through financial advisors: mutual funds, managed accounts, retirement solutions, life insurance, 401(k) and 403(b) plans, savings plans, institutional investments and comprehensive financial planning and advisory services.

Lincoln Life is subject to the laws of Indiana governing insurance companies and to regulation by the Indiana Department of Insurance (“Insurance Department”). An annual statement in a prescribed form is filed with the Insurance Department each year covering the operation of the Company for the preceding year along with the Company’s financial condition as of the end of that year. Regulation by the Insurance Department includes periodic examination to determine our contract liabilities and reserves. Our books and accounts are subject to review by the Insurance Department at all times and a full examination of our operations is conducted periodically by the Insurance Department. Among the laws and regulations applicable to us as an insurance company are those which regulate the investments we can make with assets held in our General Account. In general, those laws and regulations determine the amount and type of investments which we can make with General Account assets. Such regulation does not, however, involve any supervision of management practices or policies, or our investment practices or policies.

A blanket bond with a per event limit of \$50 million and an annual policy aggregate limit of \$100 million covers all of the officers and employees of the Company.

Capital Markets and Financial Ratings

Beginning in 2008 and continuing as of the date of this prospectus, the capital and credit markets have experienced an unusually high degree of volatility. As a result, the market for fixed income securities has experienced illiquidity, increased price volatility, credit downgrade events and increased expected probability of default. Securities that are less liquid are more difficult to value and may be hard to sell, if desired. During this time period, domestic and international equity markets have also been experiencing heightened volatility and turmoil, with issuers (such as our company) that have exposure to the real estate, mortgage and credit markets particularly affected. In any particular year, our capital may increase or decrease depending on a variety of factors—the amount of our statutory income or losses (which itself is sensitive to equity market and credit market conditions), the amount of additional capital we must hold to support business growth, changes in reserving requirements, our inability to secure capital market solutions to provide reserve relief, such as issuing letters of credit to support captive reinsurance structures, changes in equity market levels, the value of certain fixed-income and equity securities in our investment portfolio and changes in interest rates.

Nationally recognized rating agencies rate our financials as an insurance company. The ratings do not imply approval of the product and do not refer to the performance of the product, including underlying investment options, if any. Ratings are not recommendations to buy our products. Each of the rating agencies reviews its ratings periodically. Accordingly, all ratings are subject to revision or withdrawal at any time by the rating agencies, and therefore, no assurance can be given that these ratings will be maintained. In late September and early October of 2008, A.M. Best, Fitch, Moody’s and S&P each revised their outlook for the U.S. life insurance sector from stable

to negative. Our financial strength ratings, which are intended to measure our ability to meet policyholder obligations, are an important factor affecting public confidence in most of our products and, as a result, our competitiveness. A downgrade of our financial strength rating could affect our competitive position in the insurance industry by making it more difficult for us to market our products as potential customers may select companies with higher financial strength ratings and by leading to increased withdrawals by current customers seeking companies with higher financial strength ratings.

Registration Statement

A Registration Statement has been filed with the Securities and Exchange Commission under the Securities Act of 1933, as amended, with respect to the policies offered. The Registration Statement, its amendments and exhibits, contain information beyond that found in the prospectus and the SAI. Statements contained in the prospectus and the SAI as to the content of policies and other legal instruments are summaries.

Changes of Investment Policy

Lincoln Life may materially change the investment policy of the Separate Account. If this decision is made, we must inform the Owners and obtain all necessary regulatory approvals. Any change must be submitted to the various state insurance departments. The state insurance departments would not approve the change in investment policy if found to be detrimental to the interests of the Owners of the policies or the end result would render our operations hazardous to the public.

If an owner objects, his or her policy may be converted to a substantially comparable fixed benefit life insurance policy offered by us on the lives of the insureds. The owner has the later of 60 days (6 months in Pennsylvania) from the date of the investment policy change or 60 days (6 months in Pennsylvania) from being informed of such change to make this conversion. We will not require evidence of insurability for this conversion. The new policy will not be affected by the investment experience of any separate account. The new policy will be for an amount of insurance equal to or lower than the amount of the death benefit of the current policy on the date of the conversion.

Principal Underwriter

Lincoln Financial Distributors, Inc. ("LFD"), 130 North Radnor Chester Road, Radnor, PA 19087, is the principal underwriter for the policies, which are offered continuously. LFD is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934 as a broker-dealer and is a member of the Financial Industry Regulatory Authority ("FINRA"). The principal underwriter has overall responsibility for establishing a selling plan for the policies. LFD received \$ 15,614,729 in 2008 and \$13,308,564 in 2007 for the sale of policies offered through the Separate Account. LFD retains no underwriting commissions from the sale of the policies.

Disaster Plan

Lincoln's business continuity and disaster recovery strategy employs system and telecommunication accessibility, system back-up and recovery, and employee safety and communication. The plan includes documented and tested procedures that will assist in ensuring the availability of critical resources and in maintaining continuity of operations during an emergency situation.

Advertising

Lincoln Life is ranked and rated by independent financial rating services, including Moody's, Standard & Poor's, Duff & Phelps, A.M. Best Company and Fitch. The purpose of these ratings is to reflect the financial strength or claims-paying ability of Lincoln Life. The ratings are not intended to reflect the investment experience or financial strength of the Separate Account. We may advertise these ratings from time to time. In addition, we may include in certain advertisements, endorsements in the form of a list of organizations, individuals or other parties which

recommend Lincoln Life or the policies. Furthermore, we may occasionally include in advertisements comparisons of currently taxable and tax deferred investment programs, based on selected tax brackets, or discussions of alternative investment vehicles and general economic conditions.

More About the S&P 500 Index. Investors look to indexes as a standard of market performance. Indexes are model portfolios, that is, groups of stocks or bonds selected to represent an entire market. The S&P 500 Index is a widely used measure of large US company stock performance. It consists of the common stocks of 500 major corporations selected according to size, frequency and ease by which their stocks trade, and range and diversity of the American economy.

The LVIP SSgA S&P 500 Index Fund seeks to approximate as closely as possible, before fees and expenses, the total return of the S&P 500 Index. To accomplish this objective the fund's sub-adviser, SSgA Funds Management, Inc. ("SFM"), attempts to buy and sell all of the index's securities in the same proportion as they are reflected in the S&P 500 Index, although the fund reserves the right not to invest in every security in the S&P 500 Index if it is not practical to do so under the circumstances. SFM does not seek to beat the S&P 500 Index and does not seek temporary defensive positions when markets appear to be overvalued. SFM makes no attempt to apply economic, financial or market analysis when managing the fund. Including a security among the fund's holdings implies no opinion as to its attractiveness as an investment.

The fund may invest in stock index futures and options on stock index futures as a substitute for a comparable market position in the underlying securities. A stock index future obligates one party to deliver (and the other party to take), effectively, an amount of cash equal to a specific dollar amount times the difference between the value of a specific stock index at the close of the last trading day of the contract and the price at which the agreement is made. No physical delivery of the underlying stocks in the index is made. Instead, the buyer and seller settle the difference in cash between the contract price and the market price on the agreed upon date. The buyer pays the difference if the actual price is lower than the contract price and the seller pays the difference if the actual price is higher. There can be no assurance that a liquid market will exist at the time when the fund seeks to close out a futures contract or a futures option position. Lack of a liquid market may prevent liquidation of an unfavorable position.

The Product is not sponsored, endorsed, sold or promoted by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. ("S&P"). S&P makes no representation or warranty, express or implied, to the owners of the Product or any member of the public regarding the advisability of investing in securities generally or in the Product particularly or the ability of the S&P 500 Index to track general stock market performance. S&P's only relationship to the Licensee is the licensing of certain trademarks and trade names of S&P and of the S&P 500 Index which is determined, composed and calculated by S&P without regard to the Licensee or the Product. S&P has no obligation to take the needs of the Licensee or the owners of the Product into consideration in determining, composing or calculating the S&P 500 Index. S&P is not responsible for and has not participated in the determination of the prices and amount of the Product or the timing of the issuance or sale of the Product or in the determination or calculation of the equation by which the Product is to be converted into cash. S&P has no obligation or liability in connection with the administration, marketing or trading of the Product.

S&P DOES NOT GUARANTEE THE ACCURACY AND/OR THE COMPLETENESS OF THE S&P 500 INDEX OR ANY DATA INCLUDED THEREIN AND S&P SHALL HAVE NO LIABILITY FOR ANY ERRORS, OMISSIONS, OR INTERRUPTIONS THEREIN. S&P MAKES NO WARRANTY, EXPRESS OR IMPLIED, AS TO RESULTS TO BE OBTAINED BY LICENSEE, OWNERS OF THE PRODUCT, OR ANY OTHER PERSON OR ENTITY FROM THE USE OF THE S&P 500 INDEX OR ANY DATA INCLUDED THEREIN. S&P MAKES NO EXPRESS OR IMPLIED WARRANTIES, AND EXPRESSLY DISCLAIMS ALL WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE WITH RESPECT TO THE S&P 500 INDEX OR ANY DATA INCLUDED THEREIN. WITHOUT LIMITING ANY OF THE FOREGOING, IN NO EVENT SHALL S&P HAVE ANY LIABILITY FOR ANY SPECIAL, PUNITIVE, INDIRECT, OR CONSEQUENTIAL DAMAGES (INCLUDING LOST PROFITS), EVEN IF NOTIFIED OF THE POSSIBILITY OF SUCH DAMAGES.

SERVICES

Independent Registered Public Accounting Firm

The financial statements of the Separate Account and the consolidated financial statements of The Lincoln National Life Insurance Company appearing in this SAI and Registration Statement have been audited by Ernst & Young LLP, independent registered public accounting firm, Two Commerce Square, 2001 Market Street, Suite 4000, Philadelphia, Pennsylvania 19103, as set forth in their reports, also appearing in this SAI and in the Registration Statement. The financial statements audited by Ernst & Young LLP have been included herein in reliance on their reports given on their authority as experts in accounting and auditing.

Accounting Services

We have entered into an agreement with the Bank of New York Mellon, N.A., One Mellon Bank Plaza, 500 Grant Street, Pittsburgh, PA, 19203, to provide accounting services to the Separate Account. Lincoln Life makes no separate charge against the assets of the Separate Account for this service.

Checkbook Service for Disbursements

We offer a checkbook service in which the Death Benefit Proceeds are transferred into an interest-bearing account, in the Beneficiary's name as owner of the account. Your Beneficiary has quick access to the proceeds and is the only one authorized to transfer proceeds from the account. This service allows the Beneficiary additional time to decide how to manage Death Benefit Proceeds with the balance earning interest from the day the account is opened.

We also offer this same checkbook service for surrenders of your policy of \$5,000 or more. Once your request is processed, proceeds are placed in an interest-bearing account in your name. You have complete access to your proceeds through check writing privileges. You have the choice of leaving proceeds in this account or you may write checks immediately - even a check for the entire amount.

POLICY INFORMATION

Assignment

While either insured is living, you may assign your rights in the policy, including the right to change the beneficiary designation. The assignment must be in writing, signed by you and recorded at our Administrative Office. We will not be responsible for any assignment that is not submitted for recording, nor will we be responsible for the sufficiency or validity of any assignment. Any assignment is subject to any indebtedness owed to Lincoln Life at the time the assignment is recorded and any interest accrued on such indebtedness after we have recorded any assignment.

Once recorded, the assignment remains effective until released by the assignee in writing. As long as an effective assignment remains outstanding, the owner will not be permitted to take any action with respect to the policy without the consent of the assignee in writing.

Change of Ownership

As long as either insured is living, you may name a new owner by recording a change in ownership in writing at our Administrative Office. The change will be effective as of the date of the latest signature in good order. We may require that the policy be submitted to us for endorsement before making a change.

Beneficiary

The beneficiary is initially designated on the application and is the person who will receive the death benefit proceeds payable. Multiple beneficiaries will be paid in equal shares, unless otherwise specified to the Company.

You may change the beneficiary at any time while either insured is living, except when we have recorded an assignment of your policy or an agreement not to change the beneficiary. Any request for a change in the beneficiary must be in writing, signed by you, and recorded at our Administrative Office. If the owner has not reserved the right to change the beneficiary, such a request requires the consent of the beneficiary. The change will be effective as of the date of the latest signature in good order.

If any beneficiary dies before the death of the second insured, the beneficiary's potential interest shall pass to any surviving beneficiaries, unless otherwise specified to the Company. If no named beneficiary survives at the time of the death of the second insured, any death benefit proceeds will be paid to you, as the owner, or to your executor, administrator or assignee.

Right to Convert Contract

You may at any time transfer 100% of the policy's accumulation value to the general account and choose to have all future premium payments allocated to the general account. After you do this, the minimum period the policy will be in force will be fixed and guaranteed. The minimum period will depend on the amount of accumulation value, the specified amount, the sex, attained age and rating class of the insured at the time of transfer. The minimum period will decrease if you choose to surrender the policy or make a withdrawal. The minimum period will increase if you choose to decrease the specified amount, make additional premium payments, or we credit a higher interest rate or charge a lower cost of insurance rate than those guaranteed for the general account.

Change of Plan

Within 18 months of the date we issue your policy, you may exchange your policy without any evidence of insurability, for any one of the permanent life insurance policies then being issued by the Company which belong to the same class as this policy. Your request for exchange must be in writing. Unless agreed otherwise, the new policy will have the same initial amount of insurance, date of issue and age of the insured as the original policy.

You may exchange the policy for separate single life policies on each of the insureds under any of the following circumstances:

- (1) a change in the Internal Revenue Code (IRC) that would result in a less favorable tax treatment of the insurance provided under this policy,
- (2) the insureds are legally divorced while this policy is in force, or
- (3) the insureds' business is legally dissolved while the policy is in force.

An exchange for separate policies is subject to all of the following conditions:

- (1) both insureds are alive and the policy is in force at the time of the change in circumstances noted above,
- (2) both insureds furnish evidence of insurability satisfactory to the Company, unless
 - (a) the exchange is applied for within 12 months of the enactment of the change in the IRC, or (b) the exchange is applied for within 24 months of the date of legal divorce with the exchange to become effective after 24 months following the date of legal divorce,
- (3) the amount of insurance of each new policy is not larger than one half of the amount of insurance then in force under this policy, and
- (4) any other requirements as determined by the Company are met.

The new policy will not take effect until the date all such requirements are met. The premium for each new policy is determined according to the Company's rates in effect at that time for that policy based on each insured's attained age and premium class, if that premium class is available on a single-life basis. If either insured's premium class is not available on a single-life basis, the new policy for that insured cannot be issued unless satisfactory evidence of insurability is provided for an premium class that is available.

Settlement Options

You may elect or change a settlement option while at least one insured is alive. If you have not irrevocably selected a settlement option, the beneficiary may elect to change the settlement option within 90 days after the second insured dies. If no settlement option is selected, the death benefit proceeds will be paid in a lump sum.

If you assign your policy as collateral security, we will pay any amount due the assignee in one lump sum. We will pay any remaining death benefit proceeds as elected.

Your written request to elect, change, or revoke a settlement option must be received in our Administrative Office before payment of the lump sum or any settlement option is initiated. The first payment of the settlement option selected will become payable on the date proceeds are settled. Payments after the first payment will be made on the first day of each month. Once payments have begun, the policy cannot be surrendered and neither the payee nor the settlement option may be changed.

You have at least four settlement options:

- 1) an annuity for the lifetime of the payee;
- 2) an annuity for the lifetime of the payee, with monthly payments guaranteed for 60, 120, 180, or 240 months;
- 3) monthly payments for a stated number of years, at least five but no more than thirty; or
- 4) payment of a maximum of 3% interest annually on the sum left on deposit.

We may offer you or your beneficiary additional settlement options in the future.

Deferment of Payments

Amounts payable as a result of loans, surrenders or partial surrenders will be paid within seven calendar days of our receipt of such a request in a form acceptable to us. We may defer payment or transfer from the Fixed Account up to six months at our option. If we exercise our right to defer any payment from the Fixed Account, interest will accrue and be paid (as required by law) from the date you would otherwise have been entitled to receive the payment. We will not defer any payment used to pay premiums on policies with us.

Incontestability

The Company will not contest your policy or payment of the death benefit proceeds based on the initial specified amount, or an increase in the specified amount requiring evidence of insurability, after your policy or increase has been in force for two years from date of issue or increase (in accordance with state law).

Misstatement of Age or Gender

If the age or gender of either insureds has been misstated, benefits will be adjusted based on the following values:

- 1) the net amount at risk at the time of the second insured's death;
- 2) the ratio of the monthly cost of insurance applied in the policy month of death to the monthly cost of insurance that should have been applied at the true age and gender in the policy month of death; and
- 3) the accumulation value at the time of the second insured's death.

The amount of death benefit proceeds will be 1. multiplied by 2. and then the result added to 3.

Suicide

If the second insured dies by suicide, while sane or insane, within two years from the date of issue, the Company will pay no more than the sum of the premiums paid, less any indebtedness and the amount of any partial surrenders. If the second insured dies by suicide, while sane or insane, within two years from the date an application is accepted for an increase in the specified amount, the Company will pay no more than a refund of the monthly charges for the cost of the increased amount. This time period could be less depending on the state of issue.

PERFORMANCE DATA

Performance data may appear in sales literature or reports to owners or prospective buyers.

Past performance cannot guarantee comparable future results. Performance data reflects the time period shown on a rolling monthly basis and is based on Sub-Account level values adjusted for your policy's expenses.

Data reflects:

- an annual reduction for fund management fees and expenses, and
- a policy level mortality and expense charge applied on a daily equivalent basis, but
- no deductions for additional policy expenses (i.e., premium loads, administrative fees, and cost of insurance charges), which, if included, would have resulted in lower performance.

These charges and deductions can have a significant effect on policy values and benefits. Ask your financial representative for a personalized illustration reflecting these costs.

Sub-Account performance figures are historical and include change in share price, reinvestment of dividends and capital gains and are net of the asset management expenses that can be levied against the Sub-Account.

The Average Annual Returns in the table below are calculated in two ways, one for Money Market Sub-Account, one for all other Sub-Accounts. Both are according to methods prescribed by the SEC.

Money Market Sub-Account:

The Average Annual Return is the income generated by an investment in the Money Market Sub-Account over a seven-day period, annualized. The process of annualizing results when the amount of income generated by the investment during that week is assumed to be generated each week over a 52-week period and is shown as a percentage of the investment.

The Money Market Sub-Account's return is determined by:

- a) calculating the change in unit value for the base period (the 7-day period ended December 31, of the previous year); then
- b) dividing this figure by the account value at the beginning of the period; then
- c) annualizing this result by the factor of 365/7.

Other Sub-Accounts:

The Average Annual Return for each period is determined by finding the average annual compounded rate of return over each period that would equate the initial amount invested to the ending redeemable value for that period, according to the following formula:

$$P(1 + T)^n = ERV$$

Where: P = a hypothetical initial purchase payment of \$1,000

T = average annual total return for the period in question

N = number of years

ERV = ending redeemable value (as of the end of the period in question) of a hypothetical \$1,000 purchase payment made at the beginning of the 1-year, 3-year, 5-year, or 10-year period in question (or fractional period thereof)

The formula assumes that:

- (1) all recurring fees have been charged to the policy owner's accounts; and
- (2) there will be a complete redemption upon the anniversary of the 1-year, 3-year, 5-year, or 10-year period in question.

In accordance with SEC guidelines, we report Sub-Account performance back to the first date that the fund became available, which could pre-date its inclusion in this product. Where the length of the performance reporting period exceeds the period for which the fund was available, Sub-Account performance will show an "N/A".

FINANCIAL STATEMENTS

The December 31, 2008 financial statements of the Separate Account and the December 31, 2008 consolidated financial statements of the Company follow.

Lincoln Life Flexible Premium Variable Life Account R

Statement of assets and liabilities

December 31, 2008

<i>Subaccount</i>	<i>Investments</i>	<i>Contract Purchases Due From The Lincoln National Life Insurance Company</i>	<i>Total Assets</i>	<i>Contract Redemptions Due To The Lincoln National Life Insurance Company</i>	<i>Mortality & Expense Guarantee Charges Payable To The Lincoln National Life Insurance Company</i>	<i>Net Assets</i>
AIM V.I. Capital Appreciation	\$ 8,945,323	\$ —	\$ 8,945,323	\$ 98	\$194	\$ 8,945,031
AIM V.I. Core Equity	10,519,577	—	10,519,577	24,952	227	10,494,398
AIM V.I. Diversified Income	535,319	632	535,951	—	12	535,939
AIM V.I. International Growth	4,403,940	—	4,403,940	80	96	4,403,764
ABVPSF Global Technology Class A	854,596	—	854,596	—	17	854,579
ABVPSF Growth and Income Class A	5,553,559	—	5,553,559	—	111	5,553,448
ABVPSF International Value Class A	1,629,216	—	1,629,216	24	27	1,629,165
ABVPSF Large Cap Growth Class A	1,082,945	—	1,082,945	—	23	1,082,922
ABVPSF Small/Mid Cap Value Class A	5,336,922	—	5,336,922	44	104	5,336,774
American Century VP Inflation Protection	5,584,897	—	5,584,897	—	110	5,584,787
American Funds Global Growth Class 2	5,208,621	—	5,208,621	—	94	5,208,527
American Funds Global Small Capitalization Class 2	6,415,714	1,063	6,416,777	—	128	6,416,649
American Funds Growth Class 2	33,821,598	10,120	33,831,718	—	682	33,831,036
American Funds Growth-Income Class 2	26,473,905	3,816	26,477,721	—	536	26,477,185
American Funds International Class 2	15,339,275	—	15,339,275	80	303	15,338,892
Delaware VIPT Capital Reserves	820,097	—	820,097	—	14	820,083
Delaware VIPT Diversified Income	7,086,731	—	7,086,731	—	134	7,086,597
Delaware VIPT Emerging Markets	8,143,759	885	8,144,644	—	157	8,144,487
Delaware VIPT High Yield	7,421,000	7,084	7,428,084	—	147	7,427,937
Delaware VIPT REIT	5,800,771	11,183	5,811,954	—	113	5,811,841
Delaware VIPT Small Cap Value	15,131,870	4,957	15,136,827	—	310	15,136,517
Delaware VIPT Trend	7,082,592	1,944	7,084,536	—	149	7,084,387
Delaware VIPT U.S. Growth	431,980	—	431,980	—	8	431,972
Delaware VIPT Value	8,188,944	—	8,188,944	—	151	8,188,793
DWS VIP Equity 500 Index	30,554,388	—	30,554,388	425	628	30,553,335
DWS VIP Small Cap Index	4,182,619	2,662	4,185,281	—	85	4,185,196
Fidelity VIP Asset Manager	1,043,157	—	1,043,157	—	23	1,043,134
Fidelity VIP Contrafund Service Class	19,665,951	—	19,665,951	14,956	400	19,650,995
Fidelity VIP Equity-Income	2,271,629	—	2,271,629	—	49	2,271,580
Fidelity VIP Equity-Income Service Class	1,769,294	—	1,769,294	—	37	1,769,257
Fidelity VIP Growth Service Class	4,244,340	14,101	4,258,441	—	89	4,258,352
Fidelity VIP Growth Opportunities Service Class	895,518	—	895,518	7,777	19	887,722
Fidelity VIP High Income Service Class	1,337,427	—	1,337,427	—	29	1,337,398
Fidelity VIP Investment Grade Bond	2,401,059	607	2,401,666	—	53	2,401,613
Fidelity VIP Mid Cap Service Class	2,217,763	—	2,217,763	—	37	2,217,726
Fidelity VIP Overseas Service Class	2,963,110	10,120	2,973,230	—	58	2,973,172
FTVIPT Franklin Income Securities	1,381,679	—	1,381,679	25	25	1,381,629
FTVIPT Franklin Small-Mid Cap Growth Securities	2,484,780	—	2,484,780	—	48	2,484,732
FTVIPT Mutual Shares Securities	1,267,626	—	1,267,626	—	21	1,267,605
FTVIPT Templeton Foreign Securities	3,691,022	—	3,691,022	38	81	3,690,903
FTVIPT Templeton Foreign Securities Class 2	3,729,438	1,063	3,730,501	—	81	3,730,420
FTVIPT Templeton Global Asset Allocation	1,550,524	—	1,550,524	62	34	1,550,428
FTVIPT Templeton Global Income Securities	2,164,834	—	2,164,834	24	38	2,164,772
FTVIPT Templeton Growth Securities	3,233,425	—	3,233,425	—	64	3,233,361
FTVIPT Templeton Growth Securities Class 2	1,308,426	—	1,308,426	—	29	1,308,397
Janus Aspen Series Balanced	8,116,037	—	8,116,037	41	177	8,115,819
Janus Aspen Series Balanced Service Shares	1,304,377	—	1,304,377	9,200	28	1,295,149
Janus Aspen Series Global Technology Service Shares	1,009,194	1,008	1,010,202	—	22	1,010,180
Janus Aspen Series Mid Cap Growth Service Shares	1,922,797	—	1,922,797	78	41	1,922,678

See accompanying notes.

Statement of assets and liabilities (continued)

December 31, 2008

<i>Subaccount</i>	<i>Investments</i>	<i>Contract Purchases Due From The Lincoln National Life Insurance Company</i>	<i>Total Assets</i>	<i>Contract Redemptions Due To The Lincoln National Life Insurance Company</i>	<i>Mortality & Expense Guarantee Charges Payable To The Lincoln National Life Insurance Company</i>	<i>Net Assets</i>
Janus Aspen Series Worldwide Growth	\$ 4,944,928	\$ —	\$ 4,944,928	\$ 4,453	\$107	\$ 4,940,368
Janus Aspen Series Worldwide Growth Service Shares	1,137,812	—	1,137,812	—	25	1,137,787
Lincoln VIPT Baron Growth Opportunities	21,042	—	21,042	—	—	21,042
Lincoln VIPT Baron Growth Opportunities Service Class	3,500,523	—	3,500,523	—	73	3,500,450
Lincoln VIPT Capital Growth	178,980	—	178,980	—	2	178,978
Lincoln VIPT Cohen & Steers Global Real Estate	471,613	—	471,613	—	7	471,606
Lincoln VIPT Columbia Value Opportunities	108,321	—	108,321	—	2	108,319
Lincoln VIPT Delaware Bond	30,392,234	—	30,392,234	5,640	633	30,385,961
Lincoln VIPT Delaware Growth and Income	261,169	—	261,169	—	5	261,164
Lincoln VIPT Delaware Social Awareness	652,621	—	652,621	—	13	652,608
Lincoln VIPT Delaware Special Opportunities	296,772	—	296,772	—	5	296,767
Lincoln VIPT FI Equity-Income	2,541,458	7,084	2,548,542	—	53	2,548,489
Lincoln VIPT Janus Capital Appreciation	2,193,767	—	2,193,767	27	43	2,193,697
Lincoln VIPT Marsico International Growth	701,847	—	701,847	—	12	701,835
Lincoln VIPT MFS Value	1,158,706	—	1,158,706	—	20	1,158,686
Lincoln VIPT Mid-Cap Value	194,418	—	194,418	—	3	194,415
Lincoln VIPT Mondrian International Value	7,470,613	1,008	7,471,621	—	144	7,471,477
Lincoln VIPT Money Market	36,655,067	71,335	36,726,402	—	733	36,725,669
Lincoln VIPT SSgA Bond Index	192,919	—	192,919	—	3	192,916
Lincoln VIPT SSgA Emerging Markets 100	16,438	—	16,438	—	—	16,438
Lincoln VIPT SSgA International Index	18,287	—	18,287	—	—	18,287
Lincoln VIPT SSgA Large Cap 100	89,255	—	89,255	—	2	89,253
Lincoln VIPT SSgA S&P 500 Index	1,374,953	—	1,374,953	—	23	1,374,930
Lincoln VIPT SSgA Small-Cap Index	193,525	—	193,525	—	3	193,522
Lincoln VIPT SSgA Small-Mid Cap 200	19,863	—	19,863	—	—	19,863
Lincoln VIPT T. Rowe Price Growth Stock	76,263	—	76,263	—	1	76,262
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	768,814	—	768,814	—	14	768,800
Lincoln VIPT Templeton Growth	82,414	—	82,414	—	1	82,413
Lincoln VIPT Turner Mid-Cap Growth	288,861	—	288,861	—	5	288,856
Lincoln VIPT UBS Global Asset Allocation	1,809,758	—	1,809,758	—	34	1,809,724
Lincoln VIPT Wilshire 2010 Profile	112,523	—	112,523	—	2	112,521
Lincoln VIPT Wilshire 2020 Profile	85,989	—	85,989	—	1	85,988
Lincoln VIPT Wilshire 2030 Profile	461,750	—	461,750	—	8	461,742
Lincoln VIPT Wilshire 2040 Profile	86,458	—	86,458	—	1	86,457
Lincoln VIPT Wilshire Aggressive Profile	1,373,002	3,840	1,376,842	—	21	1,376,821
Lincoln VIPT Wilshire Conservative Profile	717,570	—	717,570	—	13	717,557
Lincoln VIPT Wilshire Moderate Profile	4,984,957	—	4,984,957	—	80	4,984,877
Lincoln VIPT Wilshire Moderately Aggressive Profile	6,292,111	—	6,292,111	—	106	6,292,005
M Fund Brandes International Equity	1,346,865	—	1,346,865	—	25	1,346,840
M Fund Business Opportunity Value	226,095	—	226,095	—	3	226,092
M Fund Frontier Capital Appreciation	803,862	—	803,862	—	14	803,848
M Fund Turner Core Growth	837,872	—	837,872	—	16	837,856
MFS VIT Core Equity	483,515	—	483,515	—	10	483,505
MFS VIT Growth	4,974,230	—	4,974,230	11	107	4,974,112
MFS VIT Total Return	13,978,656	—	13,978,656	11,666	295	13,966,695
MFS VIT Utilities	10,079,367	—	10,079,367	6,525	209	10,072,633
NB AMT Mid-Cap Growth	7,169,923	—	7,169,923	4,406	149	7,165,368
NB AMT Partners	1,562,064	—	1,562,064	26	34	1,562,004
NB AMT Regency	2,252,470	—	2,252,470	—	44	2,252,426
Premier VIT OPCAP Managed	326,072	—	326,072	—	7	326,065
Putnam VT Growth & Income Class IB	369,513	—	369,513	—	8	369,505
Putnam VT Health Sciences Class IB	360,273	—	360,273	—	8	360,265

See accompanying notes.

Statement of operations

Year Ended December 31, 2008

<i>Subaccount</i>	<i>Dividends from Investment Income</i>	<i>Mortality and Expense Guarantee Charges</i>	<i>Net Investment Income (Loss)</i>
AIM V.I. Capital Appreciation	\$ —	\$ (97,967)	\$ (97,967)
AIM V.I. Core Equity	300,767	(108,747)	192,020
AIM V.I. Diversified Income	56,807	(5,553)	51,254
AIM V.I. International Growth	33,905	(51,416)	(17,511)
ABVPSF Global Technology Class A	—	(9,263)	(9,263)
ABVPSF Growth and Income Class A	157,972	(54,843)	103,129
ABVPSF International Value Class A	27,644	(15,498)	12,146
ABVPSF Large Cap Growth Class A	—	(11,518)	(11,518)
ABVPSF Small/Mid Cap Value Class A	53,922	(53,610)	312
American Century VP Inflation Protection	245,986	(35,450)	210,536
American Funds Global Growth Class 2	127,774	(42,273)	85,501
American Funds Global Small Capitalization Class 2	—	(78,946)	(78,946)
American Funds Growth Class 2	402,616	(358,480)	44,136
American Funds Growth-Income Class 2	618,997	(260,418)	358,579
American Funds International Class 2	418,577	(146,428)	272,149
Delaware VIPT Capital Reserves	27,515	(3,697)	23,818
Delaware VIPT Diversified Income	279,541	(49,977)	229,564
Delaware VIPT Emerging Markets	208,278	(93,407)	114,871
Delaware VIPT High Yield	743,816	(66,325)	677,491
Delaware VIPT REIT	209,916	(64,188)	145,728
Delaware VIPT Small Cap Value	157,765	(156,157)	1,608
Delaware VIPT Trend	—	(82,274)	(82,274)
Delaware VIPT U.S. Growth	229	(4,346)	(4,117)
Delaware VIPT Value	314,540	(74,847)	239,693
DWS VIP Equity 500 Index	993,041	(310,976)	682,065
DWS VIP Small Cap Index	92,240	(43,497)	48,743
Fidelity VIP Asset Manager	36,186	(8,520)	27,666
Fidelity VIP Contrafund Service Class	252,186	(200,313)	51,873
Fidelity VIP Equity-Income	83,516	(25,694)	57,822
Fidelity VIP Equity-Income Service Class	63,258	(21,396)	41,862
Fidelity VIP Growth Service Class	46,344	(47,910)	(1,566)
Fidelity VIP Growth Opportunities Service Class	5,406	(10,880)	(5,474)
Fidelity VIP High Income Service Class	149,574	(13,918)	135,656
Fidelity VIP Investment Grade Bond	92,053	(20,385)	71,668
Fidelity VIP Mid Cap Service Class	10,330	(16,941)	(6,611)
Fidelity VIP Overseas Service Class	111,123	(31,885)	79,238
FTVIPT Franklin Income Securities	79,129	(8,824)	70,305
FTVIPT Franklin Small-Mid Cap Growth Securities	—	(24,980)	(24,980)
FTVIPT Mutual Shares Securities	54,041	(10,299)	43,742
FTVIPT Templeton Foreign Securities	126,039	(39,789)	86,250
FTVIPT Templeton Foreign Securities Class 2	121,358	(40,891)	80,467
FTVIPT Templeton Global Asset Allocation	346,017	(20,616)	325,401
FTVIPT Templeton Global Income Securities	64,031	(12,150)	51,881
FTVIPT Templeton Growth Securities	95,621	(34,242)	61,379
FTVIPT Templeton Growth Securities Class 2	32,569	(14,815)	17,754
Janus Aspen Series Balanced	255,536	(76,822)	178,714
Janus Aspen Series Balanced Service Shares	35,571	(11,564)	24,007
Janus Aspen Series Global Technology Service Shares	1,117	(10,298)	(9,181)
Janus Aspen Series Mid Cap Growth Service Shares	1,886	(21,368)	(19,482)
Janus Aspen Series Worldwide Growth	84,925	(54,638)	30,287
Janus Aspen Series Worldwide Growth Service Shares	15,984	(12,273)	3,711
Lincoln VIPT Baron Growth Opportunities	—	(321)	(321)
Lincoln VIPT Baron Growth Opportunities Service Class	—	(38,270)	(38,270)
Lincoln VIPT Capital Growth	544	(1,139)	(595)
Lincoln VIPT Cohen & Steers Global Real Estate	9,232	(3,404)	5,828
Lincoln VIPT Columbia Value Opportunities	598	(293)	305
Lincoln VIPT Delaware Bond	1,546,046	(255,342)	1,290,704

See accompanying notes.

<i>Net Realized Gain (Loss) on Investments</i>	<i>Dividends from Net Realized Gain on Investments</i>	<i>Total Net Realized Gain (Loss) on Investments</i>	<i>Net Change in Unrealized Appreciation or Depreciation on Investments</i>	<i>Net Increase (Decrease) in Net Assets Resulting from Operations</i>
\$ (87,637)	\$ —	\$ (87,637)	\$ (6,434,733)	\$ (6,620,337)
60,067	—	60,067	(4,975,869)	(4,723,782)
(37,338)	—	(37,338)	(127,630)	(113,714)
70,647	81,986	152,633	(3,396,103)	(3,260,981)
10,679	—	10,679	(768,253)	(766,837)
(247,537)	1,344,891	1,097,354	(4,985,138)	(3,784,655)
(396,730)	152,467	(244,263)	(1,661,242)	(1,893,359)
(7,663)	—	(7,663)	(686,393)	(705,574)
(190,332)	766,565	576,233	(3,543,556)	(2,967,011)
176	—	176	(405,441)	(194,729)
(35,567)	539,851	504,284	(3,635,797)	(3,046,012)
(186,309)	1,475,198	1,288,889	(8,728,398)	(7,518,455)
203,655	5,376,758	5,580,413	(31,303,109)	(25,678,560)
(129,832)	2,284,496	2,154,664	(18,390,030)	(15,876,787)
(15,517)	2,703,125	2,687,608	(13,726,626)	(10,766,869)
(3,141)	—	(3,141)	(29,321)	(8,644)
(11,119)	95,941	84,822	(726,394)	(412,008)
(29,909)	2,119,157	2,089,248	(10,713,765)	(8,509,646)
(379,316)	—	(379,316)	(2,650,961)	(2,352,786)
(815,574)	3,262,141	2,446,567	(5,804,953)	(3,212,658)
(192,832)	1,382,206	1,189,374	(7,923,340)	(6,732,358)
(172,138)	2,103,862	1,931,724	(8,004,999)	(6,155,549)
(18,164)	14,861	(3,303)	(319,355)	(326,775)
(679,748)	903,073	223,325	(4,859,522)	(4,396,504)
23,116	—	23,116	(19,186,040)	(18,480,859)
(150,401)	586,524	436,123	(2,766,273)	(2,281,407)
(8,369)	80,995	72,626	(547,620)	(447,328)
(627,652)	763,693	136,041	(14,419,529)	(14,231,615)
(68,929)	3,261	(65,668)	(1,716,730)	(1,724,576)
(197,718)	2,817	(194,901)	(1,311,667)	(1,464,706)
95,741	—	95,741	(3,784,043)	(3,689,868)
(5,750)	—	(5,750)	(1,001,439)	(1,012,663)
(43,868)	—	(43,868)	(563,774)	(471,986)
(45,373)	1,787	(43,586)	(149,765)	(121,683)
(131,352)	409,341	277,989	(1,625,887)	(1,354,509)
(154,366)	508,221	353,855	(2,885,233)	(2,452,140)
(144,313)	31,699	(112,614)	(420,821)	(463,130)
(56,337)	423,261	366,924	(2,155,736)	(1,813,792)
(80,291)	69,594	(10,697)	(769,891)	(736,846)
(113,382)	456,054	342,672	(3,005,689)	(2,576,767)
39,360	496,688	536,048	(3,174,183)	(2,557,668)
(740,758)	420,918	(319,840)	(615,738)	(610,177)
46,770	—	46,770	(1,406)	97,245
(131,024)	317,873	186,849	(2,736,304)	(2,488,076)
(7,703)	128,341	120,638	(1,130,798)	(992,406)
(12,873)	679,549	666,676	(2,593,287)	(1,747,897)
4,556	99,752	104,308	(393,129)	(264,814)
(20,271)	—	(20,271)	(677,149)	(706,601)
(6,041)	165,187	159,146	(1,637,682)	(1,498,018)
(58,967)	—	(58,967)	(3,842,890)	(3,871,570)
21,961	—	21,961	(888,331)	(862,659)
(7,958)	2,604	(5,354)	(12,052)	(17,727)
(166)	255,169	255,003	(2,483,619)	(2,266,886)
(9,316)	—	(9,316)	(87,545)	(97,456)
(78,452)	—	(78,452)	(278,807)	(351,431)
(1,308)	24,005	22,697	(63,020)	(40,018)
(270,135)	12,286	(257,849)	(2,344,531)	(1,311,676)

Statement of operations (continued)

Year Ended December 31, 2008

<i>Subaccount</i>	<i>Dividends from Investment Income</i>	<i>Mortality and Expense Guarantee Charges</i>	<i>Net Investment Income (Loss)</i>
Lincoln VIPT Delaware Growth and Income	\$ 4,567	\$ (1,860)	\$ 2,707
Lincoln VIPT Delaware Social Awareness	7,831	(6,373)	1,458
Lincoln VIPT Delaware Special Opportunities	4,093	(1,444)	2,649
Lincoln VIPT FI Equity-Income	52,969	(26,488)	26,481
Lincoln VIPT Janus Capital Appreciation	20,975	(21,719)	(744)
Lincoln VIPT Marsico International Growth	12,030	(4,899)	7,131
Lincoln VIPT MFS Value	15,367	(4,718)	10,649
Lincoln VIPT Mid-Cap Value	866	(1,337)	(471)
Lincoln VIPT Mondrian International Value	482,367	(71,942)	410,425
Lincoln VIPT Money Market	733,856	(234,703)	499,153
Lincoln VIPT SSgA Bond Index	1,215	(178)	1,037
Lincoln VIPT SSgA Emerging Markets 100	116	(9)	107
Lincoln VIPT SSgA International Index	181	(75)	106
Lincoln VIPT SSgA Large Cap 100	524	(185)	339
Lincoln VIPT SSgA S&P 500 Index	55,347	(7,462)	47,885
Lincoln VIPT SSgA Small-Cap Index	2,455	(1,211)	1,244
Lincoln VIPT SSgA Small-Mid Cap 200	194	(83)	111
Lincoln VIPT T. Rowe Price Growth Stock	284	(496)	(212)
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	—	(8,366)	(8,366)
Lincoln VIPT Templeton Growth	2,048	(380)	1,668
Lincoln VIPT Turner Mid-Cap Growth	—	(1,249)	(1,249)
Lincoln VIPT UBS Global Asset Allocation	154,720	(16,307)	138,413
Lincoln VIPT Wilshire 2010 Profile	2,163	(223)	1,940
Lincoln VIPT Wilshire 2020 Profile	1,267	(319)	948
Lincoln VIPT Wilshire 2030 Profile	4,662	(2,424)	2,238
Lincoln VIPT Wilshire 2040 Profile	326	(178)	148
Lincoln VIPT Wilshire Aggressive Profile	10,227	(8,815)	1,412
Lincoln VIPT Wilshire Conservative Profile	15,336	(4,599)	10,737
Lincoln VIPT Wilshire Moderate Profile	108,038	(26,758)	81,280
Lincoln VIPT Wilshire Moderately Aggressive Profile	80,602	(37,595)	43,007
M Fund Brandes International Equity	63,529	(11,134)	52,395
M Fund Business Opportunity Value	106	(1,345)	(1,239)
M Fund Frontier Capital Appreciation	—	(6,659)	(6,659)
M Fund Turner Core Growth	225	(7,579)	(7,354)
MFS VIT Core Equity	5,079	(5,174)	(95)
MFS VIT Growth	15,942	(55,472)	(39,530)
MFS VIT Total Return	515,701	(129,854)	385,847
MFS VIT Utilities	209,185	(106,786)	102,399
NB AMT Mid-Cap Growth	—	(78,416)	(78,416)
NB AMT Partners	13,610	(19,817)	(6,207)
NB AMT Regency	41,862	(25,064)	16,798
Premier VIT OPCAP Global Equity	6,486	(171)	6,315
Premier VIT OPCAP Managed	14,720	(3,528)	11,192
Putnam VT Growth & Income Class IB	10,570	(3,984)	6,586
Putnam VT Health Sciences Class IB	—	(3,952)	(3,952)

See accompanying notes.

<i>Net Realized Gain (Loss) on Investments</i>	<i>Dividends from Net Realized Gain on Investments</i>	<i>Total Net Realized Gain (Loss) on Investments</i>	<i>Net Change in Unrealized Appreciation or Depreciation on Investments</i>	<i>Net Increase (Decrease) in Net Assets Resulting from Operations</i>
\$ (4,316)	\$ 33,506	\$ 29,190	\$ (158,312)	\$ (126,415)
20,891	51,375	72,266	(416,301)	(342,577)
(9,584)	26,820	17,236	(137,258)	(117,373)
(127,866)	301,359	173,493	(1,827,997)	(1,628,023)
(9,695)	—	(9,695)	(1,476,319)	(1,486,758)
(48,500)	84,923	36,423	(556,433)	(512,879)
(43,142)	23,890	(19,252)	(327,128)	(335,731)
(88,285)	20,090	(68,195)	(59,641)	(128,307)
76,789	644,446	721,235	(5,636,378)	(4,504,718)
(22)	138	116	2	499,271
407	—	407	7,272	8,716
22	—	22	1,634	1,763
(140)	—	(140)	(9,581)	(9,615)
(424)	—	(424)	(28,996)	(29,081)
(276,496)	—	(276,496)	(408,511)	(637,122)
(12,869)	21,010	8,141	(95,553)	(86,168)
(95)	—	(95)	(8,019)	(8,003)
(5,916)	—	(5,916)	(43,583)	(49,711)
(116,225)	—	(116,225)	(528,030)	(652,621)
(1,502)	3,376	1,874	(38,130)	(34,588)
(70,036)	40,929	(29,107)	(95,705)	(126,061)
(70,636)	219,893	149,257	(1,202,548)	(914,878)
(4,655)	2	(4,653)	(26,085)	(28,798)
(296)	74	(222)	(20,941)	(20,215)
(2,494)	499	(1,995)	(163,902)	(163,659)
(965)	21	(944)	(16,923)	(17,719)
(17,343)	42,292	24,949	(821,146)	(794,785)
3,467	7,143	10,610	(161,187)	(139,840)
(65,176)	101,997	36,821	(1,526,652)	(1,408,551)
(88,668)	149,574	60,906	(2,942,834)	(2,838,921)
(57,599)	149,736	92,137	(953,064)	(808,532)
(2,722)	7,293	4,571	(106,963)	(103,631)
(15,838)	33,529	17,691	(514,524)	(503,492)
(6,773)	30,694	23,921	(695,958)	(679,391)
4,181	—	4,181	(313,822)	(309,736)
99,804	—	99,804	(3,114,212)	(3,053,938)
(145,992)	1,021,442	875,450	(5,477,577)	(4,216,280)
383,408	2,165,401	2,548,809	(8,858,782)	(6,207,574)
212,520	—	212,520	(5,652,834)	(5,518,730)
(35,032)	429,442	394,410	(2,016,332)	(1,628,129)
(4,184)	7,735	3,551	(1,929,169)	(1,908,820)
(127,576)	93,549	(34,027)	2,970	(24,742)
(28,995)	41,122	12,127	(177,909)	(154,590)
(26,285)	90,885	64,600	(311,287)	(240,101)
(9,356)	4,166	(5,190)	(107,371)	(116,513)

Statements of changes in net assets

Years Ended December 31, 2007 and 2008

	<i>AIM V.I. Capital Appreciation Subaccount</i>	<i>AIM V.I. Core Equity Subaccount</i>	<i>AIM V.I. Diversified Income Subaccount</i>	<i>AIM V.I. International Growth Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$14,527,585	\$15,400,302	\$ 943,460	\$ 5,942,014
Changes From Operations:				
• Net investment income (loss)	(119,577)	49,057	52,982	(26,439)
• Net realized gain (loss) on investments	109,209	276,305	(14,495)	562,202
• Net change in unrealized appreciation or depreciation on investments	<u>1,556,653</u>	<u>798,038</u>	<u>(28,190)</u>	<u>383,020</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	1,546,285	1,123,400	10,297	918,783
Changes From Unit Transactions:				
• Contract purchases	1,359,052	1,283,612	74,622	555,581
• Contract withdrawals	(1,303,403)	(1,072,610)	(177,509)	(486,370)
• Contract transfers	<u>(819,065)</u>	<u>(900,526)</u>	<u>(33,139)</u>	<u>1,242,509</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>(763,416)</u>	<u>(689,524)</u>	<u>(136,026)</u>	<u>1,311,720</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>782,869</u>	<u>433,876</u>	<u>(125,729)</u>	<u>2,230,503</u>
NET ASSETS AT DECEMBER 31, 2007	15,310,454	15,834,178	817,731	8,172,517
Changes From Operations:				
• Net investment income (loss)	(97,967)	192,020	51,254	(17,511)
• Net realized gain (loss) on investments	(87,637)	60,067	(37,338)	152,633
• Net change in unrealized appreciation or depreciation on investments	<u>(6,434,733)</u>	<u>(4,975,869)</u>	<u>(127,630)</u>	<u>(3,396,103)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(6,620,337)	(4,723,782)	(113,714)	(3,260,981)
Changes From Unit Transactions:				
• Contract purchases	1,143,673	1,022,411	35,810	475,757
• Contract withdrawals	(1,185,167)	(1,167,674)	(55,624)	(417,777)
• Contract transfers	<u>296,408</u>	<u>(470,735)</u>	<u>(148,264)</u>	<u>(565,752)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>254,914</u>	<u>(615,998)</u>	<u>(168,078)</u>	<u>(507,772)</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(6,365,423)</u>	<u>(5,339,780)</u>	<u>(281,792)</u>	<u>(3,768,753)</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 8,945,031</u>	<u>\$10,494,398</u>	<u>\$ 535,939</u>	<u>\$ 4,403,764</u>

See accompanying notes.

<i>ABVPSF Global Technology Class A Subaccount</i>	<i>ABVPSF Growth and Income Class A Subaccount</i>	<i>ABVPSF International Value Class A Subaccount</i>	<i>ABVPSF Large Cap Growth Class A Subaccount</i>	<i>ABVPSF Small/Mid Cap Value Class A Subaccount</i>	<i>American Century VP Inflation Protection Subaccount</i>	<i>American Funds Global Growth Class 2 Subaccount</i>	<i>American Funds Global Small Capitalization Class 2 Subaccount</i>	<i>American Funds Growth Class 2 Subaccount</i>
\$ 899,887	\$ 7,873,920	\$ 745,819	\$1,241,857	\$ 6,313,513	\$3,290,943	\$ 4,096,785	\$10,809,203	\$ 50,516,050
(8,918)	58,735	8,225	(11,557)	7,941	132,552	131,098	282,152	16,376
21,673	731,676	113,504	20,552	641,650	(13,380)	338,296	1,680,212	5,036,355
<u>184,654</u>	<u>(395,801)</u>	<u>(120,797)</u>	<u>157,985</u>	<u>(739,789)</u>	<u>176,855</u>	<u>256,735</u>	<u>298,480</u>	<u>809,367</u>
197,409	394,610	932	166,980	(90,198)	296,027	726,129	2,260,844	5,862,098
59,842	908,175	456,227	129,134	958,732	334,645	636,983	1,049,693	5,012,954
(46,762)	(494,140)	(97,240)	(67,344)	(430,396)	(126,978)	(427,349)	(897,048)	(3,690,776)
<u>448,242</u>	<u>497,703</u>	<u>1,668,448</u>	<u>307,708</u>	<u>1,294,784</u>	<u>67,336</u>	<u>1,884,987</u>	<u>639,498</u>	<u>(513,255)</u>
<u>461,322</u>	<u>911,738</u>	<u>2,027,435</u>	<u>369,498</u>	<u>1,823,120</u>	<u>275,003</u>	<u>2,094,621</u>	<u>792,143</u>	<u>808,923</u>
<u>658,731</u>	<u>1,306,348</u>	<u>2,028,367</u>	<u>536,478</u>	<u>1,732,922</u>	<u>571,030</u>	<u>2,820,750</u>	<u>3,052,987</u>	<u>6,671,021</u>
1,558,618	9,180,268	2,774,186	1,778,335	8,046,435	3,861,973	6,917,535	13,862,190	57,187,071
(9,263)	103,129	12,146	(11,518)	312	210,536	85,501	(78,946)	44,136
10,679	1,097,354	(244,263)	(7,663)	576,233	176	504,284	1,288,889	5,580,413
<u>(768,253)</u>	<u>(4,985,138)</u>	<u>(1,661,242)</u>	<u>(686,393)</u>	<u>(3,543,556)</u>	<u>(405,441)</u>	<u>(3,635,797)</u>	<u>(8,728,398)</u>	<u>(31,303,109)</u>
(766,837)	(3,784,655)	(1,893,359)	(705,574)	(2,967,011)	(194,729)	(3,046,012)	(7,518,455)	(25,678,560)
78,438	766,655	544,624	156,846	942,524	722,786	1,029,950	1,143,156	5,225,198
(89,423)	(420,262)	(147,383)	(136,892)	(478,180)	(282,417)	(304,002)	(700,976)	(3,607,280)
<u>73,783</u>	<u>(188,558)</u>	<u>351,097</u>	<u>(9,793)</u>	<u>(206,994)</u>	<u>1,477,174</u>	<u>611,056</u>	<u>(369,266)</u>	<u>704,607</u>
<u>62,798</u>	<u>157,835</u>	<u>748,338</u>	<u>10,161</u>	<u>257,350</u>	<u>1,917,543</u>	<u>1,337,004</u>	<u>72,914</u>	<u>2,322,525</u>
<u>(704,039)</u>	<u>(3,626,820)</u>	<u>(1,145,021)</u>	<u>(695,413)</u>	<u>(2,709,661)</u>	<u>1,722,814</u>	<u>(1,709,008)</u>	<u>(7,445,541)</u>	<u>(23,356,035)</u>
<u>\$ 854,579</u>	<u>\$ 5,553,448</u>	<u>\$ 1,629,165</u>	<u>\$1,082,922</u>	<u>\$ 5,336,774</u>	<u>\$5,584,787</u>	<u>\$ 5,208,527</u>	<u>\$ 6,416,649</u>	<u>\$ 33,831,036</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>American Funds Growth-Income Class 2 Subaccount</i>	<i>American Funds International Class 2 Subaccount</i>	<i>Delaware VIPT Capital Reserves Subaccount</i>	<i>Delaware VIPT Diversified Income Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 36,895,346	\$ 17,126,292	\$308,756	\$3,982,317
Changes From Operations:				
• Net investment income (loss)	311,509	179,835	14,020	127,227
• Net realized gain (loss) on investments	2,046,217	1,440,397	2	40,268
• Net change in unrealized appreciation or depreciation on investments	<u>(753,486)</u>	<u>1,947,758</u>	<u>(1,423)</u>	<u>196,495</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	1,604,240	3,567,990	12,599	363,990
Changes From Unit Transactions:				
• Contract purchases	3,764,314	2,424,296	13,761	859,391
• Contract withdrawals	(2,510,313)	(1,424,949)	(7,398)	(270,250)
• Contract transfers	<u>318,102</u>	<u>2,139,134</u>	<u>40,831</u>	<u>1,911,129</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>1,572,103</u>	<u>3,138,481</u>	<u>47,194</u>	<u>2,500,270</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>3,176,343</u>	<u>6,706,471</u>	<u>59,793</u>	<u>2,864,260</u>
NET ASSETS AT DECEMBER 31, 2007	40,071,689	23,832,763	368,549	6,846,577
Changes From Operations:				
• Net investment income (loss)	358,579	272,149	23,818	229,564
• Net realized gain (loss) on investments	2,154,664	2,687,608	(3,141)	84,822
• Net change in unrealized appreciation or depreciation on investments	<u>(18,390,030)</u>	<u>(13,726,626)</u>	<u>(29,321)</u>	<u>(726,394)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(15,876,787)	(10,766,869)	(8,644)	(412,008)
Changes From Unit Transactions:				
• Contract purchases	3,912,072	2,436,094	167,057	784,214
• Contract withdrawals	(2,279,591)	(1,512,969)	(30,618)	(432,614)
• Contract transfers	<u>649,802</u>	<u>1,349,873</u>	<u>323,739</u>	<u>300,428</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>2,282,283</u>	<u>2,272,998</u>	<u>460,178</u>	<u>652,028</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(13,594,504)</u>	<u>(8,493,871)</u>	<u>451,534</u>	<u>240,020</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 26,477,185</u>	<u>\$ 15,338,892</u>	<u>\$820,083</u>	<u>\$7,086,597</u>

See accompanying notes.

<i>Delaware VIPT Emerging Markets Subaccount</i>	<i>Delaware VIPT High Yield Subaccount</i>	<i>Delaware VIPT REIT Subaccount</i>	<i>Delaware VIPT Small Cap Value Subaccount</i>	<i>Delaware VIPT Trend Subaccount</i>	<i>Delaware VIPT U.S. Growth Subaccount</i>	<i>Delaware VIPT Value Subaccount</i>	<i>DWS VIP Equity 500 Index Subaccount</i>	<i>DWS VIP Small Cap Index Subaccount</i>
\$ 10,317,924	\$ 8,546,219	\$ 11,396,157	\$ 25,262,583	\$ 12,114,068	\$ 527,633	\$ 9,246,125	\$ 45,098,258	\$ 6,805,742
99,522	498,694	67,900	(71,599)	(100,242)	(4,632)	88,374	352,594	5,978
1,855,127	179,381	2,518,975	2,708,749	670,329	21,723	467,541	1,209,791	674,978
<u>2,264,960</u>	<u>(511,323)</u>	<u>(4,301,976)</u>	<u>(4,523,731)</u>	<u>603,537</u>	<u>49,048</u>	<u>(1,106,444)</u>	<u>404,895</u>	<u>(881,683)</u>
4,219,609	166,752	(1,715,101)	(1,886,581)	1,173,624	66,139	(550,529)	1,967,280	(200,727)
1,074,356	788,549	1,138,426	1,647,187	816,437	74,575	1,310,974	4,412,819	668,103
(660,970)	(593,959)	(597,627)	(1,555,258)	(921,915)	(120,441)	(481,824)	(4,530,356)	(445,760)
<u>1,496,435</u>	<u>375,978</u>	<u>(553,864)</u>	<u>(475,130)</u>	<u>(16,413)</u>	<u>88,765</u>	<u>3,469,153</u>	<u>1,706,924</u>	<u>(238,097)</u>
<u>1,909,821</u>	<u>570,568</u>	<u>(13,065)</u>	<u>(383,201)</u>	<u>(121,891)</u>	<u>42,899</u>	<u>4,298,303</u>	<u>1,589,387</u>	<u>(15,754)</u>
<u>6,129,430</u>	<u>737,320</u>	<u>(1,728,166)</u>	<u>(2,269,782)</u>	<u>1,051,733</u>	<u>109,038</u>	<u>3,747,774</u>	<u>3,556,667</u>	<u>(216,481)</u>
16,447,354	9,283,539	9,667,991	22,992,801	13,165,801	636,671	12,993,899	48,654,925	6,589,261
114,871	677,491	145,728	1,608	(82,274)	(4,117)	239,693	682,065	48,743
2,089,248	(379,316)	2,446,567	1,189,374	1,931,724	(3,303)	223,325	23,116	436,123
<u>(10,713,765)</u>	<u>(2,650,961)</u>	<u>(5,804,953)</u>	<u>(7,923,340)</u>	<u>(8,004,999)</u>	<u>(319,355)</u>	<u>(4,859,522)</u>	<u>(19,186,040)</u>	<u>(2,766,273)</u>
(8,509,646)	(2,352,786)	(3,212,658)	(6,732,358)	(6,155,549)	(326,775)	(4,396,504)	(18,480,859)	(2,281,407)
1,056,300	1,106,432	676,326	1,432,651	917,109	119,479	1,183,122	3,085,420	568,965
(599,545)	(945,000)	(570,246)	(1,108,113)	(688,836)	(45,340)	(570,100)	(2,257,304)	(442,047)
<u>(249,976)</u>	<u>335,752</u>	<u>(749,572)</u>	<u>(1,448,464)</u>	<u>(154,138)</u>	<u>47,937</u>	<u>(1,021,624)</u>	<u>(448,847)</u>	<u>(249,576)</u>
<u>206,779</u>	<u>497,184</u>	<u>(643,492)</u>	<u>(1,123,926)</u>	<u>74,135</u>	<u>122,076</u>	<u>(408,602)</u>	<u>379,269</u>	<u>(122,658)</u>
<u>(8,302,867)</u>	<u>(1,855,602)</u>	<u>(3,856,150)</u>	<u>(7,856,284)</u>	<u>(6,081,414)</u>	<u>(204,699)</u>	<u>(4,805,106)</u>	<u>(18,101,590)</u>	<u>(2,404,065)</u>
<u>\$ 8,144,487</u>	<u>\$ 7,427,937</u>	<u>\$ 5,811,841</u>	<u>\$ 15,136,517</u>	<u>\$ 7,084,387</u>	<u>\$ 431,972</u>	<u>\$ 8,188,793</u>	<u>\$ 30,553,335</u>	<u>\$ 4,185,196</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>Fidelity VIP Asset Manager Subaccount</i>	<i>Fidelity VIP Contrafund Service Class Subaccount</i>	<i>Fidelity VIP Equity-Income Subaccount</i>	<i>Fidelity VIP Equity-Income Service Class Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 829,862	\$ 27,699,823	\$ 4,567,009	\$ 2,519,199
Changes From Operations:				
• Net investment income (loss)	45,276	32,098	40,945	33,657
• Net realized gain (loss) on investments	34,195	8,846,135	426,966	309,859
• Net change in unrealized appreciation or depreciation on investments	<u>39,706</u>	<u>(4,283,893)</u>	<u>(452,271)</u>	<u>(361,340)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	119,177	4,594,340	15,640	(17,824)
Changes From Unit Transactions:				
• Contract purchases	74,640	3,145,346	213,556	259,295
• Contract withdrawals	(49,322)	(2,377,511)	(777,327)	(126,091)
• Contract transfers	<u>(89,278)</u>	<u>(414,108)</u>	<u>(44,936)</u>	<u>654,689</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>(63,960)</u>	<u>353,727</u>	<u>(608,707)</u>	<u>787,893</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>55,217</u>	<u>4,948,067</u>	<u>(593,067)</u>	<u>770,069</u>
NET ASSETS AT DECEMBER 31, 2007	885,079	32,647,890	3,973,942	3,289,268
Changes From Operations:				
• Net investment income (loss)	27,666	51,873	57,822	41,862
• Net realized gain (loss) on investments	72,626	136,041	(65,668)	(194,901)
• Net change in unrealized appreciation or depreciation on investments	<u>(547,620)</u>	<u>(14,419,529)</u>	<u>(1,716,730)</u>	<u>(1,311,667)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(447,328)	(14,231,615)	(1,724,576)	(1,464,706)
Changes From Unit Transactions:				
• Contract purchases	63,206	2,932,230	194,166	299,538
• Contract withdrawals	(55,488)	(2,048,790)	(190,422)	(132,042)
• Contract transfers	<u>597,665</u>	<u>350,880</u>	<u>18,470</u>	<u>(222,801)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>605,383</u>	<u>1,234,320</u>	<u>22,214</u>	<u>(55,305)</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>158,055</u>	<u>(12,997,295)</u>	<u>(1,702,362)</u>	<u>(1,520,011)</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$1,043,134</u>	<u>\$ 19,650,595</u>	<u>\$ 2,271,580</u>	<u>\$ 1,769,257</u>

See accompanying notes.

<i>Fidelity VIP Growth Service Class Subaccount</i>	<i>Fidelity VIP Growth Opportunities Service Class Subaccount</i>	<i>Fidelity VIP High Income Service Class Subaccount</i>	<i>Fidelity VIP Investment Grade Bond Subaccount</i>	<i>Fidelity VIP Mid Cap Service Class Subaccount</i>	<i>Fidelity VIP Overseas Service Class Subaccount</i>	<i>FTVIPT Franklin Income Securities Subaccount</i>	<i>FTVIPT Franklin Small-Mid Cap Growth Securities Subaccount</i>	<i>FTVIPT Mutual Shares Securities Subaccount</i>
\$ 7,016,391	\$ 1,391,783	\$ 2,573,164	\$ 2,810,587	\$ 1,493,639	\$ 3,801,775	\$ 693,513	\$ 3,259,260	\$ 490,509
(11,089)	(12,327)	147,831	98,556	2,499	110,935	18,985	(28,584)	7,666
423,830	48,326	2,395	(7,827)	197,192	398,121	28,384	419,003	35,864
<u>1,216,875</u>	<u>267,389</u>	<u>(100,487)</u>	<u>8,024</u>	<u>84,676</u>	<u>164,014</u>	<u>(42,973)</u>	<u>(30,061)</u>	<u>(61,631)</u>
1,629,616	303,388	49,739	98,753	284,367	673,070	4,396	360,358	(18,101)
689,848	157,267	140,248	187,032	498,687	485,427	426,780	549,350	266,064
(1,521,690)	(109,969)	(124,869)	(220,434)	(117,160)	(249,505)	(79,002)	(312,941)	(53,553)
<u>(79,594)</u>	<u>(35,669)</u>	<u>(641,680)</u>	<u>(504,262)</u>	<u>677,241</u>	<u>477,794</u>	<u>247,324</u>	<u>133,466</u>	<u>1,032,394</u>
<u>(911,436)</u>	<u>11,629</u>	<u>(626,301)</u>	<u>(537,664)</u>	<u>1,058,768</u>	<u>713,716</u>	<u>595,102</u>	<u>369,875</u>	<u>1,244,905</u>
<u>718,180</u>	<u>315,017</u>	<u>(576,562)</u>	<u>(438,911)</u>	<u>1,343,135</u>	<u>1,386,786</u>	<u>599,498</u>	<u>730,233</u>	<u>1,226,804</u>
7,734,571	1,706,800	1,996,602	2,371,676	2,836,774	5,188,561	1,293,011	3,989,493	1,717,313
(1,566)	(5,474)	135,656	71,668	(6,611)	79,238	70,305	(24,980)	43,742
95,741	(5,750)	(43,868)	(43,586)	277,989	353,855	(112,614)	366,924	(10,697)
<u>(3,784,043)</u>	<u>(1,001,439)</u>	<u>(563,774)</u>	<u>(149,765)</u>	<u>(1,625,887)</u>	<u>(2,885,233)</u>	<u>(420,821)</u>	<u>(2,155,736)</u>	<u>(769,891)</u>
(3,689,868)	(1,012,663)	(471,986)	(121,683)	(1,354,509)	(2,452,140)	(463,130)	(1,813,792)	(736,846)
624,952	167,523	92,568	164,226	630,633	566,767	233,547	451,015	315,732
(473,075)	(102,927)	(113,695)	(177,175)	(154,920)	(264,648)	(82,599)	(238,920)	(89,727)
<u>61,772</u>	<u>128,989</u>	<u>(166,091)</u>	<u>164,569</u>	<u>259,748</u>	<u>(65,368)</u>	<u>400,800</u>	<u>96,936</u>	<u>61,133</u>
<u>213,649</u>	<u>193,585</u>	<u>(187,218)</u>	<u>151,620</u>	<u>735,461</u>	<u>236,751</u>	<u>551,748</u>	<u>309,031</u>	<u>287,138</u>
<u>(3,476,219)</u>	<u>(819,078)</u>	<u>(659,204)</u>	<u>29,937</u>	<u>(619,048)</u>	<u>(2,215,389)</u>	<u>88,618</u>	<u>(1,504,761)</u>	<u>(449,708)</u>
<u>\$ 4,258,352</u>	<u>\$ 887,722</u>	<u>\$ 1,337,398</u>	<u>\$ 2,401,613</u>	<u>\$ 2,217,726</u>	<u>\$ 2,973,172</u>	<u>\$ 1,381,629</u>	<u>\$ 2,484,732</u>	<u>\$ 1,267,605</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>FTVIPT Templeton Foreign Securities Subaccount</i>	<i>FTVIPT Templeton Foreign Securities Class 2 Subaccount</i>	<i>FTVIPT Templeton Global Asset Allocation Subaccount</i>	<i>FTVIPT Templeton Global Income Securities Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 4,118,820	\$ 5,226,684	\$ 3,085,542	\$ 706,635
Changes From Operations:				
• Net investment income (loss)	54,765	68,861	549,204	20,419
• Net realized gain (loss) on investments	269,045	420,533	731,550	6,232
• Net change in unrealized appreciation or depreciation on investments	<u>304,225</u>	<u>317,355</u>	<u>(968,516)</u>	<u>70,575</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	628,035	806,749	312,238	97,226
Changes From Unit Transactions:				
• Contract purchases	179,629	334,191	142,592	163,264
• Contract withdrawals	(249,328)	(342,146)	(139,672)	(39,685)
• Contract transfers	<u>881,140</u>	<u>213,054</u>	<u>503,359</u>	<u>400,568</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	811,441	205,099	506,279	524,147
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>1,439,476</u>	<u>1,011,848</u>	<u>818,517</u>	<u>621,373</u>
NET ASSETS AT DECEMBER 31, 2007	5,558,296	6,238,532	3,904,059	1,328,008
Changes From Operations:				
• Net investment income (loss)	86,250	80,467	325,401	51,881
• Net realized gain (loss) on investments	342,672	536,048	(319,840)	46,770
• Net change in unrealized appreciation or depreciation on investments	<u>(3,005,689)</u>	<u>(3,174,183)</u>	<u>(615,738)</u>	<u>(1,406)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(2,576,767)	(2,557,668)	(610,177)	97,245
Changes From Unit Transactions:				
• Contract purchases	145,035	322,385	130,101	736,994
• Contract withdrawals	(425,714)	(328,259)	(258,691)	(145,064)
• Contract transfers	<u>990,053</u>	<u>55,430</u>	<u>(1,614,864)</u>	<u>147,589</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	709,374	49,556	(1,743,454)	739,519
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(1,867,393)</u>	<u>(2,508,112)</u>	<u>(2,353,631)</u>	<u>836,764</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 3,690,903</u>	<u>\$ 3,730,420</u>	<u>\$ 1,550,428</u>	<u>\$2,164,772</u>

See accompanying notes.

<i>FTVIPT Templeton Growth Securities Subaccount</i>	<i>FTVIPT Templeton Growth Securities Class 2 Subaccount</i>	<i>Janus Aspen Series Balanced Subaccount</i>	<i>Janus Aspen Series Balanced Service Shares Subaccount</i>	<i>Janus Aspen Series Global Technology Service Shares Subaccount</i>	<i>Janus Aspen Series Mid Cap Growth Service Shares Subaccount</i>	<i>Janus Aspen Series Worldwide Growth Subaccount</i>	<i>Janus Aspen Series Worldwide Growth Service Shares Subaccount</i>	<i>Lincoln VIPT Baron Growth Opportunities Subaccount</i>
\$ 6,165,385	\$ 2,860,971	\$ 9,023,867	\$1,479,716	\$1,322,647	\$ 2,179,459	\$ 8,346,514	\$1,909,888	\$ —
55,236	17,647	172,479	23,440	(6,686)	(17,920)	(4,395)	(5,034)	(85)
644,452	292,369	123,030	39,055	(4,889)	117,292	177,885	102,382	3
<u>(604,335)</u>	<u>(286,664)</u>	<u>579,894</u>	<u>76,466</u>	<u>283,722</u>	<u>360,417</u>	<u>542,453</u>	<u>87,557</u>	<u>(783)</u>
95,353	23,352	875,403	138,961	272,147	459,789	715,943	184,905	(865)
397,163	238,991	850,351	84,741	76,476	105,311	708,303	106,846	1,888
(586,143)	(564,935)	(742,309)	(160,162)	(110,494)	(168,993)	(614,331)	(105,569)	(1,176)
<u>(69,931)</u>	<u>(151,209)</u>	<u>365,393</u>	<u>(5,637)</u>	<u>48,993</u>	<u>276,360</u>	<u>(862,725)</u>	<u>(125,194)</u>	<u>39,415</u>
<u>(258,911)</u>	<u>(477,153)</u>	<u>473,435</u>	<u>(81,058)</u>	<u>14,975</u>	<u>212,678</u>	<u>(768,753)</u>	<u>(123,917)</u>	<u>40,127</u>
<u>(163,558)</u>	<u>(453,801)</u>	<u>1,348,838</u>	<u>57,903</u>	<u>287,122</u>	<u>672,467</u>	<u>(52,810)</u>	<u>60,988</u>	<u>39,262</u>
6,001,827	2,407,170	10,372,705	1,537,619	1,609,769	2,851,926	8,293,704	1,970,876	39,262
61,379	17,754	178,714	24,007	(9,181)	(19,482)	30,287	3,711	(321)
186,849	120,638	666,676	104,308	(20,271)	159,146	(58,967)	21,961	(5,354)
<u>(2,736,304)</u>	<u>(1,130,798)</u>	<u>(2,593,287)</u>	<u>(393,129)</u>	<u>(677,149)</u>	<u>(1,637,682)</u>	<u>(3,842,890)</u>	<u>(888,331)</u>	<u>(12,052)</u>
(2,488,076)	(992,406)	(1,747,897)	(264,814)	(706,601)	(1,498,018)	(3,871,570)	(862,659)	(17,727)
420,139	120,624	748,892	81,094	197,868	160,748	699,024	67,843	5,862
(350,103)	(116,397)	(775,006)	(67,995)	(111,676)	(138,477)	(518,609)	(59,436)	(4,099)
<u>(350,426)</u>	<u>(110,594)</u>	<u>(482,875)</u>	<u>9,245</u>	<u>20,820</u>	<u>546,499</u>	<u>337,819</u>	<u>21,163</u>	<u>(2,256)</u>
<u>(280,390)</u>	<u>(106,367)</u>	<u>(508,989)</u>	<u>22,344</u>	<u>107,012</u>	<u>568,770</u>	<u>518,234</u>	<u>29,570</u>	<u>(493)</u>
<u>(2,768,466)</u>	<u>(1,098,773)</u>	<u>(2,256,886)</u>	<u>(242,470)</u>	<u>(599,589)</u>	<u>(929,248)</u>	<u>(3,353,336)</u>	<u>(833,089)</u>	<u>(18,220)</u>
<u>\$ 3,233,361</u>	<u>\$ 1,308,397</u>	<u>\$ 8,115,819</u>	<u>\$1,295,149</u>	<u>\$1,010,180</u>	<u>\$ 1,922,678</u>	<u>\$ 4,940,368</u>	<u>\$1,137,787</u>	<u>\$ 21,042</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>Lincoln VIPT Baron Growth Opportunities Service Class Subaccount</i>	<i>Lincoln VIPT Capital Growth Subaccount</i>	<i>Lincoln VIPT Cohen & Steers Global Real Estate Subaccount</i>	<i>Lincoln VIPT Columbia Value Opportunities Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 5,909,773	\$ —	\$ —	\$ —
Changes From Operations:				
• Net investment income (loss)	(50,597)	(11)	1,497	—
• Net realized gain (loss) on investments	980,056	4	(1,926)	—
• Net change in unrealized appreciation or depreciation on investments	<u>(771,100)</u>	<u>633</u>	<u>(40,158)</u>	<u>—</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	158,359	626	(40,587)	—
Changes From Unit Transactions:				
• Contract purchases	481,913	184	32,827	—
• Contract withdrawals	(845,812)	(69)	(7,355)	—
• Contract transfers	<u>421,342</u>	<u>22,699</u>	<u>446,838</u>	<u>—</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	57,443	22,814	472,310	—
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>215,802</u>	<u>23,440</u>	<u>431,723</u>	<u>—</u>
NET ASSETS AT DECEMBER 31, 2007	6,125,575	23,440	431,723	—
Changes From Operations:				
• Net investment income (loss)	(38,270)	(595)	5,828	305
• Net realized gain (loss) on investments	255,003	(9,316)	(78,452)	22,697
• Net change in unrealized appreciation or depreciation on investments	<u>(2,483,619)</u>	<u>(87,545)</u>	<u>(278,807)</u>	<u>(63,020)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(2,266,886)	(97,456)	(351,431)	(40,018)
Changes From Unit Transactions:				
• Contract purchases	427,375	2,388	274,562	7,095
• Contract withdrawals	(331,470)	(2,076)	(55,160)	(6,464)
• Contract transfers	<u>(454,144)</u>	<u>252,682</u>	<u>171,912</u>	<u>147,706</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	(358,239)	252,994	391,314	148,337
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(2,625,125)</u>	<u>155,538</u>	<u>39,883</u>	<u>108,319</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 3,500,450</u>	<u>\$178,978</u>	<u>\$ 471,606</u>	<u>\$108,319</u>

See accompanying notes.

<i>Lincoln VIPT Core Subaccount</i>	<i>Lincoln VIPT Delaware Bond Subaccount</i>	<i>Lincoln VIPT Delaware Growth and Income Subaccount</i>	<i>Lincoln VIPT Delaware Social Awareness Subaccount</i>	<i>Lincoln VIPT Delaware Special Opportunities Subaccount</i>	<i>Lincoln VIPT FI Equity-Income Subaccount</i>	<i>Lincoln VIPT Growth Subaccount</i>	<i>Lincoln VIPT Growth Opportunities Subaccount</i>	<i>Lincoln VIPT Janus Capital Appreciation Subaccount</i>
\$ 3,563	\$31,881,345	\$ 88,739	\$1,024,868	\$ —	\$ 3,987,045	\$ 12,012	\$ 46,780	\$ 2,110,104
(7)	1,402,506	869	1,608	241	16,228	(392)	(130)	(12,927)
105	4,537	1,659	29,971	1,605	475,136	13,440	1,539	39,917
(61)	104,490	2,913	(6,148)	(4,411)	(370,701)	(734)	563	479,164
37	1,511,533	5,441	25,431	(2,565)	120,663	12,314	1,972	506,154
—	3,429,027	48,609	111,171	3,001	392,163	1,172	1,617	291,812
(111)	(3,812,469)	(8,132)	(45,938)	(604)	(239,189)	(3,444)	(1,270)	(153,576)
(3,489)	1,370,224	98,196	(2,905)	37,059	(250,505)	(22,054)	(49,099)	717,634
(3,600)	986,782	138,673	62,328	39,456	(97,531)	(24,326)	(48,752)	855,870
(3,563)	2,498,315	144,114	87,759	36,891	23,132	(12,012)	(46,780)	1,362,024
—	34,379,660	232,853	1,112,627	36,891	4,010,177	—	—	3,472,128
—	1,290,704	2,707	1,458	2,649	26,481	—	—	(744)
—	(257,849)	29,190	72,266	17,236	173,493	—	—	(9,695)
—	(2,344,531)	(158,312)	(416,301)	(137,258)	(1,827,997)	—	—	(1,476,319)
—	(1,311,676)	(126,415)	(342,577)	(117,373)	(1,628,023)	—	—	(1,486,758)
—	3,190,912	55,734	84,603	196,981	398,017	—	—	396,499
—	(2,659,145)	(24,797)	(51,050)	(35,744)	(321,660)	—	—	(218,777)
—	(3,213,790)	123,789	(150,995)	216,012	89,978	—	—	30,605
—	(2,682,023)	154,726	(117,442)	377,249	166,335	—	—	208,327
—	(3,993,699)	28,311	(460,019)	259,876	(1,461,688)	—	—	(1,278,431)
\$ —	\$30,385,961	\$ 261,164	\$ 652,608	\$ 296,767	\$ 2,548,489	\$ —	\$ —	\$ 2,193,697

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>Lincoln VIPT Marsico International Growth Subaccount</i>	<i>Lincoln VIPT MFS Value Subaccount</i>	<i>Lincoln VIPT Mid-Cap Value Subaccount</i>	<i>Lincoln VIPT Mondrian International Value Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ —	\$ —	\$ —	\$10,265,957
Changes From Operations:				
• Net investment income (loss)	955	178	230	167,111
• Net realized gain (loss) on investments	2,551	(2)	(294)	986,497
• Net change in unrealized appreciation or depreciation on investments	3,107	131	(11,654)	(24,724)
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	6,613	307	(11,718)	1,128,884
Changes From Unit Transactions:				
• Contract purchases	15,646	22,571	4,626	893,006
• Contract withdrawals	(2,880)	(2,519)	(2,482)	(566,064)
• Contract transfers	321,520	39,056	165,998	922,567
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	334,286	59,108	168,142	1,249,509
TOTAL INCREASE (DECREASE) IN NET ASSETS	340,899	59,415	156,424	2,378,393
NET ASSETS AT DECEMBER 31, 2007	340,899	59,415	156,424	12,644,350
Changes From Operations:				
• Net investment income (loss)	7,131	10,649	(471)	410,425
• Net realized gain (loss) on investments	36,423	(19,252)	(68,195)	721,235
• Net change in unrealized appreciation or depreciation on investments	(556,433)	(327,128)	(59,641)	(5,636,378)
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(512,879)	(335,731)	(128,307)	(4,504,718)
Changes From Unit Transactions:				
• Contract purchases	184,072	340,350	117,775	828,930
• Contract withdrawals	(44,555)	(78,039)	(18,353)	(555,499)
• Contract transfers	734,298	1,172,691	66,876	(941,586)
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	873,815	1,435,002	166,298	(668,155)
TOTAL INCREASE (DECREASE) IN NET ASSETS	360,936	1,099,271	37,991	(5,172,873)
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 701,835</u>	<u>\$1,158,686</u>	<u>\$ 194,415</u>	<u>\$ 7,471,477</u>

See accompanying notes.

<i>Lincoln VIPT Money Market Subaccount</i>	<i>Lincoln VIPT SSgA Bond Index Subaccount</i>	<i>Lincoln VIPT SSgA Emerging Markets 100 Subaccount</i>	<i>Lincoln VIPT SSgA International Index Subaccount</i>	<i>Lincoln VIPT SSgA Large Cap 100 Subaccount</i>	<i>Lincoln VIPT SSgA S&P 500 Index Subaccount</i>	<i>Lincoln VIPT SSgA Small-Cap Index Subaccount</i>	<i>Lincoln VIPT SSgA Small-Mid Cap 200 Subaccount</i>	<i>Lincoln VIPT T. Rowe Price Growth Stock Subaccount</i>
\$ 28,705,660	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
1,131,504	—	—	—	—	4,011	411	—	22
—	—	—	—	—	(47)	17	—	4
—	—	—	—	—	(19,459)	(1,939)	—	(70)
1,131,504	—	—	—	—	(15,495)	(1,511)	—	(44)
37,100,816	—	—	—	—	178,208	12,692	—	5,767
(5,613,703)	—	—	—	—	(20,807)	(2,343)	—	(975)
(32,357,329)	—	—	—	—	586,481	107,845	—	20,898
(870,216)	—	—	—	—	743,882	118,194	—	25,690
261,288	—	—	—	—	728,387	116,683	—	25,646
28,966,948	—	—	—	—	728,387	116,683	—	25,646
499,153	1,037	107	106	339	47,885	1,244	111	(212)
116	407	22	(140)	(424)	(276,496)	8,141	(95)	(5,916)
2	7,272	1,634	(9,581)	(28,996)	(408,511)	(95,553)	(8,019)	(43,583)
499,271	8,716	1,763	(9,615)	(29,081)	(637,122)	(86,168)	(8,003)	(49,711)
22,910,011	12,422	—	—	1	475,635	86,456	1	29,336
(5,953,701)	(3,674)	(274)	(309)	(1,797)	(97,774)	(13,296)	(346)	(7,551)
(9,696,860)	175,452	14,949	28,211	120,130	905,804	89,847	28,211	78,542
7,259,450	184,200	14,675	27,902	118,334	1,283,665	163,007	27,866	100,327
7,758,721	192,916	16,438	18,287	89,253	646,543	76,839	19,863	50,616
\$ 36,725,669	\$ 192,916	\$ 16,438	\$ 18,287	\$ 89,253	\$ 1,374,930	\$ 193,522	\$ 19,863	\$ 76,262

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth Subaccount</i>	<i>Lincoln VIPT Templeton Growth Subaccount</i>	<i>Lincoln VIPT Turner Mid-Cap Growth Subaccount</i>	<i>Lincoln VIPT UBS Global Asset Allocation Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 201,073	\$ —	\$ —	\$ 1,453,410
Changes From Operations:				
• Net investment income (loss)	(5,895)	357	(123)	23,683
• Net realized gain (loss) on investments	6,247	(26)	9	126,971
• Net change in unrealized appreciation or depreciation on investments	<u>49,120</u>	<u>(1,064)</u>	<u>971</u>	<u>(50,999)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	49,472	(733)	857	99,655
Changes From Unit Transactions:				
• Contract purchases	81,514	10,384	7,001	499,047
• Contract withdrawals	(30,392)	(1,877)	(2,050)	(129,883)
• Contract transfers	<u>1,042,035</u>	<u>16,968</u>	<u>160,480</u>	<u>424,008</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>1,093,157</u>	<u>25,475</u>	<u>165,431</u>	<u>793,172</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>1,142,629</u>	<u>24,742</u>	<u>166,288</u>	<u>892,827</u>
NET ASSETS AT DECEMBER 31, 2007	1,343,702	24,742	166,288	2,346,237
Changes From Operations:				
• Net investment income (loss)	(8,366)	1,668	(1,249)	138,413
• Net realized gain (loss) on investments	(116,225)	1,874	(29,107)	149,257
• Net change in unrealized appreciation or depreciation on investments	<u>(528,030)</u>	<u>(38,130)</u>	<u>(95,705)</u>	<u>(1,202,548)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(652,621)	(34,588)	(126,061)	(914,878)
Changes From Unit Transactions:				
• Contract purchases	112,259	31,222	89,612	260,807
• Contract withdrawals	(57,267)	(7,713)	(20,594)	(164,184)
• Contract transfers	<u>22,727</u>	<u>68,750</u>	<u>179,611</u>	<u>281,742</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>77,719</u>	<u>92,259</u>	<u>248,629</u>	<u>378,365</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(574,902)</u>	<u>57,671</u>	<u>122,568</u>	<u>(536,513)</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 768,800</u>	<u>\$ 82,413</u>	<u>\$ 288,856</u>	<u>\$ 1,809,724</u>

See accompanying notes.

<i>Lincoln VIPT Wilshire 2010 Profile Subaccount</i>	<i>Lincoln VIPT Wilshire 2020 Profile Subaccount</i>	<i>Lincoln VIPT Wilshire 2030 Profile Subaccount</i>	<i>Lincoln VIPT Wilshire 2040 Profile Subaccount</i>	<i>Lincoln VIPT Wilshire Aggressive Profile Subaccount</i>	<i>Lincoln VIPT Wilshire Conservative Profile Subaccount</i>	<i>Lincoln VIPT Wilshire Moderate Profile Subaccount</i>	<i>Lincoln VIPT Wilshire Moderately Aggressive Profile Subaccount</i>	<i>M Fund Brandes International Equity Subaccount</i>
\$ —	\$ —	\$ —	\$ —	\$ 145,729	\$ 489,207	\$ 834,879	\$ 916,473	\$1,977,353
—	77	647	—	4,335	7,069	35,735	27,473	30,614
—	25	(31)	—	9,606	4,608	12,844	45,448	436,391
—	1,715	(1,311)	—	25,588	25,323	33,113	51,434	(329,831)
—	1,817	(695)	—	39,529	37,000	81,692	124,355	137,174
—	38,858	—	—	388,871	48,628	794,429	833,535	238,063
—	(4,261)	(1,111)	—	(63,777)	(26,872)	(184,112)	(179,896)	(98,589)
—	—	201,532	22,864	608,460	67,042	2,374,073	1,130,844	(28,094)
—	34,597	200,421	22,864	933,554	88,798	2,984,390	1,784,483	111,380
—	36,414	199,726	22,864	973,083	125,798	3,066,082	1,908,838	248,554
—	36,414	199,726	22,864	1,118,812	615,005	3,900,961	2,825,311	2,225,907
1,940	948	2,238	148	1,412	10,737	81,280	43,007	52,395
(4,653)	(222)	(1,995)	(944)	24,949	10,610	36,821	60,906	92,137
(26,085)	(20,941)	(163,902)	(16,923)	(821,146)	(161,187)	(1,526,652)	(2,942,834)	(953,064)
(28,798)	(20,215)	(163,659)	(17,719)	(794,785)	(139,840)	(1,408,551)	(2,838,921)	(808,532)
5,285	45,474	45,555	37,681	985,794	64,758	1,873,709	1,996,555	259,114
(2,111)	(8,089)	(22,326)	(8,401)	(151,333)	(37,073)	(459,137)	(615,967)	(98,983)
138,145	32,404	402,446	52,032	218,333	214,707	1,077,895	4,925,027	(230,666)
141,319	69,789	425,675	81,312	1,052,794	242,392	2,492,467	6,305,615	(70,535)
112,521	49,574	262,016	63,593	258,009	102,552	1,083,916	3,466,694	(879,067)
<u>\$112,521</u>	<u>\$ 85,988</u>	<u>\$ 461,742</u>	<u>\$ 86,457</u>	<u>\$1,376,821</u>	<u>\$ 717,557</u>	<u>\$ 4,984,877</u>	<u>\$ 6,292,005</u>	<u>\$1,346,840</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

	<i>M Fund Business Opportunity Value Subaccount</i>	<i>M Fund Frontier Capital Appreciation Subaccount</i>	<i>M Fund Turner Core Growth Subaccount</i>	<i>MFS VIT Core Equity Subaccount</i>
NET ASSETS AT JANUARY 1, 2007	\$ 95,937	\$1,183,343	\$ 606,055	\$ 679,681
Changes From Operations:				
• Net investment income (loss)	719	(7,977)	(2,125)	(3,381)
• Net realized gain (loss) on investments	16,841	183,248	110,665	29,628
• Net change in unrealized appreciation or depreciation on investments	<u>(18,778)</u>	<u>(51,187)</u>	<u>61,403</u>	<u>46,237</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(1,218)	124,084	169,943	72,484
Changes From Unit Transactions:				
• Contract purchases	51,557	125,018	94,763	36,463
• Contract withdrawals	(10,477)	(42,108)	(33,663)	(33,665)
• Contract transfers	<u>92,348</u>	<u>(162,974)</u>	<u>301,529</u>	<u>24,949</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>133,428</u>	<u>(80,064)</u>	<u>362,629</u>	<u>27,747</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>132,210</u>	<u>44,020</u>	<u>532,572</u>	<u>100,231</u>
NET ASSETS AT DECEMBER 31, 2007	228,147	1,227,363	1,138,627	779,912
Changes From Operations:				
• Net investment income (loss)	(1,239)	(6,659)	(7,354)	(95)
• Net realized gain (loss) on investments	4,571	17,691	23,921	4,181
• Net change in unrealized appreciation or depreciation on investments	<u>(106,963)</u>	<u>(514,524)</u>	<u>(695,958)</u>	<u>(313,822)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(103,631)	(503,492)	(679,391)	(309,736)
Changes From Unit Transactions:				
• Contract purchases	81,821	147,828	126,197	34,809
• Contract withdrawals	(15,965)	(48,563)	(42,120)	(42,992)
• Contract transfers	<u>35,720</u>	<u>(19,288)</u>	<u>294,543</u>	<u>21,512</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>101,576</u>	<u>79,977</u>	<u>378,620</u>	<u>13,329</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(2,055)</u>	<u>(423,515)</u>	<u>(300,771)</u>	<u>(296,407)</u>
NET ASSETS AT DECEMBER 31, 2008	<u>\$ 226,092</u>	<u>\$ 803,848</u>	<u>\$ 837,856</u>	<u>\$ 483,505</u>

See accompanying notes.

<i>MFS VIT Growth Subaccount</i>	<i>MFS VIT Total Return Subaccount</i>	<i>MFS VIT Utilities Subaccount</i>	<i>NB AMT Mid-Cap Growth Subaccount</i>	<i>NB AMT Partners Subaccount</i>	<i>NB AMT Regency Subaccount</i>	<i>Premier VIT OPCAP Global Equity Subaccount</i>	<i>Premier VIT OPCAP Managed Subaccount</i>	<i>Putnam VT Growth & Income Class IB Subaccount</i>
\$ 6,856,597	\$21,858,456	\$12,254,524	\$11,356,402	\$ 3,034,110	\$ 4,235,977	\$ 569,959	\$ 597,863	\$1,167,909
(59,693)	401,206	21,091	(95,720)	(5,397)	(12,985)	69	8,451	8,218
156,658	1,088,900	1,681,327	808,913	434,317	199,224	142,346	45,714	221,894
<u>1,257,967</u>	<u>(850,716)</u>	<u>1,697,067</u>	<u>1,644,114</u>	<u>(139,689)</u>	<u>(85,862)</u>	<u>(109,573)</u>	<u>(40,664)</u>	<u>(275,241)</u>
1,354,932	639,390	3,399,485	2,357,307	289,231	100,377	32,842	13,501	(45,129)
683,667	1,481,793	866,658	950,911	129,442	464,522	30,941	22,331	84,971
(966,378)	(4,986,073)	(921,218)	(1,133,370)	(618,247)	(180,205)	(87,997)	(20,093)	(39,567)
<u>535,867</u>	<u>9,918</u>	<u>1,098,173</u>	<u>(696,965)</u>	<u>229,730</u>	<u>(7,239)</u>	<u>(63,264)</u>	<u>(16,355)</u>	<u>(510,580)</u>
<u>253,156</u>	<u>(3,494,362)</u>	<u>1,043,613</u>	<u>(879,424)</u>	<u>(259,075)</u>	<u>277,078</u>	<u>(120,320)</u>	<u>(14,117)</u>	<u>(465,176)</u>
<u>1,608,088</u>	<u>(2,854,972)</u>	<u>4,443,098</u>	<u>1,477,883</u>	<u>30,156</u>	<u>377,455</u>	<u>(87,478)</u>	<u>(616)</u>	<u>(510,305)</u>
8,464,685	19,003,484	16,697,622	12,834,285	3,064,266	4,613,432	482,481	597,247	657,604
(39,530)	385,847	102,399	(78,416)	(6,207)	16,798	6,315	11,192	6,586
99,804	875,450	2,548,809	212,520	394,410	3,551	(34,027)	12,127	64,600
<u>(3,114,212)</u>	<u>(5,477,577)</u>	<u>(8,858,782)</u>	<u>(5,652,834)</u>	<u>(2,016,332)</u>	<u>(1,929,169)</u>	<u>2,970</u>	<u>(177,909)</u>	<u>(311,287)</u>
(3,053,938)	(4,216,280)	(6,207,574)	(5,518,730)	(1,628,129)	(1,908,820)	(24,742)	(154,590)	(240,101)
547,156	1,177,411	995,329	986,530	133,289	337,301	10	22,279	33,746
(589,536)	(1,243,098)	(912,806)	(742,572)	(133,073)	(185,228)	(1,860)	(89,752)	(25,922)
<u>(394,255)</u>	<u>(754,822)</u>	<u>(499,938)</u>	<u>(394,145)</u>	<u>125,651</u>	<u>(604,259)</u>	<u>(455,889)</u>	<u>(49,119)</u>	<u>(55,822)</u>
<u>(436,635)</u>	<u>(820,509)</u>	<u>(417,415)</u>	<u>(150,187)</u>	<u>125,867</u>	<u>(452,186)</u>	<u>(457,739)</u>	<u>(116,592)</u>	<u>(47,998)</u>
<u>(3,490,573)</u>	<u>(5,036,789)</u>	<u>(6,624,989)</u>	<u>(5,668,917)</u>	<u>(1,502,262)</u>	<u>(2,361,006)</u>	<u>(482,481)</u>	<u>(271,182)</u>	<u>(288,099)</u>
<u>\$ 4,974,112</u>	<u>\$13,966,695</u>	<u>\$10,072,633</u>	<u>\$ 7,165,368</u>	<u>\$ 1,562,004</u>	<u>\$ 2,252,426</u>	<u>\$ —</u>	<u>\$ 326,065</u>	<u>\$ 369,505</u>

Statements of changes in net assets (continued)

Years Ended December 31, 2007 and 2008

Putnam VT
Health Sciences
Class IB
Subaccount

NET ASSETS AT JANUARY 1, 2007	\$ 907,766
Changes From Operations:	
• Net investment income (loss)	(203)
• Net realized gain (loss) on investments	16,470
• Net change in unrealized appreciation or depreciation on investments	<u>(29,883)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(13,616)
Changes From Unit Transactions:	
• Contract purchases	77,854
• Contract withdrawals	(32,093)
• Contract transfers	<u>(47,525)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>(1,764)</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(15,380)</u>
NET ASSETS AT DECEMBER 31, 2007	892,386
Changes From Operations:	
• Net investment income (loss)	(3,952)
• Net realized gain (loss) on investments	(5,190)
• Net change in unrealized appreciation or depreciation on investments	<u>(107,371)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	(116,513)
Changes From Unit Transactions:	
• Contract purchases	21,847
• Contract withdrawals	(382,049)
• Contract transfers	<u>(55,406)</u>
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM UNIT TRANSACTIONS	<u>(415,608)</u>
TOTAL INCREASE (DECREASE) IN NET ASSETS	<u>(532,121)</u>
NET ASSETS AT DECEMBER 31, 2008	<u><u>\$ 360,265</u></u>

See accompanying notes.

Notes to financial statements

December 31, 2008

1. Accounting Policies and Variable Account Information

The Variable Account: Lincoln Life Flexible Premium Variable Life Account R (the Variable Account) is a segregated investment account of The Lincoln National Life Insurance Company (the Company) and is registered as a unit investment trust with the Securities and Exchange Commission under the Investment Company Act of 1940, as amended. The operations of the Variable Account, which commenced on June 18, 1998, are part of the operations of Lincoln Life. The Variable Account consists of nine products which are listed below.

- Lincoln SVUL
- Lincoln SVUL-I
- Lincoln SVUL-II and SVUL-II Elite
- Lincoln SVUL-III
- Lincoln SVUL-IV
- Lincoln SVUL^{ONE}
- Lincoln Momentum SVUL^{ONE}
- Lincoln SVUL^{ONE} 2007
- Lincoln Momentum SVUL^{ONE} 2007

The assets of the Variable Account are owned by the Company. The Variable Account's assets support the variable life policies and may not be used to satisfy liabilities arising from any other business of the Company.

Basis of Presentation: The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States for unit investment trusts.

Investments: The assets of the Variable Account are divided into variable subaccounts, each of which may be invested in shares of one of one hundred two mutual funds (the Funds) of fifteen diversified open-end management investment companies, each Fund with its own investment objective. The Funds are:

AIM Variable Insurance Funds (AIM V.I.):

- AIM V.I. Capital Appreciation Fund (Series I)
- AIM V.I. Core Equity Fund (Series I)
- AIM V.I. Diversified Income Fund (Series I)
- AIM V.I. International Growth Fund (Series I)

AllianceBernstein Variable Products Series Fund, Inc. (ABVPSF):

- ABVPSF Global Technology Portfolio (Class A)
- ABVPSF Growth and Income Portfolio (Class A)
- ABVPSF International Value Portfolio (Class A)
- ABVPSF Large Cap Growth Portfolio (Class A)
- ABVPSF Small/Mid Cap Value Portfolio (Class A)

American Century Variable Portfolios, Inc. (American Century VP):

- American Century VP Inflation Protection (Class 1)

American Funds Insurance Series (American Funds):

- American Funds Global Growth Fund (Class 2)
- American Funds Global Small Capitalization Fund (Class 2)
- American Funds Growth Fund (Class 2)
- American Funds Growth-Income Fund (Class 2)
- American Funds International Fund (Class 2)

Delaware VIP Trust (Delaware VIPT)*:

- Delaware VIPT Capital Reserves Series (Standard Class)
- Delaware VIPT Diversified Income Series (Standard Class)
- Delaware VIPT Emerging Markets Series (Standard Class)
- Delaware VIPT High Yield Series (Standard Class)
- Delaware VIPT REIT Series (Standard Class)
- Delaware VIPT Small Cap Value Series (Standard Class)
- Delaware VIPT Trend Series (Standard Class)
- Delaware VIPT U.S. Growth Series (Standard Class)
- Delaware VIPT Value Series (Standard Class)

DWS Scudder VIP Funds (DWS VIP):

- DWS VIP Equity 500 Index Fund
- DWS VIP Small Cap Index Fund

Fidelity Variable Insurance Products Fund (Fidelity VIP):

- Fidelity VIP Asset Manager Portfolio
- Fidelity VIP Contrafund Portfolio (Service Class)
- Fidelity VIP Equity-Income Portfolio
- Fidelity VIP Equity-Income Portfolio (Service Class)
- Fidelity VIP Growth Portfolio (Service Class)
- Fidelity VIP Growth Opportunities Portfolio (Service Class)
- Fidelity VIP High Income Portfolio (Service Class)
- Fidelity VIP Investment Grade Bond Portfolio
- Fidelity VIP Mid Cap Portfolio (Service Class)
- Fidelity VIP Overseas Portfolio (Service Class)

Franklin Templeton Variable Insurance Products Trust (FTVIPT):

- FTVIPT Franklin Income Securities Fund (Class 1)
- FTVIPT Franklin Small-Mid Cap Growth Securities Fund (Class 1)
- FTVIPT Mutual Shares Securities Fund (Class 1)
- FTVIPT Templeton Foreign Securities Fund (Class 1)
- FTVIPT Templeton Foreign Securities Fund (Class 2)
- FTVIPT Templeton Global Asset Allocation Fund (Class 1)
- FTVIPT Templeton Global Income Securities Fund (Class 1)
- FTVIPT Templeton Growth Securities Fund (Class 1)
- FTVIPT Templeton Growth Securities Fund (Class 2)

Janus Aspen Series:

- Janus Aspen Series Balanced Portfolio
- Janus Aspen Series Balanced Portfolio (Service Shares)
- Janus Aspen Series Global Technology Portfolio (Service Shares)
- Janus Aspen Series Mid Cap Growth Portfolio (Service Shares)
- Janus Aspen Series Worldwide Growth Portfolio
- Janus Aspen Series Worldwide Growth Portfolio (Service Shares)

Notes to financial statements (continued)

1. Accounting Policies and Variable Account Information (continued)

Lincoln Variable Insurance Products Trust (Lincoln VIPT)*:

Lincoln VIPT Baron Growth Opportunities Fund
Lincoln VIPT Baron Growth Opportunities Service
Class Fund
Lincoln VIPT Capital Growth Fund
Lincoln VIPT Cohen & Steers Global Real Estate Fund
Lincoln VIPT Columbia Value Opportunities Fund
Lincoln VIPT Delaware Bond Fund
Lincoln VIPT Delaware Growth and Income Fund
Lincoln VIPT Delaware Social Awareness Fund
Lincoln VIPT Delaware Special Opportunities Fund
Lincoln VIPT FI Equity-Income Fund
Lincoln VIPT Janus Capital Appreciation Fund
Lincoln VIPT Marsico International Growth Fund
Lincoln VIPT MFS Value Fund
Lincoln VIPT Mid-Cap Value Fund
Lincoln VIPT Mondrian International Value Fund
Lincoln VIPT Money Market Fund
Lincoln VIPT SSgA Bond Index Fund
Lincoln VIPT SSgA Developed International 150 Fund**
Lincoln VIPT SSgA Emerging Markets 100 Fund
Lincoln VIPT SSgA International Index Fund
Lincoln VIPT SSgA Large Cap 100 Fund
Lincoln VIPT SSgA S&P 500 Index Fund
Lincoln VIPT SSgA Small-Cap Index Fund
Lincoln VIPT SSgA Small-Mid Cap 200 Fund
Lincoln VIPT T. Rowe Price Growth Stock Fund
Lincoln VIPT T. Rowe Price Structured Mid-Cap
Growth Fund
Lincoln VIPT Templeton Growth Fund
Lincoln VIPT Turner Mid-Cap Growth Fund
Lincoln VIPT UBS Global Asset Allocation Fund
Lincoln VIPT Wilshire 2010 Profile Fund
Lincoln VIPT Wilshire 2020 Profile Fund
Lincoln VIPT Wilshire 2030 Profile Fund
Lincoln VIPT Wilshire 2040 Profile Fund
Lincoln VIPT Wilshire Aggressive Profile Fund
Lincoln VIPT Wilshire Conservative Profile Fund
Lincoln VIPT Wilshire Moderate Profile Fund
Lincoln VIPT Wilshire Moderately Aggressive Profile
Fund

M Fund, Inc. (M Fund):

M Fund Brandes International Equity Fund
M Fund Business Opportunity Value Fund
M Fund Frontier Capital Appreciation Fund
M Fund Turner Core Growth Fund

MFS Variable Insurance Trust (MFS VIT):

MFS VIT Core Equity Series (Initial Class)
MFS VIT Growth Series (Initial Class)
MFS VIT Total Return Series (Initial Class)
MFS VIT Utilities Series (Initial Class)

Neuberger Berman Advisers Management Trust (NB AMT):

NB AMT Mid-Cap Growth Portfolio (I Class)
NB AMT Partners Portfolio (I Class)
NB AMT Regency Portfolio (I Class)

Premier Variable Insurance Trust (Premier VIT):

Premier VIT OPCAP Managed Portfolio

Putnam Variable Trust (Putnam VT):

Putnam VT Growth & Income Fund (Class IB)
Putnam VT Health Sciences Fund (Class IB)

* Denotes an affiliate of the Company.

** Available funds with no money invested at
December 31, 2008.

Investments in the Funds are stated at the closing net
asset value per share on December 31, 2008, which ap-
proximates fair value. The difference between cost and
net asset value is reflected as unrealized appreciation or
depreciation of investments.

Effective January 1, 2008, the Variable Account adopted
Financial Accounting Standards Board Statement of
Financial Accounting Standards No. 157, Fair Value
Measurements (FAS 157). FAS 157 defines fair value
as the price that the Variable Account would receive
to sell an asset or pay to transfer a liability in an orderly
transaction between market participants at the meas-
urement date. FAS 157 also establishes a framework for
measuring fair value and a three-level hierarchy for fair
value measurements based upon the transparency of
inputs to the valuation of an asset or liability. Inputs
may be observable or unobservable and refer broadly to
the assumptions that market participants would use in
pricing the asset or liability. Observable inputs reflect
the assumptions market participants would use in pric-
ing the asset or liability based on market data obtained
from sources independent of the reporting entity. Un-
observable inputs reflect the reporting entity's own as-
sessment regarding the assumptions market
participants would use in pricing the asset or liability
and are developed based on the best information
available in the circumstances. The Variable Account's
investments in the Funds are assigned a level based
upon the observability of the inputs which are signifi-
cant to the overall valuation. The three-tier hierarchy
of inputs is summarized below.

Level 1 - inputs to the valuation methodology are
quoted prices in active markets

Level 2 - inputs to the valuation methodology are
observable, directly or indirectly

Level 3 - inputs to the valuation methodology are
unobservable and reflect assumptions on the part of
the reporting entity

Notes to financial statements (continued)

1. Accounting Policies and Variable Account Information (continued)

The Separate Account's investments in the Funds are valued within the above FAS 157 fair value hierarchy as Level 2. Net asset value is quoted by the Funds as derived by the fair value of the Funds underlying investments. The Funds are not considered Level 1 as they are not traded in the open market; rather the Company sells and redeems shares at net asset value with the Funds.

Adoption of FAS 157 had no effect on the recorded amounts of the Funds in the Variable Account.

Investment transactions are accounted for on a trade date basis. The cost of investments sold is determined by the average cost method.

Dividends: Dividends paid to the Variable Account are automatically reinvested in shares of the Funds on the payable date. Dividend income is recorded on the ex-dividend date.

Federal Income Taxes: Operations of the Variable Account form a part of and are taxed with operations of the

Also during 2007 the following funds changed their names:

Previous Fund Name

Lincoln VIPT Bond Fund
Lincoln VIPT Growth and Income Fund
Lincoln VIPT Social Awareness Fund
Lincoln VIPT Equity-Income Fund
Lincoln VIPT Capital Appreciation Fund
Lincoln VIPT International Fund
Lincoln VIPT Aggressive Growth Fund
Lincoln VIPT Global Asset Allocation Fund
Lincoln VIPT Aggressive Profile Fund
Lincoln VIPT Conservative Profile Fund
Lincoln VIPT Moderate Profile Fund
Lincoln VIPT Moderately Aggressive Profile Fund
MFS VIT Capital Opportunities Series

Also during 2007, the Lincoln VIPT Core Fund, the Lincoln VIPT Growth Fund and the Lincoln VIPT Growth Opportunities Fund ceased to be available as an investment option to Variable Account Contract owners.

During 2007, the Lincoln Variable Insurance Products Trust (Lincoln VIPT) acquired the Baron Capital Asset Fund and renamed the fund Lincoln VIPT Baron Growth Opportunities Service Class Fund. This fund acquisition had no impact on the units outstanding or the unit prices to the Variable Account Contract owner.

Company, which is taxed as a "life insurance company" under the Internal Revenue Code. The Variable Account will not be taxed as a regulated investment company under Subchapter M of the Internal Revenue Code, as amended. Under current federal income tax law, no federal income taxes are payable with respect to the Variable Account's net investment income and the net realized gain on investments.

Investment Fund Changes: During 2007, the Lincoln VIPT Baron Growth Opportunities Fund, the Lincoln VIPT Capital Growth Fund, the Lincoln VIPT Cohen & Steers Global Real Estate Fund, the Lincoln VIPT Delaware Special Opportunities Fund, the Lincoln VIPT Marsico International Growth Fund, the Lincoln VIPT MFS Value Fund, the Lincoln VIPT Mid-Cap Growth Fund, the Lincoln VIPT Mid-Cap Value Fund, the Lincoln VIPT S&P 500 Index Fund, the Lincoln VIPT Small-Cap Index Fund, the Lincoln VIPT T. Rowe Price Growth Stock Fund, the Lincoln VIPT Templeton Growth Fund, the Lincoln VIPT Value Opportunities Fund, the Lincoln VIPT Wilshire 2010 Profile Fund, the Lincoln VIPT Wilshire 2020 Profile Fund, the Lincoln VIPT Wilshire 2030 Profile Fund and the Lincoln VIPT Wilshire 2040 Profile Fund became available as investment options for Account Contract owners. Accordingly, the 2007 statement of changes in net assets and total return and investment income ratios in note 3 for these subaccounts are for the period from the commencement of operations to December 31, 2007.

New Fund Name

Lincoln VIPT Delaware Bond Fund
Lincoln VIPT Delaware Growth and Income Fund
Lincoln VIPT Delaware Social Awareness Fund
Lincoln VIPT FI Equity-Income Fund
Lincoln VIPT Janus Capital Appreciation Fund
Lincoln VIPT Mondrian International Value Fund
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth Fund
Lincoln VIPT UBS Global Asset Allocation Fund
Lincoln VIPT Wilshire Aggressive Profile Fund
Lincoln VIPT Wilshire Conservative Profile Fund
Lincoln VIPT Wilshire Moderate Profile Fund
Lincoln VIPT Wilshire Moderately Aggressive Profile Fund
MFS VIT Core Equity Series

During 2008, the Lincoln VIPT SSgA Bond Index Fund, the Lincoln VIPT SSgA Developed International 150 Fund, the Lincoln VIPT SSgA Emerging Markets 100 Fund, the Lincoln VIPT SSgA International Index Fund, the Lincoln VIPT SSgA Large Cap 100 Fund and the Lincoln VIPT SSgA Small-Mid Cap 200 Fund became available as investment options for Account Contract owners. Accordingly, the 2008 statement of operations and statements of changes in net assets and total return and investment income ratios in note 3 for these subaccounts are for the period from the commencement of operations to December 31, 2008.

Notes to financial statements (continued)

1. Accounting Policies and Variable Account Information (continued)

During 2008 the Lincoln VIPT Value Opportunities Fund changed its name to the Lincoln VIPT Columbia Value Opportunities Fund, the Lincoln VIPT S&P 500 Index Fund changed its name to the Lincoln VIPT SSgA S&P 500 Index Fund, the Lincoln VIPT Small-Cap Index Fund changed its name to the Lincoln VIPT SSgA Small-Cap Index Fund, the Lincoln VIPT Mid-Cap Growth Fund changed its name to the Lincoln VIPT Turner Mid-Cap Growth Fund and the MFS VIT Emerging Growth Series changed its name to the MFS VIT Growth Series.

During 2008 the Premier VIT OPCAP Global Equity Portfolio ceased to be available as an investment option to Variable Account Contract owners.

2. Mortality and Expense Guarantees and Other Transactions with Affiliates

Amounts are paid to the Company for mortality and expense guarantees at a percentage of the current value of the Variable Account each day. The current rate of deduction, stated as an annual percentage, is .80% for all products except Lincoln SVUL-IV, Lincoln SVUL^{ONE} 2007 and Lincoln Momentum SVUL^{ONE} 2007 which are .60% and Lincoln SVUL^{ONE} and Lincoln Momentum SVUL^{ONE} which are .50%. The mortality and expense risk charges for each of the variable subaccounts are reported in the statement of operations. For the Lincoln SVUL^{ONE} 2007 and Lincoln Momentum SVUL^{ONE} 2007 products, the annual percentage changes to .20% for policy years 11 and beyond. For the Lincoln SVUL-III product, the annual percentage changes to .40% for policy years 20 and beyond. For the Lincoln SVUL-IV product, the annual percentage changes to .20% for policy years 20 and beyond.

Prior to the allocation of premiums to the Variable Account, the Company deducts a premium load to cover state taxes and federal income tax liabilities and a portion of the sales expenses incurred by the Company.

Refer to the product prospectus for the premium load charge. The premium loads for the years ended December 31, 2008 and 2007 amounted to \$5,440,421 and \$6,363,782, respectively.

The Company charges a monthly administrative fee which varies by product, refer to the product prospectus for the administrative fee rate. The administrative fees are for items such as premium billing and collection, policy value calculation, confirmations and periodic reports. Administrative fees for the years ended December 31, 2008 and 2007 amounted to \$17,192,705 and \$15,842,981, respectively.

The Company assumes responsibility for providing the insurance benefit included in the policy. On a monthly basis, a cost of insurance charge is deducted proportionately from the value of each variable subaccount and/or fixed account funding option. The fixed account is part of the general account of the Company and is not included in these financial statements. The cost of insurance charge depends on the attained age, risk classification, gender classification (in accordance with state law) and the current net amount at risk. The cost of insurance charges for the years ended December 31, 2008 and 2007 amounted to \$11,097,652 and \$9,842,640, respectively.

Under certain circumstances, the Company reserves the right to charge a transfer fee which varies by product, refer to the product prospectus for the transfer fee charge. For the years ended December 31, 2008 and 2007, no transfer fees were deducted from the variable subaccounts.

The Company, upon full surrender of a policy, may assess a surrender charge. This charge is in part a deferred sales charge and in part a recovery of certain first year administrative costs. The amount of the surrender charge assessed, if any, will depend on the face amount of the policy and the issue age of the policy. In no event will the surrender charge exceed the maximum allowed by state or federal law. No surrender charge is imposed on a partial surrender, but an administrative fee of \$25 (not to exceed 2% of the amount withdrawn) is imposed, allocated pro-rata among the variable subaccounts (and, where applicable, the fixed account) from which the partial surrender proceeds are taken. The full surrender charges and partial surrender administrative charges for the year ended December 31, 2008 and 2007 amounted to \$1,665,733 and \$1,878,722, respectively.

Notes to financial statements (continued)

3. Financial Highlights

A summary of the fee rates, unit values, units outstanding, net assets and total return and investment income ratios for variable life contracts as of and for each year or period in the five years ended December 31, 2008 follows.

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
AIM V.I. Capital Appreciation											
	2008		0.80%	0.80%	\$ 3.31	\$ 9.16	2,003,857	\$ 8,945,031	-42.95%	-42.95%	0.00%
	2007		0.80%	0.80%	5.81	16.06	1,932,500	15,310,453	11.12%	11.12%	0.00%
	2006		0.80%	0.80%	12.33	12.33	2,068,744	14,527,585	5.45%	5.45%	0.08%
	2005		0.80%	0.80%	11.69	11.69	168,799	1,972,946	7.97%	7.97%	0.09%
	2004		0.80%	0.80%	10.83	10.83	117,337	1,270,229	5.78%	5.78%	0.00%
AIM V.I. Core Equity											
	2008		0.80%	0.80%	5.59	10.60	1,594,354	10,494,398	-30.70%	-30.70%	2.22%
	2007		0.80%	0.80%	8.06	15.29	1,668,754	15,834,178	7.26%	7.26%	1.11%
	2006	4/28/06	0.80%	0.80%	7.52	14.26	1,752,860	15,400,302	8.58%	8.58%	0.57%
AIM V.I. Diversified Income											
	2008		0.80%	0.80%	10.16	10.16	52,756	535,939	-16.40%	-16.40%	8.19%
	2007		0.80%	0.80%	12.15	12.15	67,291	817,731	0.91%	0.91%	6.94%
	2006		0.80%	0.80%	12.04	12.04	78,348	943,460	3.65%	3.65%	6.05%
	2005		0.80%	0.80%	11.62	11.62	76,783	892,074	2.08%	2.08%	6.59%
	2004		0.80%	0.80%	11.38	11.38	72,158	821,267	4.20%	4.20%	4.70%
AIM V.I. International Growth											
	2008		0.80%	0.80%	7.97	14.42	477,120	4,403,764	-40.86%	-40.86%	0.53%
	2007		0.80%	0.80%	13.48	24.37	530,364	8,172,517	13.81%	13.81%	0.44%
	2006		0.80%	0.80%	11.85	21.42	443,208	5,942,014	27.21%	27.21%	1.09%
	2005		0.80%	0.80%	9.31	16.84	409,767	4,364,470	16.99%	16.99%	0.69%
	2004		0.80%	0.80%	7.96	14.39	447,691	4,137,393	23.02%	23.02%	0.75%
ABVPSF Global Technology Class A											
	2008		0.50%	0.80%	6.40	9.03	113,203	854,579	-47.79%	-47.63%	0.00%
	2007		0.50%	0.80%	12.22	17.30	107,644	1,558,618	19.24%	19.58%	0.00%
	2006		0.50%	0.80%	11.14	14.51	73,377	899,887	7.77%	7.99%	0.00%
	2005		0.60%	0.80%	10.33	13.46	69,110	783,512	3.03%	3.04%	0.00%
	2004		0.80%	0.80%	10.03	13.06	65,550	760,964	4.61%	4.62%	0.00%
ABVPSF Growth and Income Class A											
	2008		0.50%	0.80%	6.97	10.02	645,679	5,553,448	-41.08%	-40.90%	2.14%
	2007		0.50%	0.80%	11.79	17.00	627,622	9,180,269	4.28%	4.59%	1.40%
	2006		0.50%	0.80%	13.46	16.31	556,860	7,873,920	16.35%	16.59%	1.40%
	2005		0.60%	0.80%	11.54	14.01	482,696	5,912,965	4.03%	4.24%	1.44%
	2004		0.60%	0.80%	11.66	13.47	473,846	5,630,854	10.57%	10.57%	0.92%
ABVPSF International Value Class A											
	2008		0.50%	0.80%	5.82	5.86	286,132	1,629,165	-53.56%	-53.42%	1.10%
	2007		0.50%	0.80%	12.52	12.58	220,933	2,774,186	4.99%	5.31%	1.09%
	2006	6/29/06	0.50%	0.80%	11.93	11.95	62,520	745,819	6.19%	20.51%	0.00%
ABVPSF Large Cap Growth Class A											
	2008		0.60%	0.80%	7.66	8.98	133,471	1,082,922	-40.14%	-40.02%	0.00%
	2007		0.60%	0.80%	12.80	15.00	131,093	1,778,334	13.01%	13.23%	0.00%
	2006		0.60%	0.80%	11.33	13.27	102,055	1,241,857	-1.24%	-1.04%	0.00%
	2005		0.60%	0.80%	11.47	13.44	124,246	1,500,355	14.23%	14.23%	0.00%
	2004		0.80%	0.80%	10.04	11.76	74,238	804,557	7.75%	7.75%	0.00%
ABVPSF Small/Mid Cap Value Class A											
	2008		0.50%	0.80%	5.66	13.11	500,558	5,336,774	-36.09%	-35.90%	0.74%
	2007		0.50%	0.80%	10.69	20.52	469,400	8,046,435	0.89%	1.20%	0.84%
	2006		0.50%	0.80%	13.86	20.34	354,193	6,313,513	13.51%	13.74%	0.40%
	2005		0.60%	0.80%	12.19	17.92	255,828	4,247,767	6.06%	6.27%	0.70%
	2004		0.60%	0.80%	13.96	16.89	280,185	4,580,987	18.35%	18.35%	0.18%
American Century VP Inflation Protection											
	2008		0.50%	0.80%	10.55	11.61	487,317	5,584,787	-2.06%	-1.77%	4.93%
	2007		0.50%	0.80%	11.20	11.85	329,642	3,861,974	8.80%	9.12%	4.72%
	2006		0.50%	0.80%	10.64	10.89	305,529	3,290,943	1.07%	1.28%	3.50%
	2005		0.60%	0.80%	10.51	10.78	229,678	2,453,849	1.00%	1.20%	5.03%
	2004	6/8/04	0.60%	0.80%	10.38	10.67	63,760	679,294	1.17%	5.62%	1.88%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
American Funds Global Growth Class 2											
	2008		0.50%	0.80%	\$ 7.82	\$10.89	500,768	\$ 5,208,527	-38.88%	-38.70%	2.01%
	2007		0.50%	0.80%	12.76	17.81	398,531	6,917,536	13.93%	14.28%	2.89%
	2006		0.50%	0.80%	15.41	15.63	267,649	4,096,785	19.47%	19.71%	0.80%
	2005		0.60%	0.80%	12.87	13.09	160,896	2,085,336	13.17%	13.39%	0.75%
	2004	5/11/04	0.60%	0.80%	11.35	11.56	15,267	176,451	3.37%	14.41%	0.28%
American Funds Global Small Capitalization Class 2											
	2008		0.50%	0.80%	6.05	14.87	695,175	6,416,649	-53.89%	-53.75%	0.00%
	2007		0.50%	0.80%	13.09	32.24	689,094	13,862,191	20.46%	20.82%	2.92%
	2006		0.50%	0.80%	15.03	26.77	648,359	10,809,203	23.06%	23.31%	0.46%
	2005		0.60%	0.80%	12.21	21.75	569,725	7,661,143	24.35%	24.60%	0.95%
	2004		0.60%	0.80%	9.82	17.49	433,085	4,664,236	19.92%	19.92%	0.00%
American Funds Growth Class 2											
	2008		0.50%	0.80%	5.67	11.34	4,567,320	33,831,036	-44.42%	-44.25%	0.85%
	2007		0.50%	0.80%	11.78	20.41	4,288,880	57,187,071	11.45%	11.79%	0.79%
	2006		0.50%	0.80%	10.67	18.31	4,257,473	50,516,050	9.34%	9.56%	0.82%
	2005		0.60%	0.80%	9.76	16.75	3,940,127	42,347,942	15.27%	15.50%	0.73%
	2004		0.60%	0.80%	8.47	14.53	3,509,530	31,790,881	11.60%	11.60%	0.19%
American Funds Growth-Income Class 2											
	2008		0.50%	0.80%	7.11	10.42	2,862,707	26,477,185	-38.34%	-38.16%	1.79%
	2007		0.50%	0.80%	11.50	16.90	2,640,024	40,071,688	4.21%	4.52%	1.54%
	2006		0.50%	0.80%	13.20	16.21	2,505,392	36,895,346	14.28%	14.51%	1.63%
	2005		0.60%	0.80%	11.52	14.19	2,297,404	29,857,906	4.99%	5.20%	1.38%
	2004		0.60%	0.80%	12.36	13.51	2,053,542	25,691,430	9.50%	9.50%	0.95%
American Funds International Class 2											
	2008		0.50%	0.80%	6.24	14.85	1,263,229	15,338,892	-42.59%	-42.41%	2.08%
	2007		0.50%	0.80%	13.21	25.86	1,092,786	23,832,763	19.07%	19.42%	1.60%
	2006		0.50%	0.80%	16.67	21.72	918,790	17,126,292	18.03%	18.27%	1.88%
	2005		0.60%	0.80%	14.09	18.40	646,492	10,548,952	20.54%	20.78%	1.74%
	2004		0.60%	0.80%	12.99	15.26	400,831	5,623,466	18.37%	18.37%	1.56%
Delaware VIPT Capital Reserves											
	2008		0.60%	0.80%	10.55	10.79	76,521	820,083	-1.09%	-0.89%	4.58%
	2007		0.50%	0.80%	10.67	10.89	33,898	368,549	3.59%	3.84%	4.78%
	2006		0.60%	0.80%	10.48	10.48	29,464	308,756	3.94%	3.94%	4.59%
	2005	10/13/05	0.60%	0.60%	10.09	10.09	54	549	0.48%	0.48%	1.07%
Delaware VIPT Diversified Income											
	2008		0.50%	0.80%	9.81	11.77	611,992	7,086,597	-5.30%	-5.02%	3.88%
	2007		0.50%	0.80%	11.42	12.43	557,992	6,846,577	6.77%	7.10%	2.98%
	2006		0.50%	0.80%	11.44	11.64	346,068	3,982,317	7.06%	7.27%	1.41%
	2005		0.60%	0.80%	10.66	10.87	224,878	2,421,509	-1.24%	-1.04%	0.93%
	2004	6/18/04	0.60%	0.80%	10.77	11.01	37,412	411,836	0.41%	8.66%	0.00%
Delaware VIPT Emerging Markets											
	2008		0.50%	0.80%	5.82	23.63	557,868	8,144,487	-51.94%	-51.80%	1.61%
	2007		0.50%	0.80%	15.83	49.17	489,109	16,447,355	37.75%	38.16%	1.49%
	2006		0.50%	0.80%	20.48	35.70	368,202	10,317,924	26.12%	26.37%	1.28%
	2005		0.60%	0.80%	16.21	28.30	340,436	8,235,806	26.47%	26.72%	0.29%
	2004		0.60%	0.80%	20.32	22.38	178,304	3,701,099	32.41%	32.41%	2.68%
Delaware VIPT High Yield											
	2008		0.50%	0.80%	7.32	13.94	699,233	7,427,937	-24.78%	-24.55%	8.31%
	2007		0.50%	0.80%	11.08	18.53	635,291	9,283,540	1.98%	2.28%	6.10%
	2006		0.50%	0.80%	12.50	18.18	581,476	8,546,219	11.55%	11.78%	6.47%
	2005		0.60%	0.80%	11.20	16.29	520,150	6,966,306	2.76%	2.97%	6.11%
	2004		0.60%	0.80%	10.90	15.86	446,775	5,958,300	13.34%	13.34%	5.68%
Delaware VIPT REIT											
	2008		0.50%	0.80%	6.59	17.87	420,234	5,811,841	-35.58%	-35.39%	2.47%
	2007		0.50%	0.80%	10.21	27.75	437,790	9,667,990	-14.62%	-14.37%	1.36%
	2006		0.50%	0.80%	17.24	32.50	421,813	11,396,157	31.57%	31.83%	1.83%
	2005		0.60%	0.80%	13.08	24.70	423,148	9,096,101	6.32%	6.53%	1.90%
	2004		0.60%	0.80%	17.10	23.23	394,711	8,507,193	30.33%	30.33%	1.91%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Delaware VIPT Small Cap Value											
	2008		0.50%	0.80%	\$ 6.74	\$16.63	1,065,473	\$15,136,517	-30.44%	-30.22%	0.78%
	2007		0.50%	0.80%	9.66	23.91	1,118,054	22,992,800	-7.36%	-7.09%	0.50%
	2006		0.50%	0.80%	14.99	25.81	1,101,175	25,262,583	15.26%	15.49%	0.24%
	2005		0.60%	0.80%	12.98	22.39	1,038,313	21,314,986	8.55%	8.76%	0.36%
	2004		0.60%	0.80%	16.34	20.63	996,078	19,349,591	20.51%	20.51%	0.19%
Delaware VIPT Trend											
	2008		0.50%	0.80%	5.33	11.19	995,173	7,084,387	-47.16%	-47.00%	0.00%
	2007		0.50%	0.80%	10.08	21.18	970,467	13,165,800	9.87%	10.20%	0.00%
	2006		0.50%	0.80%	9.18	19.27	1,008,808	12,114,068	6.74%	6.95%	0.00%
	2005		0.60%	0.80%	8.60	18.06	1,043,232	11,935,564	5.01%	5.22%	0.00%
	2004		0.60%	0.80%	8.19	17.20	1,201,526	12,752,573	11.71%	11.71%	0.00%
Delaware VIPT U.S. Growth											
	2008		0.50%	0.80%	6.76	8.43	58,282	431,972	-43.11%	-42.94%	0.04%
	2007		0.50%	0.80%	11.85	14.82	49,145	636,671	11.67%	11.99%	0.00%
	2006		0.50%	0.80%	10.89	13.27	45,842	527,633	1.50%	1.70%	0.00%
	2005		0.60%	0.80%	10.93	13.07	22,980	265,455	13.74%	13.74%	0.55%
	2004		0.80%	0.80%	9.61	11.49	18,593	189,669	2.48%	2.48%	0.13%
Delaware VIPT Value											
	2008		0.50%	0.80%	5.88	10.96	876,115	8,188,793	-33.95%	-33.76%	2.93%
	2007		0.50%	0.80%	11.21	16.59	901,588	12,993,898	-3.50%	-3.21%	1.42%
	2006		0.50%	0.80%	14.52	17.19	599,367	9,246,125	23.11%	23.36%	1.36%
	2005		0.60%	0.80%	11.77	13.96	409,720	5,167,322	5.18%	5.39%	1.45%
	2004		0.60%	0.80%	11.81	13.27	171,310	2,140,617	14.02%	14.02%	1.44%
DWS VIP EAFE Equity Index											
	2005		0.00%	0.00%	—	—	—	—	0.00%	0.00%	2.38%
	2004		0.60%	0.80%	7.98	13.96	343,757	3,039,364	18.12%	18.12%	2.36%
DWS VIP Equity 500 Index											
	2008		0.50%	0.80%	6.54	10.03	4,050,784	30,553,335	-37.65%	-37.47%	2.44%
	2007		0.50%	0.80%	10.48	16.09	4,006,124	48,654,924	4.46%	4.77%	1.49%
	2006		0.50%	0.80%	10.04	15.40	3,912,168	45,098,258	14.60%	14.83%	1.13%
	2005		0.60%	0.80%	8.76	13.44	3,988,045	39,935,517	3.84%	4.05%	1.55%
	2004		0.60%	0.80%	8.43	12.94	3,771,608	36,037,044	9.71%	9.71%	1.09%
DWS VIP Small Cap Index											
	2008		0.50%	0.80%	6.64	12.46	418,633	4,185,196	-34.65%	-34.45%	1.63%
	2007		0.50%	0.80%	10.13	19.07	427,459	6,589,261	-2.68%	-2.39%	0.86%
	2006		0.50%	0.80%	14.32	19.59	426,826	6,805,742	16.55%	16.79%	0.65%
	2005		0.60%	0.80%	12.26	16.81	403,767	5,599,732	3.43%	3.64%	0.62%
	2004		0.60%	0.80%	12.61	16.25	392,531	5,271,670	16.82%	16.82%	0.43%
Fidelity VIP Asset Manager											
	2008		0.80%	0.80%	10.48	10.48	99,582	1,043,134	-29.29%	-29.29%	3.40%
	2007		0.80%	0.80%	14.81	14.81	59,748	885,078	14.58%	14.58%	5.96%
	2006		0.80%	0.80%	12.93	12.93	64,191	829,862	6.46%	6.46%	2.47%
	2005		0.80%	0.80%	12.14	12.14	57,692	700,574	3.22%	3.22%	2.67%
	2004		0.80%	0.80%	11.77	11.77	58,993	694,055	4.63%	4.63%	3.03%
Fidelity VIP Contrafund Service Class											
	2008		0.50%	0.80%	7.06	11.78	2,087,314	19,650,595	-43.07%	-42.90%	0.95%
	2007		0.50%	0.80%	12.36	20.69	1,950,253	32,647,890	16.57%	16.92%	0.87%
	2006		0.50%	0.80%	13.54	17.75	1,916,231	27,699,823	10.70%	10.92%	1.12%
	2005		0.60%	0.80%	12.23	16.03	1,764,550	23,188,371	15.92%	16.15%	0.18%
	2004		0.60%	0.80%	10.55	13.83	1,359,263	15,369,340	14.42%	14.42%	0.24%
Fidelity VIP Equity-Income											
	2008		0.80%	0.80%	9.26	9.26	245,350	2,271,580	-43.11%	-43.11%	2.61%
	2007		0.80%	0.80%	16.27	16.27	244,176	3,973,942	0.72%	0.72%	1.68%
	2006		0.80%	0.80%	16.16	16.16	282,642	4,567,009	19.24%	19.24%	3.33%
	2005		0.80%	0.80%	13.55	13.55	277,207	3,756,580	5.02%	5.02%	1.83%
	2004		0.80%	0.80%	12.90	12.90	350,009	4,516,345	10.64%	10.64%	1.30%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Fidelity VIP Equity-Income Service Class											
	2008		0.60%	0.80%	\$ 7.95	\$ 9.53	196,313	\$ 1,769,257	-43.16%	-43.05%	2.31%
	2007		0.60%	0.80%	13.96	16.77	208,398	3,289,267	0.61%	0.81%	1.83%
	2006		0.60%	0.80%	13.85	16.67	160,242	2,519,199	19.12%	19.36%	3.07%
	2005		0.60%	0.80%	11.60	14.00	148,553	1,962,633	4.92%	5.12%	1.47%
	2004		0.60%	0.80%	12.13	13.34	168,077	2,093,201	10.49%	10.49%	1.32%
Fidelity VIP Growth Service Class											
	2008		0.50%	0.80%	4.74	8.97	789,793	4,258,352	-47.65%	-47.50%	0.75%
	2007		0.50%	0.80%	9.05	17.14	757,112	7,734,571	25.86%	26.24%	0.64%
	2006		0.50%	0.80%	7.19	13.62	901,016	7,016,391	5.88%	6.09%	0.28%
	2005		0.60%	0.80%	6.79	12.86	921,370	6,701,458	4.83%	5.04%	0.39%
	2004		0.60%	0.80%	6.48	12.27	898,402	6,245,428	2.44%	2.44%	0.16%
Fidelity VIP Growth Opportunities Service Class											
	2008		0.80%	0.80%	4.55	4.70	191,314	887,722	-55.42%	-55.42%	0.40%
	2007		0.80%	0.80%	10.21	10.54	164,244	1,706,800	22.06%	22.06%	0.00%
	2006		0.80%	0.80%	8.37	8.64	163,508	1,391,783	4.46%	4.46%	0.58%
	2005		0.80%	0.80%	8.01	8.27	163,917	1,334,657	7.99%	7.99%	0.80%
	2004		0.80%	0.80%	7.42	7.65	182,664	1,376,294	6.21%	6.21%	0.50%
Fidelity VIP High Income Service Class											
	2008		0.80%	0.80%	8.42	8.42	158,865	1,337,398	-25.66%	-25.66%	8.61%
	2007		0.80%	0.80%	11.32	11.32	176,310	1,996,602	1.84%	1.84%	7.70%
	2006		0.80%	0.80%	11.12	11.12	231,400	2,573,164	10.29%	10.29%	7.70%
	2005		0.80%	0.80%	10.08	10.08	246,538	2,485,663	1.71%	1.71%	14.99%
	2004		0.80%	0.80%	9.91	9.91	287,350	2,848,534	8.60%	8.60%	7.53%
Fidelity VIP Investment Grade Bond											
	2008		0.80%	0.80%	15.07	15.07	159,397	2,401,613	-4.02%	-4.02%	3.61%
	2007		0.80%	0.80%	15.70	15.70	151,082	2,371,676	3.52%	3.52%	4.32%
	2006		0.80%	0.80%	15.16	15.16	185,336	2,810,587	3.52%	3.52%	3.71%
	2005		0.80%	0.80%	14.65	14.65	163,401	2,393,746	1.38%	1.38%	4.52%
	2004		0.80%	0.80%	14.45	14.45	263,474	3,807,332	3.62%	3.62%	3.97%
Fidelity VIP Mid Cap Service Class											
	2008		0.50%	0.80%	7.09	9.41	264,448	2,217,726	-39.99%	-39.81%	0.37%
	2007		0.50%	0.80%	11.78	15.65	192,168	2,836,774	14.57%	14.91%	0.74%
	2006		0.50%	0.80%	13.59	13.63	113,576	1,493,639	11.69%	11.92%	0.14%
	2005	6/8/05	0.60%	0.80%	12.17	12.18	40,987	498,964	12.70%	16.91%	0.00%
Fidelity VIP Overseas Service Class											
	2008		0.50%	0.80%	7.09	12.69	265,573	2,973,172	-44.31%	-44.14%	2.57%
	2007		0.50%	0.80%	12.70	22.79	253,745	5,188,560	16.27%	16.62%	3.17%
	2006		0.50%	0.80%	16.33	19.60	211,913	3,801,775	17.01%	17.24%	0.68%
	2005		0.60%	0.80%	13.93	16.75	162,939	2,540,942	18.02%	18.26%	0.51%
	2004		0.60%	0.80%	12.58	14.20	108,033	1,451,178	12.58%	12.58%	0.87%
FTVIPT Franklin Income Securities											
	2008		0.50%	0.80%	8.16	8.22	171,702	1,381,629	-29.97%	-29.76%	6.04%
	2007		0.50%	0.80%	11.65	11.70	110,769	1,293,010	3.18%	3.49%	2.82%
	2006	6/29/06	0.50%	0.80%	11.29	11.31	61,407	693,513	2.09%	11.72%	0.00%
FTVIPT Franklin Small-Mid Cap Growth Securities											
	2008		0.50%	0.80%	6.34	10.37	290,614	2,484,732	-42.80%	-42.63%	0.00%
	2007		0.50%	0.80%	11.05	18.13	263,841	3,989,493	10.62%	10.95%	0.00%
	2006		0.50%	0.80%	12.77	16.39	233,224	3,259,260	8.09%	8.30%	0.00%
	2005		0.60%	0.80%	11.79	15.17	191,669	2,525,481	4.25%	4.46%	0.00%
	2004		0.60%	0.80%	11.68	14.55	157,450	2,025,146	10.81%	10.81%	0.00%
FTVIPT Mutual Shares Securities											
	2008		0.50%	0.80%	7.30	7.36	173,532	1,267,605	-37.44%	-37.25%	3.30%
	2007		0.50%	0.80%	11.67	11.73	146,750	1,717,314	2.90%	3.20%	1.35%
	2006	7/13/06	0.50%	0.80%	11.34	11.37	43,210	490,509	1.15%	13.68%	0.00%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
FTVIPT Templeton Foreign Securities											
	2008		0.80%	0.80%	\$10.79	\$10.79	341,997	\$ 3,690,903	-40.71%	-40.71%	2.54%
	2007		0.80%	0.80%	18.20	18.20	305,354	5,558,297	14.87%	14.87%	2.06%
	2006		0.80%	0.80%	15.85	15.85	259,912	4,118,820	20.73%	20.73%	1.44%
	2005		0.80%	0.80%	13.13	13.13	251,385	3,299,741	9.60%	9.60%	1.22%
	2004		0.80%	0.80%	11.98	11.98	321,286	3,848,019	17.93%	17.93%	1.10%
FTVIPT Templeton Foreign Securities Class 2											
	2008		0.80%	0.80%	9.49	10.10	386,134	3,730,420	-40.85%	-40.85%	2.38%
	2007		0.80%	0.80%	16.05	17.08	382,124	6,238,533	14.54%	14.54%	1.98%
	2006		0.80%	0.80%	14.01	14.91	366,207	5,226,684	20.48%	20.48%	1.24%
	2005		0.80%	0.80%	11.63	12.38	378,744	4,486,087	9.29%	9.29%	1.18%
	2004		0.80%	0.80%	10.64	11.33	406,800	4,408,103	17.58%	17.58%	1.07%
FTVIPT Templeton Global Asset Allocation											
	2008		0.80%	0.80%	15.55	15.55	99,735	1,550,428	-25.57%	-25.57%	13.45%
	2007		0.80%	0.80%	20.89	20.89	186,931	3,904,058	9.44%	9.44%	16.95%
	2006		0.80%	0.80%	19.08	19.08	161,690	3,085,542	20.42%	20.42%	7.00%
	2005		0.80%	0.80%	15.85	15.85	154,471	2,447,868	3.03%	3.03%	3.86%
	2004		0.80%	0.80%	15.38	15.38	124,082	1,908,543	15.01%	15.01%	3.00%
FTVIPT Templeton Global Income Securities											
	2008		0.50%	0.80%	12.30	13.08	168,792	2,164,772	5.62%	5.93%	3.33%
	2007		0.50%	0.80%	12.30	12.36	107,704	1,328,007	10.39%	10.61%	2.67%
	2006		0.60%	0.80%	11.14	11.17	63,244	706,635	12.24%	12.46%	2.39%
	2005	7/8/05	0.60%	0.80%	9.92	9.94	32,547	323,347	0.13%	1.67%	0.00%
FTVIPT Templeton Growth Securities											
	2008		0.50%	0.80%	6.73	11.69	337,224	3,233,361	-42.60%	-42.42%	2.05%
	2007		0.50%	0.80%	11.68	20.36	360,559	6,001,827	1.74%	2.04%	1.55%
	2006		0.50%	0.80%	15.04	20.01	349,609	6,165,385	21.23%	21.47%	1.43%
	2005		0.60%	0.80%	12.38	16.51	282,960	4,167,268	8.19%	8.41%	1.28%
	2004		0.60%	0.80%	12.82	15.26	262,667	3,636,957	15.32%	15.32%	1.25%
FTVIPT Templeton Growth Securities Class 2											
	2008		0.80%	0.80%	9.51	11.11	129,370	1,308,397	-42.78%	-42.78%	1.76%
	2007		0.80%	0.80%	16.61	19.41	136,644	2,407,169	1.53%	1.53%	1.43%
	2006		0.80%	0.80%	16.36	19.12	162,523	2,860,971	20.84%	20.84%	1.31%
	2005		0.80%	0.80%	13.54	15.82	177,130	2,574,172	8.00%	8.00%	1.09%
	2004		0.80%	0.80%	12.54	14.65	162,993	2,192,665	15.10%	15.10%	1.21%
Janus Aspen Series Balanced											
	2008		0.80%	0.80%	11.13	12.70	688,640	8,115,819	-16.51%	-16.51%	2.66%
	2007		0.80%	0.80%	13.33	15.21	735,072	10,372,704	9.66%	9.66%	2.58%
	2006		0.80%	0.80%	12.15	13.87	701,540	9,023,867	9.84%	9.84%	2.05%
	2005		0.80%	0.80%	11.06	12.63	838,282	9,924,495	7.09%	7.09%	2.28%
	2004		0.80%	0.80%	10.33	11.79	893,008	9,853,090	7.66%	7.66%	2.29%
Janus Aspen Series Balanced Service Shares											
	2008		0.60%	0.80%	11.62	12.59	105,074	1,295,149	-16.73%	-16.56%	2.43%
	2007		0.60%	0.80%	13.93	15.12	103,951	1,537,619	9.41%	9.63%	2.29%
	2006		0.60%	0.80%	12.71	13.82	109,430	1,479,716	9.54%	9.75%	1.97%
	2005		0.60%	0.80%	11.58	12.61	109,778	1,357,219	6.80%	7.02%	2.06%
	2004		0.60%	0.80%	11.48	11.81	123,290	1,428,495	7.43%	7.43%	2.61%
Janus Aspen Series Global Technology Service Shares											
	2008		0.80%	0.80%	2.83	2.83	357,075	1,010,180	-44.42%	-44.42%	0.09%
	2007		0.80%	0.80%	5.09	5.09	316,268	1,609,769	20.73%	20.73%	0.35%
	2006		0.80%	0.80%	4.22	4.22	313,722	1,322,647	6.97%	6.97%	0.00%
	2005		0.80%	0.80%	3.94	3.94	331,360	1,305,994	10.66%	10.66%	0.00%
	2004		0.80%	0.80%	3.56	3.56	347,237	1,236,723	-0.23%	-0.23%	0.00%
Janus Aspen Series Mid Cap Growth Service Shares											
	2008		0.60%	0.80%	9.79	12.70	180,108	1,922,678	-44.30%	-44.19%	0.07%
	2007		0.60%	0.80%	17.58	22.79	147,453	2,851,925	20.77%	21.01%	0.07%
	2006		0.60%	0.80%	14.56	18.87	135,633	2,179,459	12.40%	12.63%	0.00%
	2005		0.60%	0.80%	12.95	16.79	102,234	1,497,023	11.13%	11.36%	0.00%
	2004		0.60%	0.80%	11.66	15.11	80,708	1,059,851	19.52%	19.52%	0.00%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Janus Aspen Series Worldwide Growth											
	2008		0.80%	0.80%	\$ 4.30	\$ 6.75	988,171	\$ 4,940,368	-45.10%	-45.10%	1.25%
	2007		0.80%	0.80%	7.82	12.29	907,735	8,293,704	8.75%	8.75%	0.75%
	2006		0.80%	0.80%	7.19	11.30	999,605	8,346,514	17.26%	17.26%	1.78%
	2005		0.80%	0.80%	6.14	9.63	1,058,408	7,525,833	5.02%	5.02%	1.38%
	2004		0.80%	0.80%	5.84	9.17	1,134,862	7,684,144	3.94%	3.94%	1.00%
Janus Aspen Series Worldwide Growth Service Shares											
	2008		0.80%	0.80%	7.32	8.35	145,669	1,137,787	-45.25%	-45.25%	1.04%
	2007		0.80%	0.80%	13.36	15.24	138,354	1,970,877	8.49%	8.49%	0.56%
	2006		0.80%	0.80%	12.32	14.05	145,721	1,909,888	17.00%	17.00%	1.62%
	2005		0.80%	0.80%	10.53	12.01	156,183	1,742,587	4.73%	4.73%	1.21%
	2004		0.80%	0.80%	10.05	11.47	171,854	1,823,453	3.69%	3.69%	1.04%
Lincoln VIPT Baron Growth Opportunities											
	2008		0.50%	0.80%	5.85	8.24	2,561	21,042	-39.47%	-39.29%	0.00%
	2007	6/7/07	0.50%	0.80%	9.63	13.59	3,175	39,262	-3.15%	1.72%	0.00%
Lincoln VIPT Baron Growth Opportunities Service Class											
	2008		0.50%	0.80%	5.87	12.10	339,886	3,500,450	-39.62%	-39.44%	0.00%
	2007		0.50%	0.80%	10.95	20.05	357,263	6,125,573	2.60%	2.91%	0.00%
	2006		0.50%	0.80%	16.76	19.54	335,574	5,909,773	14.60%	14.60%	0.00%
	2005		0.80%	0.80%	14.62	17.05	329,043	5,076,670	2.54%	2.54%	0.00%
	2004		0.80%	0.80%	14.26	16.63	334,568	5,032,439	24.64%	24.64%	0.00%
Lincoln VIPT Capital Growth											
	2008		0.50%	0.80%	6.24	6.27	28,533	178,978	-42.05%	-41.88%	0.24%
	2007	8/15/07	0.50%	0.80%	10.77	10.79	2,172	23,440	-1.42%	13.93%	0.05%
Lincoln VIPT Cohen & Steers Global Real Estate											
	2008		0.50%	0.80%	4.76	4.78	98,768	471,606	-42.50%	-42.32%	1.59%
	2007	6/29/07	0.50%	0.80%	8.28	8.29	52,100	431,723	-12.55%	0.53%	0.76%
Lincoln VIPT Columbia Value Opportunities											
	2008	7/17/08	0.50%	0.80%	6.17	6.20	17,524	108,319	-32.59%	-28.23%	0.66%
Lincoln VIPT Core											
	2006	11/8/06	0.60%	0.60%	11.90	11.90	299	3,563	1.78%	1.78%	0.44%
Lincoln VIPT Delaware Bond											
	2008		0.50%	0.80%	9.97	15.27	2,205,554	30,385,961	-3.70%	-3.41%	4.62%
	2007		0.50%	0.80%	11.03	15.86	2,378,393	34,379,660	4.60%	4.92%	4.96%
	2006		0.50%	0.80%	11.02	15.16	2,265,550	31,881,345	3.88%	4.09%	4.61%
	2005		0.60%	0.80%	10.58	14.59	2,059,682	28,198,986	1.82%	2.03%	4.28%
	2004		0.60%	0.80%	11.69	14.33	1,838,866	25,359,106	4.46%	4.46%	4.22%
Lincoln VIPT Delaware Growth and Income											
	2008		0.50%	0.80%	6.18	8.10	34,871	261,164	-36.28%	-36.09%	1.59%
	2007		0.50%	0.80%	12.69	12.69	18,974	232,853	5.48%	5.48%	1.28%
	2006		0.60%	0.60%	12.03	12.03	7,375	88,739	11.69%	11.69%	1.34%
	2005	8/5/05	0.60%	0.60%	10.77	10.77	3,828	41,244	2.00%	2.00%	1.63%
Lincoln VIPT Delaware Social Awareness											
	2008		0.50%	0.80%	7.20	11.28	74,821	652,608	-34.93%	-34.74%	0.90%
	2007		0.50%	0.80%	11.03	17.33	85,652	1,112,627	2.15%	2.45%	0.89%
	2006		0.50%	0.80%	11.24	16.97	80,143	1,024,868	11.41%	11.64%	0.95%
	2005		0.60%	0.80%	10.08	15.23	66,544	759,070	11.14%	11.36%	0.95%
	2004		0.60%	0.80%	9.07	13.71	44,741	457,183	11.80%	11.80%	1.05%
Lincoln VIPT Delaware Special Opportunities											
	2008		0.50%	0.80%	5.78	5.80	51,148	296,767	-37.14%	-37.01%	1.69%
	2007	7/17/07	0.60%	0.80%	9.20	9.21	4,007	36,891	-8.90%	1.12%	1.15%
Lincoln VIPT FI Equity-Income											
	2008		0.50%	0.80%	6.73	8.75	299,879	2,548,489	-38.81%	-38.63%	1.55%
	2007		0.50%	0.80%	12.44	14.30	286,146	4,010,177	3.52%	3.73%	1.20%
	2006		0.60%	0.80%	11.99	13.81	291,893	3,987,045	10.38%	10.60%	1.33%
	2005		0.60%	0.80%	12.29	12.51	260,840	3,242,048	3.66%	3.66%	1.16%
	2004		0.80%	0.80%	11.86	12.07	265,794	3,198,589	8.89%	8.89%	1.12%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Lincoln VIPT Growth											
	2006		0.60%	0.60%	\$12.00	\$12.00	1,001	\$ 12,012	5.54%	5.54%	0.00%
	2005	12/14/05	0.60%	0.60%	11.37	11.37	343	3,897	-0.91%	-0.91%	0.00%
Lincoln VIPT Growth Opportunities											
	2006	1/13/06	0.60%	0.80%	13.39	13.43	3,491	46,780	-4.69%	4.47%	0.00%
Lincoln VIPT Janus Capital Appreciation											
	2008		0.50%	0.80%	4.59	9.82	370,420	2,193,697	-41.29%	-41.12%	0.70%
	2007		0.50%	0.80%	7.82	16.73	352,912	3,470,407	19.46%	19.70%	0.30%
	2006		0.60%	0.80%	6.54	14.01	284,319	2,110,104	8.80%	9.02%	0.19%
	2005		0.60%	0.80%	6.02	12.87	302,642	2,062,920	3.37%	3.59%	0.24%
	2004		0.60%	0.80%	5.82	12.45	352,989	2,304,631	4.44%	4.44%	0.00%
Lincoln VIPT Marsico International Growth											
	2008		0.50%	0.80%	5.68	5.71	123,175	701,835	-49.35%	-49.20%	1.62%
	2007	8/9/07	0.50%	0.80%	11.22	11.24	30,361	340,898	-4.43%	17.14%	1.01%
Lincoln VIPT MFS Value											
	2008		0.50%	0.80%	6.58	6.60	176,114	1,158,686	-32.70%	-32.63%	1.98%
	2007	9/18/07	0.50%	0.60%	9.78	9.79	6,071	59,414	-1.54%	-1.31%	0.79%
Lincoln VIPT Mid-Cap Value											
	2008		0.50%	0.80%	5.13	5.14	37,888	194,415	-41.06%	-41.00%	0.38%
	2007	7/18/07	0.50%	0.60%	8.70	8.71	17,967	156,424	-14.88%	-9.26%	0.57%
Lincoln VIPT Mondrian International Value											
	2008		0.50%	0.80%	6.36	15.70	581,885	7,471,477	-37.16%	-36.97%	4.83%
	2007		0.50%	0.80%	13.16	24.98	600,038	12,644,350	10.60%	10.93%	2.15%
	2006		0.50%	0.80%	16.98	22.59	504,039	10,265,957	28.97%	29.23%	3.13%
	2005		0.60%	0.80%	13.14	17.52	433,211	6,938,947	11.65%	11.87%	2.54%
	2004		0.60%	0.80%	13.91	15.69	199,570	3,007,478	19.97%	19.97%	1.57%
Lincoln VIPT Money Market											
	2008		0.50%	0.80%	10.44	12.98	3,131,992	36,725,669	1.53%	1.83%	2.28%
	2007		0.50%	0.80%	10.78	12.79	2,482,044	28,966,948	4.13%	4.44%	4.85%
	2006		0.50%	0.80%	10.60	12.28	2,548,456	28,705,660	3.85%	4.05%	4.60%
	2005		0.60%	0.80%	10.21	11.83	1,878,251	20,558,120	1.97%	2.17%	2.77%
	2004		0.60%	0.80%	10.01	11.60	1,784,167	19,120,592	0.08%	0.08%	0.85%
Lincoln VIPT SSgA Bond Index											
	2008	8/28/08	0.60%	0.60%	10.30	10.30	18,725	192,916	3.67%	3.97%	1.42%
Lincoln VIPT SSgA Emerging Markets 100											
	2008	10/24/08	0.60%	0.60%	6.20	6.20	2,650	16,438	1.75%	18.15%	1.37%
Lincoln VIPT SSgA International Index											
	2008	7/23/08	0.80%	0.80%	5.79	5.79	3,157	18,287	-34.18%	-34.18%	0.85%
Lincoln VIPT SSgA Large Cap 100											
	2008	9/23/08	0.80%	0.80%	6.27	6.27	14,227	89,253	-26.54%	-26.54%	0.61%
Lincoln VIPT SSgA S&P 500 Index											
	2008		0.50%	0.80%	6.82	7.44	193,641	1,374,930	-37.70%	-37.51%	4.45%
	2007	4/27/07	0.50%	0.80%	10.91	11.91	63,494	728,387	-3.50%	1.37%	2.28%
Lincoln VIPT SSgA Small-Cap Index											
	2008		0.50%	0.80%	6.03	6.06	32,004	193,522	-34.50%	-34.30%	1.30%
	2007	6/25/07	0.50%	0.80%	9.21	9.22	12,664	116,682	-7.32%	0.45%	0.93%
Lincoln VIPT SSgA Small-Mid Cap 200											
	2008	7/23/08	0.80%	0.80%	6.62	6.62	2,999	19,863	-28.51%	-28.51%	0.82%
Lincoln VIPT T. Rowe Price Growth Stock											
	2008		0.60%	0.80%	5.76	5.78	13,195	76,262	-42.31%	-42.19%	0.35%
	2007	8/20/07	0.60%	0.80%	9.99	10.00	2,565	25,646	4.82%	5.23%	0.35%
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth											
	2008		0.50%	0.80%	6.54	10.22	90,299	768,800	-43.23%	-43.06%	0.00%
	2007		0.50%	0.80%	14.94	18.00	89,421	1,343,701	12.68%	12.91%	0.00%
	2006		0.60%	0.80%	13.25	15.97	14,619	201,073	8.40%	8.62%	0.00%
	2005		0.60%	0.80%	12.23	14.73	12,051	152,900	8.94%	8.94%	0.00%
	2004		0.80%	0.80%	11.22	13.52	4,493	52,881	12.76%	12.76%	0.00%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Lincoln VIPT Templeton Growth											
	2008		0.50%	0.80%	\$ 6.10	\$ 6.11	13,502	\$ 82,413	-38.14%	-38.07%	3.26%
	2007	7/18/07	0.50%	0.60%	9.87	9.87	2,507	24,742	-3.45%	-0.17%	2.93%
Lincoln VIPT Turner Mid-Cap Growth											
	2008		0.50%	0.80%	5.56	5.57	52,027	288,856	-49.61%	-49.55%	0.00%
	2007	6/22/07	0.50%	0.60%	11.03	11.04	15,069	166,288	7.45%	8.11%	0.00%
Lincoln VIPT UBS Global Asset Allocation											
	2008		0.50%	0.80%	7.71	10.80	196,590	1,809,724	-33.76%	-33.56%	6.63%
	2007		0.50%	0.80%	11.61	16.31	170,907	2,346,237	5.53%	5.84%	1.94%
	2006		0.50%	0.80%	12.54	15.45	111,902	1,453,410	13.60%	13.82%	1.36%
	2005		0.60%	0.80%	11.04	13.60	103,469	1,184,665	5.95%	6.16%	1.40%
	2004		0.60%	0.80%	10.42	12.84	71,983	783,481	12.64%	12.64%	1.68%
Lincoln VIPT Wilshire 2010 Profile											
	2008	2/11/08	0.60%	0.80%	7.93	7.96	14,144	112,521	-21.29%	-18.50%	5.32%
Lincoln VIPT Wilshire 2020 Profile											
	2008		0.50%	0.60%	7.53	7.54	11,418	85,988	-27.33%	-27.26%	2.38%
	2007	8/29/07	0.50%	0.60%	10.36	10.37	3,514	36,414	0.92%	5.08%	0.41%
Lincoln VIPT Wilshire 2030 Profile											
	2008		0.50%	0.80%	7.22	7.22	64,121	461,742	-31.12%	-31.12%	1.14%
	2007	11/6/07	0.50%	0.50%	10.48	10.48	19,064	199,726	-1.98%	-1.98%	0.40%
Lincoln VIPT Wilshire 2040 Profile											
	2008		0.50%	0.60%	6.61	6.61	13,099	86,457	-35.87%	-35.87%	0.99%
	2007	12/28/07	0.50%	0.50%	10.30	10.30	2,220	22,864	-0.43%	-0.43%	#N/A
Lincoln VIPT Wilshire Aggressive Profile											
	2008		0.50%	0.80%	7.07	8.57	180,264	1,376,821	-40.93%	-40.76%	0.68%
	2007		0.50%	0.80%	14.48	14.48	81,918	1,118,813	10.35%	10.35%	1.29%
	2006	3/21/06	0.60%	0.60%	13.13	13.13	11,103	145,729	9.55%	9.55%	0.86%
Lincoln VIPT Wilshire Conservative Profile											
	2008		0.50%	0.80%	9.25	9.96	72,580	717,557	-19.09%	-18.85%	2.31%
	2007		0.50%	0.80%	12.22	12.29	50,442	615,005	6.92%	7.13%	1.98%
	2006		0.60%	0.80%	11.43	11.47	42,748	489,207	8.47%	8.69%	1.73%
	2005	9/16/05	0.60%	0.80%	10.54	10.55	38,918	410,247	0.56%	1.68%	0.00%
Lincoln VIPT Wilshire Moderate Profile											
	2008		0.50%	0.80%	8.49	9.55	568,941	4,984,877	-27.20%	-26.98%	2.36%
	2007		0.50%	0.80%	13.03	13.10	315,304	3,900,961	8.40%	8.61%	2.49%
	2006		0.60%	0.80%	12.02	12.06	69,278	834,879	11.14%	11.37%	1.17%
	2005	11/2/05	0.60%	0.80%	10.81	10.83	26,980	291,980	2.22%	2.36%	0.00%
Lincoln VIPT Wilshire Moderately Aggressive Profile											
	2008		0.50%	0.80%	7.80	9.05	736,875	6,292,005	-33.95%	-33.75%	1.37%
	2007		0.50%	0.80%	11.78	13.68	214,601	2,825,311	8.94%	9.26%	2.25%
	2006		0.50%	0.80%	12.49	12.53	76,877	916,473	13.23%	13.46%	1.75%
	2005	8/15/05	0.60%	0.80%	11.03	11.04	20,618	227,416	-0.42%	2.82%	0.00%
M Fund Brandes International Equity											
	2008		0.50%	0.80%	7.35	15.60	113,840	1,346,840	-40.32%	-40.14%	3.91%
	2007		0.50%	0.80%	12.28	26.14	108,775	2,225,907	7.15%	7.47%	2.16%
	2006		0.50%	0.80%	16.35	24.40	101,474	1,977,353	25.77%	26.02%	1.54%
	2005		0.60%	0.80%	19.40	19.40	77,722	1,329,658	9.67%	9.67%	1.89%
	2004		0.80%	0.80%	17.69	17.69	49,248	871,224	23.01%	23.01%	1.34%
M Fund Business Opportunity Value											
	2008		0.50%	0.60%	7.43	9.62	26,349	226,092	-34.88%	-34.81%	0.04%
	2007		0.50%	0.60%	11.39	14.77	17,031	228,147	4.81%	4.91%	1.12%
	2006		0.50%	0.60%	14.10	14.10	7,237	95,937	13.21%	13.21%	0.94%
	2005	3/17/05	0.60%	0.60%	12.45	12.45	2,365	29,451	8.36%	8.36%	1.46%
M Fund Frontier Capital Appreciation											
	2008		0.50%	0.80%	6.46	12.83	78,194	803,848	-42.49%	-42.32%	0.00%
	2007		0.50%	0.80%	16.95	22.31	67,996	1,227,362	11.03%	11.25%	0.00%
	2006		0.60%	0.80%	15.24	20.10	69,362	1,183,343	15.42%	15.65%	0.00%
	2005		0.60%	0.80%	17.41	17.41	46,176	727,446	14.21%	14.21%	0.00%
	2004		0.80%	0.80%	15.25	15.25	29,268	446,222	8.46%	8.46%	0.00%

Notes to financial statements (continued)

3. Financial Highlights (continued)

Subaccount	Year	Commencement Date(1)	Minimum Fee Rate(2)	Maximum Fee Rate(2)	Minimum Unit Value(3)	Maximum Unit Value(3)	Units Outstanding	Net Assets	Minimum Total Return(4)	Maximum Total Return(4)	Investment Income Ratio(5)
M Fund Turner Core Growth											
	2008		0.50%	0.80%	\$ 6.29	\$10.29	91,193	\$ 837,856	-49.38%	-49.23%	0.02%
	2007		0.50%	0.80%	16.92	20.34	62,768	1,138,627	21.45%	21.70%	0.46%
	2006		0.60%	0.80%	13.91	16.74	39,480	606,055	7.65%	7.87%	0.71%
	2005		0.60%	0.80%	15.55	15.55	29,935	439,415	13.01%	13.01%	0.57%
	2004		0.80%	0.80%	13.76	13.76	21,753	299,396	10.30%	10.30%	0.27%
MFS VIT Core Equity											
	2008		0.60%	0.80%	7.99	9.82	55,844	483,505	-39.64%	-39.52%	0.78%
	2007		0.60%	0.80%	13.24	16.27	54,254	779,911	10.26%	10.48%	0.34%
	2006		0.60%	0.80%	12.00	14.75	51,384	679,681	12.89%	13.12%	0.45%
	2005		0.60%	0.80%	10.63	13.07	53,280	623,258	0.88%	0.88%	0.73%
	2004		0.80%	0.80%	10.54	12.96	48,473	564,292	11.57%	11.57%	0.36%
MFS VIT Growth											
	2008		0.60%	0.80%	4.36	11.41	841,046	4,974,112	-37.92%	-37.79%	0.23%
	2007		0.60%	0.80%	7.03	18.39	893,622	8,464,685	20.21%	20.45%	0.00%
	2006		0.60%	0.80%	5.85	15.30	858,918	6,856,597	7.03%	7.25%	0.00%
	2005		0.60%	0.80%	5.46	14.29	891,556	6,584,972	8.32%	8.32%	0.00%
	2004		0.80%	0.80%	5.04	13.19	947,018	6,363,126	12.06%	12.06%	0.00%
MFS VIT Total Return											
	2008		0.50%	0.80%	8.73	13.18	1,164,594	13,966,695	-22.75%	-22.52%	3.09%
	2007		0.50%	0.80%	11.27	17.06	1,223,783	19,003,484	3.38%	3.70%	2.67%
	2006		0.50%	0.80%	12.44	16.50	1,446,474	21,858,456	11.00%	11.22%	2.30%
	2005		0.60%	0.80%	11.19	14.87	1,454,431	19,926,317	2.00%	2.20%	1.99%
	2004		0.60%	0.80%	12.60	14.58	1,276,946	17,374,998	10.43%	10.43%	1.59%
MFS VIT Utilities											
	2008		0.50%	0.80%	9.95	21.10	732,088	10,072,633	-38.17%	-37.98%	1.52%
	2007		0.50%	0.80%	16.05	34.13	746,076	16,697,622	26.88%	27.26%	0.92%
	2006		0.50%	0.80%	15.31	26.90	693,323	12,254,524	30.22%	30.48%	1.97%
	2005		0.60%	0.80%	11.76	20.66	687,111	9,335,704	15.91%	16.14%	0.57%
	2004		0.60%	0.80%	10.14	17.82	685,592	8,093,924	29.16%	29.16%	1.41%
NB AMT Mid-Cap Growth											
	2008		0.50%	0.80%	5.73	11.84	1,030,583	7,165,368	-43.82%	-43.65%	0.00%
	2007		0.50%	0.80%	10.20	21.07	1,045,772	12,834,285	21.55%	21.92%	0.00%
	2006		0.50%	0.80%	8.39	17.33	1,129,070	11,356,402	13.78%	14.01%	0.00%
	2005		0.60%	0.80%	7.38	15.23	1,067,271	9,277,381	12.84%	13.06%	0.00%
	2004		0.60%	0.80%	6.54	13.50	978,158	7,451,222	15.38%	15.38%	0.00%
NB AMT Partners											
	2008		0.80%	0.80%	7.28	7.79	203,440	1,562,004	-52.77%	-52.77%	0.55%
	2007		0.80%	0.80%	15.42	16.50	188,830	3,064,266	8.46%	8.46%	0.63%
	2006		0.80%	0.80%	14.21	15.21	204,185	3,034,110	11.35%	11.35%	0.78%
	2005		0.80%	0.80%	12.76	13.66	183,795	2,452,790	17.11%	17.11%	1.02%
	2004		0.80%	0.80%	10.90	11.66	139,909	1,593,534	18.03%	18.03%	0.01%
NB AMT Regency											
	2008		0.50%	0.80%	5.80	10.29	246,469	2,252,426	-46.25%	-46.09%	1.22%
	2007		0.50%	0.80%	10.77	19.15	268,776	4,613,431	2.48%	2.79%	0.45%
	2006		0.50%	0.80%	14.27	18.68	249,584	4,235,977	10.28%	10.50%	0.43%
	2005		0.60%	0.80%	12.92	16.94	272,526	4,339,310	11.11%	11.33%	0.09%
	2004		0.60%	0.80%	13.93	15.25	200,318	3,024,819	21.39%	21.39%	0.03%
Premier VIT OPCAP Global Equity											
	2008		0.00%	0.00%	—	—	—	—	0.00%	0.00%	1.51%
	2007		0.80%	0.80%	17.71	17.71	27,248	482,481	6.55%	6.55%	0.81%
	2006		0.80%	0.80%	16.62	16.62	34,296	569,959	20.10%	20.10%	0.84%
	2005		0.80%	0.80%	13.84	13.84	35,530	491,653	6.18%	6.18%	0.32%
	2004		0.80%	0.80%	13.03	13.03	35,715	465,456	11.64%	11.64%	0.52%
Premier VIT OPCAP Managed											
	2008		0.80%	0.80%	9.26	9.26	35,212	326,065	-30.33%	-30.33%	3.34%
	2007		0.80%	0.80%	13.29	13.29	44,938	597,247	2.23%	2.23%	2.17%
	2006		0.80%	0.80%	13.00	13.00	45,989	597,863	8.78%	8.78%	1.91%
	2005		0.80%	0.80%	11.95	11.95	57,054	681,858	4.44%	4.44%	1.23%
	2004		0.80%	0.80%	11.44	11.44	80,870	925,388	9.88%	9.88%	1.31%

Notes to financial statements (continued)

3. Financial Highlights (continued)

<i>Subaccount</i>	<i>Year</i>	<i>Commencement Date(1)</i>	<i>Minimum Fee Rate(2)</i>	<i>Maximum Fee Rate(2)</i>	<i>Minimum Unit Value(3)</i>	<i>Maximum Unit Value(3)</i>	<i>Units Outstanding</i>	<i>Net Assets</i>	<i>Minimum Total Return(4)</i>	<i>Maximum Total Return(4)</i>	<i>Investment Income Ratio(5)</i>
Putnam VT Growth & Income Class IB											
	2008		0.80%	0.80%	\$ 7.76	\$ 8.85	46,856	\$ 369,505	-39.19%	-39.19%	2.13%
	2007		0.80%	0.80%	12.76	14.55	50,856	657,604	-6.79%	-6.79%	1.62%
	2006		0.80%	0.80%	13.69	15.61	84,717	1,167,909	14.99%	14.99%	1.50%
	2005		0.80%	0.80%	11.91	13.58	74,441	891,344	4.39%	4.39%	1.55%
	2004		0.80%	0.80%	11.40	13.01	70,298	805,438	10.22%	10.23%	1.59%
Putnam VT Health Sciences Class IB											
	2008		0.80%	0.80%	9.24	11.05	36,618	360,265	-17.73%	-17.73%	0.00%
	2007		0.80%	0.80%	11.23	13.44	76,817	892,385	-1.39%	-1.35%	0.78%
	2006		0.80%	0.80%	11.38	13.62	77,231	907,766	1.97%	1.97%	0.30%
	2005		0.80%	0.80%	11.16	13.36	61,283	709,225	12.29%	12.30%	0.05%
	2004		0.80%	0.80%	9.94	11.90	39,688	427,437	6.27%	6.27%	0.17%

- (1) Reflects less than a full year of activity. Funds were first received in this option on the commencement date noted or the option was inactive at the date funds were received.
- (2) These amounts represent the annualized minimum and maximum contract expenses of the separate account, consisting primarily of mortality and expense charges, for each period indicated. The ratios include only those expenses that result in a direct reduction to unit values. Charges made directly to contract owner accounts through the redemption of units and expenses of the underlying funds have been excluded.
- (3) As the unit value is presented as a range of minimum to maximum values for only those subaccounts which existed for the entire year, some individual contract unit values may not be within the ranges presented as a result of partial year activity.
- (4) These amounts represent the total return, including changes in value of mutual funds, and reflect deductions for all items included in the fee rate. The total return does not include contract charges deducted directly from policy account values. The total return is not annualized. As the total return is presented as a range of minimum to maximum values for only those subaccounts which existed for the entire year, some individual contract total returns may not be within the ranges presented as a result of partial year activity.
- (5) These amounts represent the dividends, excluding distributions of capital gains, received by the subaccount from the underlying mutual fund, net of management fees assessed by the fund manager, divided by the average net assets. These ratios exclude those expenses, such as mortality and expense guarantee charges, that result in direct reductions in the unit values. The recognition of investment income by the subaccount is affected by the timing of the declaration of dividends by the underlying fund in which the subaccounts invest. Investment income ratios are not annualized.

Note: Fee rate, unit value and total return minimum and maximum are the same where there is only one active contract level charge for the subaccount.

Notes to financial statements (continued)

4. Purchases and Sales of Investments

The aggregate cost of investments purchased and the aggregate proceeds from investments sold were as follows for 2008.

	<i>Aggregate Cost of Purchases</i>	<i>Aggregate Proceeds from Sales</i>
AIM V.I. Capital Appreciation	\$ 1,299,167	\$ 1,137,603
AIM V.I. Core Equity	1,472,144	1,866,810
AIM V.I. Diversified Income	76,429	193,993
AIM V.I. International Growth	595,283	1,031,343
ABVPSF Global Technology Class A	271,114	217,659
ABVPSF Growth and Income Class A	2,517,788	912,386
ABVPSF International Value Class A	1,631,637	713,778
ABVPSF Large Cap Growth Class A	248,656	250,108
ABVPSF Small/Mid Cap Value Class A	2,317,296	1,275,058
American Century VP Inflation Protection	3,343,221	1,205,343
American Funds Global Growth Class 2	2,700,040	729,993
American Funds Global Small Capitalization Class 2	3,679,914	2,179,176
American Funds Growth Class 2	12,394,150	4,592,051
American Funds Growth-Income Class 2	8,295,219	3,335,536
American Funds International Class 2	8,037,849	2,755,644
Delaware VIPT Capital Reserves	587,749	103,758
Delaware VIPT Diversified Income	2,503,543	1,512,464
Delaware VIPT Emerging Markets	5,111,794	2,643,069
Delaware VIPT High Yield	3,780,100	2,600,607
Delaware VIPT REIT	4,802,187	2,033,032
Delaware VIPT Small Cap Value	3,465,605	3,214,515
Delaware VIPT Trend	3,466,408	1,366,138
Delaware VIPT U.S. Growth	206,391	73,602
Delaware VIPT Value	3,367,752	2,601,854
DWS VIP Equity 500 Index	6,767,414	5,687,613
DWS VIP Small Cap Index	1,521,496	1,009,191
Fidelity VIP Asset Manager	793,445	79,436
Fidelity VIP Contrafund Service Class	5,415,171	3,324,777
Fidelity VIP Equity-Income	533,239	448,919
Fidelity VIP Equity-Income Service Class	413,156	423,947
Fidelity VIP Growth Service Class	1,139,394	920,306
Fidelity VIP Growth Opportunities Service Class	367,413	171,724
Fidelity VIP High Income Service Class	273,607	325,303
Fidelity VIP Investment Grade Bond	1,049,162	824,812
Fidelity VIP Mid Cap Service Class	1,848,317	702,719
Fidelity VIP Overseas Service Class	1,457,968	618,160
FTVIPT Franklin Income Securities	1,357,443	701,485
FTVIPT Franklin Small-Mid Cap Growth Securities	1,119,485	403,299
FTVIPT Mutual Shares Securities	743,277	337,873
FTVIPT Templeton Foreign Securities	1,833,585	580,915
FTVIPT Templeton Foreign Securities Class 2	1,110,680	483,716
FTVIPT Templeton Global Asset Allocation	972,729	1,970,075
FTVIPT Templeton Global Income Securities	1,686,223	887,601
FTVIPT Templeton Growth Securities	1,237,923	1,139,528
FTVIPT Templeton Growth Securities Class 2	292,228	252,634
Janus Aspen Series Balanced	1,624,739	1,260,933
Janus Aspen Series Balanced Service Shares	254,312	99,058
Janus Aspen Series Global Technology Service Shares	227,436	130,546
Janus Aspen Series Mid Cap Growth Service Shares	1,057,255	342,846
Janus Aspen Series Worldwide Growth	1,190,987	616,726
Janus Aspen Series Worldwide Growth Service Shares	188,106	149,200
Lincoln VIPT Baron Growth Opportunities	40,529	38,525
Lincoln VIPT Baron Growth Opportunities Service Class	911,453	1,050,452
Lincoln VIPT Capital Growth	305,867	53,467
Lincoln VIPT Cohen & Steers Global Real Estate	597,013	188,057
Lincoln VIPT Columbia Value Opportunities	178,749	6,100
Lincoln VIPT Delaware Bond	6,061,128	7,401,324
Lincoln VIPT Delaware Growth and Income	214,974	21,961

Notes to financial statements (continued)

4. Purchases and Sales of Investments (continued)

	<i>Aggregate Cost of Purchases</i>	<i>Aggregate Proceeds from Sales</i>
Lincoln VIPT Delaware Social Awareness	\$ 216,836	\$ 279,273
Lincoln VIPT Delaware Special Opportunities	444,046	37,325
Lincoln VIPT FI Equity-Income	1,115,881	619,610
Lincoln VIPT Janus Capital Appreciation	548,035	336,035
Lincoln VIPT Marsico International Growth	1,112,680	139,591
Lincoln VIPT MFS Value	1,723,582	254,024
Lincoln VIPT Mid-Cap Value	363,957	173,044
Lincoln VIPT Mondrian International Value	2,542,366	2,137,512
Lincoln VIPT Money Market	32,352,165	24,864,636
Lincoln VIPT SSgA Bond Index	199,184	13,944
Lincoln VIPT SSgA Emerging Markets 100	15,064	282
Lincoln VIPT SSgA International Index	28,391	383
Lincoln VIPT SSgA Large Cap 100	120,208	1,533
Lincoln VIPT SSgA S&P 500 Index	2,180,630	846,864
Lincoln VIPT SSgA Small-Cap Index	288,399	100,914
Lincoln VIPT SSgA Small-Mid Cap 200	28,403	426
Lincoln VIPT T. Rowe Price Growth Stock	122,076	21,961
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	302,337	229,312
Lincoln VIPT Templeton Growth	108,351	8,821
Lincoln VIPT Turner Mid-Cap Growth	501,386	213,080
Lincoln VIPT UBS Global Asset Allocation	1,191,769	452,400
Lincoln VIPT Wilshire 2010 Profile	277,105	133,842
Lincoln VIPT Wilshire 2020 Profile	75,209	4,399
Lincoln VIPT Wilshire 2030 Profile	448,915	20,503
Lincoln VIPT Wilshire 2040 Profile	109,698	5,352
Lincoln VIPT Wilshire Aggressive Profile	1,168,365	75,742
Lincoln VIPT Wilshire Conservative Profile	372,339	112,089
Lincoln VIPT Wilshire Moderate Profile	3,250,728	575,089
Lincoln VIPT Wilshire Moderately Aggressive Profile	8,297,162	1,799,011
M Fund Brandes International Equity	596,748	465,254
M Fund Business Opportunity Value	120,379	12,757
M Fund Frontier Capital Appreciation	302,503	195,493
M Fund Turner Core Growth	448,194	46,283
MFS VIT Core Equity	54,762	41,569
MFS VIT Growth	732,410	1,205,375
MFS VIT Total Return	3,435,573	2,832,559
MFS VIT Utilities	4,476,326	2,611,608
NB AMT Mid-Cap Growth	1,073,421	1,287,476
NB AMT Partners	766,009	216,455
NB AMT Regency	512,439	925,545
Premier VIT OPCAP Global Equity	99,597	457,513
Premier VIT OPCAP Managed	77,272	141,582
Putnam VT Growth & Income Class IB	140,380	90,942
Putnam VT Health Sciences Class IB	119,111	534,556

5. Investments

The following is a summary of investments owned at December 31, 2008.

	<i>Shares Owned</i>	<i>Net Asset Value</i>	<i>Fair Value of Shares</i>	<i>Cost of Shares</i>
AIM V.I. Capital Appreciation	529,622	\$16.89	\$ 8,945,323	\$13,804,266
AIM V.I. Core Equity	532,637	19.75	10,519,577	13,491,626
AIM V.I. Diversified Income	91,352	5.86	535,319	775,142
AIM V.I. International Growth	225,959	19.49	4,403,940	5,287,189
ABVPSF Global Technology Class A	78,403	10.90	854,596	1,254,840
ABVPSF Growth and Income Class A	423,936	13.10	5,553,559	9,511,782
ABVPSF International Value Class A	147,440	11.05	1,629,216	3,343,238
ABVPSF Large Cap Growth Class A	58,633	18.47	1,082,945	1,478,056

Notes to financial statements (continued)

5. Investments (continued)

	<i>Shares Owned</i>	<i>Net Asset Value</i>	<i>Fair Value of Shares</i>	<i>Cost of Shares</i>
ABVPSF Small/Mid Cap Value Class A	537,996	\$ 9.92	\$ 5,336,922	\$ 8,683,743
American Century VP Inflation Protection	563,562	9.91	5,584,897	5,894,616
American Funds Global Growth Class 2	375,261	13.88	5,208,621	7,924,155
American Funds Global Small Capitalization Class 2	581,660	11.03	6,415,714	11,461,362
American Funds Growth Class 2	1,016,579	33.27	33,821,598	52,443,878
American Funds Growth-Income Class 2	1,098,047	24.11	26,473,905	37,787,885
American Funds International Class 2	1,258,349	12.19	15,339,275	22,775,447
Delaware VIPT Capital Reserves	89,141	9.20	820,097	849,085
Delaware VIPT Diversified Income	766,133	9.25	7,086,731	7,417,840
Delaware VIPT Emerging Markets	721,964	11.28	8,143,759	13,304,778
Delaware VIPT High Yield	1,792,512	4.14	7,421,000	9,742,045
Delaware VIPT REIT	873,610	6.64	5,800,771	12,275,931
Delaware VIPT Small Cap Value	811,796	18.64	15,131,870	20,982,930
Delaware VIPT Trend	426,405	16.61	7,082,592	11,800,028
Delaware VIPT U.S. Growth	86,224	5.01	431,980	651,232
Delaware VIPT Value	638,265	12.83	8,188,944	12,477,441
DWS VIP Equity 500 Index	3,199,412	9.55	30,554,388	39,674,412
DWS VIP Small Cap Index	484,660	8.63	4,182,619	6,308,317
Fidelity VIP Asset Manager	101,179	10.31	1,043,157	1,507,195
Fidelity VIP Contrafund Service Class	1,282,841	15.33	19,665,951	33,360,648
Fidelity VIP Equity-Income	172,354	13.18	2,271,629	3,941,546
Fidelity VIP Equity-Income Service Class	134,649	13.14	1,769,294	3,179,747
Fidelity VIP Growth Service Class	180,841	23.47	4,244,340	6,081,721
Fidelity VIP Growth Opportunities Service Class	89,821	9.97	895,518	1,435,513
Fidelity VIP High Income Service Class	339,448	3.94	1,337,427	2,062,533
Fidelity VIP Investment Grade Bond	202,792	11.84	2,401,059	2,549,160
Fidelity VIP Mid Cap Service Class	120,991	18.33	2,217,763	3,682,445
Fidelity VIP Overseas Service Class	244,481	12.12	2,963,110	4,743,193
FTVIPT Franklin Income Securities	119,316	11.58	1,381,679	1,805,753
FTVIPT Franklin Small-Mid Cap Growth Securities	206,035	12.06	2,484,780	3,991,331
FTVIPT Mutual Shares Securities	106,344	11.92	1,267,626	2,083,502
FTVIPT Templeton Foreign Securities	337,080	10.95	3,691,022	5,590,321
FTVIPT Templeton Foreign Securities Class 2	346,602	10.76	3,729,438	5,071,102
FTVIPT Templeton Global Asset Allocation	179,667	8.63	1,550,524	2,735,780
FTVIPT Templeton Global Income Securities	124,273	17.42	2,164,834	2,043,995
FTVIPT Templeton Growth Securities	387,701	8.34	3,233,425	5,228,903
FTVIPT Templeton Growth Securities Class 2	159,564	8.20	1,308,426	1,971,426
Janus Aspen Series Balanced	354,412	22.90	8,116,037	8,860,265
Janus Aspen Series Balanced Service Shares	54,921	23.75	1,304,377	1,405,744
Janus Aspen Series Global Technology Service Shares	347,998	2.90	1,009,194	1,614,878
Janus Aspen Series Mid Cap Growth Service Shares	92,889	20.70	1,922,797	2,667,921
Janus Aspen Series Worldwide Growth	256,613	19.27	4,944,928	7,749,000
Janus Aspen Series Worldwide Growth Service Shares	59,571	19.10	1,137,812	1,509,726
Lincoln VIPT Baron Growth Opportunities	1,210	17.39	21,042	33,877
Lincoln VIPT Baron Growth Opportunities Service Class	202,167	17.32	3,500,523	5,117,161
Lincoln VIPT Capital Growth	11,173	16.02	178,980	265,892
Lincoln VIPT Cohen & Steers Global Real Estate	102,770	4.59	471,613	790,578
Lincoln VIPT Columbia Value Opportunities	15,883	6.82	108,321	171,341
Lincoln VIPT Delaware Bond	2,602,520	11.68	30,392,234	33,136,721
Lincoln VIPT Delaware Growth and Income	12,453	20.97	261,169	409,588
Lincoln VIPT Delaware Social Awareness	29,126	22.41	652,621	919,572
Lincoln VIPT Delaware Special Opportunities	12,318	24.09	296,772	438,441
Lincoln VIPT FI Equity-Income	271,002	9.38	2,541,458	4,346,050
Lincoln VIPT Janus Capital Appreciation	155,037	14.15	2,193,767	3,142,599
Lincoln VIPT Marsico International Growth	84,939	8.26	701,847	1,255,173
Lincoln VIPT MFS Value	66,908	17.32	1,158,706	1,485,703
Lincoln VIPT Mid-Cap Value	24,038	8.09	194,418	265,713
Lincoln VIPT Mondrian International Value	559,890	13.34	7,470,613	10,417,486
Lincoln VIPT Money Market	3,665,507	10.00	36,655,067	36,655,065
Lincoln VIPT SSgA Bond Index	18,792	10.27	192,919	185,647
Lincoln VIPT SSgA Emerging Markets 100	2,797	5.88	16,438	14,804

Notes to financial statements (continued)

5. Investments (continued)

	<i>Shares Owned</i>	<i>Net Asset Value</i>	<i>Fair Value of Shares</i>	<i>Cost of Shares</i>
Lincoln VIPT SSgA International Index	3,069	\$ 5.96	\$ 18,287	\$ 27,868
Lincoln VIPT SSgA Large Cap 100	13,606	6.56	89,255	118,251
Lincoln VIPT SSgA S&P 500 Index	220,451	6.24	1,374,953	1,802,923
Lincoln VIPT SSgA Small-Cap Index	16,958	11.41	193,525	291,017
Lincoln VIPT SSgA Small-Mid Cap 200	2,905	6.84	19,863	27,882
Lincoln VIPT T. Rowe Price Growth Stock	7,185	10.61	76,263	119,916
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	100,002	7.69	768,814	1,230,406
Lincoln VIPT Templeton Growth	4,258	19.35	82,414	121,608
Lincoln VIPT Turner Mid-Cap Growth	48,329	5.98	288,861	383,595
Lincoln VIPT UBS Global Asset Allocation	208,162	8.69	1,809,758	2,882,396
Lincoln VIPT Wilshire 2010 Profile	14,245	7.90	112,523	138,608
Lincoln VIPT Wilshire 2020 Profile	11,394	7.55	85,989	105,215
Lincoln VIPT Wilshire 2030 Profile	63,271	7.30	461,750	626,963
Lincoln VIPT Wilshire 2040 Profile	12,854	6.73	86,458	103,381
Lincoln VIPT Wilshire Aggressive Profile	166,869	8.23	1,373,002	2,151,898
Lincoln VIPT Wilshire Conservative Profile	75,757	9.47	717,570	817,720
Lincoln VIPT Wilshire Moderate Profile	549,549	9.07	4,984,957	6,425,357
Lincoln VIPT Wilshire Moderately Aggressive Profile	728,760	8.63	6,292,111	9,125,666
M Fund Brandes International Equity	142,676	9.44	1,346,865	2,322,723
M Fund Business Opportunity Value	29,401	7.69	226,095	348,816
M Fund Frontier Capital Appreciation	58,335	13.78	803,862	1,296,692
M Fund Turner Core Growth	86,379	9.70	837,872	1,385,596
MFS VIT Core Equity	46,581	10.38	483,515	583,211
MFS VIT Growth	318,453	15.62	4,974,230	6,559,751
MFS VIT Total Return	906,528	15.42	13,978,656	17,657,489
MFS VIT Utilities	552,597	18.24	10,079,367	12,983,710
NB AMT Mid-Cap Growth	444,233	16.14	7,169,923	8,132,519
NB AMT Partners	219,699	7.11	1,562,064	3,330,981
NB AMT Regency	261,915	8.60	2,252,470	3,631,300
Premier VIT OPCAP Managed	13,496	24.16	326,072	514,442
Putnam VT Growth & Income Class IB	32,216	11.47	369,513	692,128
Putnam VT Health Sciences Class IB	32,693	11.02	360,273	420,968

6. Changes in Units Outstanding

The change in units outstanding for the year ended December 31, 2008 is as follows:

	<i>Units Issued</i>	<i>Units Redeemed</i>	<i>Net Increase (Decrease)</i>
AIM V.I. Capital Appreciation	273,383	(202,026)	71,357
AIM V.I. Core Equity	173,151	(247,551)	(74,400)
AIM V.I. Diversified Income	3,230	(17,765)	(14,535)
AIM V.I. International Growth	51,249	(104,493)	(53,244)
ABVPSF Global Technology Class A	21,929	(16,370)	5,559
ABVPSF Growth and Income Class A	111,926	(93,869)	18,057
ABVPSF International Value Class A	168,940	(103,741)	65,199
ABVPSF Large Cap Growth Class A	20,426	(18,048)	2,378
ABVPSF Small/Mid Cap Value Class A	133,982	(102,824)	31,158
American Century VP Inflation Protection	269,061	(111,386)	157,675
American Funds Global Growth Class 2	161,233	(58,996)	102,237
American Funds Global Small Capitalization Class 2	185,734	(179,653)	6,081
American Funds Growth Class 2	828,449	(550,009)	278,440
American Funds Growth-Income Class 2	586,205	(363,522)	222,683
American Funds International Class 2	360,862	(190,419)	170,443
Delaware VIPT Capital Reserves	52,738	(10,115)	42,623
Delaware VIPT Diversified Income	196,989	(142,989)	54,000
Delaware VIPT Emerging Markets	174,814	(106,055)	68,759
Delaware VIPT High Yield	268,362	(204,420)	63,942
Delaware VIPT REIT	95,174	(112,730)	(17,556)
Delaware VIPT Small Cap Value	163,201	(215,782)	(52,581)

Notes to financial statements (continued)

6. Changes in Units Outstanding (continued)

	<i>Units Issued</i>	<i>Units Redeemed</i>	<i>Net Increase (Decrease)</i>
Delaware VIPT Trend	184,079	(159,373)	24,706
Delaware VIPT U.S. Growth	17,277	(8,140)	9,137
Delaware VIPT Value	230,952	(256,425)	(25,473)
DWS VIP Equity 500 Index	701,559	(656,899)	44,660
DWS VIP Small Cap Index	79,764	(88,590)	(8,826)
Fidelity VIP Asset Manager	45,288	(5,454)	39,834
Fidelity VIP Contrafund Service Class	459,993	(322,932)	137,061
Fidelity VIP Equity-Income	37,176	(36,002)	1,174
Fidelity VIP Equity-Income Service Class	29,433	(41,518)	(12,085)
Fidelity VIP Growth Service Class	159,856	(127,175)	32,681
Fidelity VIP Growth Opportunities Service Class	55,768	(28,698)	27,070
Fidelity VIP High Income Service Class	14,266	(31,711)	(17,445)
Fidelity VIP Investment Grade Bond	64,362	(56,047)	8,315
Fidelity VIP Mid Cap Service Class	133,118	(60,838)	72,280
Fidelity VIP Overseas Service Class	58,694	(46,866)	11,828
FTVIPT Franklin Income Securities	120,303	(59,370)	60,933
FTVIPT Franklin Small-Mid Cap Growth Securities	67,198	(40,425)	26,773
FTVIPT Mutual Shares Securities	65,751	(38,969)	26,782
FTVIPT Templeton Foreign Securities	81,021	(44,378)	36,643
FTVIPT Templeton Foreign Securities Class 2	49,642	(45,632)	4,010
FTVIPT Templeton Global Asset Allocation	12,870	(100,066)	(87,196)
FTVIPT Templeton Global Income Securities	137,906	(76,818)	61,088
FTVIPT Templeton Growth Securities	64,691	(88,026)	(23,335)
FTVIPT Templeton Growth Securities Class 2	11,987	(19,261)	(7,274)
Janus Aspen Series Balanced	69,314	(115,746)	(46,432)
Janus Aspen Series Balanced Service Shares	9,782	(8,659)	1,123
Janus Aspen Series Global Technology Service Shares	75,702	(34,895)	40,807
Janus Aspen Series Mid Cap Growth Service Shares	58,162	(25,507)	32,655
Janus Aspen Series Worldwide Growth	197,621	(117,185)	80,436
Janus Aspen Series Worldwide Growth Service Shares	19,775	(12,460)	7,315
Lincoln VIPT Baron Growth Opportunities	3,596	(4,210)	(614)
Lincoln VIPT Baron Growth Opportunities Service Class	71,675	(89,052)	(17,377)
Lincoln VIPT Capital Growth	32,929	(6,568)	26,361
Lincoln VIPT Cohen & Steers Global Real Estate	73,194	(26,526)	46,668
Lincoln VIPT Columbia Value Opportunities	18,426	(902)	17,524
Lincoln VIPT Delaware Bond	453,125	(625,964)	(172,839)
Lincoln VIPT Delaware Growth and Income	18,817	(2,920)	15,897
Lincoln VIPT Delaware Social Awareness	13,791	(24,622)	(10,831)
Lincoln VIPT Delaware Special Opportunities	52,656	(5,515)	47,141
Lincoln VIPT FI Equity-Income	72,675	(58,942)	13,733
Lincoln VIPT Janus Capital Appreciation	57,407	(39,899)	17,508
Lincoln VIPT Marsico International Growth	110,923	(18,109)	92,814
Lincoln VIPT MFS Value	204,605	(34,562)	170,043
Lincoln VIPT Mid-Cap Value	53,825	(33,904)	19,921
Lincoln VIPT Mondrian International Value	106,908	(125,061)	(18,153)
Lincoln VIPT Money Market	3,160,028	(2,510,080)	649,948
Lincoln VIPT SSgA Bond Index	20,131	(1,406)	18,725
Lincoln VIPT SSgA Emerging Markets 100	2,697	(47)	2,650
Lincoln VIPT SSgA International Index	3,206	(49)	3,157
Lincoln VIPT SSgA Large Cap 100	14,509	(282)	14,227
Lincoln VIPT SSgA S&P 500 Index	247,950	(117,803)	130,147
Lincoln VIPT SSgA Small-Cap Index	28,312	(8,972)	19,340
Lincoln VIPT SSgA Small-Mid Cap 200	3,045	(46)	2,999
Lincoln VIPT T. Rowe Price Growth Stock	13,704	(3,074)	10,630
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	26,249	(25,371)	878
Lincoln VIPT Templeton Growth	12,244	(1,249)	10,995
Lincoln VIPT Turner Mid-Cap Growth	66,458	(29,500)	36,958
Lincoln VIPT UBS Global Asset Allocation	65,479	(39,796)	25,683
Lincoln VIPT Wilshire 2010 Profile	14,387	(243)	14,144
Lincoln VIPT Wilshire 2020 Profile	8,405	(501)	7,904
Lincoln VIPT Wilshire 2030 Profile	47,275	(2,218)	45,057
Lincoln VIPT Wilshire 2040 Profile	11,632	(753)	10,879

Notes to financial statements (continued)

6. Changes in Units Outstanding (continued)

	<i>Units Issued</i>	<i>Units Redeemed</i>	<i>Net Increase (Decrease)</i>
Lincoln VIPT Wilshire Aggressive Profile	106,844	(8,498)	98,346
Lincoln VIPT Wilshire Conservative Profile	26,562	(4,424)	22,138
Lincoln VIPT Wilshire Moderate Profile	309,207	(55,570)	253,637
Lincoln VIPT Wilshire Moderately Aggressive Profile	575,023	(52,749)	522,274
M Fund Brandes International Equity	31,980	(26,915)	5,065
M Fund Business Opportunity Value	10,841	(1,523)	9,318
M Fund Frontier Capital Appreciation	23,775	(13,577)	10,198
M Fund Turner Core Growth	32,080	(3,655)	28,425
MFS VIT Core Equity	5,366	(3,776)	1,590
MFS VIT Growth	113,237	(165,813)	(52,576)
MFS VIT Total Return	165,069	(224,258)	(59,189)
MFS VIT Utilities	130,354	(144,342)	(13,988)
NB AMT Mid-Cap Growth	152,127	(167,316)	(15,189)
NB AMT Partners	31,603	(16,993)	14,610
NB AMT Regency	42,952	(65,259)	(22,307)
Premier VIT OPCAP Global Equity	1	(27,249)	(27,248)
Premier VIT OPCAP Managed	1,991	(11,717)	(9,726)
Putnam VT Growth & Income Class IB	4,391	(8,391)	(4,000)
Putnam VT Health Sciences Class IB	10,352	(50,551)	(40,199)

The change in units outstanding for the year ended December 31, 2007 is as follows:

	<i>Units Issued</i>	<i>Units Redeemed</i>	<i>Net Increase (Decrease)</i>
AIM V.I. Capital Appreciation	229,333	(365,577)	(136,244)
AIM V.I. Core Equity	227,279	(311,385)	(84,106)
AIM V.I. Diversified Income	8,652	(19,709)	(11,057)
AIM V.I. International Growth	223,083	(135,927)	87,156
ABVPSF Global Technology Class A	40,491	(6,224)	34,267
ABVPSF Growth and Income Class A	220,033	(149,271)	70,762
ABVPSF International Value Class A	212,194	(53,781)	158,413
ABVPSF Large Cap Growth Class A	39,324	(10,286)	29,038
ABVPSF Small/Mid Cap Value Class A	200,335	(85,128)	115,207
American Century VP Inflation Protection	120,075	(95,962)	24,113
American Funds Global Growth Class 2	166,751	(35,869)	130,882
American Funds Global Small Capitalization Class 2	178,832	(138,097)	40,735
American Funds Growth Class 2	662,085	(630,678)	31,407
American Funds Growth-Income Class 2	464,716	(330,084)	134,632
American Funds International Class 2	297,217	(123,221)	173,996
Delaware VIPT Capital Reserves	5,237	(803)	4,434
Delaware VIPT Diversified Income	282,930	(71,006)	211,924
Delaware VIPT Emerging Markets	236,631	(115,724)	120,907
Delaware VIPT High Yield	308,253	(254,438)	53,815
Delaware VIPT REIT	143,166	(127,189)	15,977
Delaware VIPT Small Cap Value	216,076	(199,197)	16,879
Delaware VIPT Trend	170,562	(208,903)	(38,341)
Delaware VIPT U.S. Growth	15,349	(12,046)	3,303
Delaware VIPT Value	402,984	(100,763)	302,221
DWS VIP Equity 500 Index	620,164	(526,208)	93,956
DWS VIP Small Cap Index	84,204	(83,571)	633
Fidelity VIP Asset Manager	5,220	(9,663)	(4,443)
Fidelity VIP Contrafund Service Class	419,554	(385,532)	34,022
Fidelity VIP Equity-Income	22,758	(61,224)	(38,466)
Fidelity VIP Equity-Income Service Class	61,651	(13,495)	48,156
Fidelity VIP Growth Service Class	139,611	(283,515)	(143,904)
Fidelity VIP Growth Opportunities Service Class	24,232	(23,496)	736
Fidelity VIP High Income Service Class	42,452	(97,542)	(55,090)
Fidelity VIP Investment Grade Bond	22,117	(56,371)	(34,254)
Fidelity VIP Mid Cap Service Class	111,548	(32,956)	78,592
Fidelity VIP Overseas Service Class	76,845	(35,013)	41,832
FTVIPT Franklin Income Securities	103,672	(54,310)	49,362
FTVIPT Franklin Small-Mid Cap Growth Securities	71,285	(40,668)	30,617

Notes to financial statements (continued)

6. Changes in Units Outstanding (continued)

	<i>Units Issued</i>	<i>Units Redeemed</i>	<i>Net Increase (Decrease)</i>
FTVIPT Mutual Shares Securities	116,191	(12,651)	103,540
FTVIPT Templeton Foreign Securities	72,763	(27,321)	45,442
FTVIPT Templeton Foreign Securities Class 2	58,587	(42,670)	15,917
FTVIPT Templeton Global Asset Allocation	36,359	(11,118)	25,241
FTVIPT Templeton Global Income Securities	49,456	(4,996)	44,460
FTVIPT Templeton Growth Securities	125,243	(114,293)	10,950
FTVIPT Templeton Growth Securities Class 2	17,976	(43,855)	(25,879)
Janus Aspen Series Balanced	95,797	(62,265)	33,532
Janus Aspen Series Balanced Service Shares	10,295	(15,774)	(5,479)
Janus Aspen Series Global Technology Service Shares	33,474	(30,928)	2,546
Janus Aspen Series Mid Cap Growth Service Shares	32,374	(20,554)	11,820
Janus Aspen Series Worldwide Growth	84,424	(176,294)	(91,870)
Janus Aspen Series Worldwide Growth Service Shares	18,765	(26,132)	(7,367)
Lincoln VIPT Baron Growth Opportunities	3,533	(358)	3,175
Lincoln VIPT Baron Growth Opportunities Service Class	99,485	(77,796)	21,689
Lincoln VIPT Capital Growth	2,177	(5)	2,172
Lincoln VIPT Cohen & Steers Global Real Estate	55,428	(3,328)	52,100
Lincoln VIPT Core	—	(299)	(299)
Lincoln VIPT Delaware Bond	534,641	(421,798)	112,843
Lincoln VIPT Delaware Growth and Income	12,029	(430)	11,599
Lincoln VIPT Delaware Social Awareness	18,996	(13,487)	5,509
Lincoln VIPT Delaware Special Opportunities	4,046	(39)	4,007
Lincoln VIPT FI Equity-Income	70,159	(75,906)	(5,747)
Lincoln VIPT Growth	34,606	(35,607)	(1,001)
Lincoln VIPT Growth Opportunities	448	(3,939)	(3,491)
Lincoln VIPT Janus Capital Appreciation	113,807	(45,214)	68,593
Lincoln VIPT Marsico International Growth	30,836	(475)	30,361
Lincoln VIPT MFS Value	6,144	(73)	6,071
Lincoln VIPT Turner Mid-Cap Growth	15,242	(173)	15,069
Lincoln VIPT Mid-Cap Value	18,189	(222)	17,967
Lincoln VIPT Mondrian International Value	251,349	(155,350)	95,999
Lincoln VIPT Money Market	3,820,856	(3,887,268)	(66,412)
Lincoln VIPT SSgA S&P 500 Index	64,106	(612)	63,494
Lincoln VIPT SSgA Small-Cap Index	12,806	(142)	12,664
Lincoln VIPT T. Rowe Price Growth Stock	2,616	(51)	2,565
Lincoln VIPT T. Rowe Price Structured Mid-Cap Growth	79,693	(4,891)	74,802
Lincoln VIPT Templeton Growth	2,614	(107)	2,507
Lincoln VIPT UBS Global Asset Allocation	82,241	(23,236)	59,005
Lincoln VIPT Wilshire 2020 Profile	3,628	(114)	3,514
Lincoln VIPT Wilshire 2030 Profile	19,172	(108)	19,064
Lincoln VIPT Wilshire 2040 Profile	2,220	—	2,220
Lincoln VIPT Wilshire Aggressive Profile	75,259	(4,444)	70,815
Lincoln VIPT Wilshire Conservative Profile	9,671	(1,977)	7,694
Lincoln VIPT Wilshire Moderate Profile	256,449	(10,423)	246,026
Lincoln VIPT Wilshire Moderately Aggressive Profile	170,056	(32,332)	137,724
M Fund Brandes International Equity	20,333	(13,032)	7,301
M Fund Business Opportunity Value	10,818	(1,024)	9,794
M Fund Frontier Capital Appreciation	14,131	(15,497)	(1,366)
M Fund Turner Core Growth	27,626	(4,338)	23,288
MFS VIT Core Equity	9,279	(6,409)	2,870
MFS VIT Growth	178,953	(144,249)	34,704
MFS VIT Total Return	164,869	(387,560)	(222,691)
MFS VIT Utilities	169,411	(116,658)	52,753
NB AMT Mid-Cap Growth	172,689	(255,987)	(83,298)
NB AMT Partners	30,812	(46,167)	(15,355)
NB AMT Regency	50,457	(31,265)	19,192
Premier VIT OPCAP Global Equity	1,752	(8,800)	(7,048)
Premier VIT OPCAP Managed	1,740	(2,791)	(1,051)
Putnam VT Growth & Income Class IB	9,412	(43,273)	(33,861)
Putnam VT Health Sciences Class IB	15,477	(15,891)	(414)

Report of Independent Registered Public Accounting Firm

Board of Directors of The Lincoln National Life Insurance Company
and

Contract Owners of Lincoln Life Flexible Premium Variable Life Account R

We have audited the accompanying statement of assets and liabilities of Lincoln Life Flexible Premium Variable Life Account R ("Variable Account"), comprised of the subaccounts described in Note 1, as of December 31, 2008, the related statement of operations for the year or period then ended, and related statements of changes in net assets for each of the two years in the period then ended, or for those sub-accounts operating for portions of such periods as disclosed in the financial statements. These financial statements are the responsibility of the Variable Account's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Variable Account's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Variable Account's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of investments owned as of December 31, 2008, by correspondence with the fund companies, or their transfer agents, as applicable. 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 financial position of each of the respective subaccounts constituting Lincoln Life Flexible Premium Variable Life Account R at December 31, 2008, the results of their operations for the year or period then ended, and changes in their net assets for the periods described above, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Philadelphia, Pennsylvania

March 13, 2009

The Lincoln National Life Insurance Company

The Lincoln National Life Insurance Company

**Consolidated Financial Statements
December 31, 2008 and 2007**

Report of Independent Registered Public Accounting Firm

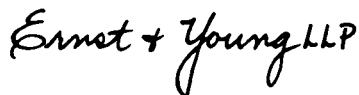
To the Board of Directors
The Lincoln National Life Insurance Company

We have audited the accompanying consolidated balance sheets of The Lincoln National Life Insurance Company and its subsidiaries (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of income, stockholder's equity and cash flows for each of the three years in the period ended December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits 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 The Lincoln National Life Insurance Company and its subsidiaries at December 31, 2008 and 2007, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2 to the consolidated financial statements, in 2007 the Company changed its method of accounting for deferred acquisition costs in connection with modifications or exchanges of insurance contracts as well as its method of accounting for uncertainty in income taxes.

The logo for Ernst & Young LLP, featuring the company name in a stylized, cursive script font.

Philadelphia, Pennsylvania
March 18, 2009

The Lincoln National Life Insurance Company

Consolidated Balance Sheets

(in millions, except share data)

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
ASSETS		
Investments:		
Available-for-sale securities, at fair value:		
Fixed maturity (amortized cost: 2008 — \$52,558; 2007 — \$53,250)	\$ 46,489	\$ 53,405
Equity (cost: 2008 — \$187; 2007 — \$132)	139	134
Trading securities	2,189	2,533
Mortgage loans on real estate	7,396	7,117
Real estate	119	258
Policy loans	2,887	2,848
Derivative investments	60	172
Other investments	948	986
Total investments	<u>60,227</u>	<u>67,453</u>
Cash and invested cash	2,116	975
Deferred acquisition costs and value of business acquired	11,184	8,574
Premiums and fees receivable	445	382
Accrued investment income	782	801
Reinsurance recoverables	11,334	7,779
Reinsurance related derivative assets	167	—
Goodwill	3,520	3,539
Other assets	3,509	2,451
Separate account assets	<u>55,655</u>	<u>82,263</u>
Total assets	<u>\$148,939</u>	<u>\$174,217</u>
LIABILITIES AND STOCKHOLDER'S EQUITY		
<i>Liabilities:</i>		
Future contract benefits	\$ 17,054	\$ 13,619
Other contract holder funds	59,441	58,168
Short-term debt	4	173
Long-term debt	2,080	1,675
Reinsurance related derivative liability	—	102
Funds withheld reinsurance liabilities	2,243	1,862
Deferred gain on business sold through reinsurance	542	696
Payables for collateral under securities loaned and derivatives	880	1,135
Other liabilities	1,382	2,083
Separate account liabilities	<u>55,655</u>	<u>82,263</u>
Total liabilities	<u>139,281</u>	<u>161,776</u>
Contingencies and Commitments (See Note 14)		
<i>Stockholder's Equity:</i>		
Common stock — 10,000,000 shares, authorized, issued and outstanding	9,132	9,105
Retained earnings	3,135	3,283
Accumulated other comprehensive income (loss)	<u>(2,609)</u>	<u>53</u>
Total stockholder's equity	<u>9,658</u>	<u>12,441</u>
Total liabilities and stockholder's equity	<u>\$148,939</u>	<u>\$174,217</u>

See accompanying Notes to Consolidated Financial Statements

The Lincoln National Life Insurance Company

Consolidated Statements of Income

(in millions)

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Revenues:			
Insurance premiums	\$1,835	\$1,664	\$1,174
Insurance fees	2,980	2,930	2,400
Net investment income	3,975	4,181	3,805
Realized loss	(831)	(127)	(35)
Amortization of deferred gain on business sold through reinsurance	76	83	76
Other revenues and fees	273	323	289
Total revenues	<u>8,308</u>	<u>9,054</u>	<u>7,709</u>
Benefits and Expenses:			
Interest credited	2,438	2,379	2,175
Benefits	2,645	2,330	1,758
Underwriting, acquisition, insurance and other expenses	2,954	2,520	2,073
Interest and debt expense	85	82	82
Total benefits and expenses	<u>8,122</u>	<u>7,311</u>	<u>6,088</u>
Income before taxes	186	1,743	1,621
Federal income tax expense (benefit)	(68)	504	460
Net income	<u>\$ 254</u>	<u>\$1,239</u>	<u>\$1,161</u>

See accompanying Notes to Consolidated Financial Statements

Consolidated Statements of Stockholder's Equity

(in millions)

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Common Stock:			
Balance at beginning-of-year	\$ 9,105	\$ 9,088	\$ 2,125
Lincoln National Corporation purchase price	—	(9)	6,932
Stock compensation	27	26	31
Balance at end-of-year	<u>9,132</u>	<u>9,105</u>	<u>9,088</u>
Retained Earnings:			
Balance at beginning-of-year	3,283	3,341	2,748
Cumulative effect of adoption of SOP 05-1	—	(41)	—
Cumulative effect of adoption of FIN 48	—	(14)	—
Comprehensive income (loss)	(2,408)	876	1,124
Less other comprehensive income (loss), net of tax:	(2,662)	(363)	(37)
Net Income	254	1,239	1,161
Dividends declared	(402)	(1,242)	(568)
Balance at end-of-year	<u>3,135</u>	<u>3,283</u>	<u>3,341</u>
Net Unrealized Gain (Loss) on Available-for-Sale Securities:			
Balance at beginning-of-year	76	421	452
Change during the year	(2,638)	(345)	(31)
Balance at end-of-year	<u>(2,562)</u>	<u>76</u>	<u>421</u>
Net Unrealized Gain (Loss) on Derivative Instruments:			
Balance at beginning-of-year	(19)	(9)	7
Change during the year	4	(10)	(16)
Balance at end-of-year	<u>(15)</u>	<u>(19)</u>	<u>(9)</u>
Minimum Pension Liability Adjustment:			
Balance at beginning-of-year	—	—	(6)
Change during the year	—	—	6
Balance at end-of-year	<u>—</u>	<u>—</u>	<u>—</u>
Funded Status of Employee Benefit Plans:			
Balance at beginning-of-year	(4)	4	—
Change during the year	(28)	(8)	4
Balance at end-of-year	<u>(32)</u>	<u>(4)</u>	<u>4</u>
Total stockholder's equity at end-of-year	<u>\$ 9,658</u>	<u>\$12,441</u>	<u>\$12,845</u>

See accompanying Notes to Consolidated Financial Statements

Consolidated Statements of Cash Flows

(in millions)

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Cash Flows from Operating Activities:			
Net income	\$ 254	\$ 1,239	\$ 1,161
Adjustments to reconcile net income to net cash provided by operating activities:			
Deferred acquisition costs, value of business acquired, deferred sales inducements and deferred front end loads deferrals and interest, net of amortization	(244)	(916)	(664)
Trading securities purchases, sales and maturities, net	177	316	165
Change in premiums and fees receivable	(61)	(88)	(3)
Change in accrued investment income	19	13	21
Change in future contract benefits	4,169	526	109
Change in other contract holder funds	(71)	453	741
Change in funds withheld reinsurance liability and reinsurance recoverables	(3,618)	(493)	304
Change in federal income tax accruals	(45)	310	150
Realized loss	831	127	35
Amortization of deferred gain on business sold through reinsurance	(76)	(83)	(76)
Stock-based compensation expense	19	26	31
Other	(31)	(160)	(1,055)
Net cash provided by operating activities	<u>1,323</u>	<u>1,270</u>	<u>919</u>
Cash Flows from Investing Activities:			
Purchases of available-for-sale securities	(5,776)	(8,606)	(9,323)
Sales of available-for-sale securities	1,506	3,453	5,328
Maturities of available-for-sale securities	3,732	4,087	3,326
Purchases of other investments	(1,163)	(2,018)	(696)
Sales or maturities of other investments	907	1,880	585
Increase (decrease) in payables for collateral under securities loaned and derivatives	(255)	(369)	538
Purchase of Jefferson-Pilot stock, net of cash acquired of \$39	—	—	154
Other	(117)	(84)	58
Net cash used in investing activities	<u>(1,166)</u>	<u>(1,657)</u>	<u>(30)</u>
Cash Flows from Financing Activities:			
Issuance of long-term debt	250	375	140
Issuance (decrease) in commercial paper	(14)	13	(13)
Deposits of fixed account values, including the fixed portion of variable	9,806	9,481	7,444
Withdrawals of fixed account values, including the fixed portion of variable	(5,910)	(6,645)	(6,660)
Transfers to and from separate accounts, net	(2,204)	(2,448)	(1,821)
Payment of funding agreements	(550)	—	—
Common stock issued for benefit plans and excess tax benefits	8	—	—
Dividends paid to stockholder	(402)	(787)	(568)
Net provided by (used in) financing activities	<u>984</u>	<u>(11)</u>	<u>(1,478)</u>
Net increase (decrease) in cash and invested cash	<u>1,141</u>	<u>(398)</u>	<u>(589)</u>
Cash and invested cash at beginning-of-year	<u>975</u>	<u>1,373</u>	<u>1,962</u>
Cash and invested cash at end-of-period	<u>\$ 2,116</u>	<u>\$ 975</u>	<u>\$ 1,373</u>

See accompanying Notes to Consolidated Financial Statements

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies

Nature of Operations

The Lincoln National Life Insurance Company ("LNL" or the "Company," which also may be referred to as "we," "our" or "us"), a wholly-owned subsidiary of Lincoln National Corporation ("LNC" or the "Parent Company"), is domiciled in the state of Indiana. We own 100% of the outstanding common stock of one insurance company subsidiary, Lincoln Life & Annuity Company of New York ("LLANY"). We also own several non-insurance companies, including Lincoln Financial Distributors ("LFD") and Lincoln Financial Advisors ("LFA"), LNC's wholesaling and retailing business units, respectively. LNL's principal businesses consist of underwriting annuities, deposit-type contracts and life insurance through multiple distribution channels. LNL is licensed and sells its products throughout the United States of America ("U.S.") and several U.S. territories, see Note 23.

Basis of Presentation

The accompanying consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). Certain GAAP policies, which significantly affect the determination of financial position, results of operations and cash flows, are summarized below.

On February 15, 2007, the North Carolina Department of Insurance approved the merger of Jefferson-Pilot Life Insurance Company ("JPL") into LNL with LNL being the survivor and Jefferson Pilot LifeAmerica Insurance Company ("JPLA") into LLANY, with JPLA being the survivor. JPLA then changed its name to LLANY. The effective date of these transactions was April 2, 2007. On May 3, 2007, LNL made a dividend to LNC that transferred ownership of our formerly wholly-owned subsidiary, First Penn-Pacific Life Insurance Company ("FPP"), to LNC. On July 2, 2007, the Nebraska Insurance Department approved the merger of Jefferson Pilot Financial Insurance Company ("JPFIC"), formerly a wholly-owned subsidiary of Jefferson-Pilot, into LNL.

Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combination" ("SFAS 141"), excludes transfers of net assets or exchanges of shares between entities under common control, and notes that certain provisions under Accounting Principles Board ("APB") Opinion No. 16, "Business Combinations," provide a source of guidance for such transactions. In accordance with APB Opinion No. 16, the consolidated financial statements are presented as if on April 3, 2006, LNL completed the merger with JPL, JPLA and JPFIC, and has included the results of operations and financial condition of JPL, JPLA and JPFIC in our consolidated financial statements beginning on April 3, 2006, in a manner similar to a pooling-of-interests. The consolidated financial statements for the period from January 1, 2006 through April 2, 2006 exclude the results of operations and financial condition of JPL, JPLA and JPFIC. The consolidated financial statements include the results of operations and financial condition of FPP from January 1, 2007 through May 3, 2007 and for the year ended December 31, 2006. FPP's results subsequent to May 3, 2007 are excluded from these consolidated financial statements.

The insurance subsidiaries also submit financial statements to insurance industry regulatory authorities. Those financial statements are prepared on the basis of statutory accounting practices ("SAP") and are significantly different from financial statements prepared in accordance with GAAP. See Note 21 for additional discussion on SAP.

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

For the two years ended December 31, 2007, we have reclassified the results of certain derivatives and embedded derivatives to realized gain (loss), which were previously reported within insurance fees, net investment income, interest credited or benefits on our Consolidated Statements of Income. The associated amortization expense of deferred acquisition costs ("DAC") and value of business acquired ("VOBA") (previously reported within underwriting, acquisition, insurance and other expenses), deferred sales inducements ("DSI") (previously reported within interest credited), deferred front-end loads ("DFEL") (previously reported within insurance fees) and changes in contract holder funds (previously reported within benefits) have also been reclassified to realized gain (loss) on our Consolidated Statements of Income. The detail of the reclassifications (in millions) from what was previously reported in prior period Consolidated Statements of Income (in millions) was as follows:

	<i>For the Years Ended December, 31</i>	
	<u>2007</u>	<u>2006</u>
Realized loss, as previously reported	\$(112)	\$ (2)
Effect of reclassifications to:		
Insurance fees	64	39
Net investment income	(5)	62
Interest credited	(19)	(66)
Benefits	(103)	(55)
Underwriting, acquisition, insurance and other expenses	<u>48</u>	<u>(13)</u>
Realized loss, as adjusted	<u>\$(127)</u>	<u>\$(35)</u>

Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of LNL and all other entities in which we have a controlling financial interest and any variable interest entities ("VIEs") in which we are the primary beneficiary. Entities in which we do not have a controlling financial interest and do not exercise significant management influence over the operating and financing decisions are reported using the equity method. The carrying value of our investments that we account for using the equity method on our Consolidated Balance Sheets and equity in earnings on our Consolidated Statements of Income is not material. All material inter-company accounts and transactions have been eliminated in consolidation. See Note 4 for additional discussion on our VIEs.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

I. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

Accounting Estimates and Assumptions

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses for the reporting period. Those estimates are inherently subject to change and actual results could differ from those estimates. Included among the material (or potentially material) reported amounts and disclosures that require extensive use of estimates are: fair value of certain invested assets and derivatives, asset valuation allowances, DAC, VOBA, goodwill, future contract benefits, other contract holder funds (including DFEL), pension plans, income taxes and the potential effects of resolving litigated matters.

Business Combinations

For all business combination transactions initiated after June 30, 2001, the purchase method of accounting has been used, and accordingly, the assets and liabilities of the acquired company have been recorded at their estimated fair values as of the merger date. The allocation of fair values may be subject to adjustment after the initial allocation for up to a one-year period as more information relative to the fair values as of the acquisition date becomes available. The consolidated financial statements include the results of operations of any acquired company since the acquisition date.

Available-For-Sale Securities

Securities classified as available-for-sale consist of fixed maturity and equity securities and are stated at fair value with unrealized gains and losses included as a separate component of accumulated other comprehensive income ("OCI"), net of associated DAC, VOBA, DSI, other contract holder funds and deferred income taxes.

We measure the fair value of our securities classified as available-for-sale based on assumptions used by market participants in pricing the security. Pursuant to SFAS No. 157, we have categorized these securities into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in "SFAS No. 157 – Fair Value Measurements" in Note 2. The most appropriate valuation methodology is selected based on the specific characteristics of the fixed maturity or equity security, and we consistently apply the valuation methodology to measure the security's fair value. Our fair value measurement is based on a market approach which utilizes prices and other relevant information generated by market transactions involving identical or comparable securities. Sources of inputs to the market approach include: third party pricing services, independent broker quotations or pricing matrices. We use observable and unobservable inputs to our valuation methodologies. Observable inputs include benchmark yields, reported trades, broker-dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data. In addition, market indicators, industry and

economic events are monitored and further market data is acquired if certain triggers are met. For certain security types, additional inputs may be used, or some of the inputs described above may not be applicable. For broker-quoted only securities, quotes from market makers or broker-dealers are obtained from sources recognized to be market participants. In order to validate the pricing information and broker-dealer quotes, we employ, where possible, procedures that include comparisons with similar observable positions, comparisons with subsequent sales, and discussions with senior business leaders and brokers as well as observations of general market movements for those security classes. For those securities trading in less liquid or illiquid markets with limited or no pricing information, we use unobservable inputs in order to measure the fair value of these securities. In cases where this information is not available, such as for privately placed securities, fair value is estimated using an internal pricing matrix. This matrix relies on management's judgment concerning: the discount rate used in calculating expected future cash flows, credit quality, industry sector performance and expected maturity.

We do not adjust prices received from third parties; however, we analyze the third party pricing services' valuation methodologies and related inputs and perform additional evaluation to determine the appropriate level within the fair value hierarchy. See Note 2 "Statement of Financial Accounting Standards ("SFAS") No. 157 ("SFAS 157") – Fair Value Measurements" for more information regarding the fair value hierarchy.

Dividends and interest income, recorded in net investment income, are recognized when earned. Amortization of premiums and accretion of discounts on investments in debt securities are reflected in net investment income over the contractual terms of the investments in a manner that produces a constant effective yield. Realized gains and losses on the sale of investments are determined using the specific identification method.

We regularly review available-for-sale securities for declines in fair value that we determine to be other-than-temporary. The cost basis of securities that are determined to be other-than-temporarily impaired is written down to current fair value with a corresponding charge to realized gain (loss) on our Consolidated Statements of Income. A write-down for impairment can be recognized for both credit-related events and for a decline in fair value due to changes in interest rates. Once a security is written down to fair value through net income, any subsequent recovery of fair value cannot be recognized in net income until the security is sold. However, in the event that the security is written down due to an interest-rate related impairment, a recovery in value is accreted through investment income over the life of the security. In evaluating whether a decline in value is other-than-temporary, we consider several factors including, but not limited to: the severity (generally if greater than 20%) and duration (generally if greater than six months) of the decline; our ability and intent to hold the security for a sufficient period of time to allow for a recovery in value; the cause of the decline; and fundamental analysis of the liquidity, business prospects and overall financial condition of the issuer.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

I. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

Trading Securities

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 pursuant to contractual terms of the reinsurance arrangements. Trading securities are carried at fair value and changes in fair value, offset by corresponding changes in the fair value of embedded derivative liabilities associated with the underlying reinsurance arrangements, are recorded in net investment income on our Consolidated Statements of Income as they occur. The fair value for our trading securities is determined in the same manner as our securities classified as available-for-sale discussed in “*Available-For-Sale Securities*” above. For discussion of how the fair value of our embedded derivatives is determined see “*Derivative Instruments*” below.

Asset-backed and Mortgage-backed Securities

For asset-backed and mortgage-backed securities, included in the trading and available-for-sale fixed maturity securities portfolios, we recognize income using a constant effective yield based on anticipated prepayments and the estimated economic life of the securities. When actual prepayments differ significantly from originally anticipated prepayments, the effective yield is recalculated prospectively to reflect actual payments to date plus anticipated future payments. Any adjustments resulting from changes in effective yield are reflected in net investment income on our Consolidated Statements of Income.

Securities Lending

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 payables for collateral under securities loaned and derivatives on our Consolidated Balance Sheets. Our pledged securities are included in fixed maturities on our Consolidated Balance Sheets. We generally obtain collateral in an amount equal to 102% and 105% of the fair value of the domestic and foreign securities, respectively. We value collateral daily and obtain additional collateral when deemed appropriate. The cash received in our securities lending program is typically invested in cash equivalents, short-term investments or fixed maturity securities. Income and expense associated with these transactions are recorded as investment income and investment expense within net investment income on our Consolidated Statements of Income.

Reverse Repurchase Agreements

Reverse repurchase agreements are treated as collateralized financing transactions, and a liability is recorded equal to the cash collateral received. This liability is included within payables for collateral under securities loaned and derivatives on our Consolidated Balance Sheets. Our pledged securities are included in fixed maturities on our Consolidated Balance Sheets. We obtain collateral in an amount equal to 95% of the fair value of the securities, and our agreements with third parties contain contractual provisions to allow for additional

collateral to be obtained when necessary. The cash received in our reverse repurchase program is typically invested in fixed maturity securities. Income and expense associated with these transactions are recorded as investment income and investment expense within net investment income on our Consolidated Statements of Income.

Mortgage Loans on Real Estate

Mortgage loans on real estate are carried at unpaid principal balances adjusted for amortization of premiums and accretion of discounts and are net of valuation allowances. Interest income is accrued on the principal balance of the loan based on the loan’s contractual interest rate. Premiums and discounts are amortized using the effective yield method over the life of the loan. Interest income and amortization of premiums and discounts are reported in net investment income on our Consolidated Statements of Income along with mortgage loan fees, which are recorded as they are incurred. Loans are considered impaired when it is probable that, based upon current information and events, we will be unable to collect all amounts due under the contractual terms of the loan agreement. When we determine that a loan is impaired, a valuation allowance is established for the excess carrying value of the loan over its estimated value. The loan’s estimated value is based on: the present value of expected future cash flows discounted at the loan’s effective interest rate, the loan’s observable market price, or the fair value of the loan’s collateral. Valuation allowances are maintained at a level we believe is adequate to absorb estimated probable credit losses. Our periodic evaluation of the adequacy of the allowance for losses is based on our 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. We do not accrue interest on impaired loans and loans 90 days past due, and any interest received on these loans is either applied to the principal or recorded in net investment income on our Consolidated Statements of Income when received, depending on the assessment of the collectibility of the loan. 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. All mortgage loans that are impaired have an established allowance for credit losses. Changes in valuation allowances are reported in realized gain (loss) on our Consolidated Statements of Income.

Policy Loans

Policy loans represent loans we issue to contract holders that use the cash surrender value of their life insurance policy as collateral. Policy loans are carried at unpaid principal balances.

Real Estate

Real estate includes both real estate held for the production of income and real estate held-for-sale. Real estate held for the production of income is carried at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset. We periodically review properties held for the production of income for impairment.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

Properties whose carrying values are greater than their projected undiscounted cash flows are written down to estimated fair value, with impairment losses reported in realized gain (loss) on our Consolidated Statements of Income. The estimated fair value of real estate 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. Real estate classified as held-for-sale is stated at the lower of depreciated cost or fair value less expected disposition costs at the time classified as held-for-sale. Real estate is not depreciated while it is classified as held-for-sale. Also, valuation allowances for losses are established, as appropriate, for real estate held-for-sale and any changes to the valuation allowances are reported in realized gain (loss) on our Consolidated Statements of Income. Real estate acquired through foreclosure proceedings is recorded at fair value at the settlement date.

Derivative Instruments

We hedge certain portions of our exposure to interest rate risk, foreign currency exchange risk, equity market risk and credit risk by entering into derivative transactions. All of our derivative instruments are recognized as either assets or liabilities on our Consolidated Balance Sheets at estimated fair value. Pursuant to SFAS No. 157, we have categorized derivatives into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in “SFAS No. 157 – Fair Value Measurements” in Note 2. The accounting for changes in the estimated 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, we must designate the hedging instrument based upon the exposure being hedged: as a cash flow hedge, a fair value hedge or a hedge of a net investment in a foreign subsidiary.

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 accumulated 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 net 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 gain or loss on the hedged item attributable to the hedged risk are recognized in net income during the period of change in estimated fair values. For derivative instruments not designated as hedging instruments but that are economic hedges, the gain or loss is recognized in net income within realized gain (loss) during the period of change.

The Company purchases and issues financial instruments and products that contain embedded derivative instruments. When it is determined that the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, and a separate instrument with the same terms would qualify as a derivative instrument, the embedded derivative is bifurcated from the host for measurement purposes. The embedded derivative, which is reported with the host instrument in the Consolidated Balance Sheets, is carried at fair value with changes in fair value reported in realized gain (loss) on our Consolidated Statements of Income. See Note 6 for additional discussion of our derivative instruments.

We employ several different methods for determining the fair value of our derivative instruments. The fair value of our derivative contracts are measured based on current settlement values, which are based on quoted market prices, industry standard models that are commercially available and broker quotes. These techniques project cash flows of the derivatives using current and implied future market conditions. We calculate the present value of the cash flows to measure the current fair value of the derivative.

We do not adjust prices received from third parties. However, we do analyze the third party pricing services’ valuation methodologies and related inputs and perform additional evaluation to determine the appropriate hierarchy levels described in Note 2 “SFAS 157 – Fair Value Measurements.”

Cash and Cash Equivalents

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

DAC, VOBA, DSI and DFEL

Commissions and other costs of acquiring UL insurance, VUL insurance, traditional life insurance, annuities and other investment contracts, which vary with and are related primarily to the production of new business, have been deferred (i.e. DAC) to the extent recoverable. VOBA is an intangible asset that reflects the estimated fair value of in-force contracts in a life insurance company acquisition and represents the portion of the purchase price that is allocated to the value of the right to receive future cash flows from the business in force at the acquisition date. Bonus credits and excess interest for dollar cost averaging contracts are considered DSI, and the unamortized balance is reported in other assets on our Consolidated Balance Sheets. Contract sales charges that are collected in the early years of an insurance contract are deferred (referred to as “DFEL”), and the unamortized balance is reported in other contract holder funds on our Consolidated Balance Sheets.

The methodology for determining the amortization of DAC, VOBA, DSI and DFEL varies by product type based on two different accounting pronouncements: SFAS No. 97, “Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments” (“SFAS 97”); and SFAS No. 60, “Accounting and Reporting by Insurance Enterprises” (“SFAS 60”). For

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

all SFAS 97 and SFAS 60 contracts, amortization is based on assumptions consistent with those used in the development of the underlying contract adjusted for emerging experience and expected trends. Both DAC and VOBA amortization is reported within underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income. DSI is expensed in interest credited on our Consolidated Statements of Income. The amortization of DFEL is reported within insurance fees on our Consolidated Statements of Income.

Under SFAS 97, acquisition costs for UL and VUL insurance and investment-type products, which include fixed and variable deferred annuities, are generally amortized over the lives of the policies in relation to the incidence of estimated gross profits ("EGPs") from surrender charges, investment, mortality net of reinsurance ceded and expense margins and actual realized gain (loss) on investments. Contract lives for UL and VUL policies are estimated to be 30 years, based on the expected lives of the contracts. Contract lives for fixed and variable deferred annuities are 14 to 20 years for the traditional, long surrender charge period products and 8 to 10 years for the more recent short-term or no surrender charge variable 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 lapse experience.

All SFAS 60 contracts, including traditional life insurance, which include individual whole life, group business 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 is currently no DAC, VOBA, DSI or DFEL balance or related amortization under SFAS 60 for fixed and variable payout annuities.

The carrying amounts of DAC, VOBA, DSI and DFEL are adjusted for the effects of realized and unrealized gains and losses on debt securities classified as available-for-sale and certain derivatives and embedded derivatives. Amortization expense of DAC, VOBA, DSI and DFEL reflects an assumption for an expected level of credit-related investment losses. When actual credit-related investment losses are realized, we recognize a true-up to our DAC, VOBA, DSI and DFEL amortization within realized gain (loss) on our Consolidated Statements of Income reflecting the incremental impact of actual versus expected credit-related investment losses. These actual to expected amortization adjustments can create volatility from period to period in realized gain (loss).

On a quarterly basis, we may record an adjustment to the amounts included on our Consolidated Balance Sheets for DAC, VOBA, DSI and DFEL with an offsetting benefit or charge to revenues or expenses for the impact of the difference between the estimates of future gross profits used in the prior quarter and the emergence of actual and updated estimates of future gross profits in the current quarter ("retrospective unlocking"). In addition, in the third quarter of each year, we conduct our annual comprehensive review of the assumptions and the projection models used for our estimates of future gross profits underlying the amortization of DAC, VOBA,

DSI and DFEL and the calculations of the embedded derivatives and reserves for annuity and life insurance products with certain guarantees. These assumptions include investment margins, mortality, retention and rider utilization. Based on our review, the cumulative balances of DAC, VOBA, DSI and DFEL are adjusted with an offsetting benefit or charge to revenues or amortization expense to reflect such change ("prospective unlocking"). The distinction between these two types of unlocking is that retrospective unlocking is driven by the emerging experience period-over-period, while prospective unlocking is driven by changes in assumptions or projection models related to estimated future gross profits.

DAC, VOBA, DSI and DFEL are reviewed periodically to ensure that the unamortized portion does not exceed the expected recoverable amounts.

Reinsurance

Our insurance companies enter into reinsurance agreements with other companies in the normal course of business. Assets and liabilities and premiums and benefits from certain reinsurance contracts that grant statutory surplus relief to other insurance companies are netted on our Consolidated Balance Sheets and Consolidated Statements of Income, respectively, because there is a right of offset explicit in the reinsurance agreements. All other reinsurance agreements are reported on a gross basis on our Consolidated Balance Sheets as an asset for amounts recoverable from reinsurers or as a component of other liabilities for amounts, such as premiums, owed to the reinsurers, with the exception of Modco agreements for which the right of offset also exists. Premiums, benefits and DAC are reported net of insurance ceded.

Goodwill

We recognize the excess of the purchase price over the fair value of net assets acquired as goodwill. Under SFAS No. 142, "Goodwill and Other Intangible Assets," ("SFAS 142") goodwill is not amortized, but is reviewed at least annually for indications of value impairment, with consideration given to financial performance and other relevant factors. In addition, certain events, including a significant adverse change in legal factors or the business climate, an adverse action or assessment by a regulator or unanticipated competition, would cause us to review the carrying amounts of goodwill for impairment. SFAS 142 requires that we perform a two-step test in our evaluation of the carrying value of goodwill for impairment. In Step 1 of the evaluation, the fair value of each reporting unit is determined and compared to the carrying value of the reporting unit. If the fair value is greater than the carrying value, then the carrying value is deemed to be sufficient and Step 2 is not required. If the fair value estimate is less than the carrying value, it is an indicator that impairment may exist and Step 2 is required to be performed. In Step 2, the implied fair value of the reporting unit's goodwill is determined by allocating the reporting unit's fair value as determined in Step 1 to all of its net assets (recognized and unrecognized) as if the reporting unit had been acquired in a business combination at the date of the impairment test. If the implied fair value of the reporting unit's goodwill is lower than its carrying amount,

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

goodwill is impaired and written down to its fair value, and a charge is reported in impairment of intangibles on our Consolidated Statements of Income.

Specifically Identifiable Intangible Assets

Specifically identifiable intangible assets, net of accumulated amortization, are reported in other assets on our Consolidated Balance Sheets. The carrying values of specifically identifiable intangible assets are reviewed periodically for indicators of impairment in value, including unexpected or adverse changes in the following: the economic or competitive environments in which the Company operates; profitability analyses; cash flow analyses; and the fair value of the relevant business operation. 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 and reported in impairment of intangibles on our Consolidated Statements of Income.

Sales force intangibles are attributable to the value of the distribution system acquired in the Insurance Solutions – Life Insurance segment. These assets are amortized on a straight-line basis over their useful life of 25 years.

Other Long-Lived Assets

Property and equipment owned for company use is included in other assets on our Consolidated Balance Sheets and 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, which include buildings, computer hardware and software and other property and equipment.

We periodically review the carrying value of our long-lived assets, including property and equipment, for impairment whenever events or circumstances indicate that the carrying amount of such assets may not be fully recoverable. For long-lived assets to be held and used, impairments are recognized when the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. An impairment loss is measured as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

Long-lived assets to be disposed of by abandonment or in an exchange for a similar productive long-lived asset are classified as held-for-use until they are disposed.

Long-lived assets to be sold are classified as held-for-sale and are no longer depreciated. Certain criteria have to be met in order for the long-lived asset to be classified as held-for-sale, including that a sale is probable and expected to occur within one year. Long-lived assets classified as held-for-sale are recorded at the lower of their carrying amount or fair value less cost to sell.

Separate Account Assets and Liabilities

We maintain separate account assets, which are reported at fair value. The related liabilities are reported at an amount equivalent to the separate account assets. Investment risks associated with market value changes are borne by the contract holders, except to the extent of minimum guarantees made by the Company with respect to certain accounts. See Note 11 for additional information regarding arrangements with contractual guarantees.

Future Contract Benefits and Other Contract Holder Funds

The liabilities for future contract benefits and claim reserves for UL and VUL insurance policies consist of contract account balances that accrue to the benefit of the contract holders, excluding surrender charges. The liabilities for future insurance contract 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 contract issue. Investment yield assumptions for traditional direct individual life reserves for all contracts range from 2.25% to 7.00% depending on the time of contract issue. The investment yield assumptions for immediate and deferred paid-up annuities range from 1.00% to 13.50%. These investment yield assumptions are intended to represent an estimation of the interest rate experience for the period that these contract benefits are payable.

The liabilities for future claim reserves for variable annuity products containing guaranteed death benefit (“GDB”) features are calculated by estimating the present value of total expected benefit payments over the life of the contract divided by the present value of total expected assessments over the life of the contract (“benefit ratio”) multiplied by the cumulative assessments recorded from the contract inception through the balance sheet date less the cumulative GDB payments plus interest. The change in the reserve for a period is the benefit ratio multiplied by the assessments recorded for the period less GDB claims paid in the period plus interest. If experience or assumption changes result in a new benefit ratio, the reserves are adjusted to reflect the changes in a manner similar to the unlocking of DAC, VOBA, DFEL and DSI.

With respect to our future contract benefits and other contract holder funds, we continually review: overall reserve position, reserving techniques and 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.

The business written or assumed by us includes participating life insurance contracts, under which the contract holder is entitled to share in the earnings of such contracts via receipt of dividends. The dividend scale for participating policies is reviewed annually and may be adjusted to reflect recent experience and future expectations.

UL and VUL products with secondary guarantees represented approximately 35% of permanent life insurance in force as of

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

December 31, 2008, and approximately 71% of sales for these products in 2008. Liabilities for the secondary guarantees on UL-type products are calculated by multiplying the benefit ratio by the cumulative assessments recorded from contract inception through the balance sheet date less the cumulative secondary guarantee benefit payments plus interest. If experience or assumption changes result in a new benefit ratio, the reserves are adjusted to reflect the changes in a manner similar to the unlocking of DAC, VOBA, DFEL and DSI. The accounting for secondary guarantee benefits impacts, and is impacted by, EGPs used to calculate amortization of DAC, VOBA, DFEL and DSI.

Future contract benefits on our Consolidated Balance Sheets include GLB features and remaining guaranteed interest and similar contracts that are carried at fair value. The fair values for the GLB contracts are based on their approximate surrender values. Our *Lincoln SmartSecurity*[®] Advantage guaranteed withdrawal benefit (“GWB”) feature, GIB and 4LATER[®] features have elements of both insurance benefits accounted for under Statement of Position (“SOP”) 03-1, “Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts” (“SOP 03-1”) and embedded derivatives accounted for under SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities” (“SFAS 133”) and SFAS 157. We weight these features and their associated reserves accordingly based on their hybrid nature. 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. We classify these items in level 3 within the hierarchy levels described in “SFAS No. 157 – Fair Value Measurements” in Note 2.

Borrowed Funds

LNL’s short-term borrowings are defined as borrowings with contractual or expected maturities of one year or less. Long-term borrowings have contractual or expected maturities greater than one year.

Deferred Gain on Business Sold Through Reinsurance

Our reinsurance operations were acquired by Swiss Re Life & Health America, Inc. (“Swiss Re”) in December 2001 through a series of indemnity reinsurance transactions. We are recognizing the gain related to these transactions at the rate that earnings on the reinsured business are expected to emerge, over a period of 15 years, in accordance with the requirements of SFAS No. 113, “Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts” (“SFAS 113”). In addition, for the deferred loss on the reinsurance ceded to LNBAR we are recognizing it over 30 years.

Commitments and Contingencies

Contingencies arising from environmental remediation costs, regulatory judgments, claims, assessments, guarantees, litigation, recourse reserves, fines, penalties and other sources are recorded when deemed probable and reasonably estimable.

Insurance Fees

Insurance fees for investment and interest-sensitive life insurance contracts consist of asset-based fees, cost of insurance charges, percent of premium charges, contract administration charges and surrender charges that are assessed against contract holder account balances. Investment products consist primarily of individual and group variable and fixed deferred annuities. Interest-sensitive life insurance products include UL insurance, VUL insurance and other interest-sensitive life insurance policies. These products include life insurance sold to individuals, corporate-owned life insurance and bank-owned life insurance.

In bifurcating the embedded derivative of our GLB features on our variable annuity products, we attribute to the embedded derivative the portion of total fees collected from the contract holder that relate to the GLB riders (the “attributed fees”), which are not reported within insurance fees on our Consolidated Statements of Income. These attributed fees represent the present value of future claims expected to be paid for the GLB at the inception of the contract plus a margin that a theoretical market participant would include for risk/profit and are reported within realized gain (loss) on our Consolidated Statements of Income.

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 contract 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 by the contract holder in accordance with contractual terms.

For investment and interest-sensitive life insurance contracts, the amounts collected from contract holders are considered deposits and are not included in revenue.

Insurance Premiums

Our insurance premiums for traditional life insurance and group insurance products are recognized as revenue when due from the contract holder. Our 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. Our group non-medical insurance products consist primarily of term life, disability and dental.

Realized Gain (Loss)

Realized gain (loss) on our Consolidated Statements of Income includes realized gains and losses from the sale of investments, write-downs for other-than-temporary impairments of investments, derivative and embedded derivative gains and losses, gains and losses on the sale of subsidiaries and businesses and

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

1. Nature of Operations, Basis of Presentation and Summary of Significant Accounting Policies (continued)

net gains and losses on reinsurance embedded derivative and trading securities on Modco and CFW reinsurance arrangements. Realized gain (loss) is recognized in net income, net of associated amortization of DAC, VOBA, DSI and DFEL. Realized gain (loss) is also net of allocations of investment gains and losses to certain contract holders and certain funds withheld on reinsurance arrangements for which we have a contractual obligation.

Other Revenues and Fees

Other revenues and fees primarily consist of amounts earned by our retail distributor, LFA, from sales of third party insurance and investment products. Such revenue is recorded as earned at the time of sale.

Interest Credited

Interest credited includes interest credited to contract holder account balances. Interest crediting rates associated with funds invested in our general account during 2006 through 2008 ranged from 3.00% to 9.00%.

Benefits

Benefits for UL and other interest-sensitive life insurance products include benefit claims incurred during the period in excess of contract account balances. Benefits also include the change in reserves for life insurance products with secondary guarantee benefits and annuity products with guaranteed death benefits. For traditional life, group health and disability income products, benefits are recognized when incurred in a manner consistent with the related premium recognition policies.

Pension and Other Postretirement Benefit Plans

Pursuant to the accounting rules for our obligations to employees under our various pension and other postretirement benefit plans, we are required to make a number of assumptions to estimate related liabilities and expenses. We use assumptions for the weighted-average discount rate and expected return on plan assets to estimate pension expense. The discount rate assumptions are determined using an analysis of current market information and the projected benefit flows associated with these plans. The expected long-term rate of return on plan assets is initially established at the beginning of the plan year based on historical and projected future rates of return and is the average rate of earnings expected on the funds invested or to be invested in the plan. The calculation of

our accumulated postretirement benefit obligation also uses an assumption of weighted-average annual rate of increase in the per capita cost of covered benefits, which reflects a health care cost trend rate. See Note 18 for additional information.

Stock-Based Compensation

In general, we expense the fair value of stock awards included in our incentive compensation plans. As of the date LNC's Board of Directors approves stock awards, the fair value of stock options is determined using a Black-Scholes options valuation methodology, and the fair value of other stock awards is based upon the market value of the stock. The fair value of the awards is expensed over the service period, which generally corresponds to the vesting period, and is recognized as an increase to common stock in stockholder's equity. We classify certain stock awards as liabilities. For these awards, the settlement value is classified as a liability on our Consolidated Balance Sheets and the liability is marked-to-market through net income at the end of each reporting period. Stock-based compensation expense is reflected in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income. See Note 20 for additional information.

Interest and Debt Expenses

Interest expense on our short-term and long-term debt is recognized as due and any associated premiums, discounts, costs or hedges are amortized (accreted) over the term of the related borrowing utilizing the effective interest method.

Income Taxes

We have elected to file consolidated federal income tax returns with LNC and its subsidiaries. Pursuant to an intercompany tax sharing agreement with LNC, we provide for income taxes on a separate return filing basis. The tax sharing agreement also provides that we will receive benefit for net operating losses, capital losses and tax credits which are not usable on a separate return basis to the extent such items may be utilized in the consolidated income tax returns of LNC. Deferred income taxes are recognized, based on enacted rates, when assets and liabilities have different values for financial statement and tax reporting purposes. A valuation allowance is recorded to the extent required to reduce the deferred tax asset to an amount that we expect, more likely than not, will be realized. See Note 7 for additional information.

2. New Accounting Standards

Adoption of New Accounting Standards

SOP 05-1 — Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts

In September 2005, the American Institute of Certified Public Accountants issued SOP 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" ("SOP 05-1"), which provides guidance on accounting for DAC on internal replacements of insurance and investment

contracts other than those specifically described in SFAS 97. An internal replacement, defined by SOP 05-1, is a modification in product benefits, features, rights or coverages that occurs by the exchange of a contract for a new contract, or by amendment, endorsement or rider to a contract, or by the election of a feature or coverage within a contract. Contract modifications that result in a substantially unchanged contract are accounted for as a continuation of the replaced contract. Contract modifications that result in a substantially changed contract are accounted for as an extinguishment of the

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

replaced contract. Unamortized DAC, VOBA, DFEL and DSI from the replaced contract must be written off. SOP 05-1 is effective for internal replacements occurring in fiscal years beginning after December 15, 2006. We adopted SOP 05-1 effective January 1, 2007, by recording decreases to total assets of \$69 million, total liabilities of \$28 million and retained earnings of \$41 million on our Consolidated Balance Sheets. In addition, the adoption of SOP 05-1 resulted in an approximately \$17 million increase to underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income for the year ended December 31, 2007, which was attributable to changes in DAC and VOBA deferrals and amortization.

FASB Staff Position FAS 115-1 and FAS 124-1 — The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments

In November 2005, the FASB issued FASB Staff Position (“FSP”) Nos. SFAS 115-1 and SFAS 124-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments” (“FSP 115-1”). The guidance in FSP 115-1 nullified the accounting and measurement provisions of Emerging Issues Task Force (“EITF”) No. 03-1 – “The Meaning of Other-Than-Temporary Impairments and Its Application to Certain Investments” and superseded EITF Topic No. D-44 “Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value.” Under the impairment model in FSP 115-1, any security in an unrealized loss position is considered impaired. An evaluation is made to determine whether the impairment is other-than-temporary based on existing accounting guidance. If an impairment is considered other-than-temporary, a realized loss is recognized to write the security’s cost or amortized cost basis down to fair value. The fair value of the security on the measurement date of the other-than-temporary impairment becomes the new cost basis for the security, which may not be adjusted for subsequent recoveries in fair value. Subsequent to the recognition of an interest-related other-than-temporary impairment for debt securities, the resulting discount, or reduction to the premium, is amortized over the remaining life of the debt security, prospectively, based on the amount and timing of the estimated future cash flows of the debt security. We adopted FSP 115-1 effective January 1, 2006. The adoption of FSP 115-1 did not have a material effect on our consolidated financial condition or results of operations.

SFAS No. 155 — Accounting for Certain Hybrid Financial Instruments — an amendment of FASB Statements No. 133 and 140

In February 2006, the FASB issued SFAS No. 155, “Accounting for Certain Hybrid Financial Instruments – an amendment of FASB Statements No. 133 and 140” (“SFAS 155”), which permits fair value remeasurement for a hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. Under SFAS 155, an entity may make an irrevocable election to measure a hybrid financial instrument at fair value, in its entirety, with changes in fair value recognized in earnings. SFAS 155 also eliminates the interim guidance in SFAS 133 Implementation Issue No. D1,

“Application of Statement 133 to Beneficial Interests in Securitized Financial Assets,” and establishes a requirement to evaluate beneficial interests in securitized financial assets to identify interests that are either freestanding derivatives or hybrid financial instruments that contain an embedded derivative requiring bifurcation.

In December 2006, the FASB issued Derivative Implementation Group (“DIG”) Statement 133 Implementation Issue No. B40, “Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets” (“DIG B40”). Because SFAS 155 eliminated the interim guidance related to securitized financial assets, DIG B40 provided a narrow scope exception for securitized interests that contain only an embedded derivative related to prepayment risk. Any other terms in the securitized financial asset that may affect cash flow in a manner similar to a derivative instrument would be subject to the requirements of paragraph 13(b) of SFAS 133.

We adopted the provisions of SFAS 155 and DIG B40 on January 1, 2007. Prior period restatement was not permitted. The adoption of SFAS 155 and DIG B40 did not have a material impact on our consolidated financial condition or results of operations.

FASB Interpretation No. 48 — Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109

In June 2006, the FASB issued FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109” (“FIN 48”). FIN 48 prescribes a comprehensive model for how companies should recognize, measure, present and disclose in their financial statements uncertain tax positions taken or expected to be taken on a tax return. FIN 48 requires companies to determine whether it is “more likely than not” that an individual tax position will be sustained upon examination by the appropriate taxing authority prior to any part of the benefit being recognized in the financial statements. Such tax positions shall initially and subsequently be measured as the largest amount of tax benefit that is greater than fifty percent likely of being realized upon settlement with the tax authority, assuming full knowledge of the position and all relevant facts. In addition, FIN 48 expands disclosure requirements to include additional information related to unrecognized tax benefits, including accrued interest and penalties, and uncertain tax positions where the estimate of the tax benefit may change significantly in the next twelve months. FIN 48 is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 effective January 1, 2007 by recording an increase in the liability for unrecognized tax benefits of \$14 million on our Consolidated Balance Sheets, offset by a reduction to the beginning balance of retained earnings. See Note 7 for more information regarding our adoption of FIN 48.

SFAS 157 — Fair Value Measurements

In September 2006, the FASB issued SFAS 157, “Fair Value Measurements,” which defines fair value, establishes a framework for measuring fair value under current accounting pronouncements that require or permit fair value measurement

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

and enhances disclosures about fair value instruments. SFAS 157 retains the exchange price notion, but clarifies that exchange price is the price in an orderly transaction between market participants to sell the asset or transfer the liability (exit price) in the principal market, or the most advantageous market in the absence of a principal market, for that asset or liability, as opposed to the price that would be paid to acquire the asset or receive a liability (entry price). Fair value measurement is based on assumptions used by market participants in pricing the asset or liability, which may include inherent risk, restrictions on the sale or use of an asset or non-performance risk, which would include the reporting entity's own credit risk. SFAS 157 establishes a three-level fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value. The three-level hierarchy for fair value measurement is defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices available in active markets for identical investments as of the reporting date. "Blockage discounts" for large holdings of unrestricted financial instruments where quoted prices are readily and regularly available for an identical asset or liability in an active market are prohibited;
- Level 2 – inputs to the valuation methodology are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value can be determined through the use of models or other valuation methodologies; and
- Level 3 – inputs to the valuation methodology are unobservable inputs in situations where there is little or no market activity for the asset or liability and the reporting entity makes estimates and assumptions related to the pricing of the asset or liability, including assumptions regarding risk.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the investment.

We have certain guaranteed benefit features within our annuity products that, prior to January 1, 2008, were recorded using fair value pricing. These benefits will continue to be measured on a fair value basis with the adoption of SFAS 157, utilizing Level 3 inputs and some Level 2 inputs, which are reflective of the hypothetical market participant perspective for fair value measurement, including liquidity assumptions and assumptions regarding the Company's own credit or non-performance risk. In addition, SFAS 157 expands the disclosure requirements for annual and interim reporting to focus on the inputs used to measure fair value, including those measurements using significant unobservable inputs and the effects of the measurements on earnings. See Note 22 for additional information about our fair value disclosures for financial instruments required by SFAS 157.

We adopted SFAS 157 effective January 1, 2008, by recording increases (decreases) to the following categories (in millions) on our consolidated financial statements:

Assets

DAC	\$ (3)
VOBA	(8)
Other assets — DSI	(1)
Total assets	<u><u>\$(12)</u></u>

Liabilities

Future contract benefits:	
Remaining guaranteed interest and similar contracts	\$ (20)
Other liabilities — income tax liabilities	3
Total liabilities	<u><u>\$(17)</u></u>

Revenues

Realized gain	\$ 10
Federal income tax	3
Increase to net income	<u><u>\$ 7</u></u>

See "Summary of Significant Accounting Policies" in Note 1 for discussion of the methodologies and assumptions used to determine the fair value of our financial instruments carried at fair value.

FSP No. FAS 157-2 — Effective Date of FASB Statement No. 157

In February 2008, the FASB issued FSP No. FAS 157-2, "Effective Date of FASB Statement No. 157" ("FSP 157-2"). FSP 157-2 delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Accordingly, we did not apply the provisions of SFAS 157 to nonfinancial assets and nonfinancial liabilities within the scope of FSP 157-2. Examples of items to which the deferral is applicable include, but are not limited to:

- Nonfinancial assets and nonfinancial liabilities initially measured at fair value in a business combination or other new basis event, but not measured at fair value in subsequent periods;
- Reporting units measured at fair value in the goodwill impairment test under SFAS 142, and indefinite-lived intangible assets measured at fair value for impairment assessment under SFAS 142;
- Nonfinancial long-lived assets measured at fair value for an impairment assessment under SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets";
- Asset retirement obligations initially measured at fair value under SFAS No. 143, "Accounting for Asset Retirement Obligations"; and
- Nonfinancial liabilities for exit or disposal activities initially measured at fair value under SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities."

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

As of January 1, 2009, the deferral from FSP 157-2 will no longer be effective. We will apply the provisions of SFAS 157 to nonfinancial assets and nonfinancial liabilities beginning on January 1, 2009, and we do not expect the application to have a material impact on our consolidated financial condition or results of operations.

FSP No. FAS 157-3 — Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active

In October 2008, the FASB issued FSP FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active" ("FSP 157-3"). FSP 157-3 clarifies the application of SFAS 157 in a market that is not active and provides an illustrative example of key considerations to analyze in determining fair value of a financial asset when the market for the asset is not active. During times when there is little market activity for a financial asset, the objective of fair value measurement remains the same, that is, to value the asset at the price that would be received by the holder of the financial asset in an orderly transaction (exit price) that is not a forced liquidation or distressed sale at the measurement date. Determining fair value of a financial asset during a period of market inactivity may require the use of significant judgment and an evaluation of the facts and circumstances to determine if transactions for a financial asset represent a forced liquidation or distressed sale. An entity's own assumptions regarding future cash flows and risk-adjusted discount rates for financial assets are acceptable when relevant observable inputs are not available. FSP 157-3 was effective on October 10, 2008, and for all prior periods for which financial statements have not been issued. Any changes in valuation techniques resulting from the adoption of FSP 157-3 shall be accounted for as a change in accounting estimated in accordance with SFAS No. 154, "Accounting Changes and Error Corrections." We adopted the guidance in FSP 157-3 in our financial statements for the reporting period ending September 30, 2008. The adoption did not have a material impact on our consolidated financial condition or results of operations.

SFAS No. 159 — The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"), which allows an entity to make an irrevocable election, on specific election dates, to measure eligible items at fair value. The election to measure an item at fair value may be determined on an instrument by instrument basis, with certain exceptions. If the fair value option is elected, unrealized gains and losses will be recognized in earnings at each subsequent reporting date, and any upfront costs and fees related to the item will be recognized in earnings as incurred. In addition, the presentation and disclosure requirements of SFAS 159 are designed to assist in the comparison between entities that select different measurement attributes for similar types of assets and liabilities. SFAS 159 applies to fiscal years beginning after November 15, 2007, with early adoption permitted for an entity that has also elected to apply the provisions of SFAS 157. At the effective date, the fair value option

may be elected for eligible items that exist on that date. Effective January 1, 2008, we elected not to adopt the fair value option for any financial assets or liabilities that existed as of that date.

Derivative Implementation Group Statement 133 Implementation Issue No. E23 — Issues Involving the Application of the Shortcut Method Under Paragraph 68

In December 2007, the FASB issued Derivative Implementation Group ("DIG") Statement 133 Implementation Issue No. E23, "Issues Involving the Application of the Shortcut Method under Paragraph 68" ("DIG E23"), which gives clarification to the application of the shortcut method of accounting for qualifying fair value hedging relationships involving an interest-bearing financial instrument and/or an interest rate swap, originally outlined in paragraph 68 in SFAS 133. We adopted DIG E23 effective January 1, 2008, for hedging relationships designated on or after that date. The adoption did not have a material impact on our consolidated financial condition or results of operations.

FSP FAS No. 133-1 and FIN 45-4 — Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161

In September 2008, the FASB issued FSP FAS No. 133-1 and FIN 45-4, "Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161" ("FSP 133-1"). FSP 133-1 amends the disclosure requirements of SFAS 133 to require the seller of credit derivatives, including hybrid financial instruments with embedded credit derivatives, to disclose additional information regarding, among other things, the nature of the credit derivative, information regarding the facts and circumstances that may require performance or payment under the credit derivative, and the nature of any recourse provisions the seller can use for recovery of payments made under the credit derivative. In addition, FSP 133-1 amends the disclosure requirements in FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45") to require additional disclosure about the payment/performance risk of a guarantee. Finally, FSP 133-1 clarifies the intent of the FASB regarding the effective date of SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities — an amendment of FASB Statement No. 133" ("SFAS 161"). The provisions of FSP 133-1 related to SFAS 133 and FIN 45 are effective for annual and interim reporting periods ending after November 15, 2008, with comparative disclosures required only for those periods ending subsequent to initial adoption. The clarification of the effective date of SFAS 161 was effective upon the issuance of FSP 133-1, and will not impact the effective date of SFAS 161 in our financial statements. We have included these required enhanced disclosures related to credit derivatives, hybrid financial instruments and guarantees in the notes to the consolidated financial statements beginning in the reporting period ended December 31, 2008.

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

FSP FAS 140-4 and FIN 46(R)-8 — Enhanced Disclosure Requirements Related to Transfers of Financial Assets and Variable Interest Entities.

In December 2008, the FASB issued FSP FAS 140-4 and FIN 46(R)-8, "Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities" ("FSP 140-4"). FSP 140-4 amends FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" ("SFAS 140") to require additional disclosures regarding a transferor's continuing involvement with transferred financial assets in a securitization or asset-backed financing arrangement. FSP 140-4 also amends FIN 46 (revised December 2003) "Consolidation of Variable Interest Entities," to expand the disclosure requirements for VIEs to include information regarding the decision to consolidate the VIE, the nature of and changes in risks related to a VIE, and the impact on the entity's financial statements due to the involvement with a VIE. Those variable interests required to comply with the guidance in FSP 140-4 include the primary beneficiary of the VIE, the holder of a significant variable interest and a sponsor that holds a variable interest. Further, FSP 140-4 requires enhanced disclosures for certain sponsors and holders of a significant variable interest in a qualifying special purpose entity. The provisions of FSP 140-4 are effective for the first reporting period ending after December 15, 2008, and comparative disclosures are not required. We included the enhanced disclosures required by FSP 140-4 in the notes to the consolidated financial statements beginning in the reporting period ended December 31, 2008.

See Note 4 for more information regarding our involvement with VIEs.

FSP EITF 99-20-1 — Amendments to the Impairment Guidance in EITF Issue No. 99-20

In January 2009, the FASB issued FSP EITF 99-20-1, "Amendments to the Impairment Guidance in EITF Issue No. 99-20" ("EITF 99-20-1"), which eliminates the requirement in EITF No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets" ("EITF 99-20") for holders of beneficial interests to estimate cash flow using current information and events that a market participant would use in determining the current fair value and other-than-temporary impairment of the beneficial interest. FSP 99-20-1 removes the reference to a market participant and requires that an other-than-temporary impairment be recognized in earnings when it is probable that there has been an adverse change in the holder's estimated cash flows from the cash flows previously projected, which is consistent with the impairment model used in SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." FSP 99-20-1 is effective for interim and annual reporting periods ending after December 15, 2008, and must be applied prospectively at the balance sheet date of the reporting period for which the assessment of cash flows is made. We adopted the guidance in FSP 99-20-1 as of December 31, 2008. The adoption did not have a material impact on our consolidated financial condition or results of operations.

Future Adoption of New Accounting Standards

SFAS No. 141(R) — Business Combinations

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS 141(R)"), which is a revision of SFAS No. 141 "Business Combinations" ("SFAS 141"). SFAS 141(R) retains the fundamental requirements of SFAS 141, but establishes principles and requirements for the acquirer in a business combination to recognize and measure the identifiable assets acquired, liabilities assumed and any noncontrolling interests in the acquiree and the goodwill acquired or the gain from a bargain purchase. The revised statement requires, among other things, that assets acquired, liabilities assumed and any noncontrolling interest in the acquiree shall be measured at their acquisition-date fair values. For business combinations completed upon adoption of SFAS 141(R), goodwill will be measured as the excess of the consideration transferred, plus the fair value of any noncontrolling interest in the acquiree, in excess of the fair values of the identifiable net assets acquired. Any contingent consideration shall be recognized at the acquisition-date fair value, which improves the accuracy of the goodwill measurement. Under SFAS 141(R), contractual pre-acquisition contingencies will be recognized at their acquisition-date fair values and non-contractual pre-acquisition contingencies will be recognized at their acquisition date fair values if it is more likely than not that the contingency gives rise to an asset or liability. Deferred recognition of pre-acquisition contingencies will no longer be permitted. Acquisition costs will be expensed in the period the costs are incurred, rather than included in the cost of the acquiree, and disclosure requirements will be enhanced to provide users with information to evaluate the nature and financial effects of the business combination. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period on or after December 15, 2008, with earlier adoption prohibited. We will adopt SFAS 141(R) for acquisitions occurring after January 1, 2009.

SFAS No. 160 — Noncontrolling Interests in Consolidated Financial Statements — an Amendment of Accounting Research Bulletin No. 51

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin ("ARB") No. 51" ("SFAS 160"), which aims to improve the relevance, comparability and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards surrounding noncontrolling interests, or minority interests, which are the portions of equity in a subsidiary not attributable, directly or indirectly, to a parent. The ownership interests in subsidiaries held by parties other than the parent shall be clearly identified, labeled and presented in the consolidated statement of financial position within equity, but separate from the parent's equity. The amount of consolidated net income attributable to the parent and to the noncontrolling interest must be clearly identified and presented on the face of the Consolidated Statements of Income. Changes in a parent's ownership

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

interest while the parent retains its controlling financial interest in its subsidiary must be accounted for consistently as equity transactions. A parent's ownership interest in a subsidiary changes if the parent purchases additional ownership interests in its subsidiary, sells some of its ownership interests in its subsidiary, the subsidiary reacquires some of its ownership interests or the subsidiary issues additional ownership interests. When a subsidiary is deconsolidated, any retained noncontrolling equity investment in the former subsidiary must be initially measured at fair value. The gain or loss on the deconsolidation of the subsidiary is measured using the fair value of any noncontrolling equity investment rather than the carrying amount of that retained investment. Entities must provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. We will adopt SFAS 160 effective January 1, 2009, and do not expect the adoption will have a material impact on our consolidated financial condition and results of operations.

FSP FAS No. 140-3 — Accounting for Transfers of Financial Assets and Repurchase Financing Transactions

In February 2008, the FASB issued FSP FAS No. 140-3, "Accounting for Transfers of Financial Assets and Repurchase Financing Transactions" ("FSP 140-3"), regarding the criteria for a repurchase financing to be considered a linked transaction under SFAS 140. A repurchase financing is a transaction where the buyer ("transferee") of a financial asset obtains financing from the seller ("transferor") and transfers the financial asset back to the seller as collateral until the financing is repaid. Under FSP 140-3, the transferor and the transferee shall not separately account for the transfer of a financial asset and a related repurchase financing unless the two transactions have a valid and distinct business or economic purpose for being entered into separately and the repurchase financing does not result in the initial transferor regaining control over the financial asset. In addition, an initial transfer of a financial asset and a repurchase financing entered into contemporaneously with, or in contemplation of, one another, must meet the criteria identified in FSP 140-3 in order to receive separate accounting treatment. FSP 140-3 is effective for financial statements issued for fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. FSP 140-3 will be applied prospectively to initial transfers and repurchase financings executed on or after the beginning of the fiscal year in which FSP 140-3 is initially applied. Early application is not permitted. We will adopt FSP 140-3 effective January 1, 2009, and do not expect the adoption will have a material impact on our consolidated financial condition and results of operations.

SFAS 161 — Disclosures about Derivative Instruments and Hedging Activities — an Amendment of FASB Statement No. 133

In March 2008, the FASB issued SFAS 161, which amends and expands current qualitative and quantitative disclosure requirements for derivative instruments and hedging activities.

Enhanced disclosures will include: how and why we use derivative instruments; how derivative instruments and related hedged items are accounted for under SFAS 133; and how derivative instruments and related hedged items affect our financial position, financial performance and cash flows. Quantitative disclosures will be enhanced by requiring a tabular format by primary underlying risk and accounting designation for the fair value amount and location of derivative instruments in the financial statements and the amount and location of gains and losses in the financial statements for derivative instruments and related hedged items. The tabular disclosures should improve transparency of derivative positions existing at the end of the reporting period and the effect of using derivatives during the reporting period. SFAS 161 also requires the disclosure of credit-risk-related contingent features in derivative instruments and cross-referencing within the notes to the consolidated financial statements to assist users in locating information about derivative instruments. The amended and expanded disclosure requirements apply to all derivative instruments within the scope of SFAS 133, non-derivative hedging instruments and all hedged items designated and qualifying as hedges under SFAS 133. SFAS 161 is effective prospectively for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We will adopt SFAS 161 effective January 1, 2009, at which time we will include these required enhanced disclosures related to derivative instruments and hedging activities in our financial statements.

FSP FAS No. 142-3 — Determination of the Useful Life of Intangible Assets

In April 2008, the FASB issued FSP FAS No. 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP 142-3"), which applies to recognized intangible assets accounted for under the guidance in SFAS 142. When developing renewal or extension assumptions in determining the useful life of recognized intangible assets, FSP 142-3 requires an entity to consider its own historical experience in renewing or extending similar arrangements. Absent the historical experience, an entity should use the assumptions a market participant would make when renewing and extending the intangible asset consistent with the highest and best use of the asset by market participants. In addition, FSP 142-3 requires financial statement disclosure regarding the extent to which expected future cash flows associated with the asset are affected by an entity's intent and/or ability to renew or extend an arrangement. FSP 142-3 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2008, with early adoption prohibited. FSP 142-3 should be applied prospectively to determine the useful life of a recognized intangible asset acquired after the effective date. In addition, FSP 142-3 requires prospective application of the disclosure requirements to all intangible assets recognized as of, and subsequent to, the effective date. We will adopt FSP 142-3 on January 1, 2009, and do not expect the adoption will have a material impact on our consolidated financial condition and results of operations.

Notes to Consolidated Financial Statements (continued)

2. New Accounting Standards (continued)

SFAS No. 163 — Accounting for Financial Guarantee Insurance Contracts — an Interpretation of FASB Statement No. 60

In May 2008, the FASB issued SFAS No. 163, "Accounting for Financial Guarantee Insurance Contracts — an interpretation of FASB Statement No. 60" ("SFAS 163"), which applies to financial guarantee insurance and reinsurance contracts not accounted for as derivative instruments, and issued by entities within the scope of SFAS No. 60, "Accounting and Reporting by Insurance Enterprises." SFAS 163 changes current accounting practice related to the recognition and measurement of premium revenue and claim liabilities such that premium revenue recognition is linked to the amount of insurance protection and the period in which it is provided, and a claim liability is recognized when it is expected that a claim loss will exceed the unearned premium revenue. In addition, SFAS 163 expands disclosure requirements to include information related to the premium revenue and claim liabilities, as well as information related to the risk-management activities used to evaluate credit deterioration in insured financial obligations. SFAS 163 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years; early application is not permitted. However, the disclosure requirements related to risk-management activities are effective in the first period (including interim periods) beginning after May 2008. Because we do not hold a significant amount of financial guarantee insurance and reinsurance contracts, no additional disclosures have been made, and we expect the adoption of SFAS 163 will not be material to our consolidated financial condition or results of operations.

EITF No. 07-5 — Determining Whether an Instrument (or Embedded Feature) is Indexed to an Entity's Own Stock

In June 2008, the FASB issued EITF No. 07-5, "Determining Whether an Instrument (or Embedded Feature) is Indexed to an Entity's Own Stock" ("EITF 07-5"). EITF 07-5 provides guidance to determine whether an instrument (or an embedded feature) is indexed to an entity's own stock when evaluating the instrument as a derivative under SFAS 133. An instrument that is both indexed to an entity's own stock and classified in stockholder's equity in the entity's statement of financial position is not considered a derivative for the purposes of applying the guidance in SFAS 133. EITF 07-5 provides a two-step process to determine whether an equity-linked instrument (or embedded feature) is indexed to its own stock first by evaluating the instrument's contingent exercise provisions, if any, and second, by evaluating the instrument's settlement provisions. EITF 07-5 is applicable to outstanding instruments as of the beginning of the fiscal year in which the issue is adopted and is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. We will adopt EITF 07-5 on January 1, 2009, and do not expect the adoption will be material to our consolidated financial condition and results of operations.

EITF No. 08-6 — Investment Accounting Considerations

In November 2008, the FASB issued EITF No. 08-6, "Equity Method Investment Accounting Considerations" ("EITF 08-6"), which addresses the effect of SFAS 141(R) and SFAS 160 on equity-method accounting under Accounting Principles Board Opinion 18, "The Equity Method of Accounting for Investments in Common Stock" ("APB 18"). EITF 08-6 will continue the APB 18 requirement that the cost basis of a new equity-method investment will follow a cost accumulation model, which includes transaction costs in the cost of the equity investment and excludes the value of contingent consideration unless it is required to be recognized under other literature. Subsequently, issuances of shares by the equity-method investee that reduce the investor's ownership percentage should be accounted for as if the investor sold a proportionate share of the investment, with gain or loss recognized through earnings. The EITF decided that the investor would not have to complete a separate impairment analysis on the investee's underlying assets, but rather the entire equity-method investment would continue to be subject to the current other-than-temporary impairment guidance in APB 18. EITF 08-6 is applicable to all investments accounted for under the equity method and is effective, prospectively, in fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. We will adopt EITF 08-6 on January 1, 2009, and do not expect the adoption will have a material impact on our financial condition and results of operations.

FSP FAS No. 132(R)-1 — Employers' Disclosures about Postretirement Benefit Plan Assets

In December 2008, the FASB issued FSP FAS No. 132(R)-1, "Employers' Disclosures about Postretirement Benefit Plan Assets" ("FSP 132(R)-1"), which requires enhanced disclosures of the plan assets of an employer's defined benefit pension or other postretirement benefit plans. The disclosures required under FSP 132(R)-1 will include information regarding the investment allocation decisions made for plan assets, the fair value of each major category of plan assets disclosed separately for pension plans and other postretirement benefit plans and the inputs and valuation techniques used to measure the fair value of plan assets including the level within the fair value hierarchy as defined by SFAS 157. FSP 132(R)-1 requires the additional disclosure in SFAS 157 for Level 3 fair value measurements, must also be provided for the fair value measurements of plan assets using Level 3 inputs. The disclosures in FSP 132(R)-1 are effective for fiscal years ending after December 15, 2009, and are not required for earlier periods that are presented for comparative purposes. We will include the disclosures required in FSP 132(R)-1 in the notes to our consolidated financial statements for the year ending December 31, 2009.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

3. Acquisition, Dividend of FPP and Reinsurance Ceded to LNBAR

Jefferson-Pilot Acquisition

On April 3, 2006, LNC completed its merger with Jefferson-Pilot Corporation ("Jefferson-Pilot") by acquiring 100% of the outstanding shares of Jefferson-Pilot in a transaction accounted for under the purchase method of accounting prescribed by SFAS 141. At that time, JPL, JPLA and JPFIC became wholly-owned by LNC.

Dividend of FPP

On May 3, 2007, LNL made a dividend to LNC that transferred ownership of our formerly wholly-owned subsidiary, FPP, to LNC. The following table summarizes the dividend of FPP to LNC (in millions):

	<u>Dividended Value</u>
Investments	\$ 1,809
Cash and invested cash	20
Deferred acquisition costs and value of business acquired	246
Premiums and fees receivable	2
Accrued investment income	24
Reinsurance recoverables	669
Goodwill	2
Future contract benefits	(705)
Other contract holder funds	(1,509)
Other liabilities	(66)
Total dividend of FPP	<u>\$ 492</u>

The caption dividends declared, in the accompanying Consolidated Statements of Stockholder's Equity, includes the \$492 million dividend of FPP presented above.

Reinsurance Ceded to LNBAR

We completed a reinsurance transaction during the fourth quarter of 2008 whereby we ceded a block of business to Lincoln National Reinsurance Company (Barbados) Limited ("LNBAR"), a wholly-owned subsidiary of LNC, which resulted in the release of approximately \$240 million of capital previously supporting a portion of statutory reserves related to our insurance products with secondary guarantees. The following summarizes the impact (in millions) on the Consolidated Balance Sheets for the ceding of this block of business to LNBAR:

Assets

Deferred acquisition costs and value of business acquired	\$(230)
Other assets	(130)
Total assets	<u>\$(360)</u>

Liabilities

Future contract benefits	\$(539)
Other contract holder funds	(47)
Funds withheld reinsurance liabilities	434
Deferred loss on business sold through reinsurance . .	(78)
Other liabilities	(130)
Total liabilities	<u>\$(360)</u>

4. Variable Interest Entities

Our involvement with VIEs is primarily to invest in assets that allow us to gain exposure to a broadly diversified portfolio of asset classes. We have carefully analyzed each VIE to determine whether we are the primary beneficiary. Based on our analysis of the expected losses and residual returns of the VIEs in which we have a variable interest, we have concluded that there are no VIEs for which we are the primary beneficiary, and, as such, we have not consolidated the VIEs in our consolidated financial statements. However, for those VIEs in which we are not the primary beneficiary, but hold a variable interest, we recognize the fair value of our variable interest in our consolidated financial statements.

Information (in millions) included in our Consolidated Balance Sheet as of December 31, 2008 for those VIEs where we had significant variable interest and where we were a sponsor that held a variable interest was as follows:

	<u>LNL Amounts Related to VIE</u>		
	<u>Total Assets</u>	<u>Total Liabilities</u>	<u>Maximum Loss Exposure</u>
Credit-linked notes	\$50	\$—	\$600

We invested in two credit-linked notes where the note holders do not have voting rights or decision-making capabilities. The entities that issued the credit-linked notes are financed by the note holders, and as such, the note holders participate in the expected losses and residual returns of the entities. Because the note holders' investment does not permit them to make decisions about the entities' activities that would have a significant effect on the success of the entities, we have determined that these entities are VIEs. We are not the primary beneficiary of the VIEs as the multi-tiered class structure of the credit-linked notes requires the subordinated classes of the investment pool to absorb credit losses prior to our class of notes. As a result, we will not absorb the majority of the expected losses and the coupon we receive on the credit-linked notes limits our participation in the residual returns. For information regarding our exposure to loss in our credit-linked notes, see "Credit-Linked Notes" in Note 5.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

5. Investments

Available-for-Sale Securities

Pursuant to SFAS No. 157, we have categorized these securities into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in "SFAS No. 157 – Fair Value Measurements" in Note 2. See Note 22 for additional disclosures regarding our fair values required by SFAS 157.

The amortized cost, gross unrealized gains and losses and fair value of available-for-sale securities (in millions) were as follows:

	<i>As of December 31, 2008</i>			
	<i>Amortized</i>	<i>Gross Unrealized</i>		<i>Fair</i>
	<i>Cost</i>	<i>Gains</i>	<i>Losses</i>	<i>Value</i>
Corporate bonds	\$39,463	\$614	\$4,993	\$35,084
U.S. Government bonds	158	36	—	194
Foreign government bonds	509	33	48	494
Mortgage-backed securities:				
Mortgage pass-through securities	1,749	57	37	1,769
Collateralized mortgage obligations	6,612	168	733	6,047
Commerical mortgage-backed securities	2,428	7	588	1,847
State and municipal bonds	118	2	2	118
Hybrid and redeemable preferred stocks	1,521	6	591	936
Total fixed maturity securities	<u>52,558</u>	<u>923</u>	<u>6,992</u>	<u>46,489</u>
Equity securities	187	9	57	139
Total available-for-sale securities	<u>\$52,745</u>	<u>\$932</u>	<u>\$7,049</u>	<u>\$46,628</u>

	<i>As of December 31, 2007</i>			
	<i>Amortized</i>	<i>Gross Unrealized</i>		<i>Fair</i>
	<i>Cost</i>	<i>Gains</i>	<i>Losses</i>	<i>Value</i>
Corporate bonds	\$42,041	\$1,049	\$ 904	\$42,186
U.S. Government bonds	153	14	—	167
Foreign government bonds	586	39	4	621
Mortgage-backed securities:				
Mortgage pass-through securities	1,185	23	4	1,204
Collateralized mortgage obligations	6,441	75	124	6,392
Commerical mortgage-backed securities	2,598	48	67	2,579
State and municipal bonds	143	2	—	145
Hybrid and redeemable preferred stocks	103	9	1	111
Total fixed maturity securities	<u>53,250</u>	<u>1,259</u>	<u>1,104</u>	<u>53,405</u>
Equity securities	132	9	7	134
Total available-for-sale securities	<u>\$53,382</u>	<u>\$1,268</u>	<u>\$1,111</u>	<u>\$53,539</u>

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

	<i>As of December 31, 2008</i>	
	<i>Amortized</i>	<i>Fair</i>
	<i>Cost</i>	<i>Value</i>
Due in one year or less	\$ 1,712	\$ 1,694
Due after one year through five years	12,568	11,869
Due after five years through ten years	14,036	12,013
Due after ten years	13,453	11,250
Subtotal	<u>41,769</u>	<u>36,826</u>
Mortgage-backed securities	<u>10,789</u>	<u>9,663</u>
Total fixed maturity available-for-sale securities	<u>\$52,558</u>	<u>\$46,489</u>

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

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

5. Investments (continued)

The fair value and gross unrealized losses of available-for-sale securities (in millions), aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were as follows:

	<i>As of December 31, 2008</i>					
	<i>Less Than or Equal to Twelve Months</i>		<i>Greater Than Twelve Months</i>		<i>Total</i>	
	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>
Corporate bonds	\$18,449	\$2,303	\$5,809	\$2,690	\$24,258	\$4,993
U.S. Government bonds	3	—	—	—	3	—
Foreign government bonds	145	15	50	33	195	48
Mortgage-backed securities:						
Mortgage pass-through securities	95	25	51	12	146	37
Collateralized mortgage obligations	807	279	688	454	1,495	733
Commercial mortgage-backed securities	1,099	169	474	419	1,573	588
State and municipal bonds	28	2	2	—	30	2
Hybrid and redeemable preferred stocks	448	261	406	330	854	591
Total fixed maturity securities	<u>21,074</u>	<u>3,054</u>	<u>7,480</u>	<u>3,938</u>	<u>28,554</u>	<u>6,992</u>
Equity securities	82	56	2	1	84	57
Total available-for-sale securities	<u>\$21,156</u>	<u>\$3,110</u>	<u>\$7,482</u>	<u>\$3,939</u>	<u>\$28,638</u>	<u>\$7,049</u>
Total number of securities in an unrealized loss position						<u>3,507</u>

	<i>As of December 31, 2007</i>					
	<i>Less Than or Equal to Twelve Months</i>		<i>Greater Than Twelve Months</i>		<i>Total</i>	
	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>
Corporate bonds	\$11,038	\$657	\$4,142	\$247	\$15,180	\$ 904
U.S. Government bonds	—	—	3	—	3	—
Foreign government bonds	81	4	—	—	81	4
Mortgage-backed securities:						
Mortgage pass-through securities	32	—	189	4	221	4
Collateralized mortgage obligations	1,672	96	1,069	28	2,741	124
Commercial mortgage-backed securities	490	46	535	21	1,025	67
State and municipal bonds	29	—	15	—	44	—
Hybrid and redeemable preferred stocks	13	1	—	—	13	1
Total fixed maturity securities	<u>13,355</u>	<u>804</u>	<u>5,953</u>	<u>300</u>	<u>19,308</u>	<u>1,104</u>
Equity securities	61	7	—	—	61	7
Total available-for-sale securities	<u>\$13,416</u>	<u>\$811</u>	<u>\$5,953</u>	<u>\$300</u>	<u>\$19,369</u>	<u>\$1,111</u>
Total number of securities in an unrealized loss position						<u>2,263</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

5. Investments (continued)

The fair value, gross unrealized losses (in millions) and number of available-for-sale securities where the fair value had declined below amortized cost by greater than 20%, were as follows:

	<i>As of December 31, 2008</i>		
	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Number of Securities</i>
Less than six months	\$ 781	\$ 389	159
Six months or greater, but less than nine months . . .	1,141	536	206
Nine months or greater, but less than twelve months . .	1,552	785	223
Twelve months or greater . .	4,027	3,509	785
Total available-for-sale securities	<u>\$7,501</u>	<u>\$5,219</u>	<u>1,373</u>
	<i>As of December 31, 2007</i>		
	<i>Fair Value</i>	<i>Gross Unrealized Losses</i>	<i>Number of Securities</i>
Less than six months	\$ 133	\$ 48	22
Six months or greater, but less than nine months . . .	425	137	30
Nine months or greater, but less than twelve months . .	363	109	17
Twelve months or greater . .	182	79	57
Total available-for-sale securities	<u>\$1,103</u>	<u>\$373</u>	<u>\$126</u>

As described more fully in Note 1, we regularly review our investment holdings for other-than-temporary impairments. Based upon this review, the cause of the \$5.9 billion increase in our gross unrealized losses for available-for-sale securities for the year ended December 31, 2008, was attributable primarily to a combination of reduced liquidity in several market segments and deterioration in credit fundamentals. We believe that the securities in an unrealized loss position as of December 31, 2008 and 2007 were not other-than-temporarily impaired due to our ability and intent to hold for a period of time sufficient for recovery.

Trading Securities

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

	<i>As of December 31,</i>	
	<i>2008</i>	<i>2007</i>
Corporate bonds	\$1,467	\$1,817
U.S. Government bonds	414	366
Foreign government bonds	38	45
Mortgage-backed securities:		
Mortgage pass-through securities	31	21
Collateralized mortgage obligations	118	153
Commercial mortgage-backed securities	76	104
State and municipal bonds	13	17
Hybrid and redeemable preferred stocks . .	30	8
Total fixed maturity securities	2,187	2,531
Equity securities	2	2
Total trading securities	<u>\$2,189</u>	<u>\$2,533</u>

The portion of the market adjustment for losses that relate to trading securities still held as of December 31, 2008, 2007 and 2006 was \$172 million, \$8 million and \$48 million, respectively.

Mortgage Loans on Real Estate

Mortgage loans on real estate principally involve commercial real estate. The commercial loans are geographically diversified throughout the U.S with the largest concentrations in California and Texas, which accounted for approximately 30% and 29% of mortgage loans as of December 31, 2008 and 2007, respectively. As of December 31, 2008, we held no impaired mortgage loans and therefore had no valuation allowance.

Net Investment Income

The major categories of net investment income (in millions) on our Consolidated Statements of Income were as follows:

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Net Investment Income			
Fixed maturity available-for-sale securities	\$3,236	\$3,264	\$2,968
Equity available-for-sale securities	8	19	11
Trading securities	154	163	181
Mortgage loans on real estate . .	473	491	466
Real estate	20	41	36
Standby real estate equity commitments	3	12	18
Policy loans	177	172	158
Invested cash	33	49	62
Alternative investments	(34)	102	46
Consent fees	5	10	8
Other investments	12	36	15
Investment income	4,087	4,359	3,969
Investment expense	(112)	(178)	(164)
Net investment income . . .	<u>\$3,975</u>	<u>\$4,181</u>	<u>\$3,805</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

5. Investments (continued)

Realized Loss Related to Investments

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

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Fixed maturity available-for-sale securities:			
Gross gains	\$ 49	\$ 120	\$ 123
Gross losses	(1,059)	(176)	(99)
Equity available-for-sale securities:			
Gross gains	1	3	2
Gross losses	(33)	(111)	—
Gain (loss) on other investments	31	22	5
Associated amortization expense of DAC, VOBA, DSI and DFEL and changes in other contract holder funds and funds withheld reinsurance liabilities	<u>244</u>	<u>29</u>	<u>(38)</u>
Total realized loss on investments, excluding trading securities	(767)	(113)	(7)
Loss on certain derivative instruments	(83)	(2)	2
Associated amortization expense of DAC, VOBA, DSI and DFEL and changes in other contract holder funds	<u>—</u>	<u>1</u>	<u>—</u>
Total realized loss on investments and certain derivative instruments, excluding trading securities	<u>\$ (850)</u>	<u>\$ (114)</u>	<u>\$ (5)</u>
Write-downs for other-than-temporary impairments included in realized loss on available-for-sale securities above	<u>\$ (900)</u>	<u>\$ (257)</u>	<u>\$ (64)</u>

See Note 15 for a comprehensive listing of realized loss reported on our Consolidated Statements of Income

Securities Lending

The carrying values of securities pledged under securities lending agreements were \$427 million and \$655 million as of December 31, 2008 and 2007, respectively. The fair values of these securities were \$410 million and \$634 million as of December 31, 2008 and 2007, respectively. The carrying value and fair value of the collateral receivable held for derivatives is \$17 million as of December 31, 2008. We did not have a collateral payable for derivatives as of December 31, 2007.

Reverse Repurchase Agreements

The carrying values of securities pledged under reverse repurchase agreements were \$470 million and \$480 million as of December 31, 2008 and 2007, respectively. The fair values of these securities were \$496 million and \$502 million as of December 31, 2008 and 2007, respectively.

Investment Commitments

As of December 31, 2008, our investment commitments for fixed maturity securities (primarily private placements), limited partnerships, real estate and mortgage loans on real estate were

\$705 million, which included \$267 million of standby commitments to purchase real estate upon completion and leasing.

Concentrations of Financial Instruments

As of December 31, 2008, we had investments in the collateralized mortgage obligation industry with a fair value of \$6.5 billion or 11% of the invested assets portfolio totaling \$60.2 billion. We utilized the industry classifications to obtain the concentration of financial instruments amount, as such, this amount will not agree to the available-for-sale securities table above. We did not have a concentration of financial instruments in a single industry as of December 31, 2007. As of December 31, 2008 and 2007, we did not have a significant concentration of financial instruments in a single investee or geographic region of the U.S.

Credit-Linked Notes

As of December 31, 2008 and 2007, other contract holder funds on our Consolidated Balance Sheets included \$600 million and \$1.2 billion outstanding in funding agreements, respectively. We invested the proceeds of \$850 million received for issuing three funding agreements in 2006 and 2007 into three separate credit-linked notes originated by third party companies. One of the credit linked notes totaling \$250 million was paid off at par in September of 2008 and as a result, the related structure, including the \$250 million funding agreement, was terminated. The two remaining credit-linked notes are asset-backed securities, classified as corporate bonds in the tables above and are reported as fixed maturity securities on our Consolidated Balance Sheets. An additional \$300 million funding agreement was assumed as a result of the merger of Jefferson-Pilot, but was not invested into credit-linked notes. This \$300 million funding agreement matured on June 2, 2008.

We earn a spread between the coupon received on the credit-linked notes and the interest credited on the funding agreement. Our credit-linked notes were created using a special purpose trust that combines highly rated assets with credit default swaps to produce a multi-class structured security. The high quality asset in these transactions is a AAA-rated asset-backed security secured by a pool of credit card receivables. Our affiliate, Delaware Investments, actively manages the credit default swaps in the underlying portfolios. As permitted in the credit-linked note agreements, Delaware Investments acts as the investment manager for the pool of underlying issuers in each of the transactions. Delaware Investments, from time to time, has directed substitutions of corporate names in the reference portfolio. When substituting corporate names, the issuing special purpose trust transacts with a third party to sell credit protection on a new issuer, selected by Delaware Investments. The cost to substitute the corporate names is based on market conditions and the liquidity of the corporate names. This new issuer will replace the issuer Delaware Investments has identified to remove from the pool of issuers. The substitution of corporate issuers does not revise the credit-linked note agreement. The subordination and the participation in credit losses may change as a result of the substitution. The amount of the change is dependant upon the relative risk of the issuers removed and replaced in the pool of issuers.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

5. Investments (continued)

Consistent with other debt market instruments, we are exposed to credit losses within the structure of the credit-linked notes, which could result in principal losses to our investments. However, we have attempted to protect our investments from credit losses through the multi-tiered class structure of the credit-linked note, which requires the subordinated classes of the investment pool to absorb all of the credit losses. We own the mezzanine tranche of these investments. To date, there has been one default in the underlying collateral pool of the \$400 million credit-linked note and two defaults in the underlying collateral pool of the \$200 million credit-linked note. There has been no event of default on the credit-linked notes themselves. We feel the remaining subordination is sufficient to absorb future credit losses, subject to changing market conditions. We do not anticipate any future payments under the credit-linked notes and there are no recourse provisions or assets held as collateral that would enable us to recover payments if made. Similar to other debt market instruments, our maximum principal loss is limited to our original investment of \$600 million as of December 31, 2008.

As in the general markets, spreads on these transactions have widened, causing unrealized losses. We had unrealized losses of \$550 million on the \$600 million in credit-linked notes as

of December 31, 2008 and \$190 million on the \$850 million in credit-linked notes as of December 31, 2007. As described more fully in Note 1, we regularly review our investment holdings for other-than-temporary impairments. Based upon this review, we believe that these securities were not other-than-temporarily impaired as of December 31, 2008 and 2007.

The following summarizes information regarding our investments in these securities (dollars in millions):

	<i>Amount and Date of Issuance</i>	
	<i>\$400 December 2006</i>	<i>\$200 April 2007</i>
Amortized cost ⁽¹⁾	\$ 400	\$ 200
Fair value ⁽¹⁾	30	20
Attachment point ⁽¹⁾	4.77%	1.48%
Maturity	12/20/2016	3/20/2017
Current rating of tranche ⁽¹⁾	BBB-	Baa2
Current rating of underlying collateral pool ⁽¹⁾	Aaa-Caa1	Aaa-Ba3
Number of entities ⁽¹⁾	124	98
Number of countries ⁽¹⁾	20	23

⁽¹⁾ As of December 31, 2008

6. Derivative Instruments

Types of Derivative Instruments and Derivative Strategies

We maintain an overall risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate risk, foreign currency exchange risk, equity market risk and credit risk. We assess these risks by continually identifying and monitoring changes in interest rate exposure, foreign currency exposure, equity market exposure and credit exposure that may adversely impact expected future cash flows and by evaluating hedging opportunities. Derivative instruments that are currently used as part of our interest rate risk management strategy include interest rate swaps, and interest rate caps. Derivative instruments that are used as part of our foreign currency risk management strategy include foreign currency swaps. Call options on LNC stock, call options on the Standard & Poor's ("S&P") 500 Index[®] ("S&P 500") are used as part of our equity market risk management strategy. We also use credit default swaps as part of our credit risk management strategy.

As of December 31, 2008 and 2007, we had derivative instruments that were designated and qualified as cash flow hedges. We also had derivative instruments that were economic hedges, but were not designated as hedging instruments under SFAS 133. See Note 1 for a detailed discussion of the accounting treatment for derivative instruments.

Our derivative instruments are monitored by LNC's risk management committee as part of that committee's oversight of our derivative activities. LNC's risk management 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 incorporated into our overall risk management strategies.

Our hedging strategy is designed to mitigate the risk and income statement volatility caused by changes in the equity markets, interest rates and volatility associated with living benefit guarantees offered in our variable annuities including the *Lincoln SmartSecurity*[®] Advantage guaranteed minimum withdrawal benefit ("GWB") feature, the 4LATER[®] Advantage guaranteed income benefit ("GIB") feature and the *i4LIFE*[®] Advantage GIB feature that is available in our variable annuity products. Certain features of these guarantees, notably our GIB and 4LATER[®] features have elements of both insurance benefits accounted for under SOP 03-1 and embedded derivatives accounted for under SFAS 133 and SFAS 157. We weight these features and their associated reserves accordingly based on their hybrid nature. The change in estimated fair value of the portion of guarantee features that are considered to be derivatives under SFAS 133 is reported in net income. The hedging strategy is designed such that changes in the value of the hedge contracts generally offset changes in the value of the embedded derivative of the GWB and GIB. As part of our current hedging program, equity markets, interest rates and volatility in market conditions are monitored on a daily basis. We rebalance our hedge positions based upon changes in these factors as needed. While we actively manage our hedge positions, our hedge positions may not be totally effective to offset changes in assets and liabilities caused by movements in these factors due to, among other things, differences in timing between when a market exposure changes and corresponding changes to the hedge positions, extreme swings in the equity markets and interest rates, market volatility, contract holder behavior, divergence between the performance of

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

6. Derivative Instruments (continued)

the underlying funds and the hedging indices, divergence between the actual and expected performance of the hedge instruments, or our ability to purchase hedging instruments at prices consistent with our desired risk and return trade-off.

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

We also distribute indexed annuity contracts. These contracts permit the holder to elect an interest rate return or an equity market component, where interest credited to the contracts is linked to the performance of the S&P 500. This feature represents an embedded derivative under SFAS 133. Contract holders may elect to rebalance index options at renewal dates, either annually or biannually. At each renewal date, we have the opportunity to re-price the indexed component by establishing participation rates, subject to minimum guarantees. We purchase S&P 500 call options that are highly correlated to the portfolio allocation decisions of our contract holders, such that we are economically hedged with respect to equity returns for the current reset period. The mark-to-market of the options held generally

offsets the change in value of the embedded derivative within the indexed annuity, both of which are recorded as a component of realized gain (loss) on our Consolidated Statements of Income. In calculating our future contract benefit liabilities under these contracts, SFAS 133 requires that we calculate fair values of index options we may purchase in the future to hedge contract holder index allocations in future reset periods.

These fair values represent an estimate of the cost of the options we will purchase in the future, discounted back to the date of the Consolidated Balance Sheet, using current market indicators of volatility and interest rates. Changes in the fair values of these liabilities are included as a component of realized gain (loss) on our Consolidated Statements of Income.

Pursuant to SFAS 157, we have categorized our derivative instruments into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in "SFAS 157 – Fair Value Measurements" in Note 2. See Note 22 for additional disclosures regarding our fair values required by SFAS 157. We have derivative instruments with off-balance-sheet risks whose notional or contract amounts exceed the credit exposure. Outstanding derivative instruments with off-balance-sheet risks, shown in notional amounts along with their carrying values and estimated fair values (in millions), were as follows:

	<i>As of December 31,</i>				
	<i>Notional Amounts</i>		<i>Assets (Liabilities)</i>		
	<i>2008</i>	<i>2007</i>	<i>Carrying or Fair Value</i>	<i>2008</i>	<i>2007</i>
Cash flow hedges:					
Interest rate swap agreements	\$ 780	\$1,372	\$ (50)	\$ (5)	
Foreign currency swaps	366	366	64	(17)	
Call options (based on LNC stock)	—	—	—	1	
Total cash flow hedges	<u>1,146</u>	<u>1,738</u>	<u>14</u>	<u>(21)</u>	
All other derivative instruments:					
Interest rate cap agreements	2,200	4,100	—	2	
Credit default swaps	149	60	(51)	—	
Call options (based on LNC stock)	18	23	—	13	
Call options (based on S&P 500 Index®)	2,951	2,858	31	149	
Total other derivative instruments	<u>5,318</u>	<u>7,041</u>	<u>(20)</u>	<u>164</u>	
Embedded derivatives per SFAS 133	—	—	(2,722)	(303)	
Total derivative instruments	<u>\$6,464</u>	<u>\$8,779</u>	<u>\$(2,728)</u>	<u>\$(160)</u>	

The carrying or fair value of total derivative instruments (in millions) reported above is reflected within the Consolidated Balance Sheets as follows:

	<i>As of December 31,</i>	
	<i>2008</i>	<i>2007</i>
Derivative investments	\$ 60	\$ 172
Reinsurance related derivative asset (liability)	167	(102)
Future contract benefits liability	(2,904)	(230)
Other liabilities — credit default swaps	(51)	—
Total	<u>\$(2,728)</u>	<u>\$(160)</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

6. Derivative Instruments (continued)

The notional amount of derivative financial instruments by maturity (in millions) was as follows:

	<i>Remaining Life as of December 31, 2008</i>				
	<i>Less Than 1 Year</i>	<i>1 - 5 Years</i>	<i>5 - 10 Years</i>	<i>After 10 Years</i>	<i>Total</i>
Cash flow hedges:					
Interest rate swap agreements	\$ 146	\$ 128	\$240	\$266	\$ 780
Foreign currency swaps	—	—	231	135	366
Total cash flow hedges	<u>146</u>	<u>128</u>	<u>471</u>	<u>401</u>	<u>1,146</u>
All other derivative instruments:					
Interest rate cap agreements	1,200	1,000	—	—	2,200
Credit default swaps	—	60	89	—	149
Call options (based on LNC stock)	—	18	—	—	18
Call options (based on S&P 500 Index [®])	2,185	766	—	—	2,951
Total other derivative instruments	<u>3,385</u>	<u>1,844</u>	<u>89</u>	<u>—</u>	<u>5,318</u>
Total derivative instruments	<u>\$3,531</u>	<u>\$1,972</u>	<u>\$560</u>	<u>\$401</u>	<u>\$6,464</u>

The settlement payments and mark-to-market adjustments on derivative instruments (in millions) recorded on our Consolidated Statements of Income were as follows:

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Cash flow hedges:			
Interest rate swap agreements ⁽¹⁾	\$ 4	\$ 5	\$ 5
Foreign currency swaps ⁽¹⁾	(1)	(1)	(1)
Total cash flow hedges	<u>3</u>	<u>4</u>	<u>4</u>
All other derivative instruments:			
Credit default swaps ⁽¹⁾	1	—	—
Call options (based on LNC stock) ⁽²⁾	(8)	(3)	10
Call options (based on S&P 500) ⁽³⁾	(204)	6	62
Total other derivative instruments	<u>(211)</u>	<u>3</u>	<u>72</u>
Total derivative instruments	<u>\$(208)</u>	<u>\$ 7</u>	<u>\$76</u>

⁽¹⁾ Reported in net investment income on our Consolidated Statements of Income.

⁽²⁾ Reported in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income.

⁽³⁾ Reported in net realized loss on our Consolidated Statements of Income.

Derivative Instruments Designated as Cash Flow Hedges

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

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Ineffective portion recognized in realized loss	<u>\$ 1</u>	<u>\$(1)</u>	<u>\$ 1</u>
Gains recognized as a component of OCI with the offset to:			
Net investment (income)	<u>\$ (2)</u>	<u>\$ (3)</u>	<u>\$ (3)</u>
Benefit expense (recovery)	<u>—</u>	<u>(1)</u>	<u>(1)</u>
	<u>\$ (2)</u>	<u>\$(4)</u>	<u>\$(4)</u>

As of December 31, 2008, \$7 million of the deferred net gains on derivative instruments in accumulated OCI were expected to be reclassified to earnings during 2009. This reclassification is due primarily to the receipt of interest payments associated with variable rate securities and forecasted purchases, payment of interest on our long-term debt, the receipt of interest payments associated with foreign currency securities, and the periodic vesting of stock appreciation rights ("SARs").

For the years ended December 31, 2008, 2007 and 2006, there were no material reclassifications to earnings due to hedged firm commitments no longer deemed probable or due to hedged forecasted transactions that had not occurred by the end of the originally specified time period.

Interest Rate Swap Agreements

We use a portion of our interest rate swap agreements to hedge our exposure to floating rate bond coupon payments, replicating a fixed rate bond. An interest rate swap is a contractual agreement to exchange payments at one or more times based on the actual or expected price level, performance or value of one or more underlying interest rates. We are required to pay the counterparty the stream of variable interest payments based on the coupon payments from the hedged bonds, and in turn, receive a fixed payment from the counterparty, at a pre-determined interest rate. The net receipts/payments from these interest rate swaps are recorded in net investment income on our Consolidated Statements of Income. Gains or losses on interest rate swaps hedging our interest rate exposure on floating rate bond coupon payments are reclassified from accumulated OCI to net income as the related bond interest is accrued.

In addition, we use interest rate swap agreements to hedge our exposure to fixed rate bond coupon payments and the change in underlying asset values as interest rates fluctuate. The net receipts/payments from these interest rate swaps are recorded in net investment income on our Consolidated Statements of Income.

Foreign Currency Swaps

We use foreign currency swaps, which are traded over-the-counter, to hedge some of the foreign exchange risk of investments in fixed maturity securities denominated in foreign currencies. A foreign currency swap is a contractual agreement to exchange the currencies of two different countries at

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

6. Derivative Instruments (continued)

a specified rate of exchange in the future. Gains or losses on foreign currency swaps hedging foreign exchange risk exposure on foreign currency bond coupon payments are reclassified from accumulated OCI to net income as the related bond interest is accrued.

Call Options (Based on LNC Stock)

We use call options on LNC stock to hedge the expected increase in liabilities arising from SARs granted on our stock. Upon option expiration, the payment, if any, is the increase in our 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 are marked-to-market through net income. Call options hedging non-vested SARs are eligible for hedge accounting and are accounted for as cash flow hedges of the forecasted vesting of the SARs 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 the related SARs. Our call option positions will be maintained until such time the related SARs are either exercised or expire and our SARs liabilities are extinguished.

All Other Derivative Instruments

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

Interest Rate Cap Agreements

The interest rate cap agreements entitle us to receive quarterly payments from the counterparties on specified future reset dates, contingent on future interest rates. For each cap, the amount of such quarterly payments, if any, is determined by the excess of a market interest rate over a specified cap rate, multiplied by the notional amount divided by four. The purpose of our interest rate cap agreement program is to provide a level of protection from the effect of rising interest rates for our annuity business, within our Retirement Solutions – Annuities and Retirement Solutions – Defined Contribution segments. The interest rate cap agreements provide an economic hedge of the annuity line of business. However, the interest rate cap agreements do not qualify for hedge accounting under SFAS 133.

Call Options (Based on LNC Stock)

We use 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 SFAS 133. Mark-to-market changes are recorded in net income as underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income.

Call Options (Based on S&P 500)

We use indexed annuity contracts to permit the holder to elect an interest rate return or an equity market component, where interest credited to the contracts is linked to the performance of the S&P 500. Contract holders may elect to rebalance index options at renewal dates, either annually or biannually. At each renewal date, we have the opportunity to re-price the indexed component by establishing participation rates, subject to minimum guarantees. We purchase call options that are highly correlated to the portfolio allocation decisions of our contract

holders, such that we are economically hedged with respect to equity returns for the current reset period. The mark-to-market of the options held generally offsets the change in value of the embedded derivative within the indexed annuity, both of which are recorded as a component of realized gain (loss) on our Consolidated Statements of Income.

Credit Default Swaps

We buy credit default swaps to hedge against a drop in bond prices due to credit concerns of certain bond issuers. A credit default swap allows us to put the bond back to the counterparty at par upon a default event by the bond issuer. A default event is defined as bankruptcy, failure to pay, obligation acceleration or restructuring. Our credit default swaps are not currently qualified for hedge accounting under SFAS 133, as amounts are insignificant

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

Information related to our open credit default swaps for which we are the seller (in millions) as of December 31, 2008, was as follows:

<i>Maturity</i>	<i>Reason for Entering</i>	<i>Nature of Recourse</i>	<i>Credit Rating of Counterparty</i>	<i>Fair Value⁽⁴⁾</i>	<i>Maximum Potential Payout</i>
3/20/2010	(1)	(3)	Aa3/A+	\$ (1)	\$ 10
6/20/2010	(1)	(3)	Aa2/A	—	10
12/20/2012	(2)	(3)	Aa2/A+	—	10
12/20/2012	(2)	(3)	Aa2/A+	—	10
12/20/2012	(2)	(3)	A1/A	—	10
12/20/2012	(2)	(3)	A1/A	(1)	10
3/20/2017	(2)	(3)	A2/A	(14)	22 ⁽⁵⁾
3/20/2017	(2)	(3)	A2/A	(10)	14 ⁽⁵⁾
3/20/2017	(2)	(3)	A2/A	(8)	18 ⁽⁵⁾
3/20/2017	(2)	(3)	A2/A	(11)	18 ⁽⁵⁾
3/20/2017	(2)	(3)	A2/A	(6)	17 ⁽⁵⁾
				<u>\$(51)</u>	<u>\$149</u>

⁽¹⁾ Credit default swap was entered into in order to generate income by providing protection on a highly rated basket of securities in return for a quarterly payment.

⁽²⁾ Credit default swap was entered into in order to generate income by providing default protection in return for a quarterly payment.

⁽³⁾ Seller does not have the right to demand indemnification/compensation from third parties in case of a loss (payment) on the contract.

⁽⁴⁾ Broker quotes are used to determine the market value of credit default swaps.

⁽⁵⁾ These credit default swaps were sold to a counter party of the issuing special purpose trust as discussed in the "Credit-Linked Notes" section in Note 5.

Notes to Consolidated Financial Statements (continued)

6. Derivative Instruments (continued)

Embedded Derivatives

Deferred Compensation Plans

We have certain deferred compensation plans that have embedded derivative instruments. The liability related to these plans varies based on the investment options selected by the participants. The liability related to certain investment options selected by the participants is marked-to-market through net income in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income.

Modco and CFW Arrangements

We are involved in various Modco and CFW reinsurance arrangements that have embedded derivatives. The change in fair value of the embedded derivatives, as well as the gains or losses on trading securities supporting these arrangements, are recorded through net income as a component of realized gain (loss) on our Consolidated Statements of Income. These embedded derivatives are included in reinsurance related derivative asset or (liability) on the Consolidated Balance Sheets; which amounts were \$15 million and \$(211) million as of December 31, 2008 and 2007, respectively.

Derivative Related to Reinsurance Ceded To Affiliate

We are involved in an inter-company reinsurance agreement where we cede to LNBAR the risk under certain UL contracts for no-lapse benefit guarantees. If our contract holders' account value is not sufficient to pay the cost of insurance charges required to keep the policy in force, and the contract holder has made required deposits, LNBAR will reimburse us for the charges. These embedded derivatives are included in reinsurance related derivative asset or (liability) on the Consolidated Balance Sheets; which amounts were \$152 million and \$109 million as of December 31, 2008 and 2007, respectively.

Variable Annuity Products

We have certain variable annuity products with GWB and GIB features that are embedded derivatives. Certain features of these guarantees, notably our GIB and 4LATER® features, have elements of both insurance benefits accounted for under SOP 03-1 and embedded derivatives accounted for under SFAS 133 and SFAS 157. We weight these features and their associated reserves accordingly based on their hybrid nature. The change in fair value of the embedded derivatives flows through net income as realized gain (loss) on our Consolidated Statements of Income. As of December 31, 2008 and 2007, we had approximately \$12.7 billion and \$18.9 billion, respectively, of account values that were attributable to variable annuities with a GWB feature. As of December 31, 2008 and 2007, we had approximately \$4.7 billion and \$4.9 billion, respectively, of account values that were attributable to variable annuities with a GIB feature. All of the outstanding contracts with a GIB feature are still in the accumulation phase.

We implemented a hedging strategy designed to mitigate the income statement volatility caused by changes in the equity markets, interest rates, and volatility associated with GWB and GIB features. The hedging strategy is designed such that changes in

the value of the hedge contracts move in the opposite direction of changes in the value of the embedded derivatives of the GWB and GIB contracts subject to the hedging strategy. While we actively manage our hedge positions, these hedge positions may not be totally effective in offsetting changes in the embedded derivative due to, among other things, differences in timing between when a market exposure changes and corresponding changes to the hedge positions, extreme swings in the equity markets and interest rates, market volatility, contract holder behavior, divergence between the performance of the underlying funds and the hedging indices, divergence between the actual and expected performance of the hedge instruments and our ability to purchase hedging instruments at prices consistent with our desired risk and return trade-off.

Available-For-Sale Securities

We own various debt securities that either: contain call options to exchange the debt security for other specified securities of the borrower, usually common stock; or contain call options to receive the return on equity-like indexes. These embedded derivatives have not been qualified for hedge accounting treatment under SFAS 133; therefore, the change in fair value of the embedded derivatives flows through net investment income on our Consolidated Statements of Income.

Credit Risk

We are exposed to credit loss in the event of nonperformance by our counterparties on various derivative contracts and reflect assumptions regarding the credit or non-performance risk. The credit risk associated with such agreements is minimized by purchasing such agreements from financial institutions with long-standing, superior performance records. Additionally, we maintain a policy of requiring all derivative contracts to be governed by an International Swaps and Derivatives Association ("ISDA") Master Agreement. We and LNC are required to maintain minimum ratings as a matter of routine practice in negotiating ISDA agreements. Under some ISDA agreements, we have agreed to maintain certain financial strength or claims-paying ratings. A downgrade below these levels could result in termination of the derivatives contract, at which time any amounts payable by us would be dependent on the market value of the underlying derivative contract. In certain transactions, we and the counterparty have entered into a collateral support agreement requiring us to post collateral upon significant downgrade. We do not believe the inclusion of termination or collateralization events pose any material threat to the liquidity position of any insurance subsidiary of the Company. The amount of such exposure is essentially the net replacement cost or market value less collateral held for such agreements with each counterparty if the net market value is in our favor. As of December 31, 2008 and 2007, the exposure was \$150 million and \$169 million, respectively.

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Notes to Consolidated Financial Statements (continued)

7. Federal Income Taxes

The components of federal income tax expense (benefit) as reported on the Consolidated Statements of Income (in millions) were as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Current	\$(292)	\$372	\$244
Deferred	224	132	216
Total federal income tax expense (benefit)	<u>\$(68)</u>	<u>\$504</u>	<u>\$460</u>

A reconciliation of the effective tax rate differences (dollars in millions) was as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Tax rate of 35% times pre-tax income	\$ 65	\$610	\$568
Effect of:			
Separate account dividend received deduction	(82)	(88)	(80)
Tax credits	(25)	(22)	(21)
Prior year tax return adjustment	(34)	(14)	(25)
Other items	8	18	18
Provision (benefit) for income taxes	<u>\$(68)</u>	<u>\$504</u>	<u>\$460</u>
Effective tax rate	<u>N/M</u>	<u>29%</u>	<u>28%</u>

The effective tax rate is a ratio of tax expense over pre-tax income. Since the pre-tax income of \$186 million resulted in a tax benefit of \$68 million in 2008, the effective tax rate was not meaningful. The separate account dividend received deduction included in the table above is exclusive of any prior years' tax return resolution.

The federal income tax asset (liability) (in millions), which is included in other assets as of December 31, 2008, and other liabilities as of December 31, 2007, on our Consolidated Balance Sheets, was as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Current	\$(66)	\$(390)
Deferred	954	(239)
Total federal income tax asset (liability)	<u>\$888</u>	<u>\$(629)</u>

Significant components of our deferred tax assets and liabilities (in millions) were as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Deferred Tax Assets		
Future contract benefits and other contract holder funds	\$1,550	\$1,904
Reinsurance deferred gain	190	244
Modco embedded derivative	—	74
Postretirement benefits other than pensions	21	8
Compensation and benefit plans	135	175
Net unrealized loss on securities available-for-sale	2,142	—
Other investments	362	77
Ceding commission asset	5	7
Other	102	55
Total deferred tax assets	<u>4,507</u>	<u>2,544</u>
Deferred Tax Liabilities		
Deferred acquisition costs	1,992	1,436
Net unrealized gain on securities available-for-sale	—	40
Net unrealized gain on trading securities	12	71
Present value of business in-force	1,317	985
Modco embedded derivative	5	—
Other	227	251
Total deferred tax liabilities	<u>3,553</u>	<u>2,783</u>
Net deferred tax asset (liability) ..	<u>\$ 954</u>	<u>\$ (239)</u>

LNL and its affiliates, with the exception of JPL, JPFIC and JPLA as noted below, are part of a consolidated federal income tax filing with LNC. JPL filed a separate federal income tax return until its merger with LNL on April 2, 2007. JPFIC filed a separate federal income tax return until its merger into LNL on July 2, 2007. JPLA was part of a consolidated federal income tax filing with JPFIC until its merger with LNY on April 2, 2007.

We are required to establish a valuation allowance for any gross deferred tax assets that are unlikely to reduce taxes payable in future years' tax returns. As of December 31, 2008 and 2007, we concluded that it was more likely than not that all gross deferred tax assets will reduce taxes payable in future years. Accordingly, no valuation allowance was necessary at December 31, 2008 and 2007.

As discussed in Note 2, we adopted FIN 48 on January 1, 2007. As of December 31, 2008 and 2007, \$142 million and \$134 million, of our unrecognized tax benefits presented below, if recognized, would have impacted our income tax expense and our effective tax rate. We anticipate a change to our unrecognized tax benefits during 2009 to range of none to \$48 million.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

7. Federal Income Taxes (continued)

A reconciliation of the unrecognized tax benefits (in millions) was as follows:

	<i>For the Years Ended December 31,</i>	
	<u>2008</u>	<u>2007</u>
Balance at beginning-of-year	\$290	\$272
Increases for prior year tax positions . .	16	5
Decreases for prior year tax positions . .	(46)	(1)
Increases for current year tax positions	20	21
Decreases for current year tax positions	(6)	(7)
Decreases for settlements with taxing authorities	(8)	—
Decreases for lapse of statute of limitations	(2)	—
Balance at end-of-year	<u>\$264</u>	<u>\$290</u>

We recognize interest and penalties accrued, if any, related to unrecognized tax benefits as a component of tax expense.

During the years ended December 31, 2008, 2007 and 2006, we recognized interest and penalty expense related to uncertain tax positions of \$1 million, \$19 million and \$13 million, respectively. We had accrued interest and penalty expense related to the unrecognized tax benefits of \$64 million and \$64 million as of December 31, 2008 and 2007, respectively.

We are subject to annual tax examinations from the Internal Revenue Service ("IRS"). During the third quarter of 2008, the IRS completed its examination for tax years 2003 and 2004 resulting in a proposed assessment. We believe a portion of the assessment is inconsistent with existing law are protesting it through the established IRS appeals process. We do not anticipate that any adjustments that might result from such audits would be material to our consolidated results of operations or financial condition. We are currently under audit by the IRS for years 2005 and 2006. The Jefferson-Pilot subsidiaries acquired in the April 2006 merger are subject to a separate IRS examination cycle. For the former Jefferson-Pilot Corporation and its subsidiaries, the IRS is examining tax year ended April 2nd, 2006.

8. DAC, VOBA, and DSI

During the fourth quarter of 2008, we recorded a decrease to income totaling \$262 million, for a reversion to the mean prospective unlocking of DAC, VOBA, and DSI as a result of significant and sustained declines in the equity markets during 2008. The pre-tax impact for these items is included within the prospective unlocking line items in the changes in DAC, VOBA, and DSI tables below.

Changes in DAC (in millions) were as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Balance at beginning-of-year	\$5,765	\$4,577	\$3,676
Cumulative effect of adoption of SOP 05-1	—	(31)	—
Dividend of FPP	—	(246)	—
Reinsurance ceded to LNBAR	(230)	—	—
Deferrals	1,811	2,002	1,479
Amortization, net of interest:			
Prospective unlocking — assumption changes	(368)	27	(9)
Prospective unlocking — model refinements	44	(49)	(2)
Retrospective unlocking	(120)	64	35
Other amortization, net of interest	(704)	(753)	(635)
Adjustment related to realized gains on available-for-sale securities and derivatives	129	78	(53)
Adjustment related to unrealized losses on available-for-sale securities and derivatives	1,094	96	86
Balance at end-of-year	<u>\$7,421</u>	<u>\$5,765</u>	<u>\$4,577</u>

Changes in VOBA (in millions) were as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Balance at beginning-of-year	\$2,809	\$3,032	\$ 742
Cumulative effect of adoption of SOP 05-1	—	(35)	—
Business acquired	—	14	2,478
Deferrals	40	46	96
Amortization, net of interest:			
Prospective unlocking — assumption changes	(7)	13	5
Prospective unlocking — model refinements	6	(2)	—
Retrospective unlocking	(38)	13	6
Other amortization	(335)	(421)	(349)
Accretion of interest	116	125	111
Adjustment related to realized gains (losses) on available-for- sale securities and derivatives . .	98	—	(9)
Adjustment related to unrealized gains (losses) on available-for- sale securities and derivatives . .	1,074	24	(48)
Balance at end-of-year	<u>\$3,763</u>	<u>\$2,809</u>	<u>\$3,032</u>

Estimated future amortization of VOBA, net of interest (in millions), as of December 31, 2008, was as follows:

2009	\$ 258
2010	241
2011	209
2012	192
2013	175
Thereafter	1,626
Total	<u>\$2,701</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

8. DAC, VOBA, and DSI (continued)

Changes in DSI (in millions) were as follows:

	<i>For the Years</i>		
	<i>Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Balance at beginning-of-year	\$ 279	\$ 194	\$ 129
Cumulative effect of adoption of SOP 05-1	—	(3)	—
Deferrals	96	116	86
Amortization, net of interest:			
Prospective unlocking — assumption changes	(37)	2	1
Prospective unlocking — model refinements	—	(1)	—
Retrospective unlocking	(6)	1	3
Other amortization, net of interest	(28)	(35)	(22)
Adjustment related to realized gains (losses) on available-for- sale securities and derivatives	6	5	(3)
Balance at end-of-year	<u>\$ 310</u>	<u>\$ 279</u>	<u>\$ 194</u>

9. Reinsurance

The following summarizes reinsurance amounts (in millions) recorded on our Consolidated Statements of Income, excluding amounts attributable to the indemnity reinsurance transaction with Swiss Re:

	<i>For the Years</i>		
	<i>Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Direct insurance premiums and fees	\$ 5,853	\$ 5,645	\$ 4,587
Reinsurance assumed	18	12	8
Reinsurance ceded	(1,056)	(1,063)	(1,021)
Total insurance premiums and fees, net	<u>\$ 4,815</u>	<u>\$ 4,594</u>	<u>\$ 3,574</u>
Direct insurance benefits	\$ 4,245	\$ 3,579	\$ 2,662
Reinsurance recoveries netted against benefits	(1,600)	(1,249)	(904)
Total benefits, net	<u>\$ 2,645</u>	<u>\$ 2,330</u>	<u>\$ 1,758</u>

We cede insurance to other companies. The portion of risks exceeding our retention limit is reinsured with other insurers. We seek reinsurance coverage within the businesses that sell life insurance in order to limit our exposure to mortality losses and enhance our capital management. As discussed in Note 25, a portion of this reinsurance activity is with affiliated companies.

Under our reinsurance program, we reinsure approximately 50% to 55% of the mortality risk on newly issued non-term life insurance contracts and approximately 40% to 45% of total mortality risk including term insurance contracts. Our policy for this program is to retain no more than \$10 million on a single insured life issued on fixed and VUL insurance contracts. Additionally, the retention per single insured life for

term life insurance and for corporate owned life insurance is \$2 million for each type of insurance. Portions of our deferred annuity business have been reinsured on a Modco basis with other companies to limit our exposure to interest rate risks. As of December 31, 2008, the reserves associated with these reinsurance arrangements totaled \$1.1 billion. To cover products other than life insurance, we acquire other insurance coverages with retentions and limits.

We obtain reinsurance from a diverse group of reinsurers, and we monitor concentration as well as financial strength ratings of our principal reinsurers. Our reinsurance operations were acquired by Swiss Re in December 2001, through a series of indemnity reinsurance transactions. Swiss Re represents our largest reinsurance exposure. Under the indemnity reinsurance agreements, Swiss Re reinsured certain of our liabilities and obligations. As we are not relieved of our legal liability to the ceding companies, the liabilities and obligations associated with the reinsured contracts remain on our Consolidated Balance Sheets with a corresponding reinsurance receivable from Swiss Re, which totaled \$4.2 billion as of December 31, 2008. Swiss Re has funded a trust, with a balance of \$1.9 billion as of December 31, 2008, to support this business. In addition to various remedies that we would have in the event of a default by Swiss Re, we continue to hold assets in support of certain of the transferred reserves. These assets consist of those reported as trading securities and certain mortgage loans. Our liabilities for funds withheld and embedded derivatives as of December 31, 2008, included \$1.8 billion and \$26 million, respectively, related to the business reinsured by Swiss Re.

We recorded the gain related to the indemnity reinsurance transactions on the business sold to Swiss Re as a deferred gain in the liability section of our Consolidated Balance Sheets in accordance with the requirements of SFAS No. 113, "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

9. Reinsurance (continued)

Contracts" ("SFAS 113"). The deferred gain is being amortized into income at the rate that earnings on the reinsured business are expected to emerge, over a period of 15 years. During 2008, 2007 and 2006 we amortized \$50 million, \$55 million and \$49 million, after-tax, respectively, of deferred gain on the sale of the reinsurance operation.

Because of ongoing uncertainty related to personal accident business, the reserves related to these exited business lines carried on our Consolidated Balance Sheets as of December 31, 2008, 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 SFAS 113 the Company 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, we would record a corresponding increase in reinsurance recoverable from Swiss Re. However, SFAS 113 does not permit us to take the full benefit in earnings for the recording of the increase in the reinsurance recoverable in the period of the change. Rather, we 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. We would not transfer any cash to Swiss Re as a result of these developments.

In the second quarter of 2007, we recognized increased reserves on the business sold and recognized a deferred gain that is being amortized into income at the rate that earnings are expected to emerge within a 15 year period. This adjustment resulted in a non-cash charge of \$13 million, after-tax, to increase reserves, which was partially offset by a cumulative "catch-up" adjustment to the deferred gain amortization of \$5 million, after-tax, for a total decrease to net income of \$8 million. The impact of the accounting for reserve adjustments related to this reinsurance treaty is excluded from our definition of income from operations.

10. Goodwill and Specifically Identifiable Intangible Assets

The changes in the carrying amount of goodwill (in millions) by reportable segment were as follows:

	<i>For the Year Ended December 31, 2008</i>			
	<i>Balance At Beginning-of-Year</i>	<i>Purchase Accounting Adjustments</i>	<i>Dividend of FPP</i>	<i>Balance At End-of-Year</i>
Retirement Solutions:				
Annuities	\$1,046	\$ (6)	\$—	\$1,040
Defined Contribution	20	—	—	20
Insurance Solutions:				
Life Insurance	2,199	(13)	—	2,186
Group Protection	274	—	—	274
Total goodwill	<u>\$3,539</u>	<u>\$(19)</u>	<u>\$—</u>	<u>\$3,520</u>
	<i>For the Year Ended December 31, 2007</i>			
	<i>Balance At Beginning-of-Year</i>	<i>Purchase Accounting Adjustments</i>	<i>Dividend of FPP</i>	<i>Balance At End-of-Year</i>
Retirement Solutions:				
Annuities	\$1,032	\$ 14	\$—	\$1,046
Defined Contribution	20	—	—	20
Insurance Solutions:				
Life Insurance	2,181	20	(2)	2,199
Group Protection	281	(7)	—	274
Total goodwill	<u>\$3,514</u>	<u>\$27</u>	<u>\$(2)</u>	<u>\$3,539</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

10. Goodwill and Specifically Identifiable Intangible Assets (continued)

The purchase accounting adjustments above relate to income tax deductions recognized when stock options attributable to mergers were exercised or the release of unrecognized tax benefits acquired through mergers.

We performed a Step 1 goodwill impairment analysis on all of our reporting units, which utilized primarily a discounted cash flow valuation technique. The discounted cash flow analysis required us to make judgments about revenues, earnings projections, growth rates and discount rates. We also considered other valuation techniques such as an analysis of peer companies and market participants. In the valuation process, we gave consideration to the current economic and market conditions. We also updated our October 1 analysis of goodwill impairment to reflect fourth quarter results and forecasts as of December 31, 2008, due to sharp declines in the equity markets and our stock price in the fourth quarter. In determining the estimated fair value of our reporting units, we incorporated consideration of discounted cash flow calculations, peer company price-to-earnings multiples, the level of our own share price and assumptions that market participants would make in valuing our reporting units. Our fair value estimations were based primarily on an in-depth analysis of future

cash flows and relevant discount rates, which considered market participant inputs (income approach).

All of our reporting units passed the Step 1 analysis. While the Step 1 analysis of our Insurance Solutions – Life reporting unit indicated that its fair value exceeded its carrying value, the margin above carrying value was relatively small. Therefore, we concluded that we should perform additional analysis for our Insurance Solutions – Life reporting unit under the Step 2 requirements of SFAS 142. In our Step 2 analysis, we estimated the implied fair value of the reporting unit's goodwill as determined by allocating the reporting unit's fair value determined in Step 1 to all of its net assets (recognized and unrecognized) as if the reporting unit had been acquired in a business combination at the date of the impairment test by performing a hypothetical purchase price allocation as if the reporting unit had been acquired for its estimated fair value on that date. We utilized very detailed forecasts of cash flows and market observable inputs in determining a fair value of the net assets for each of the reporting units similar to what would be estimated in a business combination between market participants. The implied fair value of goodwill for Insurance Solutions – Life was higher than its carrying amount; therefore, the goodwill for this reporting unit was not impaired.

The gross carrying amounts and accumulated amortization (in millions) for each major specifically identifiable intangible asset class by reportable segment were as follows:

	<i>As of December 31,</i>			
	<i>2008</i>		<i>2007</i>	
	<i>Gross Carrying Amount</i>	<i>Accumulated Amortization</i>	<i>Gross Carrying Amount</i>	<i>Accumulated Amortization</i>
Individual Markets — Life Insurance:				
Sales force	\$100	\$11	\$100	\$ 7
Retirement Solutions — Defined Contribution:				
Mutual fund contract rights ⁽¹⁾	<u>3</u>	—	<u>3</u>	—
Total	<u>\$103</u>	<u>\$11</u>	<u>\$103</u>	<u>\$ 7</u>

⁽¹⁾ No amortization recorded as the intangible asset has indefinite life.

Future estimated amortization of specifically identifiable intangible assets (in millions) as of December 31, 2008 was as follows:

2009	\$ 4
2010	4
2011	4
2012	4
2013	4
Thereafter	<u>69</u>
Total	<u>\$89</u>

11. Guaranteed Benefit Features

We issue variable annuity contracts through our separate accounts for which investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities). We also issue variable annuity and life contracts through separate

accounts that include various types of GDB, GWB and GIB features. The GDB features include those where we contractually guarantee to the contract holder either: return of no less than total deposits made to the contract less any partial withdrawals ("return of net deposits"); total deposits made to the

Notes to Consolidated Financial Statements (continued)

11. Guaranteed Benefit Features (continued)

contract less any partial withdrawals plus a minimum return (“minimum return”); or the highest contract value on any contract anniversary date through age 80 minus any payments or withdrawals following the contract anniversary (“anniversary contract value”).

Certain features of these guarantees are considered embedded derivatives and are recorded in future contract benefits on our Consolidated Balance Sheets at fair value under SFAS 133 and SFAS 157. Other guarantees that are not considered embedded derivatives meet the criteria as insurance benefits and are accounted for under the valuation techniques included in SOP 03-1. Still other guarantees contain characteristics of both an embedded derivative and an insurance benefit and are accounted for under an approach that weights these features and their associated reserves accordingly based on their hybrid nature. Effective January 1, 2008, we adopted SFAS 157, which affected the valuation of our embedded derivatives. See Note 22 for details on the adoption of SFAS 157. We use derivative instruments to hedge our exposure to the risks and earnings volatility that result from the embedded derivatives for living benefits in certain of our variable annuity products. The change in fair value of these instruments tends to move in the opposite direction of the change in fair value of the embedded derivatives. The net impact of these changes is reported as guaranteed living benefits (“GLB”), which is reported as a component of realized gain (loss) on our Consolidated Statements of Income and is discussed in Note 16.

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

	<i>As of December 31,</i>	
	<i>2008</i>	<i>2007</i>
Return of Net Deposits		
Total account value	\$33,907	\$44,833
Net amount at risk ⁽¹⁾	6,337	93
Average attained age of contract holders	56 years	55 years
Minimum Return		
Total account value	\$ 191	\$ 355
Net amount at risk ⁽¹⁾	109	25
Average attained age of contract holders	68 years	68 years
Guaranteed minimum return	5%	5%
Anniversary Contract Value		
Total account value	\$16,950	\$25,537
Net amount at risk ⁽¹⁾	8,402	359
Average attained age of contract holders	65 years	64 years

⁽¹⁾ Represents the amount of death benefit in excess of the account balance. The increase in net amount of risk when comparing December 31, 2008, to December 31, 2007, was attributable primarily to the decline in equity markets and associated reduction in the account values.

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

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Balance at beginning-of-year	\$ 38	\$23	\$15
Cumulative effect of adoption of			
SOP 05-1	—	(4)	—
Changes in reserves	312	25	14
Benefits paid	(73)	(6)	(6)
Balance at end-of-year	<u>\$277</u>	<u>\$38</u>	<u>\$23</u>

The changes to the benefit reserves amounts above are reflected in benefits on our Consolidated Statements of Income.

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

Asset Type	<i>As of December 31,</i>	
	<i>2008</i>	<i>2007</i>
Domestic equity	\$24,877	\$44,982
International equity	9,204	8,076
Bonds	6,701	8,034
Money market	5,802	6,545
Total	<u>\$46,584</u>	<u>\$67,637</u>

Percent of total variable annuity separate account values 99% 97%

Future contract benefits also include reserves for our products with secondary guarantees for our products sold through our Insurance Solutions – Life Insurance segment. These UL and VUL products with secondary guarantees represented approximately 34% of permanent life insurance in force as of December 31, 2008 and approximately 68% of sales for these products in 2008.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

12. Other Contract Holder Funds

Details of other contract holder funds (in millions) were as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Account values and other contract holder funds	\$57,875	\$56,668
Deferred front-end loads	948	768
Contract holder dividends payable	498	524
Premium deposit funds	109	113
Undistributed earnings on participating business	11	95
Total other contract holder funds	<u>\$59,441</u>	<u>\$58,168</u>

As of December 31, 2008 and 2007, participating policies comprised approximately 1.4% and 1.5%, respectively, of the face amount of insurance in force, and dividend expenses were \$92 million for the year ended December 31, 2008 and \$85 million for the years ended December 31, 2007 and 2006, respectively.

13. Short-Term and Long-Term Debt

Details underlying short-term and long-term debt (in millions) were as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Short-term debt ⁽¹⁾	\$ 4	\$ 18
Note due LNC, due 2009	—	155
Total short-term debt	<u>\$ 4</u>	<u>\$ 173</u>
Long-term debt:		
Note due LNC, due 2010	\$ 155	\$ —
LIBOR + 0.03% note, due 2017	250	—
LIBOR + 1.00% note, due 2037	375	375
Surplus Notes due LNC:		
9.76% surplus note, due 2024	50	50
6.56% surplus note, due 2028	500	500
6.03% surplus note, due 2028	750	750
Total surplus notes	<u>1,300</u>	<u>1,300</u>
Total long-term debt	<u>\$2,080</u>	<u>\$1,675</u>

⁽¹⁾ The short-term debt represents short-term notes payable to LNC.

A consolidated subsidiary of LNL issued two notes for a combined amount not to exceed \$250 million to LNC in 2006. The notes called for us to pay the principal amount of the notes on or before September 30, 2008 and interest to be paid monthly at a rate equal to the Federal Reserve Board's 30 day AA- financial commercial paper rate plus ten basis points. As of December 31, 2006, \$139 million had been advanced to us and was classified as long-term debt. During 2007, \$16 million was borrowed, bringing the outstanding balance to \$155 million, which was classified as short-term debt. During the third quarter of 2008, the notes were extended and are now due on September 30, 2010. The notes are now classified as long-term debt.

In the third quarter of 2008, LNL made an investment of \$19 million in the Federal Home Loan Bank of Indianapolis ("FHLBI"), a AAA-rated entity. This relationship provides us with another source of liquidity as an alternative to commercial paper and repurchase agreements as well as provides funding at comparatively low borrowing rates. We are allowed to borrow up to 20 times the amount of our common stock investment in FHLBI. All borrowings from the FHLBI are required to be secured by certain investments owned by LNL. As

of December 31, 2008, based on our common stock investment, we had borrowing capacity of up to approximately \$378 million from FHLBI. We also had a \$250 million floating-rate term loan outstanding under the facility due June 20, 2017, which may be prepaid beginning June 20, 2010.

On October 9, 2007, we issued a note of \$375 million to LNC. This note calls for us to pay the principal amount of the note on or before October 9, 2037 and interest to be paid quarterly at an annual rate of LIBOR + 1.00%.

During 2007, our surplus note for \$50 million to HARCO Capital Corporation was transferred to LNC. This note calls for us to pay the principal amount of the note on or before September 30, 2024 and interest to be paid semiannually at an annual rate of 9.76%. Subject to approval by the Indiana Insurance Commissioner, LNC also has a right to redeem the note for immediate repayment in total or in part twice per year. Any payment of interest or repayment of principal may be paid only if we have obtained the prior written approval of the Indiana Insurance Commissioner, have adequate earned surplus funds for such payment and if such payment would not cause us to violate the statutory capital requirements as set forth in the General Statutes of Indiana.

We issued a surplus note for \$500 million to LNC in 1998. This note calls for us to pay the principal amount of the note on or before March 31, 2028 and interest to be paid quarterly at an annual rate of 6.56%. Subject to approval by the Indiana Insurance Commissioner, LNC also has a right to redeem the note for immediate repayment in total or in part once per year on the anniversary date of the note. Any payment of interest or repayment of principal may be paid only out of our statutory earnings, only if our statutory capital surplus exceeds our statutory capital surplus as of the date of note issuance of \$2.3 billion, and subject to approval by the Indiana Insurance Commissioner.

We issued a surplus note for \$750 million to LNC in 1998. This note calls for us to pay the principal amount of the note on or before December 31, 2028 and interest to be paid quarterly at an annual rate of 6.03%. Subject to approval by the Indiana Insurance Commissioner, LNC also has a right to redeem the note for immediate repayment in total or in part once per year on the anniversary date of the note. Any payment of interest or repayment of principal may be paid only out of our statutory earnings, only if our statutory capital surplus exceeds our statutory capital surplus as of the date of note issuance of \$2.4 billion, and subject to approval by the Indiana Insurance Commissioner.

Notes to Consolidated Financial Statements (continued)

14. Contingencies and Commitments

Contingencies

Regulatory and Litigation Matters

Federal and state regulators continue to focus on issues relating to fixed and variable insurance products, including, but not limited to, suitability, replacements and sales to seniors. Like others in the industry, we have received inquiries including requests for information regarding sales to seniors from the Financial Industry Regulatory Authority, and we have responded to these inquiries. We continue to cooperate fully with such authority.

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

Commitments

Leases

We lease our home office in Fort Wayne, Indiana 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 us with the right of first refusal to purchase the properties during the terms of the lease, including renewal periods, at a price defined in the agreements. We also have 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. In 2006, we exercised the right and option to extend the Fort Wayne lease for two extended terms such that the lease shall expire in 2019. We retain our right and option to exercise the remaining four extended terms of 5 years each in accordance with the lease agreement. In 2007, we exercised the right and option to extend the Hartford lease for one extended term such that the lease shall expire in 2013.

Total rental expense on operating leases for the years ended December 31, 2008, 2007 and 2006 was \$49 million, \$56 million and \$53 million, respectively. Future minimum rental commitments (in millions) as of December 31, 2008 were as follows:

2009	\$ 50
2010	38
2011	33
2012	26
2013	21
Thereafter	<u>107</u>
Total	<u>\$275</u>

Information Technology Commitment

In February 1998, LNC signed a seven-year contract with IBM Global Services for information technology services for the Fort Wayne operations. In February 2004, LNC completed renegotiations and extended the contract through February 2010. Annual costs are dependent on usage but are expected to be approximately \$9 million.

Vulnerability from Concentrations

As of December 31, 2008, we did not have a concentration of: business transactions with a particular customer or lender; sources of supply of labor or services used in the business; or 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 our financial position.

Although we do not have any significant concentration of customers, our American Legacy Variable Annuity product offered in our Retirement Solutions – Annuities segment is significant to this segment. The American Legacy Variable Annuity product accounted for 37%, 46% and 48% of Retirement Solutions – Annuities' variable annuity product deposits in 2008, 2007 and 2006, respectively and represented approximately 62%, 66% and 67% of our total Retirement Solutions – Annuities' variable annuity product account values as of December 31, 2008, 2007 and 2006. In addition, fund choices for certain of our other variable annuity products offered in our Retirement Solutions – Annuities segment include American Fund Insurance SeriesSM ("AFIS") funds. For the Retirement Solutions – Annuities segment, AFIS funds accounted for 44%, 55% and 58% of variable annuity product deposits in 2008, 2007 and 2006 respectively and represented 70%, 75% and 75% of the segment's total variable annuity product account values as of December 31, 2008, 2007 and 2006, respectively.

Other Contingency Matters

State guaranty funds assess insurance companies to cover losses to contract holders of insolvent or rehabilitated companies. Mandatory assessments may be partially recovered through a reduction in future premium taxes in some states. We have accrued for expected assessments net of estimated future premium tax deductions of \$6 million and \$4 million as of December 31, 2008 and 2007, respectively.

Guarantees

We have guarantees with off-balance-sheet risks having contractual values of \$1 million and \$2 million as of December 31, 2008 and 2007, respectively, whose contractual amounts represent credit exposure. We have sold commercial mortgage loans through grantor trusts, which issued pass-through certificates. We 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 borrowers, we have 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 us. These guarantees expire in 2009. Our assessment of the off-balance-sheet risk was based upon the borrower's credit rating of Baa1.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

14. Contingencies and Commitments (continued)

Tax Matters

Changes to the Internal Revenue Code, administrative rulings or court decisions could increase our effective tax rate. In this regard, on August 16, 2007, the Internal Revenue Service ("IRS") issued a revenue ruling that purports, among other things, to modify the calculation of the separate account divi-

dends received deduction received by life insurance companies. Subsequently, the IRS issued another revenue ruling that suspended the August 16, 2007, ruling and announced a new regulation project on the issue. See Note 7 for the impact of the separate account dividends received deduction on our effective tax rate.

15. Stockholder's Equity

Stockholder's Equity

All authorized and issued shares of LNL are owned by LNC.

Accumulated OCI

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

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Unrealized Gains on Available-for-Sale Securities			
Balance at beginning-of-year	\$ 76	\$ 421	\$ 452
Other comprehensive income (loss):			
Unrealized holding losses arising during the year	(7,316)	(871)	(96)
Change in DAC, VOBA and other contract holder funds . . .	2,522	177	29
Income tax benefit	1,703	243	23
Change in foreign currency exchange rate adjustment	(66)	18	5
Less:			
Reclassification adjustment for gains (losses) included in net income	(1,042)	(164)	24
Associated amortization of DAC, VOBA, DSI, DFEL and changes in other contract holder funds	244	29	(37)
Income tax benefit	279	47	5
Balance at end-of-year . . .	<u>\$ (2,562)</u>	<u>\$ 76</u>	<u>\$ 421</u>

*For the Years Ended
December 31,*

	<u>2008</u>	<u>2007</u>	<u>2006</u>
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Unrealized Gains on

Derivative Instruments

Balance at beginning-of-year	\$ (19)	\$ (9)	\$ 7
Other comprehensive income (loss):			
Unrealized holding gains arising during the year	(42)	14	(22)
Change in DAC, VOBA and other contract holder funds . . .	(36)	(6)	1
Income tax (expense) benefit	27	11	2
Change in foreign currency exchange rate adjustment	1	(30)	4
Less:			
Reclassification adjustment for gains (losses) included in net income	(83)	(2)	2
Associated amortization of DAC, VOBA, DSI, DFEL and changes in other contract holder funds	—	1	—
Income tax (expense) benefit	29	—	(1)
Balance at end-of-year . . .	<u>\$ (15)</u>	<u>\$ (19)</u>	<u>\$ (9)</u>

Minimum Pension Liability

Adjustment

Balance at beginning-of-year	\$ —	\$ —	\$ (6)
Other comprehensive income (loss):			
Adjustment arising during the year	—	—	6
Balance at end-of-year . . .	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

Funded Status of Employee

Benefit Plans

Balance at beginning-of-year	\$ (4)	\$ 4	\$ —
Other comprehensive income (loss):			
Adjustment arising during the year	(45)	(13)	—
Income tax benefit	17	5	—
Adjustment for adoption of SFAS 158, net of tax	—	—	4
Balance at end-of-year . . .	<u>\$ (32)</u>	<u>\$ (4)</u>	<u>\$ 4</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

16. Realized Loss

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

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Total realized loss on investments and certain derivative instruments, excluding trading securities ⁽¹⁾	\$(850)	\$(114)	\$ (5)
Gain on certain reinsurance derivative/trading securities ⁽²⁾	5	2	4
Indexed annuity net derivative results ⁽³⁾ :			
Gross	13	(17)	(2)
Associated amortization expense of DAC, VOBA, DSI and DFEL	22	9	1
Guaranteed living benefits:			
Gross	2	(36)	(16)
Associated amortization expense of DAC, VOBA, DSI and DFEL	(23)	28	(19)
Guaranteed death benefits ⁽⁴⁾ :			
Associated amortization expense of DAC, VOBA, DSI and DFEL	<u>—</u>	<u>1</u>	<u>2</u>
Total realized (loss)	<u>\$(831)</u>	<u>\$(127)</u>	<u>\$(35)</u>

⁽¹⁾ See "Realized Loss Related to Investments" section in Note 5 for detail.

- ⁽²⁾ Represents changes in the fair value of total return swaps (embedded derivatives) related to various modified coinsurance and coinsurance with funds withheld reinsurance arrangements that have contractual returns related to various assets and liabilities associated with these arrangements. Changes in the fair value of these derivatives are offset by the change in fair value of trading securities in the portfolios that support these arrangements.
- ⁽³⁾ Represents the net difference between the change in the fair value of the S&P 500 call options that we hold and the change in the fair value of the embedded derivative liabilities of our indexed annuity products along with changes in the fair value of embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations applicable to future reset periods for our indexed annuity products as required under SFAS 133 and 157. The year ended December 31, 2008, includes a \$10 million gain from the initial impact of adopting SFAS 157.
- ⁽⁴⁾ Represents the change in the fair value of the derivatives used to hedge our GDB riders.

17. Underwriting, Acquisition, Insurance, Restructuring and Other Expenses

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

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Commissions	\$1,863	\$ 2,051	\$1,527
General and administrative expenses	1,282	1,246	1,093
DAC and VOBA deferrals and interest, net of amortization	(445)	(1,065)	(735)
Other intangibles amortization	4	4	3
Taxes, licenses and fees	200	192	158
Merger-related expenses	50	92	27
Total	<u>\$2,954</u>	<u>\$ 2,520</u>	<u>\$2,073</u>

All restructuring charges are included in underwriting, acquisition, insurance and other expenses within primarily Other Operations on our Consolidated Statements of Income in the year incurred and for the 2006 restructuring plan most

such charges are included within merger-related expenses in the table above.

2008 Restructuring Plan

Starting in December 2008, we implemented a restructuring plan in response to the current economic downturn and sustained market volatility, which focused on reducing expenses. These actions included the elimination of approximately 500 jobs across the Company. During the fourth quarter, we recorded a pre-tax charge of \$8 million and expect to record additional pre-tax charges of approximately \$7 million in 2009 for severance, benefits and related costs associated with the plan for workforce reduction and other restructuring actions. We expect to complete the plan by the end of 2009.

2006 Restructuring Plan

Upon completion of the merger with Jefferson-Pilot, we implemented a restructuring plan relating to the integration of our legacy operations with those of Jefferson-Pilot. The realignment will enhance productivity, efficiency and scalability while positioning us for future growth.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

17. Underwriting, Acquisition, Insurance, Restructuring and Other Expenses (continued)

Details underlying reserves for restructuring charges (in millions) were as follows:

	<u>Total</u>
Restructuring reserve at December 31, 2007	\$ 2
Amounts incurred in 2008	
Employee severance and termination benefits	2
Other	—
Total 2008 restructuring charges	2
Amounts expended in 2008	(3)
Restructuring reserve at December 31, 2008	<u>\$ 1</u>
Additional amounts expended in 2008 that do not qualify as restructuring charges	\$ 48
Total expected costs	190

Expected completion date: 4th Quarter 2009

The total expected costs include both restructuring charges and additional expenses that do not qualify as restructuring charges that are associated with the integration activities. Merger integration costs relating to employee severance and termination benefits of \$13 million were included in other liabilities on our Consolidated Balance Sheets in the purchase price allocation. In the first quarter of 2007, an additional \$9 million was recorded to goodwill and other liabilities as part of the final adjustment to the purchase price allocation related to employee severance and termination benefits.

18. Pension, Postretirement Health Care and Life Insurance Benefit Plans

LNC maintains qualified funded defined benefit pension plans in which many of our employees, including those of LNL, are participants. LNC also maintains non-qualified, unfunded defined benefit pension plans for certain employees, and certain employees and certain retired employees of acquired companies. In addition, for certain employees LNC has supplemental retirement plans that provide defined pension benefits in excess of limits imposed by federal tax law. All of LNC's U.S. defined benefit pension plans were "frozen" as of either December 31, 1994, or December 31, 2007, or earlier. For their frozen plans, there are no new participants and no future accruals of benefits from the date of the freeze.

The eligibility requirements for each plan are described in each plan document and vary for each plan based on completion of a specified period of continuous service or date of hire, subject to age limitations. The frozen pension plan benefits are calculated either on a traditional or cash balance formula. Those formulas are based upon years of credited service and eligible earnings as defined in each plan document. The traditional formula provides benefits stated in terms of a single life annuity payable at age 65. Under the cash balance formula benefits are stated as a lump sum hypothetical account balance. That account balance equals the sum of the employee's accumulated annual benefit credits plus interest credits. Benefit credits, which are based on years of service and base salary plus

bonus, ceased as of the date the plan was frozen. Interest Credits continue until the employee's benefit is paid.

LNC also sponsors voluntary employees' beneficiary association ("VEBA") trust that provides postretirement medical, dental and life insurance benefits to retired full-time employees and agents who, depending on the plan, have worked for us for 10 years and attained age 55 (age 60 for agents). VEBAs are a special type of tax-exempt trust used to provide employee benefits and also are subject to preferential tax treatment under the Internal Revenue Code. Medical and dental benefits are available to spouses and other eligible dependents of retired employees and agents. Retirees may be required to contribute toward the cost of these benefits. Eligibility and the amount of required contribution for these benefits varies based upon a variety of factors, including years of service and year of retirement. Effective January 1, 2008, the postretirement plan providing benefits to former employees of Jefferson-Pilot was amended such that only employees who had attained age 55 with a minimum of 10 years of service by December 31, 2007, and who later retire on or after age 60 with 15 years of service will be eligible to receive life insurance benefits when they retire.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

18. Pension, Postretirement Health Care and Life Insurance Benefit Plans (continued)

Obligations, Funded Status and Assumptions

Information (in millions) with respect to our defined benefit plan asset activity and defined benefit plan obligations was as follows:

	<i>As of and for the Years Ended December 31,</i>			
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
	<i>Pension Benefits</i>		<i>Other Postretirement Benefits</i>	
Change in Plan Assets				
Fair value at beginning-of-year	\$140	\$141	\$ —	\$ —
Actual return on plan assets	(31)	8	—	—
Company and participant contributions	—	(1)	2	2
Benefits paid	(8)	(8)	(2)	(2)
Fair value at end-of-year	<u>101</u>	<u>140</u>	<u>—</u>	<u>—</u>
Change in Benefit Obligation				
Balance at beginning-of-year	116	117	14	19
Interest cost	7	7	1	1
Plan participants' contributions	—	—	1	1
Actuarial (gains) losses	—	—	—	(4)
Benefits paid	(8)	(8)	(2)	(3)
Balance at end-of-year	<u>115</u>	<u>116</u>	<u>14</u>	<u>14</u>
Funded status of the plans	<u>\$ (14)</u>	<u>\$ 24</u>	<u>\$ (14)</u>	<u>\$ (14)</u>
Amounts Recognized on the Consolidated Balance Sheets				
Other assets	\$ 5	\$ 25	\$ —	\$ —
Other liabilities	(19)	(1)	(14)	(14)
Net amount recognized	<u>\$ (14)</u>	<u>\$ 24</u>	<u>\$ (14)</u>	<u>\$ (14)</u>
Amounts Recognized in Accumulated OCI, Net of Tax				
Net (gain) loss	\$ 35	\$ 8	\$ (3)	\$ (4)
Net amount recognized	<u>\$ 35</u>	<u>\$ 8</u>	<u>\$ (3)</u>	<u>\$ (4)</u>
Rate of Increase in Compensation				
Salary continuation plan	N/A	4.00%	N/A	0.00%
All other plans	N/A	4.00%	4.00%	4.00%
Weighted-Average Assumptions				
Benefit obligations:				
Weighted-average discount rate	6.00%	6.08%	6.00%	6.00%
Expected return on plan assets	8.00%	8.00%	6.50%	6.50%
Net periodic benefit cost:				
Weighted-average discount rate	6.00%	6.00%	6.00%	6.00%
Expected return on plan assets	8.00%	8.00%	6.50%	6.50%

Consistent with our benefit plans' year end, we use December 31 as the measurement date.

The expected return on plan assets was determined based on historical and expected future returns of the various asset classes, using the plan's target plan allocation. LNC reevaluates this assumption at an interim date each plan year. For 2009, our expected return on plan assets for the U.S. pension plan will be 8%.

The calculation of the accumulated postretirement 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) was as follows:

	<i>As of December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Health care cost trend rate	N/A	12%	12%
Pre-65 health care cost trend rate	10%	N/A	N/A
Post-65 health care cost trend rate	12%	N/A	N/A
Ultimate trend rate	5%	5%	5%
Year that the rate reaches the ultimate trend rate	2019	2018	2017

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

18. Pension, Postretirement Health Care and Life Insurance Benefit Plans (continued)

In order to improve the measurement of the health care trend rate with industry trends and practice, we separated our trend rate to assess the pre-65 and post-65 populations separately for the year ended December 31, 2008. LNC expects the health care cost trend rate for 2009 to be 10% for pre-65 and 13% for the post-65 population. The health care cost trend rate assumption is a key percentage that affects the amounts reported. A one-percentage point increase in assumed health care cost trend rates would have increased the accumulated postretirement benefit obligation by less than \$1 million and total service and interest cost components of less than \$1 million. A one-percentage point decrease in assumed health care cost trend rates would have decreased the accumulated postretirement benefit obligation by less than \$1 million and total service and interest cost components by less than \$1 million.

Information for our pension plans with an accumulated benefit obligation in excess of plan assets (in millions) was as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Accumulated benefit obligation	\$91	\$ 1
Projected benefit obligation	91	1
Fair value of plan assets	72	—

Components of Net Periodic Benefit Cost

The components of net defined benefit pension plan and postretirement benefit plan expense (in millions) were as follows:

	<i>For the Years Ended December 31,</i>					
	<i>Pension Benefits</i>			<i>Other Postretirement Benefits</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>
Interest cost	\$ 7	\$ 7	\$ 6	\$ 1	\$ 1	\$ 1
Expected return on plan assets	(11)	(11)	(9)	—	—	—
Recognized net actuarial (gain) loss	1	—	1	(1)	(1)	—
Net periodic benefit expense (recovery)	<u>\$ (3)</u>	<u>\$ (4)</u>	<u>\$ (2)</u>	<u>\$—</u>	<u>\$—</u>	<u>\$ 1</u>

For 2009, the estimated amount of amortization from accumulated OCI into net periodic benefit expense related to net actuarial (gains) losses is expected to be approximately a \$5 million loss for our pension benefit plan and approximately an \$1 million gain for our postretirement benefit plan.

Plan Assets

Our pension plan asset allocations by asset category based on estimated fair values were as follows:

	<i>As of December 31,</i>		<i>Target Allocation</i>
	<u>2008</u>	<u>2007</u>	
Domestic large cap equity	32%	37%	35%
International equity	14%	15%	15%
Fixed income securities	53%	48%	50%
Cash and cash equivalents	1%	0%	0%
Total	<u>100%</u>	<u>100%</u>	

The primary investment objective for the assets related to our U.S. defined benefit pension plan is for capital appreciation with an emphasis on avoiding undue risk. Investments can be made in various asset classes and styles, including, but not limited to: domestic and international equity, fixed income securities and other asset classes the investment managers deem prudent. Three- and five-year time horizons are utilized as there are inevitably short-run fluctuations, which will cause variations in investment performance.

Our defined benefit plan assets have been combined into a master retirement trust where a variety of qualified managers, with Northern Trust as the manager of managers, are expected to rank in the upper 50% of similar funds over the three-year periods and above an appropriate index over five-year periods. Managers

are monitored for adherence to approved investment policy guidelines, changes in material factors and legal or regulatory actions. Managers not meeting these criteria will be subject to additional due diligence review, corrective action or possible termination.

We currently target asset weightings as follows: domestic equity allocations (32%) are split into large cap growth (14%), large cap value (14%) and small cap (4%); international equity; and fixed income allocations are weighted between core fixed income and long-term bonds. The performance of the pension trust assets is monitored on a quarterly basis relative to the plan's objectives. The performance of the trust is measured against the following indices: Russell 1000 Index; Morgan Stanley Capital International Europe, Australia and Far East Index; and Lehman Brothers Aggregate Bond Index. We review this investment policy on an annual basis.

Prior to 2007, our plan assets were principally managed by LNC's Investment Management segment. During the last quarter of 2007, the management of the equity portion of these plan assets was transferred to third-party managers. LNC's Investment Management segment continues to manage the plan's fixed income securities, which comprise approximately 50% of plan assets.

Plan Cash Flows

It is LNC's practice to make contributions to the qualified pension plans to comply with minimum funding requirements of the Employee Retirement Income Security Act of 1974, as amended. In accordance with such practice, no contributions were made nor required for the years ended December 31, 2008 or 2007. No contributions are required nor expected to be made in 2009.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

18. Pension, Postretirement Health Care and Life Insurance Benefit Plans (continued)

LNC expects the following benefit payments (in millions):

	<i>Pension Plans</i>		<i>Postretirement Plans</i>	
	<i>U.S. Defined Benefit Pension Plans</i>	<i>Reflecting Medicare Part D Subsidy</i>	<i>Medicare Part D Subsidy</i>	<i>Not Reflecting Medicare Part D Subsidy</i>
2009	\$8	\$2	\$—	\$2
2010	9	2	—	2
2011	9	2	—	2
2012	9	2	—	2
2013	9	2	—	2
Following Five Years				
Thereafter	46	6	(1)	7

19. 401(k), Money Purchase and Profit Sharing Plans

LNC sponsors a contributory defined contribution plan or a 401(k) plan for our eligible employees, including those of LNL. LNL sponsors a number of contributory defined plans for agents only. These plans include a 401(k) plan for eligible agents and a defined contribution money purchase plan for eligible agents of the former Jefferson-Pilot. LNL also sponsor a money purchase plan for LNL agents that was frozen in 2004.

LNC or LNL makes contributions and matching contributions to each of the active plans in accordance with the plan document and various limitations under Section 401(a) of the Internal Revenue Code of 1986, as amended.

The expenses (in millions) for the 401(k) and profit sharing plans were as follows:

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Total expenses for the 401(k) and profit sharing plans	\$54	\$31	\$22

Deferred Compensation Plans

LNC sponsors separate non-qualified unfunded, deferred compensation plans for certain of our employees, including those of LNL. LNL sponsors non-qualified unfunded, deferred compensation plan for certain agents.

Liabilities (in millions) with respect to these deferred compensation plans were as follows:

	<i>As of December 31,</i>	
	<i>2008</i>	<i>2007</i>
Total liabilities	\$132	\$137

The Deferred Compensation Plan for Certain U.S. Employees

Certain U.S. employees may participate in the Deferred Compensation & Supplemental/Excess Retirement Plan (the “DC SERP”). All participants may elect to defer payment of a portion of their compensation as defined by the plan. DC SERP

participants may select from a menu of “phantom” investment options (identical to those offered under our qualified savings plans) used as investment measures for calculating the investment return notionally credited to their deferrals. Under the terms of the DC SERP, LNC agrees to pay out amounts based upon the aggregate performance of the investment measures selected by the participant. LNC makes matching contributions to these plans based upon amounts placed into the deferred compensation plans by individuals after participants have exceeded applicable limits of the Internal Revenue Code. The amount of our contribution is calculated in accordance with the plan document, which is similar to our 401(k) plans. Expenses (in millions) for this plan were as follows:

	<i>For the Years Ended December 31,</i>		
	<i>2008</i>	<i>2007</i>	<i>2006</i>
Employer matching contributions	\$5	\$ 1	\$ 4
Increase in measurement of liabilities, net of LNC total return swap	<u>1</u>	<u>10</u>	<u>13</u>
Total DC SERP expenses	<u>\$6</u>	<u>\$11</u>	<u>\$17</u>

The terms of the DC SERP provide that plan participants who select our stock as the measure for their investment return will receive shares of LNC stock in settlement of this portion of their accounts at the time of distribution. In addition, participants are precluded from diversifying any portion of their deferred compensation plan account that has been credited to the stock unit fund. Consequently, changes in value of our stock do not affect the expenses associated with this portion of the deferred compensation plan.

Deferred Compensation Plans for Certain Agents

LNL also sponsors a deferred compensation plan for certain eligible agents. Plan participants receive contributions based on their earnings. Plan participants may select from a menu of “phantom” investment options used as investment measures for calculating the investment return notionally credited to their deferrals. Under the terms of these plans, LNC agrees to

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

19. 401(k), Money Purchase and Profit Sharing Plans (continued)

pay out amounts based upon the aggregate performance of the investment measures selected by the participant. LNL agents invest in phantom investments that mirror those offered to qualified plan participants. Jefferson-Pilot agents invest in a different line up of "phantom" investments. Expenses (in millions) for this plan were as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Employer matching contributions	\$2	\$3	\$—
Increase in measurement of liabilities, net of LNC total return swap	<u>2</u>	<u>5</u>	<u>8</u>
Total expenses for certain agents	<u>\$4</u>	<u>\$8</u>	<u>\$ 8</u>

20. Stock-Based Incentive Compensation Plans

Our employees are included in LNC's various incentive plans that provide for the issuance of stock options, stock incentive awards, SARs, restricted stock awards, performance shares (performance-vested shares as opposed to time-vested shares) and deferred stock units – also referred to as "restricted stock units." LNC has a policy of issuing new shares to satisfy option exercises.

Total compensation expense (in millions) for all of our stock-based incentive compensation plans was as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Stock options	\$ 8	\$10	\$ 3
Shares	2	3	19
Cash awards	—	—	1
SARs	4	5	(1)
Restricted stock	<u>5</u>	<u>6</u>	<u>1</u>
Total	<u>\$19</u>	<u>\$24</u>	<u>\$23</u>
Recognized tax benefit	\$ 7	\$ 8	\$ 8

21. Statutory Information and Restrictions

We prepare financial statements in accordance with statutory accounting principles ("SAP") prescribed or permitted by the insurance departments of our states of domicile, which may vary materially from GAAP. Prescribed SAP includes the Accounting Practices and Procedures Manual of the National Association of Insurance Commissioners ("NAIC") as well as state laws, regulations and administrative rules. Permitted SAP encompasses all accounting practices not so prescribed. The principal differences between statutory financial statements and financial statements prepared in accordance with GAAP are that statutory financial statements do not reflect DAC, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, contract holder liabilities are generally valued using more conservative assumptions and certain assets are non-admitted.

Specified statutory information (in millions) was as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Capital and surplus	\$4,600	\$5,000

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Net income (loss)	\$(261)	\$971	\$299
Dividends to LNC	400	770	568

The decline in statutory net income in 2008 from that of 2007 was primarily due to a significant increase in realized losses on investments combined with reserve strain due to deteriorating market conditions throughout 2008.

Our states of domicile, Indiana for LNL and New York for LLANY, have adopted certain prescribed accounting practices that differ from those found in NAIC SAP. These prescribed practices are the use of continuous Commissioners Annuity Reserve Valuation Method ("CARVM") in the calculation of reserves as prescribed by the state of New York and the calculation of reserves on universal life policies based on the Indiana universal life method as prescribed by the state of Indiana. We also have several accounting practices permitted by the states of domicile that differ from those found in NAIC SAP. Specifically, these are the use of a more conservative valuation interest rate on certain annuities as of December 31, 2008 and 2007, the use of less conservative mortality tables on certain life insurance

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

21. Statutory Information and Restrictions (continued)

products as of December 31, 2008, and a less conservative standard in determining the admitted amount of deferred tax assets as of December 31, 2008. The effects on statutory surplus compared to NAIC statutory surplus from the use of these prescribed and permitted practices (in millions) were as follows:

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Calculation of reserves using the Indiana universal life method	\$289	\$246
Calculation of reserves using continuous CARVM	(10)	(10)
Conservative valuation rate on certain variable annuities	(12)	(14)
Less conservative mortality tables on certain life insurance products	16	—
Less conservative standard in determining the amount of deferred tax assets	298	—

A new statutory reserving standard (commonly called "VACARVM") has been developed by the NAIC replacing current statutory reserve practices for variable annuities with guaranteed benefits, such as GWBs. The effective date for VACARVM is December 31, 2009. Based upon the level of variable annuity account values as of December 31, 2008, we estimate that VACARVM would have decreased our statutory capital by \$125 to \$175 million. The actual impact of the adoption will be dependent upon account values and conditions that exist as of December 31, 2009. We plan to utilize existing affiliate reinsurance structures, as well as pursue additional

third-party reinsurance arrangements, to lessen any negative impact on statutory capital and dividend capacity. However, additional statutory reserves could lead to lower risk-based capital ("RBC") ratios and potentially reduce future dividend capacity from our insurance subsidiaries.

We are subject to certain insurance department regulatory restrictions as to the transfer of funds and the payment of dividends to the holding company. Under Indiana laws and regulations, LNL may pay dividends to LNC within the statutory limitations without prior approval of the Indiana Insurance Commissioner (the "Commissioner"). The current statutory limitation is the greater of 10% of the insurer's policyholders' surplus, as shown on its last annual statement on file with the Commissioner or the insurer's statutory net gain from operations for the previous twelve months. If a proposed dividend, along with all other dividends paid within the preceding twelve consecutive months exceeds the statutory limitation, LNL must receive prior approval of the Commissioner to pay such dividend. Indiana law gives the Commissioner broad discretion to disapprove requests for dividends in excess of these limits. LNC is also the holder of surplus notes issued by LNL. The payment of principal and interest on the surplus notes to LNC must be approved by the Commissioner as well. LLANY is subject to similar, but not identical, regulatory restrictions as LNL with regard to the transfer of funds and the payment of dividends. We expect we could pay dividends of approximately \$500 million in 2009 without prior approval from the respective insurance commissioners. However, if current conditions do not improve we believe this dividend capacity will decline.

22. Fair Value of Financial Instruments

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

	<i>As of December 31,</i>			
	<u>2008</u>		<u>2007</u>	
	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>
Assets				
Available-for-sale securities:				
Fixed maturities	\$ 46,489	\$ 46,489	\$ 53,405	\$ 53,405
Equity	139	139	134	134
Trading securities	2,189	2,189	2,533	2,533
Mortgage loans on real estate	7,396	7,116	7,117	7,291
Derivative instruments	60	60	172	172
Other investments	948	948	986	986
Cash and invested cash	2,594	2,594	1,395	1,395
Liabilities				
Future contract benefits:				
Remaining guaranteed interest and similar contracts	(252)	(252)	(619)	(619)
Embedded derivative instruments — living benefits (liabilities) contra liabilities	(2,904)	(2,904)	(229)	(229)
Other contract holder funds:				
Account value of certain investment contracts	(21,893)	(22,338)	(21,173)	(20,515)
Reinsurance related derivative assets (liabilities)	167	167	(102)	(102)
Short-term debt	(4)	(4)	(173)	(173)
Long-term debt	(2,080)	(1,503)	(1,675)	(1,569)
Off-Balance-Sheet				
Guarantees	—	(1)	—	(2)

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

22. Fair Value of Financial Instruments (continued)

See Note 1 for discussion of the methodologies and assumptions used to determine the fair value of financial instruments carried at fair value. The following discussion outlines the methodologies and assumptions used to determine the fair value of our financial instruments not carried at fair value. Considerable judgment is required to develop these assumptions used to measure fair value. Accordingly, the estimates shown are not necessarily indicative of the amounts that would be realized in a one-time, current market exchange of all of our financial instruments.

Mortgage Loans on Real Estate

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

Other Investments and Cash and Invested Cash

The carrying value of our assets classified as other investments and cash and invested cash on our Consolidated Balance Sheets approximates their fair value. Other investments include limited partnership and other privately held investments that are accounted for using the equity method of accounting.

Future Contract Benefits and Other Contract Holder Funds

Future contract benefits and other contract holder funds on our Consolidated Balance Sheets include account values of

investment contracts and certain guaranteed interest contracts. The fair value of the investment contracts is based on their approximate surrender value at the balance sheet date. The fair value for the remaining guaranteed interest and similar contracts are estimated using discounted cash flow calculations at the balance sheet date. These calculations are based on interest rates currently offered on similar contracts with maturities that are consistent with those remaining for the contracts being valued.

Short-term and Long-term Debt

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

Guarantees

Our guarantees relate to 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 mortgage loan pass-through certificates is insignificant.

Financial Instruments Carried at Fair Value

See "Summary of Significant Accounting Policies" in Note 1 and "SFAS 157 – Fair Value Measurements" in Note 2 for discussions of the methodologies and assumptions used to determine the fair value of our financial instruments carried at fair value.

The following summarizes our financial instruments carried at fair value (in millions) on a recurring basis by the SFAS 157 fair value hierarchy levels described in Note 2:

	<i>As of December 31, 2008</i>			
	<i>Quoted Prices in Active Markets for Identical Assets (Level 1)</i>	<i>Significant Observable Inputs (Level 2)</i>	<i>Significant Unobservable Inputs (Level 3)</i>	<i>Total Fair Value</i>
Assets				
Investments:				
Available-for-sale securities:				
Fixed maturities	\$220	\$ 42,977	\$ 3,292	\$ 46,489
Equity	41	5	93	139
Trading securities	2	2,110	77	2,189
Derivative instruments	—	(18)	78	60
Cash and invested cash	—	2,594	—	2,594
Separate account assets	—	55,655	—	55,655
Reinsurance related derivative assets	—	167	—	167
Total assets	<u>\$263</u>	<u>\$103,490</u>	<u>\$ 3,540</u>	<u>\$107,293</u>
Liabilities				
Future contract benefits:				
Remaining guaranteed interest and similar contracts	\$ —	\$ —	\$ (252)	\$ (252)
Embedded derivative instruments — living benefits liabilities	—	—	(2,904)	(2,904)
Total liabilities	<u>\$ —</u>	<u>\$ —</u>	<u>\$(3,156)</u>	<u>\$ (3,156)</u>

We did not have any assets or liabilities measured at fair value on a non-recurring basis as of December 31, 2008.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

22. Fair Value of Financial Instruments (continued)

The following table summarizes changes to our financial instruments carried at fair value (in millions) and classified within Level 3 of the fair value hierarchy. This information excludes any impact of amortization on DAC, VOBA, DSI and DFEL. When a determination is made to classify an asset or liability within Level 3 of the fair value hierarchy, the determination is based upon the significance of the unobservable inputs to the overall fair value measurement. Certain securities trade in less liquid or illiquid markets with limited or no

pricing information, and the determination of fair value for these securities is inherently more difficult. However, Level 3 fair value investments may include, in addition to the unobservable or Level 3 inputs, observable components (that is, components that are actively quoted or can be validated to market-based sources). The gains and losses in the table below may include changes in fair value due in part to observable inputs that are a component of the valuation methodology.

<i>For the Year Ended December 31, 2008</i>						
<i>Beginning</i>	<i>Items</i>	<i>Gains</i>	<i>Sales,</i>	<i>Transfers</i>	<i>Ending</i>	
<i>Fair</i>	<i>Included</i>	<i>(Losses)</i>	<i>Issuances,</i>	<i>In or</i>	<i>Fair</i>	
<i>Value</i>	<i>in</i>	<i>in</i>	<i>Maturities,</i>	<i>Out of</i>	<i>Value</i>	
<i>Value</i>	<i>Net</i>	<i>OCI</i>	<i>Settlements,</i>	<i>Level 3,</i>	<i>Value</i>	
<i>Value</i>	<i>Income</i>	<i>OCI</i>	<i>Calls,</i>	<i>Net⁽¹⁾</i>	<i>Value</i>	
<i>Value</i>	<i>Income</i>	<i>OCI</i>	<i>Net</i>	<i>Net⁽¹⁾</i>	<i>Value</i>	
Investments:						
Available-for-sale securities:						
Fixed maturities	\$4,325	\$ (170)	\$(1,199)	\$ 52	\$284	\$ 3,292
Equity	54	(30)	(17)	86	—	93
Trading securities	107	(28)	—	(13)	11	77
Derivative instruments	195	(237)	29	91	—	78
Future contract benefits:						
Remaining guaranteed interest and similar contracts	(389)	37	—	100	—	(252)
Embedded derivative instruments — living benefits liabilities	(279)	(2,476)	—	(149)	—	(2,904)
Total, net	<u>\$4,013</u>	<u>\$(2,904)</u>	<u>\$(1,187)</u>	<u>\$ 167</u>	<u>\$295</u>	<u>\$ 384</u>

⁽¹⁾ Transfers in or out of Level 3 for available-for-sale and trading securities are displayed at amortized cost at the beginning of the period. For available-for-sale and trading securities, the difference between beginning of period amortized cost and beginning of period fair value was included in OCI and earnings, respectively, in prior periods.

The following table provides the components of the items included in net income, excluding any impact of amortization on DAC, VOBA, DSI and DFEL and changes in future contract benefits, (in millions) as reported in the table above:

<i>For the Year Ended December 31, 2008</i>					
<i>(Amortization)</i>	<i>Other-</i>	<i>Gains</i>	<i>Unrealized</i>	<i>Total</i>	
<i>Accretion,</i>	<i>Than-</i>	<i>(Losses)</i>	<i>Holding</i>	<i>Gains</i>	
<i>Net</i>	<i>Temporary</i>	<i>from Sales,</i>	<i>Gains</i>	<i>(Losses)⁽³⁾</i>	
<i>Net</i>	<i>Impairment</i>	<i>Maturities,</i>	<i>(Losses)⁽³⁾</i>	<i>(Losses)⁽³⁾</i>	
<i>Net</i>	<i>Impairment</i>	<i>Settlements,</i>	<i>(Losses)⁽³⁾</i>	<i>(Losses)⁽³⁾</i>	
<i>Net</i>	<i>Impairment</i>	<i>Calls</i>	<i>(Losses)⁽³⁾</i>	<i>(Losses)⁽³⁾</i>	
Investments:					
Available-for-sale securities:					
Fixed maturities ⁽¹⁾	\$ 2	\$(168)	\$ (4)	\$ —	\$ (170)
Equity	—	(31)	1	—	(30)
Trading securities ⁽¹⁾	2	(7)	—	(23)	(28)
Derivative instruments ⁽²⁾	—	—	(108)	(129)	(237)
Future contract benefits:					
Remaining guaranteed interest and similar contracts ⁽²⁾	—	—	14	23	37
Embedded derivative instruments — living benefits liabilities ⁽²⁾	—	—	8	(2,484)	(2,476)
Total, net	<u>\$ 4</u>	<u>\$(206)</u>	<u>\$ (89)</u>	<u>\$(2,613)</u>	<u>\$(2,904)</u>

⁽¹⁾ Amortization and accretion, net and unrealized holding losses are included in net investment income on our Consolidated Statements of Income. All other amounts are included in realized loss on our Consolidated Statements of Income.

⁽²⁾ All amounts are included in realized loss on our Consolidated Statements of Income.

⁽³⁾ This change in unrealized gains or losses relates to assets and liabilities that we still held as of December 31, 2008.

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

22. Fair Value of Financial Instruments (continued)

The fair value of available-for-sale fixed maturity securities (in millions) classified within Level 3 of the fair value hierarchy was as follows:

	<i>As of December 31, 2008</i>	
	<i>Fair Value</i>	<i>% of Total Fair Value</i>
Corporate bonds	\$2,180	66.4%
Asset-backed securities	261	7.9%
Commercial mortgage-backed securities	238	7.2%
Collateralized mortgage obligations . .	157	4.8%
Mortgage pass-through securities . . .	21	0.5%
Municipals	106	3.2%
Government and government agencies	235	7.1%
Redeemable preferred stock	94	2.9%
Total available-for-sale fixed maturity securities	<u>\$3,292</u>	<u>100.0%</u>

	<i>As of December 31, 2007</i>	
	<i>Fair Value</i>	<i>% of Total Fair Value</i>
Corporate bonds	\$2,099	48.5%
Asset-backed securities	1,097	25.4%
Commercial mortgage-backed securities	382	8.8%
Collateralized mortgage obligations . .	295	6.8%
Mortgage pass-through securities . . .	31	0.7%
Municipals	132	3.1%
Government and government agencies	258	6.0%
Redeemable preferred stock	31	0.7%
Total available-for-sale fixed maturity securities	<u>\$4,325</u>	<u>100.0%</u>

23. Segment Information

On July 21, 2008, we announced the realignment of our segments under our former Employer Markets and Individual Markets operating businesses into two new operating businesses – Retirement Solutions and Insurance Solutions. We believe the new structure more closely aligns with consumer needs and should lead to more coordinated product development and greater effectiveness across the enterprise. The segment changes are in accordance with the provisions of SFAS No. 131, “Disclosures about Segments of an Enterprise and Related Information,” and reflect the manner in which we are organized for purposes of making operating decisions and assessing performance. Accordingly, we have restated results from prior periods in a consistent manner with our realigned segments.

Under our newly realigned segments, we report the results of the Executive Benefits business, which as of June 30, 2008, was part of the Retirement Products segment, in the Life Insurance segment. We do not view these changes to our segment reporting as material to our consolidated financial statements.

We provide products and services in two operating businesses: Retirement Solutions and Insurance Solutions, and report results through four business segments. We also have Other Operations, which includes the financial data for operations that are not directly related to the business segments. Our reporting segments reflect the manner by which our chief operating decision makers view and manage the business. The following is a brief description of these segments and Other Operations.

Retirement Solutions

The Retirement Solutions business provides its products through two segments: Annuities and Defined Contribution. The Retirement Solutions – Annuities segment provides tax-deferred investment growth and lifetime income opportunities for its clients by offering individual fixed annuities, including

indexed annuities and variable annuities. The Retirement Solutions – Defined Contribution segment provides employer-sponsored variable and fixed annuities and mutual-fund based programs in the 401(k), 403(b) and 457 marketplaces.

Insurance Solutions

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

Other Operations

Other Operations includes investments related to excess capital and other corporate investments, benefit plan net assets, the unamortized deferred gain on indemnity reinsurance, which was sold to Swiss Re in 2001, external debt and business sold through reinsurance. Other Operations also includes the Institutional Pension business, which was previously reported in Employer Markets – Retirement Products prior to our segment realignment. The Institutional Pension business is a closed-block of pension business, the majority of which was sold on a group annuity basis, and is currently in run-off.

Beginning with the quarter ended June 30, 2008, we changed our definitions of segment operating revenues and income from operations to better reflect: the underlying economics of

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

23. Segment Information (continued)

our variable and indexed annuities that employ derivative instruments to hedge policy benefits; and the manner in which management evaluates that business. Our change in the definition of income from operations is primarily the result of our adoption of SFAS 157 during the first quarter of 2008 (see Note 2). Under the fair value measurement provisions of SFAS 157, we are required to measure the fair value of these annuities from an "exit price" perspective, (i.e., the exchange price between market participants to transfer the liability). We, therefore, must include margins that a market participant buyer would require as well as a factor for non-performance risk related to our credit quality. We do not believe that these factors relate to the economics of the underlying business and do not reflect the manner in which management evaluates the business. The items that are now excluded from our operating results that were previously included are as follows: GLB net derivatives results; indexed annuity forward-starting option; and GDB derivatives results. For more information regarding this change, see LNC's current report on Form 8-K dated July 16, 2008.

We continue to exclude the effects of any realized loss on investments from segment operating revenues and income from operations as we believe that such items are not necessarily indicative of current operating fundamentals or future performance of the business segments, and, in many instances, decisions regarding these items do not necessarily relate to the operations of the individual segments.

We believe that our new definitions of operating revenues and income (loss) from operations will provide investors with a more valuable measure of our performance because it better reveals trends in our business.

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

- Realized gains and losses associated with the following ("excluded realized loss"):
 - Sale or disposal of securities;
 - Impairments of securities;
 - Change in the fair value of embedded derivatives within certain reinsurance arrangements and the change in the fair value of related trading securities;
 - Change in the fair value of the embedded derivatives of our GLBs within our variable annuities net of the change in the fair value of the derivatives we own to hedge the changes in the embedded derivative;
 - Net difference between the benefit ratio unlocking of SOP 03-1 reserves on our GDB riders within our variable annuities and the change in the fair value of the derivatives excluding our expected cost of purchasing the hedging instruments; and
 - Changes in the fair value of the embedded derivative liabilities related to index call options we may purchase in the future to hedge contract holder index allocations

applicable to future reset periods for our indexed annuity products as required under SFAS 133 and 157.

- Income (loss) from the initial adoption of changes in accounting principles;
- Income (loss) from reserve changes (net of related amortization) on business sold through reinsurance;

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

- Excluded realized gain (loss);
- Amortization of deferred gains arising from the reserve changes on business sold through reinsurance; and
- Revenue adjustments from the initial impact of the adoption of changes in accounting principles.

Operating revenues and income (loss) from operations do not replace revenues and net income as the GAAP measures of our consolidated results of operations.

Segment information (in millions) was as follows:

	<i>For the Years Ended December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Revenues			
Operating revenues:			
Retirement Solutions:			
Annuities	\$2,191	\$2,277	\$1,878
Defined Contribution ..	913	968	981
Total Retirement Solutions	<u>3,104</u>	<u>3,245</u>	<u>2,859</u>
Insurance Solutions:			
Life Insurance	3,994	3,963	3,394
Group Protection	1,640	1,500	1,032
Total Insurance Solutions	<u>5,634</u>	<u>5,463</u>	<u>4,426</u>
Other Operations	435	474	466
Excluded realized gain (loss), pre-tax	(868)	(137)	(43)
Amortization of deferred gain arising from reserve changes on business sold through reinsurance, pre-tax	<u>3</u>	<u>9</u>	<u>1</u>
Total revenues	<u>\$8,308</u>	<u>\$9,054</u>	<u>\$7,709</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

23. Segment Information (continued)

	<i>As of December 31,</i>	
	<u>2008</u>	<u>2007</u>
Assets		
Retirement Solutions:		
Annuities	\$ 65,206	\$ 81,112
Defined Contribution	<u>22,930</u>	<u>30,180</u>
Total Retirement Solutions	<u>88,136</u>	<u>111,292</u>
Insurance Solutions:		
Life Insurance	46,588	45,867
Group Protection	<u>2,482</u>	<u>1,471</u>
Total Insurance Solutions	<u>49,070</u>	<u>47,338</u>
Other Operations	<u>10,845</u>	<u>15,696</u>
Total	<u>\$148,051</u>	<u>\$174,326</u>

24. Supplemental Disclosures of Cash Flow Information

The following summarizes our supplemental cash flow data (in millions):

	<i>For the Years Ended</i>		
	<i>December 31,</i>		
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Interest paid	\$ 81	\$ 104	\$ 85
Income taxes paid (received) . .	(23)	194	310
Significant non-cash investing and financing transactions:			
Business combinations:			
Fair value of assets			
acquired (includes cash and invested cash)	\$ —	\$ 41	\$ 37,356
Fair value of liabilities			
assumed	—	(50)	(30,424)
Total purchase price . .	<u>\$ —</u>	<u>\$ (9)</u>	<u>\$ 6,932</u>
Dividend of FPP:			
Carrying value of assets (includes cash and invested cash)			
	\$ —	\$ 2,772	\$ —
Carrying value of liabilities			
	—	(2,280)	—
Total dividend of FPP . .	<u>\$ —</u>	<u>\$ 492</u>	<u>\$ —</u>
Reinsurance ceded to LNBAR:			
Carrying value of assets . .	\$ 360	\$ —	\$ —
Carrying value of liabilities	<u>(360)</u>	—	—
Total reinsurance ceded to LNBAR	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

The Lincoln National Life Insurance Company

Notes to Consolidated Financial Statements (continued)

25. Transactions with Affiliates

Transactions with affiliates (in millions) recorded on our consolidated financial statements were as follows:

	<i>As of December 31,</i>		
	<u>2008</u>	<u>2007</u>	
Assets with affiliates:			
Corporate bonds ⁽¹⁾	\$ 115	\$ 221	
Reinsurance on ceded reinsurance contracts ⁽²⁾	152	109	
Cash management agreement investment ⁽³⁾	478	420	
Service agreement receivable ⁽³⁾	(13)	(9)	
Liabilities with affiliates:			
Reinsurance future contract benefits on ceded reinsurance contracts ⁽⁴⁾	4,688	1,257	
Inter-company short-term debt ⁽⁵⁾	4	173	
Inter-company long-term debt ⁽⁶⁾	1,841	1,688	
<i>For the Years Ended</i>			
<i>December 31,</i>			
	<u>2008</u>	<u>2007</u>	<u>2006</u>
Revenues with affiliates:			
Premiums paid on ceded reinsurance contracts ⁽⁷⁾	\$(222)	\$(308)	\$(234)
Net investment income on cash management agreement ⁽⁸⁾	11	28	14
Fees for management of general account ⁽⁸⁾	(65)	(62)	(57)
Benefits and expenses with affiliates:			
Reinsurance (recoveries) benefits on ceded reinsurance contracts ⁽⁹⁾	(655)	(337)	16
Service agreement payments ⁽¹⁰⁾	100	99	59
Transfer pricing arrangement ⁽¹⁰⁾	(32)	(38)	(36)
Interest expense on inter-company debt ⁽¹¹⁾	83	82	82

- (1) Reported in fixed maturity available-for-sale securities on our Consolidated Balance Sheets.
- (2) Reported in reinsurance related derivative assets (liability) on our Consolidated Balance Sheets.
- (3) Reported in other assets on our Consolidated Balance Sheets.
- (4) Reported in future contract benefits on our Consolidated Balance Sheets.
- (5) Reported in short-term debt on our Consolidated Balance Sheets.
- (6) Reported in long-term debt on our Consolidated Balance Sheets.
- (7) Reported in insurance premiums on our Consolidated Statements of Income.
- (8) Reported in net investment income on our Consolidated Statement of Income.

- (9) Reported in benefits on our Consolidated Statements of Income.
- (10) Reported in underwriting, acquisition, insurance and other expenses on our Consolidated Statements of Income.
- (11) Reported in interest and debt expense on our Consolidated Statements of Income.

Corporate Bonds

LNC issues corporate bonds to us for a predetermined face value to be repaid by LNC at a predetermined maturity with a specified interest rate. We purchase these investments for our segmented portfolios that have yield, duration and other characteristics that take into account the liabilities being supported.

Cash Management Agreement

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

Service Agreement

In accordance with service agreements with LNC and other subsidiaries of LNC for personnel and facilities usage, general management services and investment management services, we receive services from and provide services to affiliated companies and also receive an allocation of corporate overhead from LNC. Corporate overhead expenses are assigned based on specific methodologies for each function. The majority of the expenses are assigned based on the following methodologies: assets by product, assets under management, weighted number of policy applications, weighted policies in force, and sales.

Transfer Pricing Arrangement

A transfer pricing arrangement is in place between LFD and Delaware Management Holdings, Inc. ("DMH"), a wholly owned subsidiary of LNC, related to the wholesaling of DMH's investment products.

Fees for Management of General Account

DMH is responsible for the management of our general account investments.

Ceded Reinsurance Contracts

As discussed in Note 9, we cede and accept reinsurance from affiliated companies. We cede certain Guaranteed Benefit risks (including certain GDB and GWB benefits) to Lincoln National Reinsurance Company (Barbados) Ltd. ("LNR Barbados"). We also cede reserves related to certain risks for certain UL policies, which resulted from recent actuarial reserving guidelines.

As discussed in Note 6, we cede to LNBAR the risk under certain UL contracts for no-lapse benefit guarantees.

Notes to Consolidated Financial Statements (continued)

25. Transactions with Affiliates (continued)

Substantially all reinsurance ceded to affiliated companies is with unauthorized companies. To take a reserve credit for such reinsurance, we hold assets from the reinsurer, including funds held under reinsurance treaties, and are the beneficiary on letters of credit aggregating \$1.7 billion and \$1.4 billion at December 31, 2008 and 2007, respectively. The letters of credit are issued by banks and represent guarantees of performance under the reinsurance agreement, and are guaranteed by LNC.