LINCOLN NATIONAL CORP
Form 10-Q
August 02, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2012
OR

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

For the transition period from to

Commission File Number: 1-6028

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

Indiana (State or other jurisdiction of incorporation or organization)	35-1140070 (I.R.S. Employer Identification No.)
150 N. Radnor Chester Road, Suite A305, Radnor, Pennsylvania (Address of principal executive offices)	19087 (Zip Code)

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

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

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

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

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

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

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

As of July 31, 2012, there were 279,173,774 shares of the registrant’s common stock outstanding.

Lincoln National Corporation

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

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

	As of June 30, 2012 (Unaudited)	As of December 31, 2011
ASSETS		
Investments:		
Available-for-sale securities, at fair value:		
Fixed maturity securities (amortized cost: 2012 - $71,394; 2011 - $68,988)	$ 79,191	$ 75,433
Variable interest entities' fixed maturity securities (amortized cost: 2012 - $675; 2011 - $673)	705	700
Equity securities (cost: 2012 - $143; 2011 - $135)	154	139
Trading securities	2,649	2,675
Mortgage loans on real estate	6,804	6,942
Real estate	116	137
Policy loans	2,829	2,884
Derivative investments	3,399	3,151
Other investments	1,041	1,069
Total investments	96,888	93,130
Cash and invested cash	5,257	4,510
Deferred acquisition costs and value of business acquired	6,505	6,776
Premiums and fees receivable	388	408
Accrued investment income	1,021	981
Reinsurance recoverables	6,601	6,526
Funds withheld reinsurance assets	863	874
Goodwill	2,273	2,273
Other assets	2,475	2,536
Separate account assets	88,839	83,477
Total assets	$ 211,110	$ 201,491
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities		
Future contract benefits	$ 19,930	$ 19,813
Other contract holder funds	70,422	69,466
Short-term debt	300	300
Long-term debt	5,719	5,391
Reinsurance related embedded derivatives	185	168
Funds withheld reinsurance liabilities	999	1,045
Deferred gain on business sold through reinsurance	356	394
Payables for collateral on investments	5,070	3,733
Variable interest entities' liabilities	158	193
Other liabilities	4,950	4,273
Separate account liabilities	88,839	83,477
Total liabilities	196,928	188,253

Contingencies and Commitments (See Note 8)

Stockholders' Equity		
Preferred stock - 10,000,000 shares authorized; Series A - 9,632 and 10,072 shares issued and outstanding as of June 30, 2012, and December 31, 2011, respectively	-	-
Common stock - 800,000,000 shares authorized; 279,168,971 and 291,319,222 shares issued and outstanding as of June 30, 2012, and December 31, 2011, respectively	7,310	7,590
Retained earnings	3,493	2,969
Accumulated other comprehensive income (loss)	3,379	2,679
Total stockholders' equity	14,182	13,238
Total liabilities and stockholders' equity	$ 211,110	$ 201,491

See accompanying Notes to Consolidated Financial Statements

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Revenues				
Insurance premiums	$ 630	$ 594	$ 1,219	$ 1,162
Insurance fees	887	900	1,794	1,718
Net investment income	1,197	1,181	2,362	2,372
Realized gain (loss):				
Total other-than-temporary impairment losses on securities	(50)	(47)	(147)	(91)
Portion of loss recognized in other comprehensive income	17	16	67	19
Net other-than-temporary impairment losses on securities recognized in earnings	(33)	(31)	(80)	(72)
Realized gain (loss), excluding other-than-temporaryimpairment losses on securities	76	22	37	65
Total realized gain (loss)	43	(9)	(43)	(7)
Amortization of deferred gain on business sold through reinsurance	18	19	38	37
Other revenues and fees	124	122	244	244
Total revenues	2,899	2,807	5,614	5,526
Expenses				
Interest credited	616	625	1,241	1,239
Benefits	945	1,027	1,804	1,862
Commissions and other expenses	828	674	1,684	1,443
Interest and debt expense	68	72	135	144
Total expenses	2,457	2,398	4,864	4,688
Income (loss) from continuing operations before taxes	442	409	750	838
Federal income tax expense (benefit)	118	105	180	221
Income (loss) from continuing operations	324	304	570	617
Income (loss) from discontinued operations, net of federal income taxes	-	-	(1)	-
Net income (loss)	324	304	569	617
Other comprehensive income (loss), net of tax	757	354	700	376
Comprehensive income (loss)	$ 1,081	$ 658	$ 1,269	$ 993
Earnings (Loss) Per Common Share - Basic				
Income (loss) from continuing operations	$ 1.15	$ 0.98	$ 1.99	$ 1.97
Income (loss) from discontinued operations	-	-	-	-
Net income (loss)	$ 1.15	$ 0.98	$ 1.99	$ 1.97
Earnings (Loss) Per Common Share - Diluted				
Income (loss) from continuing operations	$ 1.10	$ 0.95	$ 1.94	$ 1.92
Income (loss) from discontinued operations	-	-	-	-
Net income (loss)	$ 1.10	$ 0.95	$ 1.94	$ 1.92

See accompanying Notes to Consolidated Financial Statements

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

	For the Six Months Ended June 30,	
	2012	2011
Common Stock		
Balance as of beginning-of-year	$ 7,590	$ 8,124
Stock compensation/issued for benefit plans	20	9
Retirement of common stock/cancellation of shares	(300)	(195)
Balance as of end-of-period	7,310	7,938
Retained Earnings		
Balance as of beginning-of-year	2,969	3,934
Cumulative effect from adoption of new accounting standards	-	(1,095)
Net income (loss)	569	617
Retirement of common stock	-	(31)
Dividends declared: Common (2012 - $0.160; 2011 - $0.100)	(45)	(32)
Balance as of end-of-period	3,493	3,393
Accumulated Other Comprehensive Income (Loss)		
Balance as of beginning-of-year	2,679	748
Cumulative effect from adoption of new accounting standards	-	103
Other comprehensive income (loss), net of tax	700	376
Balance as of end-of-period	3,379	1,227
Total stockholders' equity as of end-of-period	$ 14,182	$ 12,558

See accompanying Notes to Consolidated Financial Statements

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

	For the Six Months Ended June 30, 2012	2011
Cash Flows from Operating Activities		
Net income (loss)	$ 569	$ 617
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Deferred acquisition costs, value of business acquired, deferred sales inducements		
and deferred front-end loads deferrals and interest, net of amortization	(114)	(215)
Trading securities purchases, sales and maturities, net	67	26
Change in premiums and fees receivable	20	(35)
Change in accrued investment income	(40)	(61)
Change in future contract benefits and other contract holder funds	120	371
Change in reinsurance related assets and liabilities	(111)	(72)
Change in federal income tax accruals	197	297
Realized (gain) loss	43	7
(Income) loss attributable to equity method investments	(81)	(75)
Amortization of deferred gain on business sold through reinsurance	(38)	(37)
(Gain) loss on disposal of discontinued operations	1	-
Other	(19)	55
Net cash provided by (used in) operating activities	614	878
Cash Flows from Investing Activities		
Purchases of available-for-sale securities	(5,717)	(5,901)
Sales of available-for-sale securities	369	1,042
Maturities of available-for-sale securities	2,983	2,857
Purchases of other investments	(1,398)	(1,701)
Sales or maturities of other investments	1,451	1,527
Increase (decrease) in payables for collateral on investments	1,337	146
Other	(47)	(42)
Net cash provided by (used in) investing activities	(1,022)	(2,072)
Cash Flows from Financing Activities		
Issuance of long-term debt, net of issuance costs	298	298
Increase (decrease) in commercial paper, net	-	(100)
Deposits of fixed account values, including the fixed portion of variable	4,979	5,335
Withdrawals of fixed account values, including the fixed portion of variable	(2,611)	(2,515)
Transfers to and from separate accounts, net	(1,160)	(1,391)
Common stock issued for benefit plans and excess tax benefits	(5)	(5)
Repurchase of common stock	(300)	(226)
Dividends paid to common and preferred stockholders	(46)	(31)
Net cash provided by (used in) financing activities	1,155	1,365

Net increase (decrease) in cash and invested cash, including discontinued operations		747		171
Cash and invested cash, including discontinued operations, as of beginning-of-year		4,510		2,741
Cash and invested cash, including discontinued operations, as of end-of-period	$	5,257	$	2,912

See accompanying Notes to Consolidated Financial Statements

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LINCOLN NATIONAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Nature of Operations and Basis of Presentation

Nature of Operations

Lincoln National Corporation and its majority-owned subsidiaries ("LNC" or the "Company," which also may be referred to as "we," "our" or "us") operate multiple insurance businesses through four business segments. See Note 13 for additional details. The collective group of businesses uses "Lincoln Financial Group" as its marketing identity. Through our business segments, we sell a wide range of wealth protection, accumulation and retirement income products. These products include institutional and/or retail fixed and indexed annuities, variable annuities, universal life insurance ("UL"), variable universal life insurance ("VUL"), linked-benefit UL, term life insurance, mutual funds and group life, disability and dental.

Basis of Presentation

The accompanying unaudited consolidated financial statements are prepared in accordance with United States of America generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for the Securities and Exchange Commission ("SEC") Quarterly Report on Form 10-Q, including Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. Therefore, the information contained in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 ("2011 Form 10-K"), should be read in connection with the reading of these interim unaudited consolidated financial statements.

Certain GAAP policies, which significantly affect the determination of financial position, results of operations and cash flows, are summarized in our 2011 Form 10-K.

In the opinion of management, these statements include all normal recurring adjustments necessary for a fair presentation of the Company's results. Operating results for the six month period ended June 30, 2012, are not necessarily indicative of the results that may be expected for the full year ending December 31, 2012. All material intercompany accounts and transactions have been eliminated in consolidation.

See Note 2 "Financial Services – Insurance Industry Topic" below for information about the retrospective restatement of amounts due to the adoption of new accounting guidance. In addition, certain amounts reported in prior years' consolidated financial statements have been reclassified to conform to the presentation adopted in the current year. These reclassifications had no effect on net income or stockholders' equity of the prior years.

2. New Accounting Standards

Adoption of New Accounting Standards

Comprehensive Income Topic

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-05, "Presentation of Comprehensive Income" ("ASU 2011-05"), with an objective of increasing the prominence of items reported in other comprehensive income ("OCI"); however, in December 2011, the FASB deferred a portion of the presentation requirements by issuing ASU No. 2011-12, "Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05" ("ASU 2011- 12"). For a more detailed description of ASU 2011-05 and ASU 2011-12, see "Future Adoption of New Accounting Standards – Comprehensive Income Topic" in Note 2 of our 2011 Form 10-K. We adopted the provisions of ASU 2011-05 as of January 1, 2012, after considering the deferral in ASU 2011-12, and have included a single continuous statement of comprehensive income in Item 1 of this quarterly report on Form 10-Q for the quarterly period ended June 30, 2012.

Fair Value Measurements and Disclosures Topic

In May 2011, the FASB issued ASU No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards" ("ASU 2011-04"), which was issued to create a consistent framework for the application of fair value measurement across jurisdictions. For a more detailed description of ASU 2011-04 see "Future Adoption of New Accounting Standards – Fair Value Measurements and Disclosures Topic" in Note 2 of our 2011 Form 10-K. We adopted the provisions of ASU 2011-04 effective January 1, 2012, and have included the additional disclosures required for fair value measurements in Note 12 for the quarterly period ended June 30, 2012.

Financial Services – Insurance Industry Topic

In October 2010, the FASB issued ASU No. 2010-26, "Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts" ("ASU 2010-26"), which clarifies the types of costs incurred by an insurance entity that can be capitalized in the acquisition of insurance contracts. Only those costs incurred that result directly from and are essential to the successful acquisition of new or renewal insurance contracts may be capitalized as deferrable acquisition costs. The determination of deferability must be made on a contract-level basis.

Prior to the adoption of ASU 2010-26, we defined deferred acquisition costs ("DAC") as commissions and other costs of acquiring UL insurance, VUL insurance, traditional life insurance, annuities and other investments contracts that vary with and are related primarily to new or renewal business, regardless of whether the acquisition efforts were successful or unsuccessful. Upon the adoption of ASU 2010-26, we revised our accounting policy to only defer acquisition costs directly related to successful contract acquisitions or renewals, and excluded from DAC those costs incurred for soliciting potential customers, market research, training, administration, management of distribution and underwriting functions, unsuccessful acquisition or renewal efforts and product development. In addition, indirect acquisition costs including administrative costs, rent, depreciation, occupancy costs, equipment costs and other general overhead are excluded from DAC. The costs that are considered non-deferrable acquisition costs under ASU 2010-26 are expensed in the period incurred.

We adopted the provisions of ASU 2010-26 as of January 1, 2012, and elected to retrospectively restate all prior periods. The following summarizes the prior period increases (decreases) (in millions) reflected in our Consolidated Balance Sheets and Consolidated Statements of Stockholders' Equity related to the adoption:

	As of December 31,	
	2011	2010
Assets		
Deferred acquisition costs	$ (1,415)	$ (1,516)
Liabilities and Stockholders' Equity		
Other liabilities - deferred income taxes	$ (490)	$ (524)
Stockholders' equity:		
Retained earnings	(1,157)	(1,095)
Accumulated other comprehensive income (loss)	232	103
Total stockholders' equity	(925)	(992)
Total liabilities and stockholders' equity	$ (1,415)	$ (1,516)

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The following summarizes the prior period increases (decreases) to income from continuing operations and earnings (loss) per share ("EPS") (in millions, except per share data) reflected in our Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended June 30, 2011, related to the adoption:

	For the Three Months Ended June 30, 2011	For the Six Months Ended June 30, 2011
Revenues		
Realized gain (loss)	$ 4	$ 8
Expenses		
Commissions and other expenses	(37)	(81)
Income (loss) from continuing operations before taxes	(33)	(73)
Federal income tax expense (benefit)	12	26
Income (loss) from continuing operations	$ (21)	$ (47)
Earnings (Loss) Per Common Share - Basic	$ (0.07)	$ (0.15)
Earnings (Loss) Per Common Share - Diluted	$ (0.07)	$ (0.15)

Intangibles – Goodwill and Other Topic

In September 2011, the FASB issued ASU No. 2011-08, "Testing Goodwill for Impairment" ("ASU 2011-08"), which provides an option to first assess qualitative factors to determine if it is necessary to complete the two-step goodwill impairment test. For a more detailed description of ASU 2011-08, see "Future Adoption of New Accounting Standards – Intangibles – Goodwill and Other Topic" in Note 2 of our 2011 Form 10-K. We adopted the provisions of ASU 2011-08 effective January 1, 2012. The adoption did not have a material effect on our consolidated financial condition and results of operations.

Transfers and Servicing Topic

In April 2011, the FASB issued ASU No. 2011-03, "Reconsideration of Effective Control for Repurchase Agreements" ("ASU 2011-03"), which revises the criteria for assessing effective control for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. For a more detailed description of ASU 2011-03, see "Future Adoption of New Accounting Standards – Transfers and Servicing Topic" in Note 2 of our 2011 Form 10-K. We adopted the provisions of ASU 2011-03 effective January 1, 2012. The adoption did not have a material effect on our consolidated financial condition and results of operations.

Future Adoption of New Accounting Standards

Balance Sheet Topic

In December 2011, the FASB issued ASU No. 2011-11, "Disclosures about Offsetting Assets and Liabilities" ("ASU 2011-11"), to address certain comparability issues between financial statements prepared in accordance with GAAP and those prepared in accordance with International Financial Reporting Standards. For a more detailed description of ASU 2011-11, see "Future Adoption of New Accounting Standards – Balance Sheet Topic" in Note 2 of our 2011 Form 10-K. We will adopt the disclosure requirements in ASU 2011-11 beginning with our first quarter 2013 financial statements and are currently evaluating the appropriate location for these disclosures in the notes to our financial statements.

3. Variable Interest Entities ("VIEs")

Consolidated VIEs

See Note 4 in our 2011 Form 10-K for a detailed discussion of our consolidated VIEs, which information is incorporated herein by reference.

The following summarizes information regarding the credit-linked note ("CLN") structures (dollars in millions) as of June 30, 2012:

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

The following summarizes the exposure of the CLN structures' underlying collateral by industry and rating as of June 30, 2012:

	AAA	AA	A	BBB	BB	B	CCC	Total
Industry								
Telecommunications	-%	-%	5.5%	4.5%	0.7%	0.5%	-%	11.2%
Financial intermediaries	-%	2.1%	7.5%	0.9%	-%	-%	-%	10.5%
Oil and gas	-%	1.8%	1.0%	4.6%	-%	-%	-%	7.4%
Utilities	-%	-%	2.6%	2.0%	-%	-%	-%	4.6%
Chemicals and plastics	-%	-%	2.3%	1.2%	0.3%	-%	-%	3.8%
Drugs	0.3%	2.7%	0.7%	-%	-%	-%	-%	3.7%
Retailers (except food and drug)	-%	-%	2.1%	0.9%	0.5%	-%	-%	3.5%
Industrial equipment	-%	-%	3.0%	0.3%	-%	-%	-%	3.3%
Sovereign	-%	0.7%	1.6%	1.0%	-%	-%	-%	3.3%
Conglomerates	-%	2.3%	0.9%	-%	-%	-%	-%	3.2%
Forest products	-%	-%	-%	1.6%	1.4%	-%	-%	3.0%
Other	-%	3.9%	16.0%	17.7%	3.7%	0.9%	0.3%	42.5%
Total	0.3%	13.5%	43.2%	34.7%	6.6%	1.4%	0.3%	100.0%

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

	As of June 30, 2012			As of December 31, 2011		
	Number of Instruments	Notional Amounts	Carrying Value	Number of Instruments	Notional Amounts	Carrying Value
Assets						
Fixed maturity securities:						
Asset-backed credit card loans	N/A	$ -	$ 595	N/A	$ -	$ 592
U.S. government bonds	N/A	-	110	N/A	-	108
Excess mortality swap	1	100	-	1	100	-
Total assets (1)	1	$ 100	$ 705	1	$ 100	$ 700
Liabilities						
Non-qualifying hedges:						
Credit default swaps	2	$ 600	$ 234	2	$ 600	$ 295
Contingent forwards	2	-	(3)	2	-	(4)
Total non-qualifying hedges	4	600	231	4	600	291
Federal income tax	N/A	-	(73)	N/A	-	(98)
Total liabilities (2)	4	$ 600	$ 158	4	$ 600	$ 193

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

For details related to the fixed maturity available-for-sale ("AFS") securities for these VIEs, see Note 4.

As described more fully in Note 1 of our 2011 Form 10-K, we regularly review our investment holdings for other-than-temporary impairment ("OTTI"). Based upon this review, we believe that the fixed maturity securities were not other-than-temporarily impaired as of June 30, 2012.

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Non-Qualifying Hedges				
Credit default swaps	$ (10)	$ 6	$ 61	$ 13
Contingent forwards	-	(1)	(2)	(3)
Total non-qualifying hedges (1)	$ (10)	$ 5	$ 59	$ 10

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

Unconsolidated VIEs

See Note 4 in our 2011 Form 10-K for a detailed discussion of our unconsolidated VIEs, which information is incorporated herein by reference.

4. Investments

AFS Securities

Pursuant to the Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards CodificationTM ("ASC"), we have categorized AFS securities into a three-level hierarchy, based on the priority of the inputs to the respective valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3), as described in Note 1 in our 2011 Form 10-K, which also includes additional disclosures regarding our fair value measurements.

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

	As of June 30, 2012				
	Amortized	Gross Unrealized			Fair
	Cost	Gains	Losses	OTTI	Value
Fixed maturity securities:					
Corporate bonds	$ 57,342	$ 7,068	$ 393	$ 103	$ 63,914
U.S. Government bonds	449	68	-	-	517
Foreign government bonds	583	81	-	-	664
Residential mortgage-backed securities ("RMBS")	6,808	522	41	92	7,197
Commercial mortgage-backed securities ("CMBS")	1,304	71	43	25	1,307
Collateralized debt obligations ("CDOs")	135	-	15	-	120
State and municipal bonds	3,525	767	8	-	4,284
Hybrid and redeemable preferred securities	1,248	63	123	-	1,188
VIEs' fixed maturity securities	675	30	-	-	705
Total fixed maturity securities	72,069	8,670	623	220	79,896
Equity securities	143	19	8	-	154
Total AFS securities	$ 72,212	$ 8,689	$ 631	$ 220	$ 80,050

	As of December 31, 2011				
	Amortized	Gross Unrealized			Fair
	Cost	Gains	Losses	OTTI	Value
Fixed maturity securities:					
Corporate bonds	$ 53,661	$ 6,185	$ 517	$ 68	$ 59,261
U.S. Government bonds	439	55	-	-	494
Foreign government bonds	668	65	-	-	733
RMBS	7,690	548	73	126	8,039
CMBS	1,642	73	106	9	1,600
CDOs	121	-	19	-	102
State and municipal bonds	3,490	566	9	-	4,047
Hybrid and redeemable preferred securities	1,277	50	170	-	1,157
VIEs' fixed maturity securities	673	27	-	-	700
Total fixed maturity securities	69,661	7,569	894	203	76,133
Equity securities	135	16	12	-	139
Total AFS securities	$ 69,796	$ 7,585	$ 906	$ 203	$ 76,272

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The amortized cost and fair value of fixed maturity AFS securities by contractual maturities (in millions) as of June 30, 2012, were as follows:

	Amortized Cost	Fair Value
Due in one year or less	$ 2,931	$ 2,989
Due after one year through five years	12,188	13,136
Due after five years through ten years	23,651	26,185
Due after ten years	25,052	28,962
Subtotal	63,822	71,272
Mortgage-backed securities ("MBS")	8,112	8,504
CDOs	135	120
Total fixed maturity AFS securities	$ 72,069	$ 79,896

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

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

	As of June 30, 2012					
	Less Than or Equal to Twelve Months		Greater Than Twelve Months		Total	
	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI
Fixed maturity securities:						
Corporate bonds	$ 2,389	$ 175	$ 1,293	$ 321	$ 3,682	$ 496
RMBS	521	90	314	43	835	133
CMBS	110	25	146	43	256	68
CDOs	-	-	68	15	68	15
State and municipal bonds	5	-	22	8	27	8
Hybrid and redeemable preferred securities	125	4	425	119	550	123
Total fixed maturity securities	3,150	294	2,268	549	5,418	843
Equity securities	10	1	4	7	14	8
Total AFS securities	$ 3,160	$ 295	$ 2,272	$ 556	$ 5,432	$ 851

Total number of AFS securities in an unrealized loss position	734

	As of December 31, 2011					
	Less Than or Equal to Twelve Months		Greater Than Twelve Months		Total	
	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI
Fixed maturity securities:						
Corporate bonds	$ 2,848	$ 162	$ 1,452	$ 423	$ 4,300	$ 585
RMBS	565	125	429	74	994	199
CMBS	178	15	146	100	324	115
CDOs	9	1	80	18	89	19
State and municipal bonds	31	-	30	9	61	9
Hybrid and redeemable preferred securities	324	23	353	147	677	170
Total fixed maturity securities	3,955	326	2,490	771	6,445	1,097
Equity securities	38	12	-	-	38	12
Total AFS securities	$ 3,993	$ 338	$ 2,490	$ 771	$ 6,483	$ 1,109
Total number of AFS securities in an unrealized loss position						897

For information regarding our investments in VIEs, see Note 3.

We perform detailed analysis on the AFS securities backed by pools of residential and commercial mortgages that are most at risk of impairment based on factors discussed in Note 1 in our 2011 Form 10-K. Selected information for these securities in a gross unrealized loss position (in millions) was as follows:

	As of June 30, 2012		
	Amortized Cost	Fair Value	Unrealized Loss
Total			
AFS securities backed by pools of residential mortgages	$ 1,734	$ 1,363	$ 371
AFS securities backed by pools of commercial mortgages	355	274	81
Total	$ 2,089	$ 1,637	$ 452
Subject to Detailed Analysis			
AFS securities backed by pools of residential mortgages	$ 1,724	$ 1,353	$ 371
AFS securities backed by pools of commercial mortgages	79	42	37
Total	$ 1,803	$ 1,395	$ 408

	As of December 31, 2011		
	Amortized Cost	Fair Value	Unrealized Loss
Total			
AFS securities backed by pools of residential mortgages	$ 2,023	$ 1,553	$ 470
AFS securities backed by pools of commercial mortgages	472	344	128
Total	$ 2,495	$ 1,897	$ 598

Subject to Detailed Analysis			
AFS securities backed by pools of residential mortgages	$ 2,015	$ 1,545	$ 470
AFS securities backed by pools of commercial mortgages	126	61	65
Total	$ 2,141	$ 1,606	$ 535

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For the six months ended June 30, 2012 and 2011, we recorded OTTI for AFS securities backed by pools of residential and commercial mortgages of $34 million and $44 million, pre-tax, respectively, and before associated amortization expense for DAC, value of business acquired ("VOBA"), deferred sales inducements ("DSI") and deferred front-end loads ("DFEL"), of which $(3) million and $4 million, respectively, was recognized in OCI and $37 million and $40 million, respectively, was recognized in net income (loss).

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

	As of June 30, 2012			
	Fair Value	Gross Unrealized Losses	OTTI	Number of Securities (1)
Less than six months	$ 115	$ 41	$ 2	25
Six months or greater, but less than nine months	13	4	1	4
Nine months or greater, but less than twelve months	104	40	12	17
Twelve months or greater	584	342	165	167
Total	$ 816	$ 427	$ 180	213

	As of December 31, 2011			
	Fair Value	Gross Unrealized Losses	OTTI	Number of Securities (1)
Less than six months	$ 385	$ 125	$ 31	56
Six months or greater, but less than nine months	53	30	12	18
Nine months or greater, but less than twelve months	2	-	1	7
Twelve months or greater	615	470	111	175
Total	$ 1,055	$ 625	$ 155	256

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

We regularly review our investment holdings for OTTI. Our gross unrealized losses on AFS securities decreased $258 million for the six months ended June 30, 2012. As discussed further below, we believe the unrealized loss position as of June 30, 2012, did not represent OTTI as we did not intend to sell these fixed maturity AFS securities, it is not more likely than not that we will be required to sell the fixed maturity AFS securities before recovery of their amortized cost basis, the estimated future cash flows were equal to or greater than the amortized cost basis of the debt securities, or we had the ability and intent to hold the equity AFS securities for a period of time sufficient for recovery.

Based upon this evaluation as of June 30, 2012, management believed we had the ability to generate adequate amounts of cash from our normal operations (e.g., insurance premiums and fees and investment income) to meet cash requirements with a prudent margin of safety without requiring the sale of our temporarily-impaired securities.

As of June 30, 2012, the unrealized losses associated with our corporate bond securities were attributable primarily to securities that were backed by commercial loans and individual issuer companies. For our corporate bond securities with commercial loans as the underlying collateral, we evaluated the projected credit losses in the underlying collateral and concluded that we had sufficient subordination or other credit enhancement when compared with our estimate of credit losses for the individual security and we expected to recover the entire amortized cost for each security. For individual issuers, we performed detailed analysis of the financial performance of the issuer and determined that we expected to recover the entire amortized cost for each security.

As of June 30, 2012, the unrealized losses associated with our MBS and CDOs were attributable primarily to collateral losses and credit spreads. We assessed for credit impairment using a cash flow model as discussed above. The key assumptions included default rates, severities and prepayment rates. We estimated losses for a security by forecasting the underlying loans in each transaction. The forecasted loan performance was used to project cash flows to the various tranches in the structure, as applicable. Our forecasted cash flows also considered, as applicable, independent industry analyst reports and forecasts, sector credit ratings and other independent market data. Based upon our assessment of the expected credit losses of the security given the performance of the underlying collateral compared to our subordination or other credit enhancement, we expected to recover the entire amortized cost basis of each security.

As of June 30, 2012, the unrealized losses associated with our hybrid and redeemable preferred securities were attributable primarily to wider credit spreads caused by illiquidity in the market and subordination within the capital structure, as well as credit risk of specific issuers. For our hybrid and redeemable preferred securities, we evaluated the financial performance of the issuer based upon credit performance and investment ratings and determined we expected to recover the entire amortized cost of each security.

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Balance as of beginning-of-period	$ 410	$ 352	$ 390	$ 319
Increases attributable to:				
Credit losses on securities for which an OTTI was not previously recognized	21	3	56	29
Credit losses on securities for which an OTTI was previously recognized	19	19	42	40
Decreases attributable to:				
Securities sold	(35)	(34)	(73)	(48)
Balance as of end-of-period	$ 415	$ 340	$ 415	$ 340

During 2012 and 2011, we recorded credit losses on securities for which an OTTI was not previously recognized as we determined the cash flows expected to be collected would not be sufficient to recover the entire amortized cost basis of the debt security. The credit losses we recorded on securities for which an OTTI was not previously recognized were attributable primarily to one or a combination of the following reasons:

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

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

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

	As of June 30, 2012				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses and OTTI	Fair Value	OTTI in Credit Losses
Corporate bonds	$ 239	$ 1	$ 104	$ 136	$ 73

RMBS		697		5		91		611		268
CMBS		46		-		24		22		74
Total	$	982	$	6	$	219	$	769	$	415

	As of December 31, 2011				
	Amortized Cost	Gains	Gross Unrealized Losses and OTTI	Fair Value	OTTI in Credit Losses
Corporate bonds	$ 169	$ 1	$ 67	$ 103	$ 51
RMBS	690	1	128	563	301
CMBS	17	-	10	7	38
Total	$ 876	$ 2	$ 205	$ 673	$ 390

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 31% and 32% of mortgage loans on real estate as of June 30, 2012, and December 31, 2011, respectively.

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

	As of June 30, 2012	As of December 31, 2011
Current	$ 6,736	$ 6,858
60 to 90 days past due	3	26
Greater than 90 days past due	80	76
Valuation allowance associated with impaired mortgage loans on real estate	(26)	(31)
Unamortized premium (discount)	11	13
Total carrying value	$ 6,804	$ 6,942

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

	As of June 30, 2012	As of December 31, 2011
Number of impaired mortgage loans on real estate	9	12
Principal balance of impaired mortgage loans on real estate	$ 66	$ 100
Valuation allowance associated with impaired mortgage loans on real estate	(26)	(31)
Carrying value of impaired mortgage loans on real estate	$ 40	$ 69

The average carrying value on the impaired mortgage loans on real estate (in millions) was as follows:

For the Three Months Ended June 30,		For the Six Months Ended June 30,	
2012	2011	2012	2011

Average carrying value for impaired mortgage loans on real estate	$ 49	$ 53	$ 56	$ 54
Interest income recognized on impaired mortgage loans on real estate	-	-	-	1
Interest income collected on impaired mortgage loans on real estate	-	1	-	2

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As described in Note 1 in our 2011 Form 10-K, we use the loan-to-value and debt-service coverage ratios as credit quality indicators for our mortgage loans, which were as follows (dollars in millions):

	As of June 30, 2012			As of December 31, 2011		
Loan-to-Value	Principal Amount	% of Total	Debt-Service Coverage Ratio	Principal Amount	% of Total	Debt-Service Coverage Ratio
Less than 65%	$ 5,395	79.1%	1.63	$ 5,338	76.7%	1.61
65% to 74%	1,008	14.8%	1.41	1,198	17.2%	1.37
75% to 100%	334	4.9%	0.90	308	4.4%	0.92
Greater than 100%	82	1.2%	0.32	116	1.7%	0.36
Total mortgage loans on real estate	$ 6,819	100.0%		$ 6,960	100.0%	

Alternative Investments

As of June 30, 2012, and December 31, 2011, alternative investments included investments in 97 and 96 different partnerships, respectively, and the portfolio represented less than 1% of our overall invested assets.

Realized Gain (Loss) Related to Certain Investments

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Fixed maturity AFS securities:				
Gross gains	$ 3	$ 31	$ 8	$ 67
Gross losses	(49)	(51)	(112)	(114)
Equity AFS securities:				
Gross gains	-	1	1	9
Gain (loss) on other investments	(5)	(8)	2	5
Associated amortization of DAC, VOBA, DSI and DFEL and changes in other contract holder funds	-	(5)	2	(14)
Total realized gain (loss) related to certain investments	$ (51)	$ (32)	$ (99)	$ (47)

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
OTTI Recognized in Net Income (Loss)				
Corporate bonds	$ (10)	$ (2)	$ (29)	$ (6)
RMBS	(14)	(23)	(32)	(43)
CMBS	(16)	(15)	(36)	(39)
CDOs	-	-	-	(1)
Hybrid and redeemable preferred securities	-	-	-	(2)
Gross OTTI recognized in net income (loss)	(40)	(40)	(97)	(91)
Associated amortization of DAC, VOBA, DSI and DFEL	7	9	17	19
Net OTTI recognized in net income (loss), pre-tax	$ (33)	$ (31)	$ (80)	$ (72)
Portion of OTTI Recognized in OCI				
Gross OTTI recognized in OCI	$ 21	$ 19	$ 79	$ 27
Change in DAC, VOBA, DSI and DFEL	(4)	(3)	(12)	(8)
Net portion of OTTI recognized in OCI, pre-tax	$ 17	$ 16	$ 67	$ 19

Determination of Credit Losses on Corporate Bonds and CDOs

As of June 30, 2012, and December 31, 2011, we reviewed our corporate bond and CDO portfolios for potential shortfall in contractual principal and interest based on numerous subjective and objective inputs. The factors used to determine the amount of credit loss for each individual security, include, but are not limited to, near term risk, substantial discrepancy between book and market value, sector or company-specific volatility, negative operating trends and trading levels wider than peers.

Credit ratings express opinions about the credit quality of a security. Securities rated investment grade, that is those rated BBB- or higher by Standard & Poor's ("S&P") Rating Services or Baa3 or higher by Moody's Investors Service ("Moody's"), are generally considered by the rating agencies and market participants to be low credit risk. As of June 30, 2012, and December 31, 2011, 96% of the fair value of our corporate bond portfolio was rated investment grade. As of June 30, 2012, and December 31, 2011, the portion of our corporate bond portfolio rated below investment grade had an amortized cost of $2.7 billion and $2.6 billion and a fair value of $2.5 billion and $2.4 billion, respectively. As of June 30, 2012, and December 31, 2011, 98% and 97%, respectively, of the fair value of our CDO portfolio was rated investment grade. As of June 30, 2012, and December 31, 2011, the portion of our CDO portfolio rated below investment grade had an amortized cost and fair value of $3 million. Based upon the analysis discussed above, we believed as of June 30, 2012, and December 31, 2011, that we would recover the amortized cost of each investment grade corporate bond and CDO security.

For securities where we recorded an OTTI recognized in net income (loss) for the six months ended June 30, 2012 and 2011, the recovery as a percentage of amortized cost was 92% and 98%, respectively, for corporate bonds and 0% for CDOs.

Determination of Credit Losses on MBS

As of June 30, 2012, and December 31, 2011, default rates were projected by considering underlying MBS loan performance and collateral type. Projected default rates on existing delinquencies vary between 25% to 100% depending on loan type and severity of delinquency status. In addition, we estimate the potential contributions of currently performing loans that may become delinquent in the future based on the change in delinquencies and loan liquidations experienced in the recent history. Finally, we develop a default rate timing curve by aggregating the defaults for all loans (delinquent loans, foreclosure and real estate owned and new delinquencies from currently performing loans) in the pool to project the future expected cash flows.

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

Payables for Collateral on Investments

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

	As of June 30, 2012		As of December 31, 2011	
	Carrying Value of Payables	Fair Value of Collateral	Carrying Value of Payables	Fair Value of Collateral
Collateral payable held for derivative investments (1)	$ 3,441	$ 3,441	$ 2,980	$ 2,980
Securities pledged under securities lending agreements (2)	200	194	200	193
Securities pledged under reverse repurchase agreements (3)	280	293	280	294
Securities pledged for Term Asset-Backed Securities Loan Facility ("TALF") (4)	49	66	173	199
Investments pledged for Federal Home Loan Bank of Indianapolis ("FHLBI") (5)	1,100	2,013	100	142
Total payables for collateral on investments	$ 5,070	$ 6,007	$ 3,733	$ 3,808

(1) We obtain collateral based upon contractual provisions with our counterparties. These agreements take into consideration the counterparties' credit rating as compared to ours, the fair value of the derivative investments and specified thresholds that if exceeded result in the receipt of cash that is typically invested in cash and invested cash. See Note 6 for details about maximum collateral potentially required to post on our credit default swaps.
(2) Our pledged securities under securities lending agreements are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We generally obtain collateral in an amount equal to 102% and 105% of the fair value of the domestic and foreign securities, respectively. We value collateral daily and obtain additional collateral when deemed appropriate. The cash received in our securities lending program is typically invested in cash and invested cash or fixed maturity AFS securities.
(3) Our pledged securities under reverse repurchase agreements are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We obtain collateral in an amount equal to 95% of the fair value of the securities, and our agreements with third parties contain contractual provisions to allow for additional collateral to be obtained when necessary. The cash received in our reverse repurchase program is typically invested in fixed maturity AFS securities.
(4) Our pledged securities for TALF are included in fixed maturity AFS securities on our Consolidated Balance Sheets. We obtain collateral in an amount that has typically averaged 90% of the fair value of the TALF securities. The cash received in these transactions is invested in fixed maturity AFS securities.
(5) Our pledged investments for FHLBI are included in fixed maturity AFS securities and mortgage loans on real estate on our Consolidated Balance Sheets. The collateral requirements are generally 105% to 115% of the fair value for fixed maturity AFS securities and 155% to 175% of the fair value for mortgage loans on real estate. The cash received in these transactions is primarily invested in cash and invested cash or fixed maturity AFS securities.

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

	For the Six Months Ended June 30,

	2012	2011
Collateral payable held for derivative investments	$ 461	$ 223
Securities pledged under securities lending agreements	-	1
Securities pledged for TALF	(124)	(78)
Investments pledged for FHLBI	1,000	-
Total increase (decrease) in payables for collateral on investments	$ 1,337	$ 146

Investment Commitments

As of June 30, 2012, our investment commitments were $754 million, which included $233 million of limited partnerships (“LPs”), $339 million of private placements and $182 million of mortgage loans on real estate.

Concentrations of Financial Instruments

As of June 30, 2012, and December 31, 2011, our most significant investments in one issuer were our investments in securities issued by the Federal Home Loan Mortgage Corporation with a fair value of $4.5 billion and $5.0 billion, respectively, or 5% of our invested assets portfolio and our investments in securities issued by Fannie Mae with a fair value of $2.5 billion and $2.6 billion, respectively, or 3% of our invested assets portfolio. These investments are included in corporate bonds in the tables above.

As of June 30, 2012, and December 31, 2011, our most significant investments in one industry were our investment securities in the electric industry with a fair value of $8.1 billion and $7.7 billion, respectively, or 8% of our invested assets portfolio, and our investment securities in the collateralized mortgage obligations industry with a fair value of $5.0 billion and $5.6 billion, or 5% and 6% of our invested assets portfolio, respectively. We utilized the industry classifications to obtain the concentration of financial instruments amount; as such, this amount will not agree to the AFS securities table above.

5. Derivative Instruments

We maintain an overall risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate risk, foreign currency exchange risk, equity market risk, default risk, basis risk and credit risk. See Note 1 in our 2011 Form 10-K for a detailed discussion of the accounting treatment for derivative instruments. See Note 6 in our 2011 Form 10-K for a detailed discussion of our derivative instruments and use of them in our overall risk management strategy which information is incorporated herein by reference. In addition, we have entered into forward-starting interest rate swaps that hedge the interest rate risk of floating rate bond coupon payments by replicating a fixed rate bond. See Note 12 for additional disclosures related to the fair value of our derivative instruments and Note 3 for derivative instruments related to our consolidated VIEs.

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

	As of June 30, 2012			As of December 31, 2011		
	Notional	Fair Value		Notional	Fair Value	
	Amounts	Asset	Liability	Amounts	Asset	Liability
Qualifying Hedges						
Cash flow hedges:						
Interest rate contracts (1)	$ 3,418	$ 190	$ -	$ 2,512	$ 130	$ -
Foreign currency contracts (1)	420	37	-	340	38	-
Total cash flow hedges	3,838	227	-	2,852	168	-
Fair value hedges:						
Interest rate contracts (1)	1,175	325	-	1,675	319	-
Equity collar (1)	9	-	-	-	-	-
Total fair value hedges	1,184	325	-	1,675	319	-
Non-Qualifying Hedges						
Interest rate contracts (1)	36,599	777	-	30,232	568	-
Foreign currency contracts (1)	196	-	-	4	-	-
Equity market contracts (1)	19,182	2,071	-	16,401	2,096	-
Credit contracts (1)	46	(1)	-	48	-	-
Credit contracts (2)	148	-	11	148	-	16
Embedded derivatives:						

Indexed annuity contracts (3)	-	-	431	-	-	399
Guaranteed living benefits ("GLB") reserves (3)	-	-	1,926	-	-	2,217
Reinsurance related (4)	-	-	185	-	-	168
Total derivative instruments	$ 61,193	$ 3,399	$ 2,553	$ 51,360	$ 3,151	$ 2,800

(1) Reported in derivative investments on our Consolidated Balance Sheets.
(2) Reported in other liabilities on our Consolidated Balance Sheets.
(3) Reported in future contract benefits on our Consolidated Balance Sheets.
(4) Reported in reinsurance related embedded derivatives on our Consolidated Balance Sheets.

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

	Remaining Life as of June 30, 2012					
	Less Than 1 Year	1 – 5 Years	6 – 10 Years	11 – 30 Years	Over 30 Years	Total
Interest rate contracts (1)	$ 3,389	$ 11,942	$ 14,478	$ 10,169	$ 1,213	$ 41,191
Foreign currency contracts (2)	196	179	130	111	-	616
Equity market contracts	9,978	3,305	5,881	24	3	19,191
Credit contracts	40	155	-	-	-	195
Total derivative instruments with notional amounts	$ 13,603	$ 15,581	$ 20,489	$ 10,304	$ 1,216	$ 61,193

(1) As of June 30, 2012, the latest maturity date for which we were hedging our exposure to the variability in future cash flows for these instruments was April 2067.
(2) As of June 30, 2012, the latest maturity date for which we were hedging our exposure to the variability in future cash flows for these instruments was April 2028.

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

	For the Six Months Ended June 30,	
	2012	2011
Unrealized Gain (Loss) on Derivative Instruments		
Balance as of beginning-of-year	$ 119	$ (15)
Other comprehensive income (loss):		
Cumulative effect from adoption of new accounting standards	-	3
Unrealized holding gains (losses) arising during the year:		
Cash flow hedges:		
Interest rate contracts	38	(41)
Foreign currency contracts	(3)	5
Fair value hedges:		
Interest rate contracts	2	2
Change in foreign currency exchange rate adjustment	2	(14)
Change in DAC, VOBA, DSI and DFEL	4	-
Income tax benefit (expense)	(16)	18
Less:		
Reclassification adjustment for gains (losses) included in net income (loss):		
Cash flow hedges:		
Interest rate contracts (1)	(11)	(5)
Interest rate contracts (2)	-	1
Foreign currency contracts (1)	2	(7)
Fair value hedges:		
Interest rate contracts (2)	2	2
Associated amortization of DAC, VOBA, DSI and DFEL	1	1
Income tax benefit (expense)	2	3
Balance as of end-of-period	$ 150	$ (37)

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

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Qualifying Hedges				
Cash flow hedges:				
Interest rate contracts (1)	$ (4)	$ (4)	$ (11)	$ (5)
Foreign currency contracts (1)	-	(1)	2	1
Total cash flow hedges	(4)	(5)	(9)	(4)
Fair value hedges:				
Interest rate contracts (2)	11	13	23	25
Non-Qualifying Hedges				
Interest rate contracts (1)	(16)	(10)	(18)	(16)
Interest rate contracts (3)	622	88	208	27
Foreign currency contracts (3)	-	(1)	(4)	(5)
Equity market contracts (3)	241	64	(430)	(135)
Equity market contracts (4)	26	(15)	(109)	(34)
Credit contracts (1)	(1)	-	(2)	-
Credit contracts (3)	1	(1)	6	3
Embedded derivatives:				
Indexed annuity contracts (3)	23	6	(80)	54
GLB reserves (3)	(862)	(160)	291	130
Reinsurance related (3)	(27)	(28)	(18)	(18)
AFS securities (1)	-	-	-	1
Total derivative instruments	$ 14	$ (49)	$ (142)	$ 28

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

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Gain (loss) recognized as a component of OCI with the offset to net investment income	$ (6)	$ (4)	$ (10)	$ (4)

As of June 30, 2012, $21 million of the deferred net losses on derivative instruments in accumulated OCI were expected to be reclassified to earnings during the next 12 months. This reclassification would be due primarily to the interest rate variances related to the interest rate swap agreements.

For the three and six months ended June 30, 2012 and 2011, 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.

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Gain (loss) recognized as a component of OCI with the offset to interest expense	$ 1	$ 1	$ 2	$ 2

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

As of June 30, 2012						
Maturity	Reason for Entering	Nature of Recourse	Credit Rating of Underlying Obligation (1)	Number of Instruments	Fair Value (2)	Maximum Potential Payout
12/20/2012(3)	(5)	(6)	BBB+	4	$ -	$ 40
12/20/2016(4)	(5)	(6)	BBB	3	(8)	68
03/20/2017(4)	(5)	(6)	BBB	2	(3)	40
				9	$ (11)	$ 148

As of December 31, 2011						
Maturity	Reason for Entering	Nature of Recourse	Credit Rating of Underlying Obligation (1)	Number of Instruments	Fair Value (2)	Maximum Potential Payout
12/20/2012(3)	(5)	(6)	BBB+	4	$ -	$ 40
12/20/2016(4)	(5)	(6)	BBB+	3	(12)	68
03/20/2017(4)	(5)	(6)	BBB	2	(4)	40
				9	$ (16)	$ 148

(1) Represents average credit ratings based on the midpoint of the applicable ratings among Moody's, S&P and Fitch Ratings, as scaled to the corresponding S&P ratings.
(2) Broker quotes are used to determine the market value of credit default swaps.
(3) These credit default swaps were sold to our contract holders prior to 2007, where we determined there was a spread versus premium mismatch.
(4) These credit default swaps were sold to a counter-party of the consolidated VIEs as discussed in Note 4 in our 2011 Form 10-K.
(5) Credit default swaps were entered into in order to generate income by providing default protection in return for a quarterly payment.
(6) Sellers do not have the right to demand indemnification or compensation from third parties in case of a loss (payment) on the contract.

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

	As of	As of

	June 30, 2012	December 31, 2011
Maximum potential payout	$ 148	$ 148
Less:		
Counterparty thresholds	-	-
Maximum collateral potentially required to post	$ 148	$ 148

Certain of our credit default swap agreements contain contractual provisions that allow for the netting of collateral with our counterparties related to all of our collateralized financing transactions that we have outstanding. If these netting agreements were not in place, we would have been required to post approximately $11 million as of June 30, 2012, after considering the fair values of the associated investments counterparties' credit ratings as compared to ours and specified thresholds that once exceeded result in the payment of cash.

Credit Risk

We are exposed to credit loss in the event of nonperformance by our counterparties on various derivative contracts and reflect assumptions regarding the credit or nonperformance risk. The nonperformance risk is based upon assumptions for each counterparty's credit spread over the estimated weighted average life of the counterparty exposure less collateral held. As of June 30, 2012, the nonperformance risk adjustment was $6 million. The credit risk associated with such agreements is minimized by purchasing such agreements from financial institutions with long-standing, superior performance records. Additionally, we maintain a policy of requiring all derivative contracts to be governed by an International Swaps and Derivatives Association ("ISDA") Master Agreement. We are required to maintain minimum ratings as a matter of routine practice in negotiating ISDA agreements. Under some ISDA agreements, our insurance subsidiaries have agreed to maintain certain financial strength or claims-paying ratings. A downgrade below these levels could result in termination of derivative contracts, at which time any amounts payable by us would be dependent on the market value of the underlying derivative contracts. In certain transactions, we and the counterparty have entered into a collateral support agreement requiring either party to post collateral when net exposures exceed pre-determined thresholds. These thresholds vary by counterparty and credit rating. 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 June 30, 2012, our exposure was $47 million.

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

	As of June 30, 2012		As of December 31, 2011	
S&P Credit Rating of Counterparty	Collateral Posted by Counter-Party (Held by LNC)	Collateral Posted by LNC (Held by Counter-Party)	Collateral Posted by Counter-Party (Held by LNC)	Collateral Posted by LNC (Held by Counter-Party)
AA	$ 43	$ -	$ 35	$ -
AA-	121	-	219	-
A+	908	-	848	-
A	845	(109)	1,681	(120)
A-	1,529	-	387	-
	$ 3,446	$ (109)	$ 3,170	$ (120)

6. Federal Income Taxes

The effective tax rate is a ratio of tax expense over pre-tax income (loss). The effective tax rate was 27% and 24% for the three and six months ended June 30, 2012, respectively. The effective tax rate was 26% for the three and six months ended June 30, 2011. The effective tax rate on pre-tax income from continuing operations was lower than the prevailing corporate federal income tax rate. Differences in the effective rates and the U.S. statutory rate of 35% were the result of certain tax preferred investment income, separate account dividends-received deduction, foreign tax credits and other tax preference items.

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7. Guaranteed Benefit Features

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

	As of June 30, 2012	As of December 31, 2011
Return of Net Deposits		
Total account value	$ 58,260	$ 54,004
Net amount at risk (1)	812	1,379
Average attained age of contract holders	59 years	59 years
Minimum Return		
Total account value	$ 151	$ 155
Net amount at risk (1)	42	48
Average attained age of contract holders	72 years	72 years
Guaranteed minimum return	5%	5%
Anniversary Contract Value		
Total account value	$ 22,255	$ 21,648
Net amount at risk (1)	1,963	2,939
Average attained age of contract holders	67 years	67 years

(1) Represents the amount of death benefit in excess of the account balance. The decrease in net amount at risk when comparing June 30, 2012, to December 31, 2011, was attributable primarily to the increase in the equity markets during the first six months of 2012.

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

	For the Six Months Ended June 30, 2012	2011
Balance as of beginning-of-year	$ 84	$ 44
Changes in reserves	7	16
Benefits paid	(24)	(19)
Balance as of end-of-period	$ 67	$ 41

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

	As of June 30,	As of December 31,

	2012	2011
Asset Type		
Domestic equity	$ 34,700	$ 34,286
International equity	13,194	13,095
Bonds	18,148	17,735
Money market	5,948	5,892
Total	$ 71,990	$ 71,008
Percent of total variable annuity separate account values	93%	98%

Future contract benefits also includes reserves for our products with secondary guarantees for our products sold through our Life Insurance segment. These UL and VUL products with secondary guarantees represented 38% of permanent life insurance in force as of June 30, 2012, and 34% and 33% of total sales for these products for the three and six months ended June 30, 2012, respectively.

8. Contingencies and Commitments

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

LNC and its subsidiaries are involved in various pending or threatened legal or regulatory proceedings, including purported class actions, arising from the conduct of business both in the ordinary course and otherwise. In some of the matters, very large and/or indeterminate amounts, including punitive and treble damages, are sought. Modern pleading practice in the U.S. permits considerable variation in the assertion of monetary damages or other relief. Jurisdictions may permit claimants not to specify the monetary damages sought or may permit claimants to state only that the amount sought is sufficient to invoke the jurisdiction of the trial court. In addition, jurisdictions may permit plaintiffs to allege monetary damages in amounts well exceeding reasonably possible verdicts in the jurisdiction for similar matters. This variability in pleadings, together with the actual experiences of LNC in litigating or resolving through settlement numerous claims over an extended period of time, demonstrates to management that the monetary relief which may be specified in a lawsuit or claim bears little relevance to its merits or disposition value.

Due to the unpredictable nature of litigation, the outcome of a litigation matter and the amount or range of potential loss at particular points in time is normally difficult to ascertain. Uncertainties can include how fact finders will evaluate documentary evidence and the credibility and effectiveness of witness testimony, and how trial and appellate courts will apply the law in the context of the pleadings or evidence presented, whether by motion practice, or at trial or on appeal. Disposition valuations are also subject to the uncertainty of how opposing parties and their counsel will themselves view the relevant evidence and applicable law.

We establish liabilities for litigation and regulatory loss contingencies when information related to the loss contingencies shows both that it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated. It is possible that some matters could require us to pay damages or make other expenditures or establish accruals in amounts that could not be estimated as of June 30, 2012. While the potential future charges could be material in the particular quarterly or annual periods in which they are recorded, based on information currently known by management, management does not believe any such charges are likely to have a material adverse effect on LNC’s financial position.

See Note 13 to the consolidated financial statements in our 2011 Form 10-K for a discussion of commitments and contingencies, which information is incorporated herein by reference.

9. Shares and Stockholders' Equity

Common and Preferred Shares

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Series A Preferred Stock				
Balance as of beginning-of-period	9,632	10,914	10,072	10,914
Conversion of convertible preferred stock (1)	-	(60)	(440)	(60)
Balance as of end-of-period	9,632	10,854	9,632	10,854
Common Stock				
Balance as of beginning-of-period	285,412,303	313,456,824	291,319,222	315,718,554
Conversion of convertible preferred stock (1)	-	960	7,040	960
Stock compensation/issued for benefit plans	230,198	30,772	334,395	182,906
Retirement/cancellation of shares	(6,473,530)	(5,149,393)	(12,491,686)	(7,563,257)
Balance as of end-of-period	279,168,971	308,339,163	279,168,971	308,339,163
Common Stock as of End-of-Period				
Assuming conversion of preferred stock	279,323,083	308,512,827	279,323,083	308,512,827
Diluted basis	286,820,300	316,821,550	286,820,300	316,821,550

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

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

Average Shares

A reconciliation of the denominator (number of shares) in the calculations of basic and diluted EPS was as follows:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Weighted-average shares, as used in basic calculation	282,085,602	311,391,263	285,570,764	313,192,667
Shares to cover exercise of outstanding warrants	10,150,192	10,150,292	10,150,231	10,150,292
Shares to cover conversion of preferred stock	154,112	174,603	154,305	174,613
Shares to cover non-vested stock	1,110,662	816,834	1,060,676	794,095
Average stock options outstanding during the period	507,944	633,711	554,614	796,792
Assumed acquisition of shares with assumed proceeds from exercising outstanding warrants	(4,887,102)	(3,846,217)	(4,760,822)	(3,758,105)
Assumed acquisition of shares with assumed proceeds and benefits from exercising stock options (at average market price for the period)	(346,700)	(400,374)	(380,239)	(517,329)
Shares repurchaseable from measured but unrecognized stock option expense	(1,768)	(36,857)	(8,224)	(104,962)
Average deferred compensation shares	1,187,598	1,031,814	1,206,501	1,053,100
Weighted-average shares, as used in diluted calculation	289,960,540	319,915,069	293,547,806	321,781,163

In the event the average market price of LNC common stock exceeds the issue price of stock options and the options have a dilutive effect to our EPS, such options will be shown in the table above.
We have participants in our deferred compensation plans who selected LNC stock as the measure for the investment return attributable to their deferral amounts. For the three and six months ended June 30, 2012 and 2011, the effect of settling this obligation in LNC stock ("equity classification") was more dilutive than the scenario of settling it in cash ("liability classification"). Therefore, for our EPS calculation for these periods, we added these shares to the denominator and adjusted the numerator to present net income as if the shares had been accounted for under equity classification by removing the mark-to-market adjustment included in net income attributable to these deferred units of LNC stock. The amount of this adjustment was $4 million and $(2) million for the three and six months ended June 30, 2012, respectively, and $1 million for the three months ended June 30, 2011.

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

Accumulated OCI

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

	For the Six Months Ended June 30, 2012	2011
Unrealized Gain (Loss) on AFS Securities		
Balance as of beginning-of-year	$ 2,947	$ 1,072
Cumulative effect from adoption of new accounting standards	-	105
Unrealized holding gains (losses) arising during the period	1,276	627
Change in foreign currency exchange rate adjustment	(6)	22
Change in DAC, VOBA, DSI and other contract holder funds	(261)	(168)
Income tax benefit (expense)	(395)	(136)
Less:		
Reclassification adjustment for gains (losses) included in net income (loss)	(103)	(38)
Associated amortization of DAC, VOBA, DSI and DFEL	1	(15)
Income tax benefit (expense)	36	19
Balance as of end-of-period	$ 3,627	$ 1,556
Unrealized OTTI on AFS Securities		
Balance as of beginning-of-year	$ (110)	$ (129)
(Increases) attributable to:		
Cumulative effect from adoption of new accounting standards	-	(5)
Gross OTTI recognized in OCI during the period	(79)	(27)
Change in DAC, VOBA, DSI and other contract holder funds	12	8
Income tax benefit (expense)	26	7
Decreases attributable to:		
Sales, maturities or other settlements of AFS securities	62	67
Change in DAC, VOBA, DSI and other contract holder funds	(8)	(13)
Income tax benefit (expense)	(20)	(19)
Balance as of end-of-period	$ (117)	$ (111)
Unrealized Gain (Loss) on Derivative Instruments		
Balance as of beginning-of-year	$ 119	$ (15)
Cumulative effect from adoption of new accounting standards	-	3
Unrealized holding gains (losses) arising during the period	37	(34)
Change in foreign currency exchange rate adjustment	2	(14)
Change in DAC, VOBA, DSI and DFEL	4	-
Income tax benefit (expense)	(16)	18
Less:		
Reclassification adjustment for gains (losses) included in net income (loss)	(7)	(9)
Associated amortization of DAC, VOBA, DSI and DFEL	1	1
Income tax benefit (expense)	2	3
Balance as of end-of-period	$ 150	$ (37)
Foreign Currency Translation Adjustment		
Balance as of beginning-of-year	$ 1	$ 1
Foreign currency translation adjustment arising during the period	(8)	(6)

Income tax benefit (expense)		3		2
Balance as of end-of-period	$	(4)	$	(3)
Funded Status of Employee Benefit Plans				
Balance as of beginning-of-year	$	(278)	$	(181)
Adjustment arising during the period		1		5
Income tax benefit (expense)		-		(2)
Balance as of end-of-period	$	(277)	$	(178)

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10. Realized Gain (Loss)

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2012	2011	2012	2011
Total realized gain (loss) related to certain investments (1)	$ (51)	$ (32)	$ (99)	$ (47)
Realized gain (loss) on the mark-to-market on certain instruments (2)	(19)	(1)	39	9
Indexed annuity net derivative results: (3)				
Gross gain (loss)	(3)	1	19	7
Associated amortization of DAC, VOBA, DSI and DFEL	1	-	(5)	(2)
Variable annuity net derivatives results: (4)				
Gross gain (loss)	148	34	14	44
Associated amortization of DAC, VOBA, DSI and DFEL	(33)	(11)	(11)	(18)
Total realized gain (loss)	$ 43	$ (9)	$ (43)	$ (7)

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

11. Stock-Based Incentive Compensation Plans

We sponsor various incentive plans for our employees and directors and for the employees and agents of our subsidiaries that provide for the issuance of stock options, performance shares (performance-vested shares as opposed to time-vested shares), stock appreciation rights ("SARs") and restricted stock units. We have a policy of issuing new shares to satisfy option exercises.

LNC stock-based awards granted were as follows:

	For the Three Months Ended June 30, 2012	For the Six Months Ended June 30, 2012
Awards		

10-year LNC stock options	41,536	870,210
Performance shares	15,815	294,758
SARs	-	80,225
Restricted stock units	82,004	686,230
Non-employee:		
Agent stock options	90	99,178
Director stock options	-	51,140
Director restricted stock units	12,218	22,346

12. Fair Value of Financial Instruments

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

	As of June 30, 2012		As of December 31, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
AFS securities:				
Fixed maturity securities	$ 79,191	$ 79,191	$ 75,433	$ 75,433
VIEs' fixed maturity securities	705	705	700	700
Equity securities	154	154	139	139
Trading securities	2,649	2,649	2,675	2,675
Mortgage loans on real estate	6,804	7,463	6,942	7,608
Derivative investments	3,399	3,399	3,151	3,151
Other investments	1,041	1,041	1,069	1,069
Cash and invested cash	5,257	5,257	4,510	4,510
Separate account assets	88,839	88,839	83,477	83,477
Liabilities				
Future contract benefits:				
Indexed annuity contracts embedded derivatives	(431)	(431)	(399)	(399)
GLB reserves embedded derivatives	(1,926)	(1,926)	(2,217)	(2,217)
Other contract holder funds:				
Remaining guaranteed interest and similar contracts	(1,034)	(1,034)	(1,114)	(1,114)
Account values of certain investment contracts	(27,916)	(31,554)	(27,468)	(30,812)
Short-term debt (1)	(300)	(302)	(300)	(309)
Long-term debt	(5,719)	(6,659)	(5,391)	(5,345)
Reinsurance related embedded derivatives	(185)	(185)	(168)	(168)
VIEs' liabilities - derivative instruments	(231)	(231)	(291)	(291)
Other liabilities:				
Deferred compensation plans	(358)	(358)	(354)	(354)
Credit default swaps	(11)	(11)	(16)	(16)

(1) The difference between the carrying value and fair value of short-term debt as of June 30, 2012, and December 31, 2011, related to current maturities of long-term debt.

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

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

Mortgage Loans on Real Estate

The fair value of mortgage loans on real estate is established using a discounted cash flow method based on credit rating, maturity and future income. The ratings for mortgages in good standing are based on property type, location, market conditions, occupancy, debt-service coverage, loan-to-value, quality of tenancy, borrower and payment record. The fair value for impaired mortgage loans 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. The inputs used to measure the fair value of our mortgage loans on real estate are classified as Level 2 within the fair value hierarchy.

Other Investments

The carrying value of our assets classified as other investments approximates fair value. Other investments include LPs and other privately held investments that are accounted for using the equity method of accounting and the carrying value is based on our proportional share of the net assets of the LPs. The inputs used to measure the fair value of our other investments are classified as Level 3 within the fair value hierarchy.

Other Contract Holder Funds

Other contract holder funds include remaining guaranteed interest and similar contracts and account values of certain investment contracts. The fair value for the remaining guaranteed interest and similar contracts is estimated using discounted cash flow calculations as of the balance sheet date. These calculations are based on interest rates currently offered on similar contracts with maturities that are consistent with those remaining for the contracts being valued. As of June 30, 2012, and December 31, 2011, the remaining guaranteed interest and similar contracts carrying value approximated fair value. The fair value of the account values of certain investment contracts is based on their approximate surrender value as of the balance sheet date. The inputs used to measure the fair value of our other contract holder funds are classified as Level 3 within the fair value hierarchy.

Short-Term and Long-Term Debt

The fair value of long-term debt is based on quoted market prices. For short-term debt, excluding current maturities of long-term debt, the carrying value approximates fair value. The inputs used to measure the fair value of our short-term and long-term debt are classified as Level 2 within the fair value hierarchy.

Financial Instruments Carried at Fair Value

We did not have any assets or liabilities measured at fair value on a nonrecurring basis as of June 30, 2012, or December 31, 2011, and we noted no changes in our valuation methodologies between these periods.

The following summarizes our financial instruments carried at fair value (in millions) on a recurring basis by the fair value hierarchy levels described in "Summary of Significant Accounting Policies" in Note 1 of our 2011 Form 10-K:

	As of June 30, 2012			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets				
Investments:				
Fixed maturity AFS securities:				
Corporate bonds	$ 62	$ 62,174	$ 1,678	$ 63,914
U.S. government bonds	482	34	1	517
Foreign government bonds	-	562	102	664
RMBS	-	7,013	184	7,197
CMBS	-	1,268	39	1,307
CDOs	-	-	120	120
State and municipal bonds	-	4,252	32	4,284
Hybrid and redeemable preferred securities	20	1,039	129	1,188
VIEs' fixed maturity securities	110	595	-	705
Equity AFS securities	45	24	85	154
Trading securities	2	2,575	72	2,649
Derivative investments	-	882	2,517	3,399
Cash and invested cash	-	5,257	-	5,257
Separate account assets	-	88,839	-	88,839
Total assets	$ 721	$ 174,514	$ 4,959	$ 180,194
Liabilities				
Future contract benefits:				
Indexed annuity contracts embedded derivatives	$ -	$ -	$ (431)	$ (431)
GLB reserves embedded derivatives	-	-	(1,926)	(1,926)
Long-term debt	-	(1,203)	-	(1,203)
Reinsurance related embedded derivatives	-	(185)	-	(185)
VIEs' liabilities - derivative instruments	-	-	(231)	(231)
Other liabilities:				
Deferred compensation plans	-	-	(358)	(358)
Credit default swaps	-	-	(11)	(11)
Total liabilities	$ -	$ (1,388)	$ (2,957)	$ (4,345)

	As of December 31, 2011			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets				
Investments:				
Fixed maturity AFS securities:				
Corporate bonds	$ 63			