November 21, 2003

Mr. Thomas Ray
Deputy Chief Auditor
Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Reference: PCAOB Rulemaking Docket Matter No. 008

Dear Mr. Ray:

We are pleased to submit this comment letter to the Public Company Accounting Oversight Board (PCAOB) in response to the PCAOB's request for comments regarding the proposed auditing standard, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction With an Audit of Financial Statements*, Release No. 2003-017. Our comments pertain to the financial reporting by Lincoln National Corporation, (LNC), that relates to life reinsurance operations that LNC has disposed of by transferring the business to an unrelated reinsurance company under indemnity reinsurance agreements.

LNC is a Fortune 500 financial services company providing life insurance, annuities, qualified retirement plans, and investment management products to retail and institution clients. In 2001, LNC disposed of its life reinsurance business by transferring the business to Swiss Re. The disposition was accomplished by a combination of sales of certain stock subsidiaries that had been wholly engaged in the reinsurance business and indemnity reinsurance transfers. Because a primary LNC subsidiary insurance company formerly engaged in the reinsurance business also conducts ongoing direct life insurance and annuity businesses, the indemnity reinsurance agreements were necessary for LNC to completely exit the life reinsurance business. In exiting these lines of business, LNC also entered into administration agreements with Swiss Re under which the administration and accounting for the business has been transferred to Swiss Re. Accordingly, LNC no longer manages or maintains the accounting records of the exited reinsurance business.

An indemnity reinsurance transfer, combined with an administrative services agreement, is typically used within the life insurance industry by companies that are completely exiting selected lines of business, while retaining other lines of business.

An alternative structure would be an assumption reinsurance transfer, which results in a complete release of the selling company from all legal liability associated with the underlying insurance business. However, obtaining the regulatory and policyholder consents required in an assumption reinsurance transfer is a very time-consuming, costly, and uncertain endeavor. For these reasons, dispositions of entire lines of business within the life insurance industry are often structured as indemnity reinsurance transfers.

Since the selling company is not relieved of its legal obligation with respect to the underlying insurance policies in an indemnity reinsurance transfer, FAS 113 requires the seller to retain the policyholder liabilities on its balance sheet along with an offsetting recoverable from the acquiring reinsurance company. Because the acquiring company obtains all rights and obligations relating to the underlying transferred business, the ongoing FAS 113 accounting associated with the life reinsurance business will have no net impact on selling company's financial statements. At the same time, by reflecting both the policyholder liabilities and an offsetting recoverable from the acquiring company on its balance sheet, the selling company's ongoing credit exposure to the acquiring company is reflected on the face of the selling company's balance sheet.

In addition to reflecting the policyholder liabilities and the recoverable from the acquiring company on its financial statements, FAS 113 also requires that the selling company defer the gain associated with the indemnity reinsurance disposition. The selling company must amortize this deferred gain into net income over the estimated life of the underlying business.

Since the selling company does not maintain or administer the life reinsurance business due to the sale and the corresponding transfer of administrative responsibilities, the selling company's financial reporting control processes related to the exited business are typically focused on the following matters: (a) the accurate accumulation of financial information supplied by the acquiring company, (b) reviewing the financial information for reasonableness, (c) reporting this information in the selling company's financial statements, and (d) properly accounting for the selling company's FAS 113 deferred gain. In addition, on an ongoing basis the selling company will monitor and evaluate the credit worthiness of the acquiring company.

Under these circumstances, the design and the operation of the policies and procedures related to internal controls over the financial reporting associated with the exited lines of business are not the responsibility of the selling company. The administrative efforts and costs that would be incurred by the selling company to document and test the acquiring company's controls over financial reporting, as it relates to the information provided to the selling company for the exited lines of business, would not produce any meaningful benefit to the selling company or to the users of the selling company's financial statements. Once again, this is because there simply is no net impact on the selling company's financial statements related to the exited business.

Support for this view can be derived from the general concepts included within Appendix B of PCAOB Release No. 2003-017, at paragraph B16 and footnote 1 which provide that some accounts can be excluded from the documenting and testing of controls when the company does not have sufficient control or responsibility with respect to those accounts. In addition, paragraphs B18 and B19 provide some relevant guidance under the topic of *Identifying Significant Accounts*.

To clarify this matter, we request that the PCAOB issue explicit guidance providing that LNC, and other similarly situated life insurers, should not be required to document and test the internal controls of the acquiring company related to the reporting of financial information on exited lines of business that have been transferred under indemnity reinsurance agreements.

Thank you for the opportunity to comment on this proposed auditing standard. If questions arise, or additional discussion on this topic is desired, please contact me at 215 448-1408.

Very truly yours,

Casey J Trumble
Senior Vice President, Tax & Reporting