

IDS LIFE INSURANCE COMPANY

MANAGEMENT'S DISCUSSION AND ANALYSIS OF CONSOLIDATED FINANCIAL CONDITION AND RESULTS OF OPERATIONS

2002 Compared to 2001:

Consolidated net income was \$382 million in 2002, compared to consolidated net loss of \$65 million in 2001. Consolidated income before income tax expense totaled \$470 million in 2002, compared with a consolidated loss before income tax benefit and cumulative effect of accounting change of \$189 million in 2001. The significant increase in net income was primarily a result of the 2001 writedown and sale of high-yield securities that reduced risk within the investment portfolio, as explained below.

Total revenues increased by 34% to \$2.8 billion in 2002, compared with \$2.1 billion in 2001. The increase was primarily due to higher net investment income and lower levels of realized losses, primarily reflecting the impact of the 2001 high-yield securities' realized losses. In addition, invested assets were higher in 2002. Insurance premiums and policyholder and contractholder charges also increased. Partially offsetting were declines in management and other fees, as separate account assets dropped 20% from 2001 levels.

Insurance and investment contract considerations received increased to \$8.3 billion in 2002, compared with \$5.8 billion in 2001. The increase is primarily due to higher fixed annuity sales in both the advisor distribution channel and through third parties.

Net investment income, the largest component of revenues, increased by \$76 million from the prior year. This increase primarily reflects the effect of credit related yield adjustments on fixed maturity investments in 2001 and higher invested asset levels in 2002, which were somewhat offset by lower portfolio yields in 2002, driven by investment portfolio repositioning as described below. Investment income also benefited from the effect of less depreciation in the S&P 500 this year on the value of options hedging outstanding equity indexed annuities, which is offset in the related provisions for losses and benefits.

Policyholder and contractholder charges, which consist primarily of cost of insurance charges on universal life-type policies, increased 7% to \$523 million in 2002, compared with \$490 million in 2001. This increase relates to the 10% growth in total life insurance in force, which grew to \$119 billion at December 31, 2002.

Management and other fees decreased 14 percent to \$405 million in 2002, compared with \$473 million in 2001. This decrease was primarily due to lower levels of average separate account assets, resulting primarily from market depreciation of equity securities as weak equity markets continued throughout the year. The Company provides investment management services for many of the mutual funds that are available as investment options for variable annuities and variable life insurance. The Company also receives mortality and expense risk fees from the separate accounts based on the level of assets.

Net realized losses on investments were \$5 million in 2002, compared to net realized losses of \$650 million in 2001. The 2002 net realized losses include \$146 million from impairments recognized on available-for-sale securities during the year (including \$45 million related to directly-held WorldCom debt holdings). The Company sold approximately \$10.5 billion of its invested assets on a consolidated basis during 2002. In addition, approximately \$3 billion in investments were redeemed during the year. The cash generated by these sales and redemptions has been or will be invested. The net realized loss for 2001 was comprised of a \$143 million pretax net loss in the first quarter resulting primarily from the recognition of impairment losses and the sale of certain high-yield securities; a \$227 million writedown in the second quarter to recognize the impact of higher default rate assumptions on certain structured investments; a \$262 million writedown of lower-rated securities (most of which were sold during 2001) in the second quarter primarily in connection with the Company's decision to lower its risk profile by reducing the level of its high-yield fixed maturity investment portfolio, allocating holdings toward stronger credits, and reducing the

concentration of exposure to individual companies and industry sectors; and \$18 million of other net losses primarily related to the sale and write-down of other investments.

Total benefits and expenses increased to \$2.4 billion in 2002 from \$2.3 billion in 2001. The largest component of expenses, interest credited to policyholder accounts for universal life-type insurance and investment contracts, increased 2% to \$1.2 billion, reflecting the growth in fixed annuities in force and the effect of less depreciation in the S&P 500 on equity indexed annuities, despite lower interest crediting rates from the lower interest rate environment. The \$56 million increase in total death and other benefits reflects higher insurance claims and a significant increase in guaranteed minimum death benefits on variable annuity contracts with \$37 million expensed in 2002 versus \$16 million in 2001. 2001's results also include an \$11 million charge for anticipated insured loss claims from the September 11th terrorist attacks while 2002 results include a \$7 million reversal of a portion of these reserves as a result of lower than anticipated insured loss claims. Deferred acquisition costs (DAC) of \$3.3 billion and \$3.1 billion are on the Company's balance sheet at December 31, 2002 and 2001, respectively. These balances are approximately \$1.7 billion related to life and health insurance and \$1.6 billion to annuities. In 2001, approximately \$1.6 billion related to life and health insurance and \$1.5 billion to annuities. Amortization of DAC decreased to \$312 million in 2002, compared to \$371 million in 2001. The decrease in 2002's amortization was primarily from the \$67 million amortization increase in the first quarter of 2001 of DAC for variable annuity and insurance products as a result of the significant decline in equity-based separate account values and the associated fee revenues. In addition, during the third quarter of 2002 the Company completed a comprehensive review of its DAC related practices that resulted in a net increase in DAC amortization, as described below.

Other insurance and operating expenses increased to \$438 million in 2002, compared to \$408 million in 2001. This increase was primarily due to lower levels of expenses deferred in 2002 as described below and from business growth and technology costs related to growth initiatives.

The costs of acquiring new business, including for example, direct sales commissions, related sales incentive bonuses and awards, underwriting costs, policy issue costs and other related costs, have been deferred on the sale of insurance and annuity contracts. The DAC for universal life and variable universal life insurance and certain installment annuities are amortized as a percentage of the estimated gross profits expected to be realized on the policies. DAC for other annuities are amortized using the interest method. For traditional life, disability income and long-term care insurance policies, the costs are amortized in proportion to premium revenue.

Amortization of DAC requires the use of certain assumptions including interest margins, mortality rates, persistency rates, maintenance expense levels and customer asset value growth rates for variable products. The customer asset value growth rate is the rate at which contract values are assumed to appreciate in the future. This rate is net of asset fees, and anticipates a blend of equity and fixed income investments. Management routinely monitors a wide variety of trends in the business, including comparisons of actual and assumed experience. Management reviews and, where appropriate, adjusts its assumptions with respect to customer asset value growth rates on a quarterly basis.

Management monitors other principal DAC assumptions, such as persistency rates, mortality rates, interest margins and maintenance expense levels each quarter. Unless management identifies a material deviation over the course of the quarterly monitoring process, management reviews and updates these DAC assumptions annually in the third quarter of each year. When assumptions are changed, the percentage of estimated gross profits or portion of interest margins used to amortize DAC may also change. A change in the required amortization percentage is applied retrospectively; an increase in amortization percentage will result in an acceleration of DAC amortization while a decrease in amortization percentage will result in a deceleration of DAC amortization. The impact on results of operations of changing assumptions with respect to the amortization of DAC can be either positive or negative in any particular period, and is reflected in the period that such changes are made. In 2002, excluding the third quarter, the impact of resetting these assumptions, along with the impact of unfavorable equity market performance, was an acceleration of \$22 million pretax of DAC amortization. Third quarter impacts are described below.

During the third quarter of 2002, the Company completed a comprehensive review of its DAC related practices. The specific areas reviewed included costs deferred, DAC amortization periods, customer asset value growth rate

assumptions (which are typically reviewed on a quarterly basis) and other assumptions, including mortality rates and product persistency (which are typically updated on an annual basis in the third quarter). As a result of this review, the Company took certain actions that resulted in a net \$37 million increase in expenses in the third quarter of 2002.

The Company reset its customer asset value growth rate assumptions for variable annuity and variable life products to anticipate near-term and long-term growth at an annual rate of 7%. The customer asset value growth rate is the rate at which contract values are assumed to appreciate in the future. This rate is net of asset fees, and anticipates a blend of equity and fixed income investments. Prior to resetting these assumptions, the Company was projecting long-term customer asset value growth at 7.5% and near-term growth at approximately twice that rate. The impact of resetting these assumptions, along with the impact of unfavorable third quarter 2002 equity market performance, was an acceleration of \$173 million pretax of DAC amortization.

Going forward, the Company intends to continue to use a mean reversion method as a guideline in setting the near-term customer asset value growth rate, also referred to as the mean reversion rate. In periods when market performance results in actual contract value growth at a rate different than that assumed, the Company will reassess the near-term rate in order to continue to project its best estimate of long-term growth. For example, if actual contract value growth during a quarter is less than 7% on an annualized basis, the Company would increase the mean reversion rate assumed over the near term to the rate needed to achieve the long-term annualized growth rate of 7% by the end of that period, assuming this long-term view is still appropriate.

The Company revised certain mortality and persistency assumptions for universal and variable universal life insurance products and fixed and variable annuity products to better reflect actual experience and future expectations. The Company updated the mortality table used in pricing universal and variable universal life products and in valuing the associated DAC. The most recently published life insurance industry mortality table was used as a starting point, and was then modified based on the Company's experience. The Company also observed that recent persistency of its universal life products was consistently better than expected, and determined the trend justified an improvement in assumed persistency rates. Additionally, the Company reviewed and updated persistency assumptions for fixed and variable deferred annuity products. The Company also reviewed the periods over which DAC is amortized for fixed and variable deferred annuity products. Analysis showed that significant volumes of advisor-distributed fixed annuities were expected to persist beyond the Company's ten-year DAC amortization period. As a result, the Company extended the amortization period from 10 to 15 years to be more consistent with the period over which significant profits were expected and that would result in a more appropriate matching of revenues and expense. Similarly, the Company made slight increases in the amortization periods used for certain blocks of advisor-distributed variable annuities. These changes, along with revised assumptions projecting more favorable persistency and mortality rates, resulted in a decrease in DAC expense of \$155 million pretax.

Finally, the Company reviewed its acquisition costs to clarify those costs that vary with and are primarily related to the acquisition of new and renewable annuity and insurance contracts. The Company revised the types and amounts of costs deferred, in part to reflect the impact of advisor platform changes and the effects of related reengineering. This resulted in an increase in expense of \$19 million pretax recognized in the third quarter of 2002.

The adjustments made to customer asset value growth rate assumptions should reduce the risk of adverse DAC adjustments going forward, while changes made to mortality and persistency assumptions and DAC amortization periods somewhat increase the risk of adverse adjustments. Overall, the Company believes it is less exposed to the risk of adverse DAC adjustments as a result of these changes. The changes relating to the types and amounts of costs deferred will somewhat accelerate the recognition of ongoing expenses, although the impact of this should be offset to some extent as reengineering and other cost control initiatives are expected to mitigate their impact.

2001 Compared to 2000:

Consolidated net loss was \$65 million in 2001, compared to consolidated net income of \$586 million in 2000. Consolidated loss before income tax benefit and cumulative effect of accounting change totaled \$189 million in

2001, compared with consolidated income before income tax expense of \$807 million in 2000. This decline was primarily the result of a \$633 million increase in net realized loss on investments and a \$245 million decrease in investment income.

Total revenues decreased to \$2.1 billion in 2001, compared with \$3.0 billion in 2000. The decrease was primarily due to decreases in net investment income and from the realized investments losses. Net investment income, the largest component of revenues, decreased by \$245 million from the prior year, primarily reflecting credit related yield adjustments on fixed maturity investments and overall lower investment yields.

Total premiums and investment contract deposits received decreased to \$5.8 billion in 2001, compared with \$6.9 billion in 2000. The reduction is primarily due to lower variable annuity sales.

Policyholder and contractholder charges, which consist primarily of cost of insurance charges on universal life-type policies, increased 12 percent to \$490 million in 2001, compared with \$438 million in 2000. This increase reflects increased total life insurance in force, which grew 10 percent to \$108 billion at December 31, 2001.

Management and other fees decreased 21 percent to \$473 million in 2001, compared with \$598 million in 2000. This decrease reflects lower average separate account assets outstanding, resulting primarily from equity market depreciation. The Company provides investment management services for many of the mutual funds that are available as investment options for variable annuities and variable life insurance. The Company also receives a mortality and expense risk fee from the separate accounts.

Net realized losses on investments were \$650 million in 2001, compared to net realized losses of \$17 million in 2000. The net loss for the year was comprised of a \$143 million pretax net loss in the first quarter resulting primarily from the recognition of impairment losses and the sale of certain high-yield securities; a \$227 million writedown in the second quarter to recognize the impact of higher default rate assumptions on certain structured investments; a \$262 million writedown of lower-rated securities (most of which were sold during 2001) in the second quarter primarily in connection with the Company's decision to lower its risk profile by reducing the level of its high-yield fixed maturity investment portfolio, allocating holdings toward stronger credits, and reducing the concentration of exposure to individual companies and industry sectors; and \$18 million of other net losses primarily related to the sale and write-down of other investments.

Total benefits and expenses increased slightly to \$2.3 billion in 2001 from \$2.2 billion in 2000. The largest component of expenses, interest credited to policyholder accounts for universal life-type insurance and investment contracts, decreased slightly to \$1.1 billion, reflecting a slight decrease in fixed annuities in force and lower interest crediting rates due to the lower interest rate environment. Amortization of DAC increased to \$371 million in 2001, compared to \$362 million in 2000. The increase was primarily due to DAC unlocking adjustments (see footnote one of the attached financial statements for the definition of unlocking adjustments), which resulted in a net increase in amortization of \$33.6 million in 2001 and a net decrease in amortization of \$12.3 million in 2000. Amortization, excluding unlocking adjustments, was significantly less in 2001 than in 2000, due primarily to the significant drop in equity-based separate account values and associated fee revenue.

Other insurance and operating expenses increased to \$408 million in 2001, compared to \$379 million in 2000. This increase was primarily a result of business growth and technology costs related to growth initiatives.

Impact of Market Volatility on Results of Operations

Various aspects of the Company's business can be significantly impacted by equity market levels and other market-based factors. One of these items is the management fee revenue which is based on the market value of separate account assets. Other areas impacted by market volatility involve DAC (as noted above), structured investments and the variable annuity guaranteed minimum death benefit feature. The value of the Company's structured investment portfolio is impacted by various market factors. These investments include collateralized debt obligations and

secured loan trusts (backed by high-yield bonds and bank loans), which are held by the Company through interests in special purpose entities. The carrying value of these investments is based on estimated cash flow projections, which are affected by factors such as default rates, persistency of defaults, recovery rates and interest rates, among others. Persistency of, or increases in, these default rates could result in negative adjustments to the market values of these investments in the future, which would adversely impact results of operations. Conversely, a decline in the default rates would result in higher values and would benefit future results of operations.

The majority of the variable annuity contracts offered by the Company contain guaranteed minimum death benefit (GMDB) provisions. At time of issue, these contracts typically guarantee the death benefit payable will not be less than the amount invested, regardless of the performance of the customer's account. Most contracts also provide for some type of periodic adjustment of the guaranteed amount based on the change in the value of the contract. A large portion of the Company's contracts containing a GMDB provision adjust once every six years. The periodic adjustment of these contracts can either increase or decrease the guaranteed amount though not below the amount invested adjusted for withdrawals. When market values of the customer's accounts decline, the death benefit payable on a contract with a GMDB may exceed the accumulated contract value. Currently, the amount paid in excess of contract value is expensed when payable.

Certain Critical Accounting Policies

The Company's significant accounting policies are described in Note 1 to the Consolidated Financial Statements. The following provides information about certain critical accounting policies that are important to the Consolidated Financial Statements and that involve estimates requiring significant management assumptions and judgments about the effect of matters that are uncertain. These policies relate to the recognition of impairment within the investment portfolio, deferred policy acquisition costs and insurance and annuity reserves.

Investments

All fixed maturity securities and marketable equity securities are classified as available-for-sale and carried at fair value. Unrealized gains and losses on securities classified as available-for-sale are carried as a separate component of accumulated other comprehensive income (loss), net of the related deferred policy acquisition costs and income taxes. Gains and losses are recognized in the results of operations upon disposition of the securities using the specific identification method. In addition, losses are also recognized when management determines that a decline in value is other-than-temporary, which requires judgment regarding the amount and timing of recovery. Indicators of other-than-temporary impairment for fixed maturity securities include, but are not limited to, issuer downgrade, default or bankruptcy. The Company also considers the extent to which cost exceeds fair value, the duration of time of that decline, and management's judgment about the issuer's current and prospective financial condition. The charges are reflected in net realized gain (loss) on investments within the Consolidated Statements of Income.

Fair value of fixed maturity and equity securities is generally based on quoted market prices. However, the Company's investment portfolio also contains structured investments of various asset quality, including collateralized debt obligations (CDOs) and secured loan trusts (SLTs) (backed by high-yield bonds and bank loans), which are not readily marketable. As a result, the carrying values of these structured investments are based on estimated cash flow projections which require a significant degree of management judgment as to default and recovery rates of the underlying investments and, as such, are subject to change. If actual future cash flows are less than projected, additional losses would be realized.

The reserve for losses on mortgage loans on real estate is measured as the excess of the loan's recorded investment over its present value of expected principal and interest payments discounted at the loan's effective interest rate or the fair value of collateral. Additionally, the level of the reserve for losses considers other factors, including historical experience and current economic and political conditions. Management regularly evaluates the adequacy of the reserve for mortgage loan losses and believes it is adequate to absorb estimated losses in the portfolio.

Deferred policy acquisition costs

The costs of acquiring new business, including for example, direct sales commissions, related sales incentive bonuses and awards, underwriting costs, policy issue costs and other related costs, have been deferred on the sale of insurance and annuity contracts. The DAC for universal life and variable universal life insurance and certain installment annuities are amortized as a percentage of the estimated gross profits expected to be realized on the policies. DAC for other annuities are amortized using the interest method. For traditional life, disability income and long-term care insurance policies, the costs are amortized in proportion to premium revenue.

Amortization of DAC requires the use of certain assumptions including interest margins, mortality rates, persistency rates, maintenance expense levels and customer asset value growth rates for variable products. The customer asset value growth rate is the rate at which contract values are assumed to appreciate in the future. This rate is net of asset fees, and anticipates a blend of equity and fixed income investments. Management routinely monitors a wide variety of trends in the business, including comparisons of actual and assumed experience. Management reviews and, where appropriate, adjusts its assumptions with respect to customer asset value growth rates on a quarterly basis.

Management monitors other principal DAC assumptions, such as persistency rates, mortality rates, interest margins and maintenance expense levels each quarter. Unless management identifies a material deviation over the course of the quarterly monitoring, management reviews and updates these DAC assumptions annually in the third quarter of each year. When assumptions are changed, the percentage of estimated gross profits or portion of interest margins used to amortize DAC may also change. A change in the required amortization percentage is applied retrospectively; an increase in amortization percentage will result in an acceleration of DAC amortization while a decrease in amortization percentage will result in a deceleration of DAC amortization. The impact on results of operations of changing assumptions with respect to the amortization of DAC can be either positive or negative in any particular period, and is reflected in the period that such changes are made.

Liabilities for future policy benefits

Liabilities for fixed and variable universal life insurance and fixed and variable deferred annuities are accumulation values.

Liabilities for equity indexed deferred annuities issued before 1999 are equal to the present value of guaranteed benefits and the intrinsic value of index-based benefits. Liabilities for equity indexed deferred annuities issued in 1999 or later are equal to the accumulation of host contract values covering guaranteed benefits and the market value of embedded equity options.

Liabilities for fixed annuities in a benefit status are based on established industry mortality tables and interest rates ranging from 5% to 9.5%, depending on year of issue, with an average rate of approximately 6.5%.

Liabilities for future benefits on traditional life insurance, principally term and whole life insurance, are based on the net level premium method, using anticipated mortality, policy persistency and interest earning rates. Anticipated mortality rates are based on established industry mortality tables, with modifications based on Company experience. Anticipated policy persistency rates vary by policy form, issue age and policy duration with persistency on level term and cash value plans generally anticipated to be better than persistency on yearly renewable term insurance plans. Anticipated interest rates range from 4% to 10%, depending on policy form, issue year and policy duration.

Liabilities for future disability income and long-term care policy benefits include both policy reserves and claim reserves. Policy reserves are based on the net level premium method, using anticipated morbidity, mortality, policy persistency and interest earning rates. Anticipated morbidity and mortality rates are based on established industry morbidity and mortality tables. Anticipated policy persistency rates vary by policy form, issue age, policy duration and, for disability income policies, occupation class. Anticipated interest rates for disability income and long-term care policy reserves are 3% to 9.5% at policy issue and grade to ultimate rates of 5% to 7% over 5 to 10 years.

Claim reserves are calculated based on claim continuance tables and anticipated interest earnings. Anticipated claim continuance rates are based on established industry tables. Anticipated interest rates for claim reserves for both disability income and long-term care range from 5% to 8%.

Liabilities for reported and unpaid life insurance claims are equal to the death benefits payable. For disability income and long-term care claims, unpaid claims liabilities are equal to benefit amounts due and accrued. Liabilities for incurred but not reported claims are estimated based on periodic analysis of the actual reported claim lag. Where applicable, amounts recoverable from reinsurers are separately recorded as receivables. For life insurance, no claim adjustment expense reserve is held. The claim adjustment expense reserves for disability income and long-term care are based on the claim reserves.

Risk Management

The sensitivity analysis discussed below estimates the effects of hypothetical sudden and sustained changes in the applicable market conditions of two different types of market risk on the ensuing year's earnings, based on year-end positions. The market changes, assumed to occur as of year-end, are a 100 basis point increase in market interest rates and a 10 percent decline in the value of equity securities held in separate accounts. Computations of the prospective effects of hypothetical interest rate and equity market changes are based on numerous assumptions, including relative levels of market interest rates and equity prices, as well as the levels of assets and liabilities. The hypothetical changes and assumptions will be different from what actually occur. Furthermore, the computations do not incorporate actions that management could take if the hypothetical market changes actually took place. As a result, actual earnings consequences will differ from those quantified below.

The Company primarily invests in fixed income securities over a broad range of maturities for the purpose of providing fixed annuity and fixed universal life contractholders with a competitive rate of return on their investments while controlling risk, and to provide a dependable and targeted spread between the interest rate earned on investments and the interest rate credited to contractholders' accounts. The Company does not invest in securities to generate short-term trading profits.

IDS Life and each of its insurance subsidiaries' investment committees meet periodically. With respect to IDS Life of New York and American Centurion Life, the full Board acts as the investment committee. At these meetings, the committee or Board reviews models projecting different interest rate scenarios, risk/return measures, and their effect on profitability. The committee or Board also reviews the distribution of assets in the portfolio by type and credit risk sector. The objective of the committee or Board is to structure the investment security portfolio based upon the type and expected behavior of products in the liability portfolio so as to meet contractual obligations and to achieve targeted levels of profitability within defined risk parameters.

Rates credited to contract owners' accounts are generally reset at shorter intervals than the maturity of underlying investments. Therefore, margins may be negatively impacted by increases in the general level of interest rates. Part of the investment committee's or Board's strategy includes the use of derivatives, such as interest rate caps, swaps and floors, for risk management purposes. These derivatives help protect margins by increasing investment returns if there is a sudden and severe rise in interest rates, thereby mitigating the impact of an increase in rates credited to contract owner's fixed accounts. Conversely, in a low interest rate environment, such as that experienced recently, margins may be negatively impacted as the interest rates available on the Company's investments approaches the guaranteed minimum interest rates on insurance or annuity contracts. This negative impact may be compounded by the fact that many of the Company's interest bearing investments are callable or prepayable by the issuer and calls and prepayments are more likely to occur in a low interest rate environment.

The negative effect on the Company's pretax earnings of a 100 basis point increase in interest rates, which assumes repricings and customer behavior based on the application of proprietary models to the book of business at December 31, 2002, would be approximately \$11 million.

On a certain annuity product, the interest is credited to contractholders' accounts based upon the relative change in a major stock market index between the beginning and end of the product's term. As a means of hedging the Company's obligation under the provisions of this product, the committee's strategy is to purchase and write options on a major stock market index, and to purchase futures which are marked to market daily and exchange traded, exposing the Company to no counterparty risk. At December 31, 2002 equity-based derivatives with a net notional amount of \$225 million were outstanding to hedge these equity market exposures.

The amount of the fee income the Company receives is based upon the daily market value of the separate account assets. As a result, the Company's fee income would be negatively impacted by a decline in the equity markets. Another part of the investment committee's strategy is to use index options to manage the equity market risk related to fee income. These derivatives help protect fee income by providing option income when there is a significant decline in the equity markets. The Company did not have equity-based derivatives outstanding at December 31, 2002 for this purpose.

The negative effect on the Company's pretax earnings of a 10 percent decline in equity prices would be approximately \$23 million based on separate account assets under management as of December 31, 2002.

Liquidity and Capital Resources

The liquidity requirements of the Company are generally met by funds provided by premiums, investment income, proceeds from sales of investments as well as maturities, periodic repayments of investment principal and capital contributions. Maturities of the Company's investments is largely matched with the expected future payments of insurance and annuity obligations.

The primary uses of funds are policy benefits, commissions and operating expenses, policy loans, dividends and investment purchases.

The Company has available lines of credit with AEFC aggregating \$200 million (\$100 million committed and \$100 million uncommitted). There were no borrowings outstanding at December 31, 2002. At December 31, 2002, the Company had outstanding reverse repurchase agreements totaling \$225 million. Both the line of credit and the reverse repurchase agreements are used strictly as short-term sources of funds.

At December 31, 2002, investments in fixed maturities comprised 84 percent of the Company's total invested assets and primarily include corporate debt, mortgage and other asset-backed securities. Approximately 49 percent is invested in GNMA, FNMA and FHLMC mortgage-backed securities which are considered AAA quality. The Company's corporate securities comprise a diverse portfolio with the largest concentrations accounting for approximately 63 percent of the portfolio, in the following industries: banking and finance, utilities, communication and media and transportation.

At December 31, 2002, approximately 7 percent of the Company's investments in fixed maturities were below investment grade bonds. These investments may be subject to a higher degree of risk than the investment grade issues because of the borrower's generally greater sensitivity to adverse economic conditions, such as a recession or increasing interest rates, and in certain instances, the lack of an active secondary market. Expected returns on below investment grade bonds reflect consideration of such factors. The Company has identified those fixed maturities for which a decline in fair value is determined to be other-than-temporary, and has written them down to fair value with a charge to earnings.

During 2002, the Company continued to hold investments in CDOs and SLTs, some of which are also managed by a related party. The Company invested in CDOs and SLTs as part of its investment strategy in order to pay a competitive rate to contractholders' accounts. The Company's exposure as an investor is limited solely to its aggregate investment in the CDOs and SLTs, and it has no obligations or commitments, contingent or otherwise, that could require any further funding of such investments. As of December 31, 2002, the carrying values of the CDO

residual tranches and SLT notes were \$13 million and \$657 million, respectively. CDOs and SLTs are illiquid investments. As an investor in the residual tranche of CDOs, the Company's return correlates to the performance of portfolios of high-yield bonds and/or bank loans. As a noteholder of SLTs, the Company's return is based on a reference portfolio of loans. The carrying value of the CDO and SLT investments and the Company's projected return are based on discounted cash flow projections that require a significant degree of management judgment as to assumptions primarily related to default and recovery rates of the high-yield bonds and/or bank loans either held directly by the CDO or in the reference portfolio of the SLT and, as such, are subject to change. Generally, the SLTs are structured such that the principal amount of the loans in the reference portfolio may be up to five times that of the par amount of the notes held by the Company. Although the exposure associated with the Company's investment in CDOs and SLTs is limited to the carrying value of such investments, they are volatile investments and have a substantial degree of risk associated with them because the amount of the initial value of the loans and/or other debt obligations in the related portfolios is significantly greater than the Company's exposure. Deterioration in the value of the high-yield bonds or bank loans would likely result in deterioration of the Company's investment return with respect to the relevant CDO or SLT, as the case may be. In the event of significant deterioration of a portfolio, the relevant CDO or SLT may be subject to early liquidation, which could result in further deterioration of the investment return or, in severe cases, loss of the carrying amount.

During 2001, the Company placed a majority of its rated CDO securities and related accrued interest, as well as a relatively minor amount of other liquid securities, (collectively referred to as transferred assets), having an aggregate book value of \$675 million, into a securitization trust. In return, the Company received \$90 million in cash (excluding transaction expenses) relating to sales to unaffiliated investors and retained interests in the trust with allocated book amounts aggregating \$586 million. As of December 31, 2002, the retained interests had a carrying value of \$562 million, of which \$388 million is considered investment grade. The Company has no obligations, contingent or otherwise, to such unaffiliated investors. One of the results of this transaction is that increases or decreases in future cash flows of the individual CDOs are combined into one overall cash flow for purposes of determining the carrying value of the retained interests and related impact on results of operations.

At December 31, 2002, net unrealized gains on available-for-sale fixed maturity securities included \$1,029 million of gross unrealized gains and \$186 million of gross unrealized losses. The Company does not classify fixed maturity securities as held-to-maturity.

At December 31, 2002, the Company had a reserve for losses on mortgage loans totaling \$35 million and on real estate investments totaling \$nil.

In 2002, the Company received capital contributions from AEFC totaling \$400 million and paid dividends of \$70 million to AEFC.

The economy and other factors cause insurance companies to go under regulatory supervision. These situations result in assessments by state guaranty associations to cover losses to policyholders of insolvent or rehabilitated companies. Some assessments can be partially recovered through a reduction in future premium taxes in certain states. The Company established an asset for guaranty association assessments paid to those states allowing a reduction in future premium taxes over a reasonable period of time. The asset is being amortized as premium taxes are reduced. The Company has also estimated the potential effect of future assessments on the Company's financial position and results of operations and has established a reserve for such potential assessments.

The National Association of Insurance Commissioners (NAIC) established risk-based capital (RBC) standards for life insurance companies to determine capital requirements based upon the risks inherent in its operations. These standards require the computation of a RBC amount which is then compared to a company's actual total adjusted statutory capital. The computation involves applying factors to various statutory financial data to address four primary risks: asset default, adverse insurance experience, interest rate risk and external events. These standards provide for regulatory attention when the percentage of total adjusted capital to authorized control level RBC is below certain levels. As of December 31, 2002, the Company's total adjusted capital was well in excess of the levels

requiring regulatory attention. In 2003, any dividend distributions in excess of 10 percent of the statutory capital of the Company would require approval of the Department of Commerce of the State of Minnesota.

Forward-Looking Statements

Certain statements in item #7 of this Form 10-K Annual Report contain forward-looking statements which are subject to risks and uncertainties that could cause results to differ materially from such statements. The words “believe,” “expect,” “anticipate,” “optimistic,” “intend,” “plan,” “aim,” “will,” “should,” “could,” “likely,” and similar expressions are intended to identify forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date on which they are made. The Company undertakes no obligation to publicly update or revise any forward-looking statements. Important factors that could cause actual results to differ materially from the Company’s forward-looking statements include, but are not limited to: fluctuations in external markets, which can affect the amount and types of investment products sold, the market value of its managed assets, management and other fees received based on those assets and the amount of amortization of DAC; potential deterioration in high-yield and other investments, which could result in further losses in the Company’s investment portfolio; changes in assumptions relating to DAC which also could impact the amount of DAC amortization; the ability to sell certain high-yield investments at expected values and within anticipated timeframes and to maintain its high-yield portfolio at certain levels in the future; the types and the value of certain death benefit features on variable annuity contracts; the affect of assessments and other surcharges for guaranty funds; the response of reinsurance companies under reinsurance contracts; the impact of reinsurance rates and the availability and adequacy of reinsurance to protect the Company against losses; negative changes in the Company’s and its subsidiaries’ credit ratings; increasing competition in all the Company’s major businesses; the adoption of recently issued rules related to the consolidation of variable interest entities, including those involving CDOs and SLTs that the Company invests in which could affect both the Company’s balance sheet and results of operations; and outcomes of litigation.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED BALANCE SHEETS
December 31,
(In thousands, except share amounts)

	2002	2001
<u>ASSETS</u>		
Investments:		
Available-for-sale:		
Fixed maturities, at fair value (amortized cost: 2002, \$23,209,226; 2001, \$20,022,072)	\$24,052,104	\$20,157,137
Common stocks, at fair value (cost: 2002, \$19; 2001, \$805)	21	1,704
Mortgage loans on real estate	3,417,651	3,680,394
Policy loans	597,144	619,571
Other investments	<u>752,558</u>	<u>621,897</u>
Total investments	28,819,478	25,080,703
Cash and cash equivalents	4,424,061	1,150,251
Amounts recoverable from reinsurers	633,510	529,166
Amounts due from brokers	501	90,794
Other accounts receivable	56,245	46,349
Accrued investment income	296,595	278,199
Deferred policy acquisition costs	3,309,783	3,107,187
Deferred income taxes, net	--	156,308
Other assets	117,788	123,246
Separate account assets	<u>21,980,674</u>	<u>27,333,697</u>
Total assets	<u>\$59,638,635</u>	<u>\$57,895,900</u>

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED BALANCE SHEETS (continued)
December 31,
(In thousands, except share amounts)

<u>LIABILITIES AND STOCKHOLDER'S EQUITY</u>	<u>2002</u>	<u>2001</u>
Liabilities:		
Future policy benefits:		
Fixed annuities	\$23,411,314	\$19,592,273
Universal life-type insurance	3,515,010	3,433,904
Traditional life insurance	247,441	241,165
Disability income and long-term care insurance	1,466,171	1,227,172
Policy claims and other policyholders' funds	85,400	71,879
Amounts due to brokers	3,342,989	1,740,031
Deferred income taxes, net	182,059	--
Other liabilities	463,326	437,017
Separate account liabilities	<u>21,980,674</u>	<u>27,333,697</u>
Total liabilities	<u>54,694,384</u>	<u>54,077,138</u>
Commitments and contingencies		
Stockholder's equity:		
Capital stock, \$30 par value per share;		
100,000 shares authorized, issued and outstanding	3,000	3,000
Additional paid-in capital	1,088,327	688,327
Accumulated other comprehensive income, net of tax:		
Net unrealized securities gains	497,319	83,443
Net unrealized derivative gains (losses)	<u>764</u>	<u>1,332</u>
Total accumulated other comprehensive income	498,083	84,775
Retained earnings	<u>3,354,841</u>	<u>3,042,660</u>
Total stockholder's equity	<u>4,944,251</u>	<u>3,818,762</u>
Total liabilities and stockholder's equity	<u>\$59,638,635</u>	<u>\$57,895,900</u>

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF INCOME
Years ended December 31,
(In thousands)

	<u>2002</u>	<u>2001</u>	<u>2000</u>
<u>REVENUES</u>			
Premiums:			
Traditional life insurance	\$ 67,978	\$ 59,415	\$ 56,187
Disability income and long-term care insurance	<u>273,737</u>	<u>255,428</u>	<u>231,311</u>
Total premiums	341,715	314,843	287,498
Net investment income	1,561,856	1,485,688	1,730,605
Policyholder and contractholder charges	522,777	489,583	438,127
Management and other fees	404,787	473,406	598,168
Net realized loss on investments	<u>(4,507)</u>	<u>(649,752)</u>	<u>(16,975)</u>
Total revenues	<u>2,826,628</u>	<u>2,113,768</u>	<u>3,037,423</u>
<u>BENEFITS AND EXPENSES</u>			
Death and other benefits:			
Traditional life insurance	36,881	35,519	29,042
Universal life-type insurance and investment contracts	221,544	175,247	131,467
Disability income and long-term care insurance	52,962	44,725	40,246
Increase in liabilities for future policy benefits:			
Traditional life insurance	2,768	7,231	5,765
Disability income and long-term care insurance	134,605	123,227	113,239
Interest credited on universal life-type insurance and investment contracts	1,157,636	1,137,636	1,169,641
Amortization of deferred policy acquisition costs	312,402	371,342	362,106
Other insurance and operating expenses	<u>437,823</u>	<u>407,798</u>	<u>378,653</u>
Total benefits and expenses	<u>2,356,621</u>	<u>2,302,725</u>	<u>2,230,159</u>
Income (loss) before income tax expense (benefit) and cumulative effect of accounting change	470,007	(188,957)	807,264
Income tax expense (benefit)	<u>87,826</u>	<u>(145,222)</u>	<u>221,627</u>
Income (loss) before cumulative effect of accounting change	382,181	(43,735)	585,637
Cumulative effect of accounting change (net of income tax benefit of \$11,532)	<u>—</u>	<u>(21,416)</u>	<u>—</u>
Net income (loss)	<u>\$ 382,181</u>	<u>\$ (65,151)</u>	<u>\$ 585,637</u>

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY
For the three years ended December 31, 2002
(In thousands)

	<u>Capital stock</u>	<u>Additional paid-in capital</u>	<u>Accumulated other comprehensive income (loss), net of tax</u>	<u>Retained earnings</u>	<u>Total stockholder's equity</u>
Balance, January 1, 2000	\$ 3,000	\$ 288,327	\$ (411,230)	\$ 2,932,174	\$ 2,812,271
Comprehensive income:					
Net income	-	-	-	585,637	585,637
Net unrealized holding gains on available-for-sale securities arising during the year, net of deferred policy acquisition costs of (\$5,154) and income tax expense of (\$46,921)	-	-	87,138	-	87,138
Reclassification adjustment for gains included in net income, net of income tax expense of \$5,192	-	-	<u>(9,642)</u>	-	<u>(9,642)</u>
Other comprehensive income	-	-	<u>77,496</u>	-	<u>77,496</u>
Comprehensive income	-	-	-	-	663,133
Cash dividends	<u>-</u>	<u>-</u>	<u>-</u>	<u>(410,000)</u>	<u>(410,000)</u>
Balance, December 31, 2000	3,000	288,327	(333,734)	3,107,811	3,065,404
Comprehensive income:					
Net loss	-	-	-	(65,151)	(65,151)
Cumulative effect of adopting SFAS No. 133, net of income tax benefit of \$626	-	-	(1,162)	-	(1,162)
Net unrealized holding losses on available-for-sale securities arising during the year, net of deferred policy acquisition costs of (\$20,191) and income tax benefit of \$6,064	-	-	(11,262)	-	(11,262)
Reclassification adjustment for losses on available-for-sale securities included in net loss, net of income tax benefit of \$228,003	-	-	423,434	-	423,434
Reclassification adjustment for losses on derivatives included in net loss, net of income tax benefit of \$4,038	-	-	<u>7,499</u>	-	<u>7,499</u>
Other comprehensive income	-	-	<u>418,509</u>	-	<u>418,509</u>
Comprehensive income	-	-	-	-	353,358
Capital contribution	<u>-</u>	<u>400,000</u>	<u>-</u>	<u>-</u>	<u>400,000</u>
Balance, December 31, 2001	\$ 3,000	\$ 688,327	\$ 84,775	\$ 3,042,660	\$ 3,818,762

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY (continued)
For the three years ended December 31, 2002
(In thousands)

	<u>Capital stock</u>	<u>Additional paid-in capital</u>	<u>Accumulated other comprehensive income (loss), net of tax</u>	<u>Retained earnings</u>	<u>Total stockholder's equity</u>
Balance, December 31, 2001	\$3,000	\$ 688,327	\$ 84,775	\$3,042,660	\$3,818,762
Comprehensive income:					
Net income	-	-	-	382,181	382,181
Net unrealized holding gains on available-for-sale securities arising during the year, net of deferred policy acquisition costs of (\$75,351) and income tax expense of (\$228,502)	-	-	424,360	-	424,360
Reclassification adjustment for gains on available-for-sale securities included in net income, net of income tax expense of \$5,645	-	-	(10,484)	-	(10,484)
Reclassification adjustment for gains on derivatives included in net income, net of income tax expense of \$305	-	-	<u>(568)</u>	-	<u>(568)</u>
Other comprehensive income	-	-	<u>413,308</u>	-	<u>413,308</u>
Comprehensive income	-	-	-	-	795,489
Cash dividends	-	-	-	(70,000)	(70,000)
Capital contribution	<u>-</u>	<u>400,000</u>	<u>-</u>	<u>-</u>	<u>400,000</u>
Balance, December 31, 2002	<u>\$3,000</u>	<u>\$1,088,327</u>	<u>\$498,083</u>	<u>\$3,354,841</u>	<u>\$4,944,251</u>

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended December 31,
(In thousands)

	<u>2002</u>	<u>2001</u>	<u>2000</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income (loss)	\$ 382,181	\$ (65,151)	\$ 585,637
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Cumulative effect of accounting change, net of tax	--	21,416	--
Policy loans, excluding universal life-type insurance:			
Issuance	(35,345)	(43,687)	(61,313)
Repayment	49,256	54,004	56,088
Change in amounts recoverable from reinsurers	(104,344)	(112,686)	(89,312)
Change in other accounts receivable	(9,896)	(4,025)	6,254
Change in accrued investment income	(5,139)	56,729	8,521
Change in deferred policy acquisition costs, net	(277,947)	(175,723)	(291,634)
Change in liabilities for future policy benefits for traditional life, disability income and long-term care insurance	245,275	223,177	206,377
Change in policy claims and other policyholder's funds	13,521	19,812	27,467
Deferred income tax provision (benefit)	116,995	(246,205)	37,704
Change in other liabilities	26,309	(24,509)	(120,256)
Amortization of premium, net	65,869	108,958	37,909
Net realized loss on investments	4,507	649,752	16,975
Policyholder and contractholder charges, non-cash	(232,725)	(217,496)	(151,745)
Other, net	<u>13,820</u>	<u>(83,023)</u>	<u>(9,279)</u>
Net cash provided by operating activities	\$ 252,337	\$161,343	\$ 259,393

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
Years ended December 31,
(In thousands)

	<u>2002</u>	<u>2001</u>	<u>2000</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Held-to-maturity securities:			
Purchases	\$ -	\$ -	\$ (4,487)
Maturities, sinking fund payments and calls	-	-	589,742
Sales	-	-	50,067
Available-for-sale securities:			
Purchases	(16,287,891)	(9,477,740)	(1,454,010)
Maturities, sinking fund payments and calls	3,078,509	2,706,147	1,019,403
Sales	10,093,228	5,493,141	1,237,116
Other investments, excluding policy loans:			
Purchases	(543,843)	(442,876)	(706,082)
Sales	509,588	370,636	435,633
Change in amounts due from brokers	90,293	(75,492)	(15,157)
Change in amounts due to brokers	<u>1,602,958</u>	<u>1,293,684</u>	<u>298,236</u>
Net cash (used in) provided by investing activities	<u>(1,457,158)</u>	<u>(132,500)</u>	<u>1,450,461</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Activities related to universal life-type insurance and investment contracts:			
Considerations received	4,638,111	2,088,114	1,842,026
Surrenders and other benefits	(1,655,631)	(2,810,401)	(3,974,966)
Interest credited to account balances	1,157,636	1,137,636	1,169,641
Universal life-type insurance policy loans:			
Issuance	(80,831)	(83,720)	(134,107)
Repayment	89,346	72,805	82,193
Capital contribution	400,000	400,000	-
Dividends paid	<u>(70,000)</u>	<u>-</u>	<u>(410,000)</u>
Net cash provided by (used in) financing activities	<u>4,478,631</u>	<u>804,434</u>	<u>(1,425,213)</u>
Net increase in cash and cash equivalents	3,273,810	833,277	284,641
Cash and cash equivalents at beginning of year	<u>1,150,251</u>	<u>316,974</u>	<u>32,333</u>
Cash and cash equivalents at end of year	<u>\$ 4,424,061</u>	<u>\$ 1,150,251</u>	<u>\$ 316,974</u>
Supplemental disclosures:			
Income taxes paid	\$ -	\$ -	\$ 225,704
Interest on borrowings	7,906	23,688	3,299

See accompanying notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands)

1. Summary of significant accounting policies

Nature of business

IDS Life Insurance Company (the Company) is a stock life insurance company organized under the laws of the State of Minnesota whose products are primarily distributed through branded financial advisors. The Company is a wholly-owned subsidiary of American Express Financial Corporation (AEFC), which is a wholly-owned subsidiary of American Express Company. The Company serves residents of all states except New York. IDS Life Insurance Company of New York is a wholly-owned subsidiary of the Company and serves New York State residents. The Company also wholly-owns American Enterprise Life Insurance Company, which issues fixed and variable annuity contracts for sale through insurance agencies and broker-dealers who may also be associated with financial institutions, such as banks. American Centurion Life Assurance Company is a wholly-owned subsidiary that offers fixed and variable annuities to American Express® Cardmembers and others in New York and through insurance agencies and broker-dealers who may also be associated with financial institutions, such as banks, in New York. American Partners Life Insurance Company is a wholly-owned subsidiary that offers fixed and variable annuities to American Express® Cardmembers and others who reside in states other than New York. The Company also wholly-owns IDS REO 1, LLC and American Express Corporation. These subsidiaries hold real estate, mortgage loans on real estate and/or affordable housing investments.

The Company's principal products are deferred annuities and universal life insurance which are issued primarily to individuals. It offers single premium and flexible premium deferred annuities on both a fixed and variable dollar basis. Immediate annuities are offered as well. The Company's fixed deferred annuities guarantee a relatively low annual interest rate during the accumulation period (the time before annuity payments begin). However, the Company has the option of paying a higher rate set at its discretion. In addition, persons owning one type of annuity may have their interest calculated based on any increase in a broad-based stock market index. The Company also offers variable annuities, including the American Express Retirement Advisor Advantage® Variable Annuity and the American Express Retirement Advisor Select® Variable Annuity. Life insurance products currently offered by the Company include universal life (fixed and variable, single life and joint life), single premium life and term products. Waiver of premium and accidental death benefit riders are generally available with these life insurance products. The Company also markets disability income insurance. Although the Company discontinued marketing proprietary long-term care insurance at the end of 2002, long-term care insurance is available through a non-proprietary product distributed by an affiliate.

Under the Company's variable life insurance and variable annuity products described above, the purchaser may choose among investment options that include the Company's "general account" as well as from a variety of portfolios including common stocks, bonds, managed assets and/or short-term securities.

Basis of presentation

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States which vary in certain respects from reporting practices prescribed or permitted by state insurance regulatory authorities (see Note 4). Certain prior year amounts have been reclassified to conform to the current year's presentation.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

Profits on fixed deferred annuities are the excess of contractholder charges and investment income earned from investment of contract considerations over interest credited to contract values, amortization of deferred acquisition costs, and other expenses. Profits on variable deferred annuities also include the excess of management and other fees over the costs of guaranteed benefits provided. Policyholder and contractholder charges include policy fees and surrender charges. Management and other fees include investment management fees from underlying proprietary mutual funds, certain fee revenues from underlying nonproprietary mutual funds and mortality and expense risk fees from the variable annuity separate accounts.

Profits on fixed universal life insurance are the excess of contractholder charges and investment income earned from investment of contract considerations over interest credited to contract values, death and other benefits paid in excess of contract values, amortization of deferred acquisition costs, and other expenses. Profits on variable universal life insurance also include management and other fees. Policyholder and contractholder charges include the monthly cost of insurance charges, issue and administrative fees and surrender charges. These charges also include the minimum death benefit guarantee fees received from the variable life insurance separate accounts. Management and other fees include investment management fees from underlying proprietary mutual funds, certain fee revenues from underlying nonproprietary mutual funds and mortality and expense risk fees from the variable life insurance separate accounts.

Premiums on traditional life, disability income and long-term care insurance policies are recognized as revenue when due, and related benefits and expenses are associated with premium revenue in a manner that results in recognition of profits over the lives of the insurance policies. This association is accomplished by means of the provision for future policy benefits and the deferral and subsequent amortization of policy acquisition costs.

Investments – Fixed maturity and equity securities

All fixed maturity securities and marketable equity securities are classified as available-for-sale and carried at fair value. Unrealized gains and losses on securities classified as available-for-sale are carried as a separate component of accumulated other comprehensive income (loss), net of the related deferred policy acquisition costs and income taxes. Gains and losses are recognized in the results of operations upon disposition of the securities using the specific identification method. In addition, losses are also recognized when management determines that a decline in a security's fair value is other-than-temporary, which requires judgment regarding the amount and timing of recovery.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

Indicators of other-than-temporary impairment for fixed maturity securities include, but are not limited to, issuer downgrade, default, or bankruptcy. The Company also considers the extent to which cost exceeds fair value, the duration of time of that decline, and management's judgment about the issuer's current and prospective financial condition. The charges are reflected in net realized loss on investments within the Consolidated Statements of Income.

Fair value of fixed maturity and equity securities is generally based on quoted market prices. However, the Company's investment portfolio also contains structured investments of various asset quality, including collateralized debt obligations (CDOs) and secured loan trusts (backed by high-yield bonds and bank loans), which are not readily marketable. As a result, the carrying values of these structured investments are based on estimated cash flow projections which require a significant degree of management judgment as to default and recovery rates of the underlying investments and, as such, are subject to change. The Company's CDO investments are accounted for in accordance with Emerging Issues Task Force (EITF) Issue 99-20 "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets". The Company's secured loan trusts are accounted for in accordance with EITF Issue 96-12 "Recognition of Interest Income and Balance Sheet Classification of Structured Notes".

Net investment income, which primarily consists of interest earned on fixed maturity securities, is generally accrued as earned using the effective interest method, which makes an adjustment of the yield for security premiums, discounts and anticipated prepayments on mortgage-backed securities. Prepayment estimates are based on information received from brokers who deal in mortgage-backed securities.

Investments - Mortgage loans on real estate

Mortgage loans on real estate reflect principal amounts outstanding less reserves for losses. The estimated fair value of the mortgage loans is determined by discounted cash flow analyses using mortgage interest rates currently offered for mortgages of similar maturities.

The reserve for losses is measured as the excess of the loan's recorded investment over its present value of expected principal and interest payments discounted at the loan's effective interest rate or the fair value of collateral. Additionally, the level of the reserve for losses considers other factors, including historical experience and current economic and political conditions. Management regularly evaluates the adequacy of the reserve for mortgage loan losses and believes it is adequate to absorb estimated losses in the portfolio.

The Company generally stops accruing interest on mortgage loans for which interest payments are delinquent more than three months. Based on management's judgment as to the ultimate collectibility of principal, interest payments received are either recognized as income or applied to the recorded investment in the loan.

Investments - Policy loans

Policy loans are carried at the aggregate of the unpaid loan balances, which do not exceed the cash surrender values of the related policies.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

Investment - Other investments

Included in Other investments are affordable housing investments, trading securities, syndicated loans and real estate. Affordable housing investments are carried at amortized cost as the Company has no influence over the operating or financial policies of the general partner. Trading securities are held at fair market value with changes in value recognized in the Consolidated Statements of Income within Net investment income. Syndicated loans reflect principal amounts outstanding less reserves for losses and real estate is carried at its estimated fair value.

Cash and cash equivalents

The Company considers investments with a maturity at the date of their acquisition of three months or less to be cash equivalents. These securities are carried principally at amortized cost, which approximates fair value.

Deferred policy acquisition costs

The costs of acquiring new business, including for example, direct sales commissions, related sales incentive bonuses and awards, underwriting costs, policy issue costs and other related costs, have been deferred on the sale of insurance and annuity contracts. The deferred acquisition costs (DAC) for universal life and variable universal life insurance and certain installment annuities are amortized as a percentage of the estimated gross profits expected to be realized on the policies. DAC for other annuities are amortized using the interest method. For traditional life, disability income and long-term care insurance policies, the costs are amortized in proportion to premium revenue.

Amortization of DAC requires the use of certain assumptions including interest margins, mortality rates, persistency rates, maintenance expense levels and customer asset value growth rates for variable products. The customer asset value growth rate is the rate at which contract values are assumed to appreciate in the future. This rate is net of asset fees, and anticipates a blend of equity and fixed income investments. Management routinely monitors a wide variety of trends in the business, including comparisons of actual and assumed experience. Management reviews and, where appropriate, adjusts its assumptions with respect to customer asset value growth rates on a quarterly basis.

Management monitors other principal DAC assumptions, such as persistency rates, mortality rate, interest margin and maintenance expense level assumptions each quarter. Unless management identifies a material deviation over the course of the quarterly monitoring, management reviews and updates these DAC assumptions annually in the third quarter of each year.

When assumptions are changed, the percentage of estimated gross profits or portion of interest margins used to amortize DAC may also change. A change in the required amortization percentage is applied retrospectively; an increase in amortization percentage will result in an acceleration of DAC amortization while a decrease in amortization percentage will result in a deceleration of DAC amortization. The impact on results of operations of changing assumptions with respect to the amortization of DAC can be either positive or negative in any particular period, and is reflected in the period that such changes are made. These adjustments are collectively referred to as unlocking

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

adjustments. Unlocking adjustments resulted in net increases in amortization of \$40,000 in 2002 and \$33,600 in 2001, with a net decrease in amortization of \$12,300 in 2000.

Guaranteed Minimum Death Benefits

The majority of the variable annuity contracts offered by the Company contain guaranteed minimum death benefit (GMDB) provisions. At time of issue, these contracts typically guarantee that the death benefit payable will not be less than the amount invested, regardless of the performance of the customer's account. Most contracts also provide for some type of periodic adjustment of the guaranteed amount based on the change in value of the contract. A large portion of the Company's contracts containing a GMDB provision adjust once every six years. The periodic adjustment of these contracts can either increase or decrease the guaranteed amount, though not below the amount invested, adjusted for withdrawals. When market values of the customer's accounts decline, the death benefit payable on a contract with a GMDB may exceed the accumulated contract value. Currently, the amount paid in excess of contract value is expensed when payable. Amounts expensed in 2002, 2001 and 2000 were \$37,361, \$16,202 and \$835, respectively.

Liabilities for future policy benefits

Liabilities for fixed and variable universal life insurance and fixed and variable deferred annuities are accumulation values.

Liabilities for equity indexed deferred annuities issued before 1999 are equal to the present value of guaranteed benefits and the intrinsic value of index-based benefits. Liabilities for equity indexed deferred annuities issued in 1999 or later are equal to the accumulation of host contract values covering guaranteed benefits and the market value of embedded equity options.

Liabilities for fixed annuities in a benefit status are based on established industry mortality tables and interest rates ranging from 5% to 9.5%, depending on year of issue, with an average rate of approximately 6.5%.

Liabilities for future benefits on traditional life insurance, principally term and whole life insurance, are based on the net level premium method, using anticipated mortality, policy persistency and interest earning rates. Anticipated mortality rates are based on established industry mortality tables, with modifications based on Company experience. Anticipated policy persistency rates vary by policy form, issue age and policy duration with persistency on level term and cash value plans generally anticipated to be better than persistency on yearly renewable term insurance plans. Anticipated interest rates range from 4% to 10%, depending on policy form, issue year and policy duration.

Liabilities for future disability income and long-term care policy benefits include both policy reserves and claim reserves. Policy reserves are based on the net level premium method, using anticipated morbidity, mortality, policy persistency and interest earning rates. Anticipated morbidity and mortality rates are based on established industry morbidity and mortality tables. Anticipated policy persistency rates vary by policy form, issue age, policy duration and, for disability income policies,

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

occupation class. Anticipated interest rates for disability income and long-term care policy reserves are 3% to 9.5% at policy issue and grade to ultimate rates of 5% to 7% over 5 to 10 years.

Claim reserves are calculated based on claim continuance tables and anticipated interest earnings. Anticipated claim continuance rates are based on established industry tables. Anticipated interest rates for claim reserves for both disability income and long-term care range from 5% to 8%.

Liabilities for reported and unpaid life insurance claims are equal to the death benefits payable. For disability income and long-term care claims, unpaid claims liabilities are equal to benefit amounts due and accrued. Liabilities for incurred but not reported claims are estimated based on periodic analysis of the actual reported claim lag. Where applicable, amounts recoverable from reinsurers are separately recorded as receivables. For life insurance, no claim adjustment expense reserve is held. The claim adjustment expense reserves for disability income and long-term care are based on the claim reserves.

The Company does not issue participating insurance contracts and has no short-duration life insurance liabilities.

Reinsurance

Reinsurance premiums and benefits paid or provided are accounted for on a basis consistent with that used in accounting for original policies issued and with the terms of the reinsurance contracts.

The maximum amount of life insurance risk retained by the Company is \$750 on any policy insuring a single life and \$1,500 on any policy insuring a joint-life combination. The Company generally retains 10% of the mortality risk on new life insurance policies. Risk not retained is reinsured with other life insurance companies. Risk on universal life and variable universal life policies is reinsured on a yearly renewable term basis. Risk on term insurance and long-term care policies is reinsured on a coinsurance basis. The Company retains all accidental death benefit, disability income and waiver of premium risk.

Federal income taxes

The Company's taxable income is included in the consolidated federal income tax return of American Express Company. The Company provides for income taxes on a separate return basis, except that, under an agreement between AEFC and American Express Company, tax benefit is recognized for losses to the extent they can be used on the consolidated tax return. It is the policy of AEFC and its subsidiaries that AEFC will reimburse subsidiaries for all tax benefits.

Separate account business

The separate account assets and liabilities represent funds held for the exclusive benefit of the variable annuity and variable life insurance contract owners. The Company receives investment management fees from the proprietary mutual funds used as investment options for variable annuities and variable life insurance. The Company receives mortality and expense risk fees from the separate accounts.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

The Company makes contractual mortality assurances to the variable annuity contract owners that the net assets of the separate accounts will not be affected by future variations in the actual life expectancy experience of the annuitants and beneficiaries from the mortality assumptions implicit in the annuity contracts. The Company makes periodic fund transfers to, or withdrawals from, the separate account assets for such actuarial adjustments for variable annuities that are in the benefit payment period. The Company also guarantees that the rates at which administrative fees are deducted from contract funds will not exceed contractual maximums.

For variable life insurance, the Company guarantees that the rates at which insurance charges and administrative fees are deducted from contract funds will not exceed contractual maximums. The Company also guarantees that the death benefit will continue to be payable at the initial level regardless of investment performance so long as minimum premium payments are made.

Accounting developments

In July 2000, the Financial Accounting Standards Board's (FASB's) Emerging Issues Task Force (EITF) issued a consensus on Issue 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The Company adopted the consensus as of January 1, 2001. Issue 99-20 prescribes procedures for recording interest income and measuring impairment on retained and purchased beneficial interests. The consensus primarily affects the Company's CDO investments. Adoption of the consensus required the Company to adjust the carrying amount of these investments downward by \$21,416, net of tax, which is reflected as a cumulative effect of accounting change in the Consolidated Statement of Income.

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended (SFAS No. 133), which requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet and measure those instruments at fair value. Changes in the fair value of a derivative are recorded in earnings or directly to other comprehensive income, depending on the instrument's designated use. The adoption of SFAS No. 133 resulted in a cumulative after-tax reduction to other comprehensive income of \$1,162. The cumulative impact to earnings was not significant. See Note 8 for further discussion of the Company's derivative and hedging activities.

SFAS No. 133 also provided a one-time opportunity to reclassify held-to-maturity security investments to available-for-sale without tainting the remaining securities in the held-to-maturity portfolio. The Company elected to take the opportunity in 2001 to reclass all its held-to-maturity investments to available-for-sale.

The Company adopted SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which superseded SFAS No. 125. The Statement was effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. The Statement was effective for recognition and reclassification of collateral and for disclosures relating to securitization transactions and collateral for fiscal years ending after December 15, 2000. The impact on the Company's financial position or results of operations of adopting the Statement was not significant.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

1. Summary of significant accounting policies (continued)

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46), which addresses consolidation by business enterprises of variable interest entities (VIEs). The accounting provisions and expanded disclosure requirements for VIEs existing at December 31, 2002, are fully effective for reporting periods beginning after June 15, 2003. An entity shall be subject to consolidation according to the provisions of FIN 46, if, by design, either (i) the total equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties, or (ii) as a group, the holders of the equity investment at risk lack: (a) direct or indirect ability to make decisions about an entity's activities; (b) the obligation to absorb the expected losses of the entity if they occur; or (c) the right to receive the expected residual return of the entity if they occur. In general, FIN 46 will require a VIE to be consolidated when an enterprise has a variable interest that will absorb a majority of the VIE's expected losses or receive a majority of the VIE's expected residual return.

It is likely that the Company will consolidate or disclose information about VIEs when FIN 46 becomes effective in the third quarter of 2003. The entities primarily impacted by FIN 46 relate to structured investments, including CDOs and secured loan trusts (SLTs), which are owned by the Company. The application of FIN 46 for CDOs and SLTs will have no effect on the cash flows of the Company. The CDO entities contain debt issued to investors, which are non-recourse to the Company and are solely supported by portfolios of high-yield bonds and loans. The Company often invests in the residual and rated debt tranches of the CDO structures that are either managed by a related party or a third-party. With regards to those CDOs in which the Company owns a residual tranche and which a related party manages, the portfolios of high-yield bonds and loans have a fair value at December 31, 2002 of approximately \$2.0 billion for the benefit of the \$2.7 billion in CDO debt investors.

Substantially all of the Company's interest in the rated debt tranches along with rated tranches owned by AEFC were placed in a securitization trust described in Note 2. The SLTs provide returns to investors primarily based on the performance of an underlying portfolio of up to \$3.3 billion in high-yield loans. Currently, the underlying portfolio consists of \$2.9 billion in high-yield loans with a market value of \$2.6 billion, which are managed by a related party.

While the potential consolidation of these entities may impact the results of operations at adoption and for each reporting period thereafter, the Company's maximum exposure to economic loss as a result of its investment in these entities is represented by the carrying values at December 31, 2002 because any further reduction in the value of the assets will be absorbed by the non-recourse debt or other unrelated entities. The CDO residual tranches have an adjusted cost basis of \$13,363 and the SLTs have an adjusted cost basis of \$656,565.

The Company continues to evaluate other relationships and interests in entities that may be considered VIEs, including affordable housing investments. The impact of adopting FIN 46 on the Consolidated Financial Statements is still being reviewed.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

2. Investments

Fixed maturity and equity securities

The following is a summary of securities available-for-sale at December 31, 2002:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
Fixed maturities:				
U.S. Government agency obligations	\$ 84,075	\$ 12,015	\$ 687	\$ 95,403
State and municipal obligations	29,202	2,522	-	31,724
Corporate bonds and obligations	9,614,296	611,060	116,345	10,109,011
Mortgage and other asset-backed securities	12,145,797	393,342	10,067	12,529,072
Structured investments	1,306,245	2,112	59,101	1,249,256
Foreign government bonds and obligations	<u>29,611</u>	<u>8,027</u>	<u>-</u>	<u>37,638</u>
Total fixed maturity securities	<u>\$23,209,226</u>	<u>\$1,029,078</u>	<u>\$186,200</u>	<u>\$24,052,104</u>
Common stocks	<u>\$ 19</u>	<u>\$ 2</u>	<u>\$ -</u>	<u>\$ 21</u>

The amortized cost and fair value of fixed maturity securities at December 31, 2002 by contractual maturity are as follows:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Due within one year	\$ 768,066	\$ 779,833
Due from one to five years	2,740,513	2,887,899
Due from five to ten years	5,865,084	6,165,165
Due in more than ten years	1,689,766	1,690,135
Mortgage and other asset-backed securities	<u>12,145,797</u>	<u>12,529,072</u>
Total	<u>\$23,209,226</u>	<u>\$24,052,104</u>

The timing of actual receipts may differ from contractual maturities because issuers may have the right to call or prepay obligations.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

2. Investments (continued)

The following is a summary of securities available-for-sale at December 31, 2001:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
Fixed maturities:				
U.S. Government agency obligations	\$ 31,074	\$ 2,190	\$ 56	\$ 33,208
State and municipal obligations	7,826	149	-	7,975
Corporate bonds and obligations	10,281,693	272,539	113,061	10,441,171
Mortgage and other asset-backed securities	8,292,576	103,109	32,801	8,362,884
Structured investments	1,377,195	3,793	105,304	1,275,684
Foreign government bonds and obligations	<u>31,708</u>	<u>4,507</u>	<u>-</u>	<u>36,215</u>
Total fixed maturity securities	<u>\$20,022,072</u>	<u>\$386,287</u>	<u>\$251,222</u>	<u>\$20,157,137</u>
Common stocks	<u>\$ 805</u>	<u>\$ 899</u>	<u>\$ -</u>	<u>\$ 1,704</u>

Pursuant to the adoption of SFAS No. 133 the Company reclassified all held-to-maturity securities with a carrying value of \$6,463,613 and net unrealized gains of \$8,185 to available-for-sale as of January 1, 2001.

At December 31, 2002 and 2001, bonds carried at \$14,523 and \$14,639, respectively, were on deposit with various states as required by law.

At December 31, 2002, fixed maturity securities comprised approximately 84 percent of the Company's total investments. These securities are rated by Moody's and Standard & Poor's (S&P), except for approximately \$1.4 billion of securities which are rated by AEFC's internal analysts using criteria similar to Moody's and S&P. Ratings are presented using S&P's convention and if the two agencies' ratings differ, the lower rating is used. A summary of fixed maturity securities, at fair value, by rating on December 31, is as follows:

<u>Rating</u>	<u>2002</u>	<u>2001</u>
AAA	53%	45%
AA	1	1
A	14	15
BBB	25	34
Below investment grade	<u>7</u>	<u>5</u>
Total	<u>100%</u>	<u>100%</u>

At December 31, 2002, approximately 93 percent of the securities rated AAA are GNMA, FNMA and FHLMC mortgage-backed securities. No holdings of any other issuer were greater than ten percent of stockholder's equity.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

2. Investments (continued)

Available-for-sale securities were sold during 2002 with proceeds of \$10,093,228 and gross realized gains and losses of \$297,477 and \$135,824, respectively. Available-for-sale securities were sold during 2001 with proceeds of \$5,493,141 and gross realized gains and losses of \$116,565 and \$390,732, respectively. Available-for-sale securities were sold during 2000 with proceeds of \$1,237,116 and gross realized gains and losses of \$25,101 and \$21,147, respectively.

During the years ended December 31, 2002, 2001, and 2000, the Company also recognized losses of \$145,524, \$348,730, and \$38,816 respectively due to other-than-temporary impairments on structured investments and corporate debt securities. These amounts are reflected in the net realized loss on investments in the Consolidated Statements of Income. The 2001 realized losses and other-than temporary impairments include the effect of the write-downs and sale of high-yield securities discussed below.

The net unrealized gain on available-for-sale securities as of December 31, 2002 and 2001, was \$842,880 and \$135,964, respectively, with the \$706,916 change, net of taxes and deferred policy acquisition costs, reflected as a separate component in accumulated other comprehensive income for the year ended December 31, 2002. For the years ended December 31, 2001 and 2000 the change in net unrealized losses on available-for-sale securities was a decrease of \$667,340 and \$122,196, respectively.

During 2001, the Company recorded pretax losses of \$828,175 to recognize the impact of higher default rate assumptions on certain structured investments; to write down lower rated securities (most of which were sold during 2001) in connection with Company's decision to lower its risk profile by reducing the level of its high-yield portfolio, allocating holdings toward stronger credits, and reducing the concentration of exposure to individual companies and industry sectors; to write down certain other investments; and, to adopt EITF Issue 99-20, as previously discussed. Within the Consolidated Statements of Income, \$623,958 of these losses are included in Net realized losses on investments and \$171,269 are included in Net investment income, with the remaining losses recorded as a cumulative effect of accounting change.

During 2001, the Company placed a majority of its rated CDO securities and related accrued interest, (collectively referred to as transferred assets), having an aggregate book value of \$675,347, into a securitization trust. In return, the Company received \$89,535 in cash relating to sales to unaffiliated investors and retained interests with allocated book amounts aggregating \$585,812. As of December 31, 2002, the retained interests had a carrying value of approximately \$562,000, of which approximately \$388,000 is considered investment grade. The book amount is determined by allocating the previous carrying value of the transferred assets between assets sold and the retained interests based on their relative fair values. Fair values are based on the estimated present value of future cash flows. The retained interests are accounted for in accordance with EITF Issue 99-20.

Fair values of fixed maturity and equity securities represent quoted market prices and estimated values when quoted prices are not available. Estimated values are determined by established procedures involving, among other things, review of market indices, price levels of current offerings of comparable issues, price estimates, estimated future cash flows and market data from independent brokers.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

2. Investments (continued)

Mortgage loans on real estate

At December 31, 2002, approximately 12 percent of the Company's investments were mortgage loans on real estate. Concentration of credit risk by region of the United States and by type of real estate are as follows:

<u>Region</u>	<u>December 31, 2002</u>		<u>December 31, 2001</u>	
	<u>On Balance Sheet</u>	<u>Funding Commitments</u>	<u>On Balance Sheet</u>	<u>Funding Commitments</u>
East North Central	\$ 611,886	\$ -	\$ 670,387	\$ 1,873
West North Central	493,310	25,500	549,015	-
South Atlantic	765,443	2,800	815,837	9,490
Middle Atlantic	318,699	19,100	352,821	9,363
New England	227,150	5,800	274,486	8,700
Pacific	355,622	5,250	355,945	14,618
West South Central	210,435	1,000	214,000	600
East South Central	63,859	-	55,798	-
Mountain	<u>406,459</u>	<u>-</u>	<u>413,053</u>	<u>27</u>
	3,452,863	59,450	3,701,342	44,671
Less reserves for losses	<u>35,212</u>	<u>-</u>	<u>20,948</u>	<u>-</u>
Total	<u>\$3,417,651</u>	<u>\$ 59,450</u>	<u>\$3,680,394</u>	<u>\$ 44,671</u>

<u>Property type</u>	<u>December 31, 2002</u>		<u>December 31, 2001</u>	
	<u>On Balance Sheet</u>	<u>Funding Commitments</u>	<u>On Balance Sheet</u>	<u>Funding Commitments</u>
Department/retail stores	\$ 991,984	\$ 20,722	\$1,117,195	\$ 13,200
Apartments	622,185	-	694,214	11,531
Office buildings	1,178,434	25,628	1,203,090	7,650
Industrial buildings	344,604	13,100	333,713	2,263
Hotels/motels	102,184	-	108,019	-
Medical buildings	95,189	-	106,927	6,000
Nursing/retirement homes	35,873	-	39,590	-
Mixed use	54,512	-	86,972	27
Other	<u>27,898</u>	<u>-</u>	<u>11,622</u>	<u>4,000</u>
	3,452,863	59,450	3,701,342	44,671
Less reserves for losses	<u>35,212</u>	<u>-</u>	<u>20,948</u>	<u>-</u>
Total	<u>\$3,417,651</u>	<u>\$ 59,450</u>	<u>\$3,680,394</u>	<u>\$ 44,671</u>

Mortgage loan fundings are restricted by state insurance regulatory authorities to 80 percent or less of the market value of the real estate at the time of origination of the loan. The Company holds the mortgage document, which gives it the right to take possession of the property if the borrower fails to perform according to the terms of the agreement. Commitments to fund mortgages are made in the ordinary course of business. The fair value of the mortgage commitments is \$nil.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

2. Investments (continued)

At December 31, 2002, 2001 and 2000, the Company's investment in impaired loans was \$33,130, \$39,601 and \$24,999, respectively, with related reserves of \$9,100, \$7,225 and \$4,350, respectively.

During 2002, 2001 and 2000, the average recorded investment in impaired loans was \$36,583, \$24,498 and \$27,063, respectively.

The Company recognized \$1,090, \$1,285 and \$1,033 of interest income related to impaired loans for the years ended December 31, 2002, 2001 and 2000, respectively.

The following table presents changes in the reserves for mortgage loan losses:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Balance, January 1	\$20,948	\$11,489	\$28,283
Provision for mortgage loan losses	14,264	14,959	(14,894)
Loan payoffs	-	-	(1,200)
Foreclosures and write-offs	-	(5,500)	(700)
Balance, December 31	<u>\$35,212</u>	<u>\$20,948</u>	<u>\$11,489</u>

Sources of investment income and realized losses on investments

Net investment income for the years ended December 31 is summarized as follows:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Income on fixed maturities	\$1,331,547	\$1,276,966	\$1,473,560
Income on mortgage loans	274,524	290,608	286,611
Other	<u>(15,642)</u>	<u>(41,927)</u>	<u>9,834</u>
	1,590,429	1,525,647	1,770,005
Less investment expenses	<u>28,573</u>	<u>39,959</u>	<u>39,400</u>
Total	<u>\$1,561,856</u>	<u>\$1,485,688</u>	<u>\$1,730,605</u>

Net realized losses on investments for the years ended December 31 is summarized as follows:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Fixed maturities	\$ 16,129	\$ (622,897)	\$ (34,862)
Mortgage loans	(15,586)	(17,834)	16,794
Other investments	<u>(5,050)</u>	<u>(9,021)</u>	<u>1,093</u>
Total	<u>\$ (4,507)</u>	<u>\$ (649,752)</u>	<u>\$ (16,975)</u>

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

3. Income taxes

The Company qualifies as a life insurance company for federal income tax purposes. As such, the Company is subject to the Internal Revenue Code provisions applicable to life insurance companies.

The income tax expense (benefit) for the years ended December 31 consists of the following:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Federal income taxes			
Current	\$(30,648)	\$ 88,121	\$176,397
Deferred	<u>116,996</u>	<u>(234,673)</u>	<u>37,704</u>
	86,348	(146,552)	214,101
State income taxes-current	<u>1,478</u>	<u>1,330</u>	<u>7,526</u>
Income tax expense (benefit) before cumulative effect of accounting change	87,826	(145,222)	221,627
Cumulative effect of accounting change income tax benefit	<u>-</u>	<u>(11,532)</u>	<u>-</u>
Income tax expense (benefit)	<u>\$87,826</u>	<u>\$(156,754)</u>	<u>\$221,627</u>

Income tax expense (benefit) before the cumulative effect of accounting change differs from that computed by using the federal statutory rate of 35%. The principal causes of the difference in each year are shown below:

	<u>2002</u>		<u>2001</u>		<u>2000</u>	
	<u>Provision</u>	<u>Rate</u>	<u>Provision</u>	<u>Rate</u>	<u>Provision</u>	<u>Rate</u>
Federal income taxes based on the statutory rate	\$164,502	35.0%	(\$66,136)	(35.0)%	\$282,542	35.0%
Tax-exempt interest and dividend income	(5,260)	(1.1)	(4,663)	(2.5)	(3,788)	(0.5)
State taxes, net of federal benefit	961	0.2	865	0.4	4,892	0.6
Affordable housing credits	(70,000)	(14.9)	(73,200)	(38.7)	(54,569)	(6.8)
Other, net	<u>(2,377)</u>	<u>(0.5)</u>	<u>(2,088)</u>	<u>(1.1)</u>	<u>(7,450)</u>	<u>(0.8)</u>
Total income taxes	<u>\$ 87,826</u>	<u>18.7%</u>	<u>(\$145,222)</u>	<u>(76.9)%</u>	<u>\$221,627</u>	<u>27.5%</u>

A portion of life insurance company income earned prior to 1984 was not subject to current taxation but was accumulated, for tax purposes, in a "policyholders' surplus account". At December 31, 2002, the Company had a policyholders' surplus account balance of \$20,114. The policyholders' surplus account is only taxable if dividends to the stockholder exceed the stockholder's surplus account or if the Company is liquidated. Deferred income taxes of \$7,040 have not been established because no distributions of such amounts are contemplated.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

3. Income taxes (continued)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred income tax assets and liabilities as of December 31 are as follows:

	<u>2002</u>	<u>2001</u>
Deferred income tax assets:		
Policy reserves	\$ 683,144	\$ 705,637
Other investments	319,829	333,857
Other	<u>29,789</u>	<u>24,640</u>
Total deferred income tax assets	<u>1,032,762</u>	<u>1,064,134</u>
Deferred income tax liabilities:		
Deferred policy acquisition costs	929,751	861,892
Net unrealized gain - available-for-sale securities	267,787	45,934
Other	<u>17,283</u>	<u>-</u>
Total deferred income tax liabilities	<u>1,214,821</u>	<u>907,826</u>
Net deferred income tax (liability) asset	<u>\$ (182,059)</u>	<u>\$ 156,308</u>

The Company is required to establish a valuation allowance for any portion of the deferred income tax assets that management believes will not be realized. In the opinion of management, it is more likely than not that the Company will realize the benefit of the deferred income tax assets and, therefore, no such valuation allowance has been established.

4. Stockholder's equity

Retained earnings available for distribution as dividends to AEFC are limited to the Company's surplus as determined in accordance with accounting practices prescribed by state insurance regulatory authorities. The Company's statutory unassigned surplus aggregated \$1,323,324 and \$1,262,335 as of December 31, 2002 and 2001, respectively (see Note 3 with respect to the income tax effect of certain distributions). In addition, any dividend distributions in 2003 in excess of \$240,838 would require approval of the Department of Commerce of the State of Minnesota.

Statutory net income (loss) for the years ended December 31 and capital and surplus as of December 31 are summarized as follows:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Statutory net income (loss)	\$ 159,794	\$ (317,973)	\$ 344,973
Statutory capital and surplus	2,408,379	1,947,350	1,778,306

The National Association of Insurance Commissioners (NAIC) revised the Accounting Practices and Procedures Manual in a process referred to as Codification. The revised regulations took effect January 1, 2001. The domiciliary states of the Company and its insurance subsidiaries adopted the provisions of the revised manual, with the exception of certain provisions not adopted by its subsidiaries organized in the state of New York. The revised manual changed, to some extent, prescribed statutory accounting practices and resulted in changes to the accounting practices that the Company uses to prepare its statutory-basis financial statements. The impact of implementing these changes was a decrease of \$39,997 to the Company's statutory-basis capital and surplus as of January 1, 2001. Effective January 1, 2002 the Company's subsidiaries organized in the state of New York

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

4. Stockholder's equity (continued)

adopted additional provisions of the manual which resulted in an increase of \$5,597 to the Company's statutory-basis capital and surplus as of January 1, 2002.

5. Related party transactions

The Company loans funds to AEFC under a collateral loan agreement. The balance of the loan was \$nil at December 31, 2002 and 2001. This loan can be increased to a maximum of \$75,000 and pays interest at a rate equal to the preceding month's effective new money rate for the Company's permanent investments. Interest income on related party loans totaled \$nil in 2002, 2001 and 2000.

The Company participates in the American Express Company Retirement Plan which covers all permanent employees age 21 and over who have met certain employment requirements. Company contributions to the plan are based on participants' age, years of service and total compensation for the year. Funding of retirement costs for this plan complies with the applicable minimum funding requirements specified by ERISA. The Company's share of the total net periodic pension cost was \$294, \$263 and \$250 in 2002, 2001 and 2000, respectively.

The Company also participates in defined contribution pension plans of American Express Company which cover all employees who have met certain employment requirements. Company contributions to the plans are a percent of either each employee's eligible compensation or basic contributions. Costs of these plans charged to operations in 2002, 2001 and 2000 were \$1,411, \$662 and \$1,707, respectively.

The Company participates in defined benefit health care plans of AEFC that provide health care and life insurance benefits to retired employees and retired financial advisors. The plans include participant contributions and service related eligibility requirements. Upon retirement, such employees are considered to have been employees of AEFC. AEFC expenses these benefits and allocates the expenses to its subsidiaries. The cost of these plans charged to operations in 2002, 2001 and 2000 was \$1,835, \$1,011 and \$1,136, respectively.

Charges by AEFC for use of joint facilities, technology support, marketing services and other services aggregated \$526,081, \$505,526 and \$582,836 for 2002, 2001 and 2000, respectively. Certain of these costs are included in DAC. Expenses allocated to the Company may not be reflective of expenses that would have been incurred by the Company on a stand-alone basis.

Included in other liabilities at December 31, 2002 and 2001 are \$55,602 and \$68,919, respectively, payable to AEFC for federal income taxes.

6. Lines of credit

The Company has available lines of credit with AEFC aggregating \$200,000 (\$100,000 committed and \$100,000 uncommitted). The interest rate for any borrowings is established by reference to various indices plus 20 to 45 basis points, depending on the term. There were no borrowings outstanding under this agreement at December 31, 2002 and 2001.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

7. Commitments and contingencies

At December 31, 2002, 2001 and 2000, traditional life and universal life-type insurance in force aggregated \$119,173,734, \$108,255,014 and \$98,060,472 respectively, of which \$38,008,734, \$25,986,706 and \$17,429,851 was reinsured at the respective year ends. The Company also reinsures a portion of the risks assumed under long-term care policies. Under all reinsurance agreements, premiums ceded to reinsurers amounted to \$129,345, \$114,534 and \$89,506 and reinsurance recovered from reinsurers amounted to \$60,567, \$43,388, and \$32,500 for the years ended December 31, 2002, 2001 and 2000, respectively. Reinsurance contracts do not relieve the Company from its primary obligation to policyholders.

At December 31, 2002, the Company had no commitments to purchase investments other than mortgage loan fundings (see Note 2).

The Company is a party to litigation and arbitration proceedings in the ordinary course of its business, none of which is expected to have a material adverse affect on the Company.

In recent years, life insurance companies have been named as defendants in lawsuits, including class action lawsuits, alleging improper life insurance sales practices, alleged agent misconduct, failure to properly supervise agents and other matters relating to life insurance policies and annuity contracts. The Company and its affiliates were named defendants in three purported class-action lawsuits alleging improper insurance and annuity sales practices including improper replacement of existing annuity contracts and insurance policies, improper use of annuities to fund tax deferred contributory retirement plans, alleged agent misconduct, failure to properly supervise agents and other matters relating to life insurance policies and annuity contracts. A fourth lawsuit was filed against the Company and its affiliates in federal court. In January 2000, AEFC reached an agreement in principle to settle the four class action lawsuits described above. It is expected the settlement will provide \$215,000 of benefits to more than two million participants in exchange for a release by class members of all insurance and annuity state and federal market conduct claims dating back to 1985. The settlement received court approval. Implementation of the settlement commenced October 15, 2001 and is substantially complete. Claim review payments have been made. Numerous individuals opted out of the settlement described above and therefore did not release their claims against AEFC and its subsidiaries. Some of these class members who opted out were represented by counsel and presented separate claims to AEFC and the Company. Most of their claims have been settled.

The outcome of any litigation or threatened litigation cannot be predicted with any certainty. However, in the aggregate, the Company does not consider any lawsuits in which it is named as a defendant to have a material impact on the Company's financial position or operating results.

The IRS routinely examines the Company's federal income tax returns and is currently conducting an audit for the 1993 through 1996 tax years. Management does not believe there will be a material adverse effect on the Company's consolidated financial position as a result of these audits.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

8. Derivative financial instruments

The Company maintains an overall risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings caused by interest rate and equity market volatility. The Company does not enter into derivative instruments for speculative purposes. As prescribed by SFAS No. 133, derivative instruments that are designated and qualify as hedging instruments are classified as cash flow hedges, fair value hedges, or hedges of a net investment in a foreign operation, based upon the exposure being hedged. The Company currently has economic hedges that either do not qualify or are not designated for hedge accounting treatment under SFAS No. 133.

The Company enters into interest rate swaps, caps and floors to manage the Company's interest rate risk and options and futures to manage equity-based risk. The values of derivative financial instruments are based on market values, dealer quotes or pricing models.

Market risk is the possibility that the value of the derivative financial instruments will change due to fluctuations in a factor from which the instrument derives its value, primarily an interest rate or equity market index. The Company is not impacted by market risk related to derivatives held for non-trading purposes beyond that inherent in cash market transactions. Derivatives held for purposes other than trading are largely used to manage risk and, therefore, the cash flow and income effects of the derivatives are inverse to the effects of the underlying transactions. Credit risk is the possibility that the counterparty will not fulfill the terms of the contract. The Company monitors credit risk related to derivative financial instruments through established approval procedures, including setting concentration limits by counterparty, and requiring collateral, where appropriate. A vast majority of the Company's counterparties are rated A or better by Moody's and Standard & Poor's.

Interest rate caps, swaps and floors are primarily used to protect the margin between interest rates earned on investments and the interest rates credited to related annuity contract holders. No interest rate swaps or floors were outstanding as of December 31, 2002. The interest rate caps expire in January 2003. The fair value of the interest rate caps is included in Other assets. Changes in the value of the interest rate caps are included in Other insurance and operating expenses.

A purchased (written) option conveys the right (obligation) to buy or sell an instrument at a fixed price for a set period of time or on a specific date. The Company writes and purchases index options to manage the risks related to annuity products that pay interest based upon the relative change in a major stock market index between the beginning and end of the product's term (equity-indexed annuities). The Company views this strategy as a prudent management of equity market sensitivity, such that earnings are not exposed to undue risk presented by changes in equity market levels.

The equity indexed annuities contain embedded derivatives, essentially the equity based return of the product, which must be separated from the host contract and accounted for as derivative instruments per SFAS No. 133. As a result of fluctuations in equity markets, and the corresponding changes in value of the embedded derivatives, the amount of interest credited incurred by the Company related to the annuity product will positively or negatively impact reported earnings.

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

8. Derivative financial instruments (continued)

The purchased and written options are carried at fair value and included in Other assets and Other liabilities, respectively. The fair value of the embedded options are included in Future policy benefits for fixed annuities. The changes in fair value of the options are recognized in Other insurance and operating expenses and the embedded derivatives are recognized in Interest credited on universal life-type insurance and investment contracts. The purchased and written options expire on various dates through 2009.

The Company also purchases futures to hedge its obligations under equity indexed annuities. The futures purchased are marked-to-market daily and exchange traded, exposing the Company to no counterparty risk. The futures contracts mature in 2003.

Index options may be used to manage the equity market risk related to the fee income that the Company receives from its separate accounts and the underlying mutual funds. The amount of the fee income received is based upon the daily market value of the separate account and mutual fund assets. As a result, the Company's fee income could be impacted significantly by fluctuations in the equity market. There are no index options outstanding as of December 31, 2002 related to this strategy.

9. Fair values of financial instruments

The Company discloses fair value information for financial instruments for which it is practicable to estimate that value. Fair values of life insurance obligations and all non-financial instruments, such as DAC, are excluded. Off-balance sheet intangible assets, such as the value of the field force, are also excluded. Management believes the value of excluded assets and liabilities is significant. The fair value of the Company, therefore, cannot be estimated by aggregating the amounts presented.

	2002		2001	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<u>Financial Assets</u>				
Fixed maturities	\$24,052,104	\$24,052,104	\$20,157,137	\$20,157,137
Common stocks	21	21	1,704	1,704
Mortgage loans on real estate	3,417,651	3,815,362	3,680,394	3,845,950
Cash and cash equivalents	4,424,061	4,424,061	1,150,251	1,150,251
Other investments	110,574	108,813	75,721	75,721
Derivatives	24,016	24,016	34,477	34,477
Separate account assets	21,980,674	21,980,674	27,333,697	27,333,697
<u>Financial Liabilities</u>				
Future policy benefits for fixed annuities	\$21,911,497	\$21,282,750	\$18,139,462	\$17,671,777
Derivatives	9,099	9,099	2,506	2,506
Separate account liabilities	19,391,316	18,539,425	24,280,092	23,716,854

IDS LIFE INSURANCE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(In thousands)

9. Fair values of financial instruments

At December 31, 2002 and 2001, the carrying amount and fair value of future policy benefits for fixed annuities exclude life insurance-related contracts carried at \$1,432,294 and \$1,368,254, respectively, and policy loans of \$67,523 and \$84,557, respectively. The fair value of these benefits is based on the status of the annuities at December 31, 2002 and 2001. The fair value of deferred annuities is estimated as the carrying amount less any applicable surrender charges and related loans. The fair value for annuities in non-life contingent payout status is estimated as the present value of projected benefit payments at rates appropriate for contracts issued in 2002 and 2001.

At December 31, 2002 and 2001, the fair value of liabilities related to separate accounts is estimated as the carrying amount less any applicable surrender charges and less variable insurance contracts carried at \$2,589,358 and \$3,053,605, respectively.

Report of Independent Auditors

The Board of Directors
IDS Life Insurance Company

We have audited the accompanying consolidated balance sheets of IDS Life Insurance Company (a wholly-owned subsidiary of American Express Financial Corporation) as of December 31, 2002 and 2001, 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, 2002. 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 auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of IDS Life Insurance Company at December 31, 2002 and 2001, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States.

January 27, 2003
Minneapolis, Minnesota