

IDS LIFE INSURANCE COMPANY

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

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 pretax loss on investments and a \$245 million decrease in investment income.

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.

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.

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.

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 investments.

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.

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 deferred policy acquisition costs (DACs) 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.

2000 Compared to 1999:

Consolidated net income decreased 8 percent to \$586 million in 2000, compared to \$636 million in 1999. Consolidated income before income taxes totaled \$807 million in 2000, compared with \$904 million in 1999. The decrease resulted primarily from a decrease in net investment income. This reflects decreases in investments owned and decreased investment yields during 2000.

Total premiums and investment contract deposits received increased to \$6.9 billion in 2000, compared with \$5.0 billion in 1999. This increase is primarily due to an increase in variable annuity deposits in 2000.

Total revenues decreased to \$3.0 billion in 2000, compared with \$3.1 billion in 1999. Decreases in net investment income and net realized gains (losses) on investments were partially offset by increases in insurance premiums, contractholder charges and management and other fees. Net investment income, the largest component of revenues, decreased by \$189 million from the prior year, reflecting decreases in investments owned and investment yields.

Contractholder charges, which consist primarily of cost of insurance charges on universal life-type policies, increased 6 percent to \$438 million in 2000, compared with \$412 million in 1999. This increase reflects increased total life insurance in force, which grew 10 percent to \$98 billion at December 31, 2000.

Net realized loss on investments was \$17 million in 2000, compared to a net realized gain of \$27 million in 1999. The loss was primarily due to the loss on sales and writedowns of fixed maturity investments.

Management and other fees increased 26 percent to \$598 million in 2000, compared with \$473 million in 1999. This is primarily due to an increase in separate account fees, which grew 25 percent to \$543 million at December 31, 2000, due to market appreciation and sales. The Company provides investment management services for mutual funds used as investment options for variable annuities and variable life insurance. The Company also receives a mortality and expense risk fee from the separate accounts.

Total benefits and expenses increased slightly to \$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 \$1.2 billion, reflecting a decrease in fixed annuities in force. Amortization of deferred policy acquisition costs increased to \$362 million, compared to \$321 million in 1999. This increase was due primarily to the impact of changing prospective separate account investment performance assumptions.

Other insurance and operating expenses increased to \$379 million in 2000, compared to \$347 million in 1999. This increase was primarily a result of business growth and technology costs related to growth initiatives.

Certain Critical Accounting Policies

In December 2001, The Securities and Exchange Commission (SEC) issued a financial reporting release, #FR-60, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies." In this connection, the following information has been provided about certain critical accounting policies that are important to the Consolidated Financial Statements and that entail, to a significant extent, the use of estimates, assumptions and the application of management's judgment. These policies relate to the recognition of impairment within the investment portfolio and deferred acquisition costs.

Generally, investment securities are carried at fair value on the balance sheet. Gains and losses are recognized in the results of operations upon disposition of the securities. In addition, losses are also recognized when management determines that a decline in value is not temporary, which requires judgment regarding the amount and timing of recovery. Typically, the Company defines an event of impairment for debt securities as issuer default or bankruptcy. Fair value 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 Structured Loan Trusts (backed by high-yield bonds and bank loans, respectively), which are not readily marketable. As a result, the carrying values of these structured investments are based on cash flow projections which require a significant degree of judgment and as such are subject to change. If actual future cash flows are less than projected, additional losses would be realized.

The Company's deferred acquisition costs (DACs) represent costs of acquiring new business, principally sales and other distribution and underwriting costs, that have been deferred on the sale of annuity, insurance, and certain mutual fund and long-term products. DACs are amortized over the lives of the products, either as a constant percentage of projected earnings or as a constant percentage of projected liabilities associated with such products. Such projections require use of certain assumptions, including interest margins, mortality rates, persistency rates, maintenance expense levels and, for variable products, separate account performance. As actual experience differs from the current assumptions, management considers on a quarterly basis the need to change key assumptions underlying the amortization models prospectively. For example, if the stock market trend rose or declined appreciably, it could impact assumptions made about separate account performance and result in an adjustment to income, either positively or negatively. The impact on results of operations of changing prospective assumptions with respect to the amortization of DACs is reflected in the period in which such changes are made.

Risk Management

The sensitivity analysis of two different types of market risk discussed below estimate the effects of hypothetical sudden and sustained changes in the applicable market conditions 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% decline in the value of equity securities under management. 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 occurred. 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 clients 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 trading profits.

The Company has an investment committee that holds regularly scheduled meetings and, when necessary, special meetings. At these meetings, the committee reviews models projecting different interest rate scenarios, risk/return measures, and their effect on profitability. The objective of the committee is to structure the investment security portfolio based upon the type and behavior of products in the liability portfolio so as to achieve targeted levels of profitability within defined risk parameters and to meet contractual obligations.

Rates credited to contractholders' 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 committee's strategy includes the use of derivatives, such as interest rate caps, swaps and floors, for risk management purposes. These derivatives 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 contractholders' accounts.

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, 2001, would be approximately \$12 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 the major stock market index, and to purchase futures which are marked to market daily and exchange traded, exposing the Company to no counterparty risk.

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 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 negative effect on the Company's pretax earnings of a 10% decline in equity prices would be approximately \$30 million based on assets under management as of December 31, 2001.

Liquidity and Capital Resources

The liquidity requirements of the Company are met by funds provided by premiums, investment income, proceeds from sales of investments as well as maturities and periodic repayments of investment principal.

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 its parent aggregating \$200 million (\$100 million committed and \$100 million uncommitted). The line of credit is used strictly as a short-term source of funds. There were no borrowings outstanding at December 31, 2001. At December 31, 2001, there were no outstanding reverse repurchase agreements.

At December 31, 2001, investments in fixed maturities comprised 80 percent of the Company's total invested assets. Of the fixed maturity portfolio, approximately 42 percent is invested in GNMA, FNMA and FHLMC mortgage-backed securities which are considered AAA/Aaa quality.

At December 31, 2001, approximately 4 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 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 2001, the Company placed a majority of its rated Collateralized Debt Obligation (CDO) (obligations that are backed primarily by high-yield bonds) securities and related accrued interest, (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 relating to sales to unaffiliated investors and retained interests with allocated book amounts aggregating \$586 million. 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.

At December 31, 2001, net unrealized appreciation on available-for-sale fixed maturities included \$386 million of gross unrealized appreciation and \$251 million of gross unrealized depreciation. The Company does not have any held-to-maturity fixed maturities at December 31, 2001.

At December 31, 2001, the Company had a reserve for losses for mortgage loans totaling \$21 million and for real estate investments totaling \$nil.

In 2001, the Company received a capital contribution from its parent of \$400 million.

The economy and other factors have caused a number of insurance companies to go under regulatory supervision. This circumstance has resulted 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 has established risk-based capital standards to determine the capital requirements of a life insurance company based upon the risks inherent in its operations. These standards require the computation of a risk-based capital amount which is then compared to a company's actual total adjusted 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 risk-based capital is below certain levels. As of December 31, 2001, the Company's total adjusted capital was well in excess of the levels requiring regulatory attention.

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. 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 update publicly or revise any forward-looking statements. Important factors that could cause actual results to differ materially from the Company's forward-looking statements include, among other things, changes in the ability of issuers of investment securities held by the Company to meet their debt obligations, which could result in further losses in the Company's investment portfolio.

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

<u>ASSETS</u>	<u>2001</u>	<u>2000</u>
Investments:		
Fixed maturities:		
Held-to-maturity, at amortized cost (fair value: 2000, \$6,471,798)	\$ -	\$ 6,463,613
Available-for-sale, at fair value (amortized cost: 2001, \$20,022,072; 2000, \$12,929,870)	20,157,137	12,399,990
Common stocks	1,704	10,333
Mortgage loans on real estate	3,680,394	3,738,091
Policy loans	619,571	618,973
Other investments	621,897	575,551
Total investments	<u>25,080,703</u>	<u>23,806,551</u>
Cash and cash equivalents	1,150,251	316,974
Amounts recoverable from reinsurers	529,166	416,480
Amounts due from brokers	90,794	15,302
Other accounts receivable	46,349	42,324
Accrued investment income	278,199	334,928
Deferred policy acquisition costs	3,107,187	2,951,655
Deferred income taxes, net	156,308	136,588
Other assets	123,246	80,054
Separate account assets	<u>27,333,697</u>	<u>32,349,347</u>
Total assets	<u>\$57,895,900</u>	<u>\$60,450,203</u>

See 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>2001</u>	<u>2000</u>
Liabilities:		
Future policy benefits:		
Fixed annuities	\$19,592,273	\$19,417,446
Universal life-type insurance	3,433,904	3,410,871
Traditional life insurance	241,165	232,913
Disability income and long-term care insurance	1,227,172	1,012,247
Policy claims and other policyholders' funds	71,879	52,067
Amounts due to brokers	1,740,031	446,347
Other liabilities	437,017	463,561
Separate account liabilities	<u>27,333,697</u>	<u>32,349,347</u>
Total liabilities	<u>54,077,138</u>	<u>57,384,799</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	688,327	288,327
Accumulated other comprehensive income (loss), net of tax:		
Net unrealized securities gains (losses)	85,549	(333,734)
Net unrealized derivative (losses)	<u>(774)</u>	<u>-</u>
Total accumulated other comprehensive income (loss)	84,775	(333,734)
Retained earnings	<u>3,042,660</u>	<u>3,107,811</u>
Total stockholder's equity	<u>3,818,762</u>	<u>3,065,404</u>
Total liabilities and stockholder's equity	<u>\$57,895,900</u>	<u>\$60,450,203</u>

See notes to consolidated financial statements.

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
<u>REVENUES</u>			
Premiums:			
Traditional life insurance	\$ 59,415	\$ 56,187	\$ 53,790
Disability income and long-term care insurance	<u>255,428</u>	<u>231,311</u>	<u>201,637</u>
Total premiums	314,843	287,498	255,427
Net investment income	1,485,688	1,730,605	1,919,573
Contractholder charges	489,583	438,127	411,994
Management and other fees	473,406	598,168	473,108
Net realized (loss) gain on investments	<u>(649,752)</u>	<u>(16,975)</u>	<u>26,608</u>
Total revenues	<u>2,113,768</u>	<u>3,037,423</u>	<u>3,086,710</u>
<u>BENEFITS AND EXPENSES</u>			
Death and other benefits:			
Traditional life insurance	35,519	29,042	29,819
Universal life-type insurance and investment contracts	175,247	131,467	118,561
Disability income and long-term care insurance	44,725	40,246	30,622
Increase in liabilities for future policy benefits:			
Traditional life insurance	7,231	5,765	7,311
Disability income and long-term care insurance	123,227	113,239	87,620
Interest credited on universal life-type insurance and investment contracts	1,137,636	1,169,641	1,240,575
Amortization of deferred policy acquisition costs	371,342	362,106	321,036
Other insurance and operating expenses	<u>407,798</u>	<u>378,653</u>	<u>346,849</u>
Total benefits and expenses	<u>2,302,725</u>	<u>2,230,159</u>	<u>2,182,393</u>
(Loss) income before income tax (benefit) expense and cumulative effect of accounting change	(188,957)	807,264	904,317
Income tax (benefit) expense	<u>(145,222)</u>	<u>221,627</u>	<u>267,864</u>
(Loss) income before cumulative effect of accounting change	(43,735)	585,637	636,453
Cumulative effect of accounting change (net of income tax benefit of \$11,532)	<u>(21,416)</u>	<u>-</u>	<u>-</u>
Net (loss) income	<u>\$ (65,151)</u>	<u>\$ 585,637</u>	<u>\$ 636,453</u>

See notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY
For the three years ended December 31, 2001
(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, 1999	\$ 3,000	\$ 288,327	\$ 169,584	\$ 2,645,721	\$ 3,106,632
Comprehensive income:					
Net income	-	-	-	636,453	636,453
Unrealized holding losses arising during the year, net of deferred policy acquisition costs of \$28,444 and income taxes of \$304,936	-	-	(566,311)	-	(566,311)
Reclassification adjustment for gains included in net income, net of income tax of \$7,810	-	-	<u>(14,503)</u>	-	<u>(14,503)</u>
Other comprehensive loss	-	-	(580,814)	-	<u>(580,814)</u>
Comprehensive income					55,639
Cash dividends	<u>-</u>	<u>-</u>	<u>-</u>	<u>(350,000)</u>	<u>(350,000)</u>
Balance, December 31, 1999	3,000	288,327	(411,230)	2,932,174	2,812,271
Comprehensive income:					
Net income	-	-	-	585,637	585,637
Unrealized holding gains arising during the year, net of deferred policy acquisition costs of (\$5,154) and income taxes of (\$46,921)	-	-	87,138	-	87,138
Reclassification adjustment for gains included in net income, net of income tax of \$5,192	-	-	<u>(9,642)</u>	-	<u>(9,642)</u>
Other comprehensive income	-	-	77,496	-	<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

See notes to consolidated financial statements.

IDS LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY (continued)
For the three years ended December 31, 2001
(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, 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)
Unrealized holding losses on available-for-sale securities arising during the year, net of deferred policy acquisition costs of (\$20,191) and income taxes of \$15,037	-	-	(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	-	-	418,509	-	<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	<u>\$3,000</u>	<u>\$ 688,327</u>	<u>\$ 84,775</u>	<u>\$ 3,042,660</u>	<u>\$ 3,818,762</u>

See notes to consolidated financial statements.

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Net (loss) income	\$ (65,151)	\$ 585,637	\$ 636,453
Adjustments to reconcile net (loss) income 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	(43,687)	(61,313)	(56,153)
Repayment	54,004	56,088	54,105
Change in amounts recoverable from reinsurers	(112,686)	(89,312)	(64,908)
Change in other accounts receivable	(4,025)	6,254	(615)
Change in accrued investment income	56,729	8,521	23,125
Change in deferred policy acquisition costs, net	(175,723)	(291,634)	(140,379)
Change in liabilities for future policy benefits for traditional life, disability income and long-term care insurance	223,177	206,377	153,157
Change in policy claims and other policyholder's funds	19,812	27,467	(45,709)
Deferred income tax (benefit) provision	(246,205)	37,704	79,796
Change in other liabilities	(24,509)	(120,256)	169,395
Amortization of premium (accretion of discount), net	108,958	37,909	(17,907)
Net realized loss (gain) on investments	649,752	16,975	(26,608)
Contractholder charges, non-cash	(217,496)	(151,745)	(175,059)
Other, net	(83,023)	(9,279)	(5,324)
	<u>\$161,343</u>	<u>\$ 259,393</u>	<u>\$ 583,369</u>
Net cash provided by operating activities	\$161,343	\$ 259,393	\$ 583,369

See notes to consolidated financial statements.

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Held-to-maturity securities:			
Purchases	\$ -	\$ (4,487)	\$ (3,030)
Maturities, sinking fund payments and calls	-	589,742	741,949
Sales	-	50,067	66,547
Available-for-sale securities:			
Purchases	(9,477,740)	(1,454,010)	(3,433,128)
Maturities, sinking fund payments and calls	2,706,147	1,019,403	1,442,507
Sales	5,493,141	1,237,116	1,691,389
Other investments, excluding policy loans:			
Purchases	(442,876)	(706,082)	(657,383)
Sales	370,636	435,633	406,684
Change in amounts due from brokers	(75,492)	(15,157)	182
Change in amounts due to brokers	<u>1,293,684</u>	<u>298,236</u>	<u>(47,294)</u>
Net cash (used in) provided by investing activities	<u>(132,500)</u>	<u>1,450,461</u>	<u>208,423</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Activities related to universal life-type insurance and investment contracts:			
Considerations received	2,088,114	1,842,026	2,031,630
Surrenders and other benefits	(2,810,401)	(3,974,966)	(3,669,759)
Interest credited to account balances	1,137,636	1,169,641	1,240,575
Universal life-type insurance policy loans:			
Issuance	(83,720)	(134,107)	(102,239)
Repayment	72,805	82,193	67,881
Capital contribution	400,000	-	-
Dividends paid	<u>-</u>	<u>(410,000)</u>	<u>(350,000)</u>
Net cash provided by (used in) financing activities	<u>804,434</u>	<u>(1,425,213)</u>	<u>(781,912)</u>
Net increase in cash and cash equivalents	833,277	284,641	9,880
Cash and cash equivalents at beginning of year	<u>316,974</u>	<u>32,333</u>	<u>22,453</u>
Cash and cash equivalents at end of year	<u>\$ 1,150,251</u>	<u>\$ 316,974</u>	<u>\$ 32,333</u>
Supplemental disclosures:			
Income taxes paid	\$ -	\$225,704	\$214,940
Interest on borrowings	23,688	3,299	4,521

See 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. 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, American Centurion Life Assurance Company, American Partners Life Insurance Company and American Express Corporation.

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 insurance products include universal life (fixed and variable), whole life, single premium life and term products (including waiver of premium and accidental death benefits). The Company also markets disability income and long-term care insurance.

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. 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. 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 received 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.

1. Summary of significant accounting policies (continued)

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.

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.

Investments - securities

Debt securities that the Company has both the positive intent and the ability to hold to maturity are classified as held-to-maturity and carried at amortized cost. All other debt 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. When evidence indicates there is a decline in a security's value, which is other than temporary, the security is written down to fair value through a charge to current year's earnings.

The Company's investment portfolio contains structured investments, including Collateralized Debt Obligations (CDO's) (obligations that are primarily backed by high-yield bonds), which are not readily marketable. The carrying values of these investments are based on cash flow projections and, as such, these values are subject to change. If actual cash flows are less than projected, losses would be recognized; increases in cash flows would be recognized over future periods.

Realized investment gains or losses are determined on an identified cost basis.

Prepayments are anticipated on certain investments in mortgage-backed securities in determining the constant effective yield used to recognize interest income. 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 are carried at amortized cost 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.

1. Summary of significant accounting policies (continued)

Impairment of mortgage loans 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. The amount of the impairment is recorded in a reserve for losses. The reserve for losses is maintained at a level that management believes is adequate to absorb estimated losses in the portfolio. The level of the reserve account is determined based on several factors, including historical experience, expected future principal and interest payments, estimated collateral values, and current economic and political conditions. Management regularly evaluates the adequacy of the reserve for mortgage loan losses.

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 collectability of principal, interest payments received are either recognized as income or applied to the recorded investment in the loan.

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.

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, principally sales compensation, policy issue costs, underwriting and certain sales expenses, have been deferred on insurance and annuity contracts. The deferred acquisition costs for most single premium deferred annuities and installment annuities are amortized using the interest method. The costs 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. For traditional life, disability income and long-term care insurance policies, the costs are amortized over an appropriate period in proportion to premium revenue.

Amortization of deferred policy acquisition costs requires the use of assumptions including interest margins, mortality margins, persistency rates, maintenance expense levels and, for variable products, separate account performance. For fixed and variable universal life insurance and deferred annuities, actual experience is reflected in the Company's amortization models monthly. As actual experience differs from the current assumptions, management considers the need to change key prospective assumptions underlying the amortization models. The impact of changing prospective assumptions is reflected in the period that such changes are made and is generally referred to as an unlocking adjustment. Unlocking adjustments resulted in a net increase in amortization of \$33,600 in 2001 and net decreases in amortization of \$12,300 in 2000 and \$56,800 in 1999.

1. Summary of significant accounting policies (continued)

In amortizing deferred policy acquisition costs associated with variable annuities, the Company assumes contract values will appreciate at a specified long-term annual rate. The Company may project near-term appreciation at a different rate in order to maintain the long-term rate assumption.

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 in 1997 and 1998 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.

Liabilities for future benefits on traditional 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. Anticipated policy persistency rates vary by policy form, issue age and policy duration with persistency on cash value plans generally anticipated to be better than persistency on 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%.

Reinsurance

Reinsurance premiums and benefits paid or provided are accounted for on a basis consistent with those 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 retains 20% of the mortality risk on new variable universal life insurance policies and 10% of the risk on new

1. Summary of significant accounting policies (continued)

term insurance policies. Risk not retained is reinsured with other life insurance companies, primarily on a yearly renewable term basis. Long-term care policies are primarily 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.

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 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 new procedures for recording interest income and measuring impairment on retained and purchased beneficial interests. The consensus primarily affects certain high-yield investments contained in structured securities. Adoption of the consensus required the Company to adjust the carrying amount of these investments downward by \$21,416, net of tax, upon adoption. See Note 2 for further discussion.

1. Summary of significant accounting policies (continued)

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 equity, depending on the instrument's designated use. The adoption of SFAS No. 133 on January 1, 2001, 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 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.

2. Investments

Securities

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.

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
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	11,658,888	276,332	218,365	11,716,855
Mortgage-backed securities	8,292,576	103,109	32,801	8,362,884
Foreign government bonds and obligations	31,708	4,507	-	36,215
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>

2. Investments (continued)

The amortized cost and fair value of fixed maturity securities at December 31, 2001 by contractual maturity are as follows:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Due within one year	\$ 1,093,557	\$ 1,114,618
Due from one to five years	2,885,509	3,007,435
Due from five to ten years	5,503,284	5,519,588
Due in more than ten years	2,247,146	2,152,612
Mortgage-backed securities	<u>8,292,576</u>	<u>8,362,884</u>
Total	<u>\$20,022,072</u>	<u>\$20,157,137</u>

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

The following is a summary of held-to-maturity and available-for-sale securities at December 31, 2000:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<u>Held-to-maturity</u>				
U.S. Government agency obligations	\$ 38,302	\$ 3,455	\$ 80	\$ 41,677
State and municipal obligations	7,678	16	-	7,694
Corporate bonds and obligations	5,248,517	111,466	114,330	5,245,653
Mortgage-backed securities	<u>1,169,116</u>	<u>9,130</u>	<u>1,472</u>	<u>1,176,774</u>
Total fixed maturity securities	<u>\$ 6,463,613</u>	<u>\$ 124,067</u>	<u>\$ 115,882</u>	<u>\$6,471,798</u>
<u>Available-for-sale</u>				
Fixed maturities:	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
U.S. Government agency obligations	\$ 96,408	\$ 6,134	\$ 268	\$ 102,274
State and municipal obligations	12,848	247	-	13,095
Corporate bonds and obligations	7,586,423	123,691	693,303	7,016,811
Mortgage-backed securities	<u>5,234,191</u>	<u>57,697</u>	<u>24,078</u>	<u>5,267,810</u>
Total fixed maturity securities	<u>\$12,929,870</u>	<u>\$187,769</u>	<u>\$717,649</u>	<u>\$12,399,990</u>
Common stocks	<u>\$ 11,829</u>	<u>\$ -</u>	<u>\$ 1,496</u>	<u>\$ 10,333</u>

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

At December 31, 2001, fixed maturity securities comprised approximately 80 percent of the Company's total investments. These securities are rated by Moody's and Standard & Poor's (S&P), except for approximately \$2.6 billion of securities which are rated by AEFC's internal analysts using criteria similar to Moody's and S&P. A summary of fixed maturity securities, at amortized cost, by rating on December 31, is as follows:

2. Investments (continued)

<u>Rating</u>	<u>2001</u>	<u>2000</u>
Aaa/AAA	\$ 8,977,075	\$ 6,559,188
Aaa/AA	-	32,001
Aa/AA	261,252	220,446
Aa/A	372,120	327,147
A/A	2,602,027	2,494,621
A/BBB	911,477	747,636
Baa/BBB	5,904,013	5,828,847
Baa/BB	274,228	287,583
Below investment grade	719,880	2,896,014
Total	<u>\$ 20,022,072</u>	<u>\$19,393,483</u>

At December 31, 2001, approximately 93 percent of the securities rated Aaa/AAA are GNMA, FNMA and FHLMC mortgage-backed securities. No holdings of any other issuer were greater than ten percent of stockholder's equity.

During the years ended December 31, 2000 and 1999, fixed maturities classified as held-to-maturity were sold with amortized cost of \$53,169 and \$68,470, respectively. Net gains and losses on these sales were not significant. The sale of these fixed maturities was due to significant deterioration in the issuers' credit worthiness.

Available-for-sale securities were sold during 2001 with proceeds of \$5,493,141 and gross realized gains and losses of \$116,485 and \$767,144, 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 \$10,267, respectively. Available-for-sale securities were sold during 1999 with proceeds of \$1,691,389 and gross realized gains and losses of \$36,568 and \$14,255, respectively.

The net unrealized gain (loss) on available-for-sale securities as of December 31, 2001 and 2000, was \$135,964 and (\$531,376), respectively, with the \$667,340 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, 2001. For the year ended December 31, 2000 the change in net unrealized losses on available-for-sale securities was a decrease of \$122,196. For the year ended December 31, 1999 the change in net unrealized gain on available-for-sale securities was a decrease of \$921,920.

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, approximately \$623,958 of these losses are included in Net realized (losses) gains on investments and approximately \$171,269 are included in Net investment income, with the remaining losses recorded as a cumulative effect of accounting change.

2. Investments (continued)

During 2001, the Company placed a majority of its rated Collateralized Debt Obligation (CDO) (obligations that are backed primarily by high-yield bonds) 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. 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.

There was no cash flow related to this transaction other than the receipt of the initial \$89,535. Cash flows on the assets sold to investors and retained interests are not scheduled to begin until March 31, 2002 in accordance with governing documents.

Included in Other investments are affordable housing investment credits, trading securities, and real estate.

Fair values of investments 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.

Mortgages loans on real estate

At December 31, 2001, approximately 15 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, 2001</u>		<u>December 31, 2000</u>	
	<u>On Balance Sheet</u>	<u>Funding Commitments</u>	<u>On Balance Sheet</u>	<u>Funding Commitments</u>
East North Central	\$ 670,387	\$ 1,873	\$ 691,694	\$ 18,868
West North Central	549,015	-	564,576	7,621
South Atlantic	815,837	9,490	884,723	7,667
Middle Atlantic	352,821	9,363	378,702	13,813
New England	274,486	8,700	279,147	4,604
Pacific	355,945	14,618	318,727	921
West South Central	214,000	600	173,158	28,548
East South Central	55,798	-	49,176	2,763
Mountain	413,053	27	409,677	10,209
	<u>3,701,342</u>	<u>44,671</u>	<u>3,749,580</u>	<u>95,014</u>
Less reserves for losses	20,948	-	11,489	-
Total	<u>\$3,680,394</u>	<u>\$ 44,671</u>	<u>\$3,738,091</u>	<u>\$ 95,014</u>

2. Investments (continued)

<u>Property type</u>	<u>December 31, 2001</u>		<u>December 31, 2000</u>	
	<u>On Balance Sheet</u>	<u>Funding Commitments</u>	<u>On Balance Sheet</u>	<u>Funding Commitments</u>
Department/retail stores	\$1,117,195	\$ 13,200	\$1,174,763	\$ 11,130
Apartments	694,214	11,531	780,228	-
Office buildings	1,203,090	7,650	1,085,948	59,941
Industrial buildings	333,713	2,263	323,766	23,943
Hotels/motels	108,019	-	100,680	-
Medical buildings	106,927	6,000	128,101	-
Nursing/retirement homes	39,590	-	49,822	-
Mixed use	86,972	27	87,537	-
Other	11,622	4,000	18,735	-
	<u>3,701,342</u>	<u>44,671</u>	<u>3,749,580</u>	<u>95,014</u>
Less reserves for losses	20,948	-	11,489	-
Total	<u>\$3,680,394</u>	<u>\$ 44,671</u>	<u>\$3,738,091</u>	<u>\$ 95,014</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.

At December 31, 2001, 2000 and 1999, the Company's recorded investment in impaired loans was \$39,601, \$24,999 and \$21,375, respectively, with reserves of \$7,225, \$4,350 and \$5,750, respectively. During 2001, 2000 and 1999, the average recorded investment in impaired loans was \$24,498, \$27,063 and \$23,815, respectively.

The Company recognized \$1,285, \$1,033 and \$1,190 of interest income related to impaired loans for the years ended December 31, 2001, 2000 and 1999, respectively.

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Balance, January 1	\$11,489	\$28,283	\$39,795
Provision (reduction) for mortgage loan losses	14,959	(14,894)	(9,512)
Loan payoffs	-	(1,200)	(500)
Foreclosures and write-offs	(5,500)	(700)	(1,500)
Balance, December 31	<u>\$20,948</u>	<u>\$11,489</u>	<u>\$28,283</u>

2. Investments (continued)

Sources of investment income and realized (losses) gains on investments

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Interest on fixed maturities	\$1,276,966	\$1,473,560	\$1,598,059
Interest on mortgage loans	290,608	286,611	285,921
Interest on cash equivalents	2,218	8,084	5,871
Other	<u>(44,145)</u>	<u>1,750</u>	<u>70,892</u>
	1,525,647	1,770,005	1,960,743
Less investment expenses	<u>39,959</u>	<u>39,400</u>	<u>41,170</u>
Total	<u>\$1,485,688</u>	<u>\$1,730,605</u>	<u>\$1,919,573</u>

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Fixed maturities	\$ (621,400)	\$ (34,857)	\$ 8,802
Mortgage loans	(22,443)	15,845	10,210
Other investments	<u>(5,909)</u>	<u>2,037</u>	<u>7,596</u>
	<u>\$ (649,752)</u>	<u>\$ (16,975)</u>	<u>\$ 26,608</u>

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Federal income taxes			
Current	\$ 88,121	\$176,397	\$178,444
Deferred	<u>(234,673)</u>	<u>37,704</u>	<u>79,796</u>
	(146,552)	214,101	258,240
State income taxes-current	<u>1,330</u>	<u>7,526</u>	<u>9,624</u>
Income tax (benefit) expense before cumulative effect of accounting change	(145,222)	221,627	267,864
Cumulative effect of accounting change income tax benefit	<u>(11,532)</u>	<u>-</u>	<u>-</u>
Income tax (benefit) expense	<u>\$ (156,754)</u>	<u>\$221,627</u>	<u>\$267,864</u>

3. Income taxes (continued)

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

	2001		2000		1999	
	<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	(\$66,136)	(35.0)%	\$282,542	35.0%	\$316,511	35.0%
Tax-excluded interest and dividend income	(4,663)	(2.5)	(3,788)	(0.5)	(9,626)	(1.1)
State taxes, net of federal benefit	865	0.4	4,892	0.6	6,256	0.7
Affordable housing credits	(73,200)	(38.7)	(54,569)	(6.8)	(31,000)	(3.4)
Other, net	<u>(2,088)</u>	<u>(1.1)</u>	<u>(7,450)</u>	<u>(0.8)</u>	<u>(14,277)</u>	<u>(1.6)</u>
Total income taxes	<u>(\$145,222)</u>	<u>(76.9)%</u>	<u>\$221,627</u>	<u>27.5%</u>	<u>\$267,864</u>	<u>29.6%</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, 2001, 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.

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>2001</u>	<u>2000</u>
Deferred income tax assets		
Policy reserves	\$ 705,637	\$ 730,239
Unrealized loss - available-for-sale securities	-	179,702
Investments, other	330,675	34,600
Life insurance guaranty fund assessment reserve	1,330	1,365
Other	<u>26,492</u>	<u>-</u>
Total deferred income tax assets	<u>1,064,134</u>	<u>945,906</u>
Deferred income tax liabilities		
Deferred policy acquisition costs	861,892	796,292
Unrealized gain - available-for-sale securities	45,934	-
Other	<u>-</u>	<u>13,026</u>
Total deferred income tax liabilities	<u>907,826</u>	<u>809,318</u>
Net deferred income tax assets	<u>\$ 156,308</u>	<u>\$ 136,588</u>

3. Income taxes (continued)

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 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. Statutory unassigned surplus aggregated \$1,262,335 as of December 31, 2001 and \$1,493,292 as of December 31, 2000 (see Note 3 with respect to the income tax effect of certain distributions). In addition, any dividend distributions in 2002 in excess of approximately \$194,435 would require approval of the Department of Commerce of the State of Minnesota.

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

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Statutory net (loss) income	\$ (317,973)	\$ 344,973	\$ 478,173
Statutory capital and surplus	1,947,350	1,778,306	1,978,406

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 have adopted the provisions of the revised manual. The revised manual has 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 an increase of \$4,660 to the Company's statutory-basis capital and surplus as of January 1, 2001.

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, 2001 and 2000. 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 2001, 2000 and 1999.

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 \$263, \$250 and \$223 in 2001, 2000 and 1999, respectively.

5. Related party transactions (continued)

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 2001, 2000 and 1999 were \$662, \$1,707 and \$1,906, 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 2001, 2000 and 1999 was \$1,011, \$1,136 and \$1,147, respectively.

Charges by AEFC for use of joint facilities, technology support, marketing services and other services aggregated \$505,526, \$582,836 and \$485,177 for 2001, 2000 and 1999, respectively. Certain of these costs are included in deferred policy acquisition costs. 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, 2001 and 2000 are \$68,919 and \$41,059, respectively, payable to and receivable from 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. Borrowings outstanding under this agreement were \$nil and \$50,000 uncommitted at December 31, 2001 and 2000, respectively.

7. Commitments and contingencies

At December 31, 2001, 2000 and 1999, traditional life and universal life-type insurance in force aggregated \$108,255,014, \$98,060,472 and \$89,271,957 respectively, of which \$25,986,706, \$17,429,851 and \$8,281,576 were 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 \$114,534, \$89,506 and \$76,970 and reinsurance recovered from reinsurers amounted to \$43,388, \$32,500, and \$27,816 for the years ended December 31, 2001, 2000 and 1999, respectively. Reinsurance contracts do not relieve the Company from its primary obligation to policyholders.

At December 31, 2001, the Company had no commitments to purchase investments other than mortgage loan fundings (see Note 2).

7. Commitments and contingencies (continued)

In January 2000, AEFC reached an agreement in principle to settle three class-action lawsuits related to the sales of insurance and annuity products anticipated to provide for approximately \$215 million of benefits. The Company had been named as a co-defendant in all three of these lawsuits. In September 2000, both state and federal courts gave preliminary approval to the proposed settlement and AEFC mailed notices to all of the over two million class members. In May 2001 the courts entered orders approving the settlement. The orders became final in August 2001 and in October 2001 the settlement was implemented. The anticipated costs of settlement remain unchanged from prior years. The settlement as approved provides for release by class members of all insurance and annuity market conduct claims dating back to 1985. Some class members opted out of the settlement and therefore did not release their claims against AEFC or the Company. Some of these class members who opted out were represented by counsel and presented separate claims to AEFC or the Company. Most of their claims have been settled.

The Company is named as a defendant in various other lawsuits. The outcome of any litigation cannot be predicted with certainty. In the opinion of management, however, the ultimate resolution of these lawsuits, taken in aggregate should not have a material adverse effect on the Company's consolidated financial position.

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.

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 per SFAS No. 133, derivative instruments that are designated and qualify as hedging instruments are classified as a cash flow hedge, fair value hedge, or a hedge 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. For the year ended December 31, 2001, the net effect on earnings of accounting for the net changes in fair value of the following undesignated derivatives under SFAS No. 133 compared with prior rules was not significant.

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-

8. Derivative financial instruments (continued)

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 used principally to manage the Company's interest rate risk. These instruments 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, 2001. The interest rate caps expire by 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. 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 annuity products 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.

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 from 2002 to 2008.

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

8. Derivative financial instruments (continued)

Index options are 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, 2001 related to this strategy.

9. Fair values of financial instruments

The Company discloses fair value information for most on- and off-balance sheet financial instruments for which it is practicable to estimate that value. Fair values of life insurance obligations and all non-financial instruments, such as deferred acquisition costs 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.

	2001		2000	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<u>Financial Assets</u>				
Fixed maturities:				
Held-to-maturity securities	\$ -	\$ -	\$ 6,463,613	\$ 6,471,798
Available-for-sale securities	20,157,137	20,157,137	12,399,990	12,399,990
Common stocks	1,704	1,704	10,333	10,333
Mortgage loans on real estate	3,680,394	3,845,950	3,738,091	3,821,825
Cash and cash equivalents	1,150,251	1,150,251	316,974	316,974
Other securities	75,721	75,721	1,130	1,130
Derivative financial instruments	34,477	34,477	50,387	60,615
Separate account assets	27,333,697	27,333,697	32,349,347	32,349,347
<u>Financial Liabilities</u>				
Future policy benefits for fixed annuities	\$18,139,462	\$17,671,777	\$18,020,824	\$17,479,187
Derivative financial instruments	2,506	2,506	3,098	6,069
Separate account liabilities	24,280,092	23,716,854	28,791,949	27,822,667

At December 31, 2001 and 2000, the carrying amount and fair value of future policy benefits for fixed annuities exclude life insurance-related contracts carried at \$1,368,254 and \$1,300,018, respectively, and policy loans of \$84,557 and \$96,603, respectively. The fair value of these benefits is based on the status of the annuities at December 31, 2001 and 2000. 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 2001 and 2000.

At December 31, 2001 and 2000, 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 \$3,053,605 and \$3,557,398, 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, 2001 and 2000, 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, 2001. 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, 2001 and 2000, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

January 28, 2002
Minneapolis, Minnesota