Equitable Life

Interim Review

for the half year

ended 30 June 2006

The Equitable Life Assurance Society

Registered office

20-22 Bedford Row
London
WC1R 4JS
www.equitable.co.uk

Policyholder administration

Walton Street
Aylesbury
Buckinghamshire
HP21 7QW

Board of Directors

Vanni Treves, Chairman (a, b, c, e)
Peter Smith, Deputy Chairman (a, b, c, e)
Charles Thomson, Chief Executive (b, d, e)
David Adams OBE, Non-executive Director (a, d)
Ron Bullen, Non-executive Director (a)
Michael Pickard, Non-executive Director (a, d)
Fred Shedden, Non-executive Director (b, d)
Andrew Threadgold, Non-executive Director (d)
Jean Wood, Non-executive Director (c, d)

Key to membership of the principal Board Committees

(a)	–	Audit
(b)	–	Legal Audit
(c)	–	Remuneration
(d)	–	Investment
(e)	–	Nominations

With-Profits Actuary and Head of Actuarial Function

Tim Bateman

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Dear Members,

Once again we are pleased to report steady improvement in the financial security of the Society. We remain confident that, with careful management, we can continue to run the Society as a closed fund paying benefits to policyholders as they fall due. However, we also continue to make good progress in our search for strategic developments that will benefit policyholders.

At the mid year point:

- The Society is now stronger than at any time since your current Board was appointed.
- Our key measure of solvency, Excess Realistic Assets, has increased by £117m since 31 December 2005 to £786 million. This now represents 8.0% of the with-profits realistic assets.
- We have agreed to transfer around 90% of our non-profit pension annuities in payment to Canada Life, greatly reducing a key risk to the Society.

Interim report

Following the successful introduction of summary financial statements for our last year-end report, we have taken the opportunity similarly to simplify the presentation of the interim report. We hope that you find this easier to read. The simpler presentation also enables us to make further savings in production, printing and postage.

Financial position

Our financial strength has continued to improve, reflecting further good performance from our equity and property investments and reductions in certain provisions. Excess Realistic Assets have increased by 17% over the period, from £669 million at the last year-end to £786 million. Excess Realistic Assets represent 8.0% of with-profits realistic assets at the end of June 2006, rising from 6.6% at the 2005 year-end.

Transfer of non-profit pension annuities to Canada Life Limited

We wrote to members in May to explain that we have agreed to transfer most of our non-profit pension annuity business to Canada Life – around £4.6 billion of liabilities. The transfer significantly reduces the risk that the with-profits fund will suffer a cost from unexpected future improvements in life expectancy. It also thereby reduces the additional reserves we are required to retain for this risk.

The competitive process we used to negotiate this agreement enabled us to secure attractive terms for the transfer. As a result the transfer, together with all related costs, does not reduce Equitable Life's Excess Realistic Assets.

The proposed transfer is subject to the approval of the High Court, which we expect to obtain early in 2007. This process is proceeding well and we will soon be writing to all policyholders with further details. However, the life expectancy and investment risks have already passed to Canada Life with effect from 1 January 2006, under a reassurance agreement.

Investment strategy

Although the Society's financial strength continues to improve, the regulatory standards for the industry have also been raised. Consequently, we do not expect our improving financial strength to allow us to increase our exposure to equity and property markets for some time to come. This is one reason why the Society continues to explore strategic options which could improve the longer term prospects for policyholders. The Society's overall investment strategy will remain heavily weighted towards fixed-income securities because we still need to manage risk carefully and to continue to build the strength of the fund.

The Summary Balance Sheet figures at the half year show that there has been a reduction in the amount invested in 'shares and units in unit trusts'. However, that is a temporary reduction resulting from successful disposals of certain property related assets. We continue to seek attractive opportunities in which to reinvest the proceeds.

Parliamentary Ombudsman and European Parliamentary Inquiry

We continue to give all possible support to the Parliamentary Ombudsman's Inquiry into the regulation of Equitable Life. We look forward to the publication of the Ombudsman's report, which is currently expected to be towards the end of this year.

We also continue to assist the European Parliament's Committee of Inquiry. Our Chief Executive, Charles Thomson, gave evidence to the Committee in April and has accepted an invitation to give further information later this year. The Committee's final report has been deferred until April 2007 to allow the Committee the opportunity first to study the Parliamentary Ombudsman's report.

Customer service

On 6 April 2006, the new pension simplification rules came into force. The changes to the pensions regime were extensive and required major work on our computer systems, at substantial cost. The new rules were successfully implemented by the Society.

These rule changes generated a delay in the settlement of some compensation payments, as we were required to wait for clarification of certain issues by Her Majesty's Revenue and Customs (HMRC). Most of these transitional problems have now been resolved by HMRC.

Your Board

We announced in the annual report for 2005 that the planned evolution of the Board had begun. Ron Bullen and Michael Pickard will retire from the Board at the end of October and we wish to record our thanks to both for their outstanding contribution to re-establishing the financial security of the Society.

After a rigorous selection process, including the use of a search consultancy, we have appointed Ian Reynolds as a Non-executive Director with effect from 1 October 2006. Ian has over forty years' experience in the insurance industry and is currently a non-executive director of HSBC Life Assurance and also a member of the Council of the Institute of Actuaries. We are delighted to welcome Ian to the Board. We expect to appoint a further Non-executive Director before long.

Looking ahead

This review shows that the Society's financial position has continued to improve during the first half of 2006. As noted above, we do not anticipate that this improved strength will allow us to make any substantial change to our investment strategy for some time to come. For this reason, the Society continues to explore options that could improve the longer term prospects for policyholders.

The agreement we have reached with Canada Life is an important step which has greatly reduced a significant risk for the with-profits fund. We are now working hard on further strategic initiatives. Payments to with-profits annuitants are materially affected by the bonus performance of their policies and they have no option but to remain with their current pension arrangements. Consequently, they feel the impact of the Society's financial position particularly acutely. For this reason, consideration of strategic options for with-profits annuitants remains an important priority but, as any practical option will be complex, it is likely to be some way off.

Your Board will continue to do everything it possibly can to improve the stability and the security of your Society and the prospects for all policyholders.

Vanni Treves and Charles Thomson on behalf of the Society's Board of Directors

Vanni Treves

Chairman

Charles Thomson

Chief Executive

28 September 2006

Review of the Society's financial position

Under the new financial reporting regime, a key performance measure is the amount of the Society's net resources, as represented by the excess of realistic assets over liabilities before deduction of the estimate of the value of future discretionary increases to policy values ("Excess Realistic Assets"). Although this amount is reported as a policy-related liability in the technical provisions in the Balance Sheet, it is available to meet any unforeseen liabilities and liabilities in excess of those provided for at the balance sheet date and to enhance bonuses in the future.

Also as a result of the new reporting requirements, the underlying movements in the Excess Realistic Assets no longer appear in the Profit and Loss Account. For this reason, we have not included a Profit and Loss Account in this review. Instead, we have focused this report upon the Society's Balance Sheet and a consideration of the key movements in the value of Excess Realistic Assets.

At 30 June 2006, the Excess Realistic Assets were £786 million, an increase of £117 million over the previous year-end. The analysis of the with-profits assets and liabilities is as follows:

	30 June 2006 £m	31 December 2005 £m
Realistic value of with-profits assets	9,785	10,162
Less:		
Policy values	7,863	8,181
Future charges	(299)	(300)
Impact of early surrenders	(48)	(46)
Cost of guarantees	698	847
Other long-term liabilities	441	469
Other liabilities	344	342
	8,999	9,493
Excess Realistic Assets	**786**	**669**

Note: The above analysis excludes the matching assets and liabilities of the Canada Life 'deposit back' arrangement, as explained further on page 8.

The Society seeks to maintain the Excess Realistic Assets balance at a level that protects solvency whilst treating continuing and exiting customers fairly. The balance at 30 June 2006 represents 8.0% of the with-profits realistic assets, an increase from the equivalent figure of 6.6% at 31 December 2005.

The key movements in the Excess Realistic Assets during the period are shown in the following table:

	January to June 2006 £m	January to December 2005 £m
Opening Excess Realistic Assets	**669**	**455**
Favourable investment performance	48	465
Mortality assumption changes	–	(275)
Surrender experience and assumption changes	26	(55)
Changes in other valuation assumptions	5	66
Variances in provisions and expenses	25	(3)
Other movements	13	16
Closing Excess Realistic Assets	**786**	**669**

Excess Realistic Assets have continued to benefit from investment performance being in excess of assumptions, mainly from equities and property. There have also been positive contributions from surrender experience and reductions in certain provisions. The arrangements with Canada Life have minimal impact and do not reduce the value of the Excess Realistic Assets.

The policy value attributable to with-profits policies may include an element of non-guaranteed final bonus. Estimated final bonus, sometimes referred to as terminal bonus, included in the policy value, is not guaranteed. However, for realistic reporting, a prudent allowance for future bonuses, based on assumed future net investment returns that take account of deductions for potential risks, is included in the valuation of the long-term business technical provisions in the financial statements. Any enhancements to the bonuses assumed would be met from the Excess Realistic Assets.

It is possible that accounting changes resulting from the convergence of UK and international accounting standards, including the introduction of FRS 26, could result in some differences in the presentation and the measurement of assets and liabilities in future financial statements.

Impact of the arrangements with Canada Life Limited

On 11 May 2006, the Society entered into various agreements with Canada Life, which are expected to lead to the transfer of around 90% of the Society's non-profit pension annuities in payment. The actual transfer of those policies will take place following High Court approval of a Part VII scheme of arrangement. Until that date, this business is subject to a reassurance arrangement under which Canada Life bears substantially all the risks and rewards from this business with effect from 1 January 2006. This transfer is reflected as an increase within the 'Reinsurers' share of technical provisions' asset on the Summary Balance Sheet.

In order to protect the policyholders from a large counterparty credit exposure, the initial premium has been deposited back with the Society until the final transfer is approved by the High Court and completed. This deposit is held in assets with a similar investment mix to that previously held by the Society. Canada Life holds a secured charge over these assets. The investment returns from those secured assets are attributed to Canada Life and payments of related annuities are deducted from the deposited assets. The net balance due to Canada Life at 30 June 2006, of £4,361m, is shown within 'Deposits received from reinsurer – secured' as a new category of liability on the Summary Balance Sheet. This deposit back arrangement has the effect of increasing the Society's total assets and total liabilities by the deposited amount.

In the unlikely event that High Court approval for the Part VII scheme is not granted, the reassurance arrangement permits termination by either party.

Investment performance and capacity to pay bonuses

During the period, the Society continued to operate a cautious investment strategy of retaining a low proportion of the with-profits fund in equities and property, in order that its assets match closely its liabilities. The weighting in favour of fixed-income securities within the investment portfolio results in there being limited scope for growth of the fund, as any changes to asset values resulting from movements in yields are substantially mirrored in equivalent and offsetting changes in the value of liabilities.

The Society sold £578m of indirect property holdings during the period. This action was taken to improve the liquidity of the property portfolio. The Society continues to seek attractive opportunities in which to reinvest the proceeds.

The gross return on all with-profits assets was 0.6% for the period, compared with 5.3% for the similar period in 2005. However, after adjusting for bond yield movements (which affect both assets and liabilities), the with-profits assets produced a return during the period of 3.8%, before charges and tax, compared with 4.0% for the similar period in 2005. This is not necessarily a meaningful indicator of the expected investment return for the full year.

Protection of the fund and policy surrenders

Where a policyholder surrenders his or her with-profits policy (or switches to a unit-linked fund) before maturity, contractual obligations in respect of payouts under the policy generally do not apply. The Society takes account of the interests of all policyholders in these circumstances by paying the policy value (or equivalent), less a financial adjustment. In setting the financial adjustment, the aim is for the amounts paid to surrendering policies to be fair, but not to disadvantage continuing policyholders. In particular, the amounts paid to surrendering policyholders should not reduce the payout prospects of the continuing policyholders.

This adjustment can be varied at any time without advance notice to policyholders and any such change would reflect the financial position of the Society at that time.

Policyholders' withdrawals from the fund have continued in an orderly manner during the period.

Business risks

Full details of material contingent liabilities and uncertainties are set out in the 2005 annual financial statements. Updates on the positions with the Parliamentary Ombudsman Inquiry, European Parliamentary Inquiry and the tax treatment of payments arising from reviews of pension products have been provided in the Corporate Review. The risks relating to the provisions for annuitant mortality have been significantly reduced by the arrangements with Canada Life announced in May.

As previously reported, the Society was unable to reach agreement with HBOS over the initial premium on the 2001 reassurance arrangement with HBOS and the matter was referred to an independent umpire for resolution. The umpire has recently issued his final determination and it has been possible to reduce the provision established for this liability.

A case management conference has been conducted in respect of the litigation commenced by 413 with-profits annuitants and this case continues to progress towards a trial, which is now expected to take place in early 2008.

The increase in medium term interest rates during the reporting period has reduced the risk that the provisions for guarantees might not be adequate.

Discussions continue with the FSA in respect of the appropriate level of capital to be held by the Society under the individual capital adequacy regulatory framework.

As noted in the 2005 annual financial statements, there remains the possibility that further complaints and claims could be made against the Society, alleging fraud or mis-selling or otherwise seeking compensation.

The Board's conclusions on provisions and going concern

The Board is responsible for making a formal assessment as to whether the "going concern" basis is appropriate for preparing any financial statements. The going concern basis presumes that the Society will continue to be able to meet its guaranteed obligations to policyholders and other creditors as they fall due. To do this, the Society must have sufficient assets not only to meet the payments associated with its business, but also to withstand the impact of other events that might reasonably be expected to happen.

The Board has given due consideration to potential risks and possible actions and has concluded that it remains appropriate to prepare the Society's financial statements on a going concern basis.

Summary Balance Sheet
as at 30 June 2006

Assets	30 June 2006 £m	31 December 2005 £m
Investments		
Land and buildings	761	710
Investments in group undertakings	19	16
Shares and units in unit trusts	572	1,172
Fixed-income securities	11,822	12,073
Deposits and other investments	474	352
	13,648	14,323
Assets held to cover linked liabilities	722	741
	14,370	15,064
Reinsurers' share of technical provisions	7,274	2,989
Other assets	394	425
Total assets	**22,038**	**18,478**

Liabilities		
Subordinated liabilities	167	167
Technical Provisions		
Excess realistic assets	786	669
Other with-profits technical provisions	8,655	9,151
Non-profit technical provisions	4,649	5,006
Linked liabilities and claims	3,256	3,312
	17,346	18,138
Deposits received from reinsurer – secured	4,361	–
Other liabilities	164	173
Total liabilities	**22,038**	**18,478**

Note:

The Equitable Life Assurance Society's Summary Balance Sheet is not consolidated and represents the position of the Society only and is unaudited and does not constitute statutory financial statements as defined in Section 240 of the Companies Act 1985.

Equitable Life