

The Equitable Life Assurance Society

Registered office

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Policyholder administration

Walton Street, Aylesbury, Buckinghamshire HP21 7QW

Board of Directors

Ian Brimecome, Chairman (b) (c) (d)

Peter Smith, Deputy Chairman (a) (b) (d)

Chris Wiscarson, Chief Executive (c) (d)

Tim Bateman, Finance Director (c)

Mark Earls, Chief Operating Officer

David Adams OBE, Non-executive Director (a) (c)

Keith Nicholson, Non-executive Director (a) (c)

Ian Reynolds, Non-executive Director (a) (c) (d)

Cathryn Riley, Non-executive Director (b) (c)

Key to membership of the principal Board Committees

- (a) Audit
- (b) Remuneration
- (c) Investment
- (d) Nomination

With-profits Actuary

Rob Merry

Head of Actuarial Function

Tim Bateman

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2 Corporate review

The Society's Chairman, Ian Brimecome,
and Chief Executive, Chris Wiscarson, on behalf of the Board

Dear Members

Since the beginning of 2009, the unprecedented financial turbulence has given way to uncertainty about the impact of the recession. We are pleased to report our continued financial stability as well as progress in preparing the business for the years ahead.

Key milestones since our last report are:

- The Society's key measure of solvency, Excess Realistic Assets, is £414m at 30 June 2009, representing 7.5% of the with-profits fund;
- Ian Brimecome and Chris Wiscarson have taken over from Vanni Treves and Charles Thomson as Chairman and Chief Executive respectively;
- Mark Earls has been appointed as an executive Director;
- Cathryn Riley and Keith Nicholson have joined the Board as non-executive Directors;
- The Parliamentary Ombudsman issued a further report to Parliament *Injustice Unremedied: The Government's response on Equitable Life* in which she concludes that whatever the outcome of the Government's proposed process, the injustice which she identified will not be remedied;
- The Government's adviser, Sir John Chadwick, has issued an interim report regarding a possible Government ex-gratia scheme for policyholders; and
- Our selection process for outsourced administration services has progressed well and we expect to be able to enter into a new contract by the end of 2009.

Financial position

Investment performance in the first half of the year has reflected the very difficult market conditions for property, equity and Government bonds, though we are pleased to report that corporate bond values have increased from the lows seen around the end of March to the extent that most of the losses incurred in the first quarter have been reversed. There has also been a significant increase in the cost of the former staff pension scheme. These factors have been offset by reductions in technical provisions thereby maintaining the Excess Realistic Assets at £414m at 30 June 2009 (£414m at 31 December 2008). The Excess Realistic Assets represents 7.5% of the with-profits fund (7% at 31 December 2008).

Your Board

As previously announced, Ian Brimecome was appointed Chairman of the Board when Vanni Treves stood down at the end of August. At the same time, Chris Wiscarson joined the Society as Chief Executive, replacing Charles Thomson.

Ian Brimecome has been a Director of the Society since January 2007 and is currently also Chairman of our Investment Committee and Nominations Committee. He has a number of senior roles in financial services including Chairman of Fox-Pitt Kelton Ltd.'s Advisory Board. He is a non-executive Director of AXA UK plc where he also chairs their With-profits Committee. He is also Chairman of AXA's subsidiary Bluefin Group.

Chris Wiscarson joined the Society as Chief Executive on 2 September 2009, coming from Lloyds Banking Group, where he held very senior roles on the Group Executive Committee, most recently Group Integration Director. Chris started his career with Equitable Life, leaving in 1979 to move to Southern Life in South Africa. He returned to England in 1986 as Chief Executive of Save & Prosper Insurance and became European Director of Lloyds Abbey Life Group in 1990. He was Group Finance Director, then Chief Executive of Lloyds TSB Life. Chris's wealth of financial services experience, including outsourcing, will be an invaluable asset for the next phase of Equitable Life's development.

The Board has also appointed Mark Earls, Chief Operating Officer, as an executive Director. Mark has worked for Equitable Life since 2002 as Head of Operations and Programmes. During his time at Equitable, Mark has led and completed the Rectification and Managed Pension reviews. He was responsible for managing the programmes which led to the transfer of the non-profit annuities to Canada Life and the transfer of the with-profits annuities to Prudential. He is playing the leading role in securing the new administration arrangements. Prior to joining Equitable, Mark was a Programme Director at PricewaterhouseCoopers, working in the finance industry and, prior to that, spent 20 years at Marks & Spencer.

We are also pleased to welcome Cathryn Riley and Keith Nicholson, who joined the Board in late August as non-executive Directors.

Cathryn is Chief Operating Officer and Chief Information Officer Europe, at Aviva plc, after having served in a number of executive roles within the Aviva Group. In a wide ranging career covering human resources, customer services, operations and general management, she has worked for British Coal, British Airways, Coopers & Lybrand and BUPA before joining Aviva in 1996.

Keith was with KPMG until 2009 spending more than 30 years with the firm, over 20 of them as a partner. He has wide experience with financial services companies covering audit and advisory roles. These included FTSE 100 companies in the UK and non-UK multinationals. He has also served on the Auditing Practices Board and on the Insurance Sub-committee of the Institute of Chartered Accountants in England and Wales.

These appointments complete the establishment of the new team that will take the Society forward.

Jean Wood also retired from the Board with Vanni and Charles at the end of August. Vanni, Charles and Jean have performed an admirable job stewarding the Society from its near collapse in 2001 through to its relative stability today. The Board thanks them for their outstanding contribution through some extremely challenging times.

Government compensation

As previously reported, the Society believes that the Government's response to the Parliamentary Ombudsman's report was wholly unsatisfactory. The Ombudsman herself submitted a further report to Parliament in May entitled *Injustice Unremedied: The Government's response on Equitable Life*. Only Parliament can influence the Government's response to their Ombudsman and we have continued to lobby MPs to exert as much pressure on the Government as possible. Although 328 MPs have openly supported the Ombudsman's recommendations through signing an Early Day Motion, we see no evidence that the Government is minded to change its view.

John Bercow MP, the new Speaker of the House of Commons, said in his election address: "the case for strengthening Back Benchers, to revive Parliament as a whole, is incontrovertible. ...The Prime Minister recently asserted his desire to restore authority to Parliament, and, if elected, I would seek to hold him and any successor to that pledge. This House must seize back control of its own core functions by making a number of changes. For instance, there must be a business committee which it really runs;". With these comments in mind, we have written to the Speaker noting the substantial endorsement of back bench MPs for the Ombudsman's recommendations, as evidenced by the Early Day Motion, and calling for his support for a debate on the floor of the chamber and a free vote on the issue.

The Government asked Sir John Chadwick, a retired Lord Justice of the Court of Appeal, to advise them on certain aspects of their proposed alternative scheme. The Society has provided Sir John with assistance including detailed policy data in order to encourage progress as early as possible. Following initial consultation in June, Sir John issued an interim report in August setting out a new approach to a scheme and asking for comments. His new approach has the potential to include a very wide range of policyholders and also could support a level of simplification which could reduce further delays.

Looking ahead

We have invited bids from specialist companies to provide outsourced administration services to Equitable Life in its run-off. We received significant proposals from a number of leading providers and Equitable Life staff and advisers investigated the different proposals in great detail and visited the companies to verify their capabilities. We now plan to finalise the details of a new agreement by the end of 2009.

Your Board will continue to work tirelessly to maintain the stability and the security of your Society and to improve further the prospects for all policyholders.

On behalf of the Society's Board of Directors on 25 September 2009



Ian Brimecome
Chairman



Chris Wiscarson
Chief Executive

Personal message from the Chairman

On behalf of the Board, I wish to express particular appreciation for the outstanding contribution of Vanni Treves, who served as Chairman of the Society for the best part of a decade, one of the most challenging in the Society's very long history. Having become Chairman when Equitable Life was on the brink of insolvency, Vanni leaves the company in a stronger, simpler and more stable position from which we look to the future with confidence. He was already a long standing member of the Society before he joined the Board and in dealings with members, journalists, politicians and other stakeholders, policyholders could not have had a better advocate for their cause during those most challenging times.

A handwritten signature in black ink, appearing to read 'I Brimecome', with a stylized flourish at the end.

Ian Brimecome
Chairman

Review of the Society's financial position

The key performance measure of the Society's net resources, Excess Realistic Assets ("ERA"), is represented by the excess of realistic assets over liabilities before deduction of the estimate of the value of future discretionary increases to policy values. This amount, which is reported as a policy-related liability in the technical provisions in the Balance Sheet, 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.

At 30 June 2009, the ERA was £414m, the same as the previous year end. The analysis of the with-profits assets and liabilities is as follows:

	30 June 2009 £m	31 December 2008 £m
Realistic value of with-profits assets	5,523	5,951
less:		
Policy values	4,167	4,552
Future charges	(286)	(300)
Impact of early surrenders	(32)	(34)
Cost of guarantees	783	814
Other long-term liabilities	262	287
Other liabilities	215	218
	5,109	5,537
Excess Realistic Assets	414	414

The policy value attributable to with-profits policies can include an element of non-guaranteed final bonus, sometimes referred to as terminal bonus. Further, for reporting purposes, a prudent allowance for future bonuses, based on assumed future net investment returns less deductions for potential risks, is included in the valuation of the long-term business technical provisions in the financial statements.

The key movements in the ERA during the period are shown in the following table:

	January to June 2009 £m	January to December 2008 £m
Opening Excess Realistic Assets	414	621
Investment performance net of the benefit of reduction in Policy Values	(62)	(311)
Mortality experience and assumption changes	-	3
Surrender experience and assumption changes	5	52
Changes in other valuation assumptions	83	26
Variances in provisions and expenses	(39)	(7)
Other movements	13	30
Closing Excess Realistic Assets	414	414

The Society seeks to maintain the ERA balance at a level that protects solvency while treating continuing and exiting customers fairly. The balance at 30 June 2009 represents 7.5% of the with-profits realistic assets, an increase from the equivalent figure of 7% at 31 December 2008.

Key elements affecting the Society over the period were investment performance, changes to valuation assumptions and variances in provisions.

Investment performance

Over the first half of the year, the Society experienced very difficult market conditions. Property and equity values fell, and rising Government bond yields reduced the value of fixed income securities. However, corporate bond markets rallied in the second quarter, reversing most of the losses sustained in the period to the end of March. The solvency position also improved due to the effect of the policy value reductions earlier in the year and the impact of rising Government bond yields on the cost of guarantees.

Valuation assumptions

In the light of the corporate bond market rally and the low level of defaults, the valuation of the Society's non-profit annuities has been amended to take more credit for the high yield on corporate bonds supporting this business.

Provisions

The provision for our commitments to the former staff pension scheme increased by over £50m as a result of the adverse market conditions and more conservative valuation assumptions by the Scheme Actuary. Further expenses incurred in the selection process for outsourced administration services were more than offset by reductions to provisions for future expenses and other long running reviews now coming to a close.

Developments during the year

The Society continues to work on key changes to secure a more stable financial future for policyholders. Based on our evaluation of alternative outsourced administration service providers, the Society is finalising the details of a new agreement. The Board has approved costs up to the conclusion of this agreement and an allowance for this expenditure is reflected in the ERA above.

The Society's process of managing risks has enabled it to remain solvent during the recent financial crisis. Valuable lessons have been learnt through this period and the Society is considering a number of steps to reduce the risks faced by the Society with the aim of ensuring greater stability in similar extreme conditions. Those steps include: ensuring the fair treatment of policyholders in sustained periods of low returns; seeking to reduce risk in relation to the former staff pension scheme; and reviewing the investment strategy for the Society. We will keep policyholders abreast of progress.

The Society continues to prepare for the significant regulatory changes anticipated as part of the European Union's Solvency II legislative programme. This programme will have an impact on both the governance and solvency framework for all insurers and is anticipated to come into force at the end of 2012. We support the recent ABI letter to the Chancellor of the Exchequer setting

out concerns about the effect of this new regulatory framework on the financial stability of the insurance industry.

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.

As noted in the Annual Report in March, the financial market's re-evaluation of the risk of default and illiquid market conditions in 2008 resulted in a reduction in value of corporate bonds held by the Society of £380m (after allowance for movements in Government bond yields). This downward re-evaluation continued during the first quarter of 2009 to increase this loss significantly but conditions improved during the second quarter of 2009, restoring the position broadly to that at the 2008 year-end. In the long term, as we will hold many of these bonds to maturity we anticipate that we will recover more of the reduction in value suffered. The Society should also benefit from improving corporate bond prices as the financial markets continue to re-evaluate default risk and market liquidity improves.

The Society achieved a gross return on the with-profits fund of -0.8% in the first half of 2009. After adjusting for changes in Government bond yields in the period, the effective gross return was 2%. The Society currently deducts 1% p.a. (0.5% for the period) for the cost of administration and 1% p.a. (0.5% for the period) for the future cost of guarantees arising from policies maturing where the minimum guaranteed benefit exceeds the policy value. After taking account of those deductions and the impact of changes in provisions, the effective net return on the with-profits fund in the first half of 2009 was -0.1%.

As noted in the Annual Report in March, policy values were reduced by 2% for applicable with-profits pension policies and by 1.6% for life assurance policies from 1 March 2009 to reflect the deterioration in asset values early in 2009. Following this reduction all policy values have been maintained at the same level. We will keep investment performance under continuing review as the financial conditions evolve and will take action to amend bonuses where appropriate.

Protection of the fund and policy surrenders

Where a policyholder surrenders their with-profits policy (or switches to a unit-linked fund) before maturity, the Society takes account of the interests of all policyholders 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.

The approach and the level of the adjustment can be varied at any time, without advance notice to policyholders, reflecting the financial position of the Society at that time.

Policyholders' withdrawals from the fund have continued to be stable during the period and the financial adjustment for individual policies has been maintained at 5%. The financial adjustment for group schemes is assessed scheme by scheme and is subject to a minimum of 5%.

Financial Services Authority capital requirements

In common with all insurers, the Society prepares an annual confidential assessment of its capital needs, as required by FSA rules introduced under the Individual Capital Assessment framework. The calculations are underpinned by consideration of the underlying risks, which include credit risk, market risk, liquidity risk, operational risk and insurance risk.

The Society continually monitors its capital resources in the light of changing financial conditions and, in adverse financial conditions, will take all actions available to protect the Society's solvency. The uncertainty in the financial markets has led to a steady dialogue with the FSA in these rapidly changing circumstances. The FSA continues to be regularly apprised of the Society's position.

Business risks

Full details of material contingent liabilities and uncertainties are set out in the 2008 annual financial statements. Updates on the positions with the Parliamentary Ombudsman's report and the strategic approaches being undertaken for the Society have been provided in the Corporate review.

Provisions continue to be made for the Society's contractual commitments in respect of the two pension schemes for which HBOS is the principal employer. Since the last triennial valuation at the end of 2007, these commitments have increased very significantly as financial conditions have worsened. Further, there remains a possibility that a more conservative basis may need to be adopted in future in calculating the Society's obligations.

As noted in the 2008 Annual Report, the Society has made appropriate provisions for future expenses, alleged mis-selling and other risks based on currently available information. As more information becomes available, the range of possible outcomes in relation to these issues has narrowed and the degree of confidence around the levels of the individual provisions has increased. The Society now considers that the potential impact of these uncertainties has diminished significantly over the past few years, but the potential impact of the range of uncertainties relating to provisions could still be significant.

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 examined the issues relevant to the going concern basis which include the exposure to: investment losses; increases in corporate bond defaults in excess of current levels assumed in market prices; increases in provisions; the impact of discretionary bonus payments; the effect of lower interest rates on the behaviour of policyholders with Guaranteed Investment Returns; future expense levels; the costs of continuing pension obligations to former staff; persistency risks (the age or duration at which benefits are taken), and mortality rates.

The volatility in investment and property markets and the uncertain nature of provisions and other potential strains on the Society's finances remain under close management scrutiny, but the Board recognises the possibility that the Society may not meet regulatory capital requirements at all times. Any such failure does not, of itself, cause the Society to become insolvent.

The Board is confident of its ability to manage adverse scenarios that may arise but extremely adverse scenarios could prejudice the continuing solvency of the Society and so there cannot be absolute assurance.

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 2009

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	30 June 2009 £m	31 December 2008 £m
Assets		
Investments		
Land and buildings	400	442
Investments in Group undertakings	24	30
Shares and other variable yield securities and units in unit trusts	333	430
Debt and other fixed-income securities	4,864	5,203
Deposits and other investments	283	264
	5,904	6,369
Assets held to cover linked liabilities	75	74
Reinsurers' share of technical provisions	2,012	2,113
Other assets	135	198
Total assets	8,126	8,754
Liabilities		
Technical provisions		
Excess realistic assets	414	414
Other with-profits technical provisions	4,894	5,319
Non-profit technical provisions	819	959
Linked liabilities and claims	1,786	1,845
	7,913	8,537
Other liabilities	213	217
Total liabilities	8,126	8,754

Note:

The Equitable Life Assurance Society's Summary Balance Sheet is not consolidated and represents the position of the Society only, is unaudited and does not constitute statutory financial statements as defined in section 435 of the Companies Act 2006.

