Equitable Life

NEWS RELEASE

For immediate release
27 March 2009

Equitable Life's Preliminary Results Announcement for the year ended 31 December 2008

Business Highlights:

- The strategic review looking at a sale to a third party concluded that there was no proposal that would necessarily improve prospects for policyholders;
- The decision was taken to remain closed to new business and allow the Society to run down gradually over many years paying policy benefits as they fall due (known as 'run-off'). The Society is now seeking alternative administration arrangements to reduce costs for policyholders;
- The publication of the Parliamentary Ombudsman's report recommending Government compensation for policyholders.

2008, and the early months of 2009, have seen the worst global economic crisis in living memory. All the work that has been done in the previous seven years to rebuild the Society's financial position has allowed it to weather the storm. While the Society is not immune to the effects of the crisis, and reserves have been reduced sharply on both the regulatory and accounting bases, the underlying financial position of the Society remains sound. While in the face of such global economic uncertainty, there can be no absolute assurance, the matching of investment income with future policy payments gives confidence that the Society can deal with the effects of the current recession.

Vanni Treves, Equitable Life's Chairman, said: "The durability of the Society's financial position in the face of the global economic turmoil is clear evidence of the success of the steps we have taken. We are also pleased to update our policyholders on our plan to secure the run-off strategy for the future. We will also continue to lobby Government to pay the compensation which our policyholders deserve."

Charles Thomson, the Society's Chief Executive, said: "With careful management the Society continues to ride out the most challenging of financial conditions. We continue to look for the best outcomes for our policyholders and we are making progress with our negotiations for a long term administration agreement which will offer expense security for the future."

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Notes to editors:

1) A copy of this announcement can be found in the Media Centre/latest release section and in the Financials/financial reports section of our website www.equitable.co.uk

2) **Financial calendar**
17 April 2009 – Annual report and accounts published and sent to members.
11 May 2009 – 11 am, AGM, Holiday Inn – Regents Park, Carburton Street, London W1W 5EE

3) **Non-Statutory Accounts**
The information shown in respect of the year ended 31 December 2008 is extracted from the Society's Accounts for that year, which were approved by the Board of Directors on 26 March 2009 and will be filed with the Registrar of Companies. The financial information contained in this announcement does not constitute statutory accounts within the meaning of Section 240 of the Companies Act 1985. The report of the auditors on these Accounts is unqualified and does not contain a statement under Section 237(2) or (3) of the Companies Act 1985. The audit report refers to contingent liabilities and uncertainties in respect of the potential additional claims against the Society, expenses and increases in provisions that could arise as a result of different legal and regulatory views on its historical conduct and any changes in provisions arising from policyholder behaviour. The audit opinion is not qualified in respect of the contingent liabilities and uncertainties disclosed in note 23 and under the heading 'the Board's conclusion on provisions and going concern' in the Financial Review, which is referred to in note 23.

4) **FSA returns**
The Society will also be submitting its Annual FSA Insurance Returns for the year ended 31 December 2008. Copies are available from the Society's registered office: 20-22 Bedford Row, London WC1R 4JS. The Returns will also available on the Society's website at www.equitable.co.uk

Corporate review

Dear Members

2008, and the early months of 2009, have seen the worst global economic crisis in living memory. All the work that has been done in the previous seven years to rebuild our financial position has allowed the Society to weather the storm. While we are not immune to the effects of the crisis, and reserves have been reduced sharply on both the regulatory and accounting bases, the underlying financial position of the Society remains sound. While in the face of such global economic uncertainty, there can be no absolute assurance, our matching of investment income with future policy payments gives us confidence that we can deal with the effects of the current recession.

2008 also saw some important milestones for the Society:

- Our strategic review looking at a sale to a third party concluded that there was no proposal that would necessarily improve prospects for policyholders;

- The decision to remain closed to new business and allow the Society to run down gradually over many years paying policy benefits as they fall due. This is known as 'run-off'. We are seeking alternative administration arrangements to reduce costs for policyholders;

- The publication of the Parliamentary Ombudsman's report recommending Government compensation for policyholders.

The continuing uncertainty in the financial markets and the global economy remains a threat to all companies. However, subject to that profound uncertainty, we believe that the Society, in run-off, can continue to take whatever action is necessary to secure our future. One significant remaining concern is that of future expenses and we are currently looking to negotiate a contract to address that risk for a significant period into the future. We will also adapt our internal organisation to reduce costs.

2008 Bonus declaration

During 2008, the Society achieved a gross return on the with-profits fund of 0.1%. In such a harsh economic climate, we expect that to be a relatively good return compared with other with-profits funds. After adjusting for a rise in the value of liabilities corresponding to the fall in interest rates, the effective gross return was -6.1%. The Society currently deducts 1.0% p.a. to cover the cost of administration (this figure allows for future diseconomies of scale) and, in 2008, 0.5% p.a. to cover the cost of guarantees. The effective net return on the with-profits fund in 2008 was -7.7% (2007: 1.9%). Further details of the factors affecting the Board's bonus decisions are given in the Financial review.

A number of changes to policy values have been made since our last report:

- Policy values (or their equivalents) were reduced at 31 December 2008 by 3.0% for UK with-profits pensions policies and by 2.4% for UK life policies (2007: increased by 5.0% p.a. and 4.0% p.a. respectively);

- Policy values (or their equivalents) were subsequently reduced at 1 March 2009 by a further 2.0% for UK with-profits pensions policies and by 1.6% for UK life policies to recognise the further falls in values of assets;

- No interim bonus will be added to UK with-profits pensions policies and UK life policies from 1 January 2008 until further notice;

- Consistent with previous years, there is no guaranteed reversionary bonus for 2008; and
- The financial adjustment applied to the early surrender of with-profits policies remains at 5.0%. This adjustment can be varied at any time and is kept under regular review.

Where a contractual policy payment is due and the guaranteed benefit exceeds the policy value (or its equivalent), it is the guaranteed benefit which will be paid.

The allowance for the cost of guarantees has been increased to 1.0% p.a. from 1 January 2009.

Financial position

In spite of the unprecedented economic circumstances of 2008 and the further decline in the opening months of 2009 the Society has maintained a solvent financial position.

The excess realistic assets at 31 December 2008 were £414 million (2007: £621 million) representing 7.0% of the with-profits fund (2007: 9.2%). Such a fall is to be expected during a significant financial crisis, particularly with the falls in value of corporate bonds discussed below. The Board keeps this measure under close scrutiny and a number of adjustments to interim bonuses were made during 2008 in order to protect the Society's long-term stability.

An important element in the change in the Society's financial position comes from our holdings of corporate bonds. Market fears concerning default and liquidity have dramatically reduced the price of these bonds. It is worth noting that, although we use market prices to value the bonds in our accounts, we normally hold bonds to maturity. So far, actual defaults by companies have not increased materially. Consequently, we intend to continue to hold these bonds to maturity, so, unless actual levels of default increase, the (unrealised) losses reflected in these accounts and the further losses in the opening months of 2009 should reverse.

Parliamentary Ombudsman

The Parliamentary Ombudsman presented her report *Equitable Life: a decade of regulatory failure* to Parliament in July 2008 and we wrote to policyholders regarding the report in August.

The Government finally responded to the Ombudsman's report in January 2009. We welcomed the apology which the Government made at that time and their acceptance of the Ombudsman's findings of maladministration in some areas. However, we are concerned that the Government has decided to 'act as judge on its own behalf' in rejecting some of the Ombudsman's findings of maladministration and injustice. We are also disappointed by the suggestion that the Treasury will consider some form of 'means testing' for policyholders. We are frustrated that there is, as yet, no timescale given for the Government's alternative proposed scheme.

We found the Government's response to the Ombudsman's thorough and authoritative report to be wholly unsatisfactory and we gave evidence to Parliament's Public Administration Select Committee ("PASC") to that effect. In March 2009, PASC issued its second report *Justice denied? The Government's response to the Ombudsman's report on Equitable Life.* The Committee concluded that the scheme proposed by the Government "is inadequate as a remedy for injustice". The Ombudsman is Parliament's Ombudsman and it is for Parliament to uphold her role. Consequently, we have worked hard to lobby political opinion, giving evidence to the Select Committee, writing to the Treasury Minister and meeting many MPs to encourage Parliamentarians to seek to influence the Government's response. (Some examples of this are published in the media section of the Society's website.) This lobbying activity will continue as we support the Parliamentary process.

The Government has asked Sir John Chadwick, a former Lord Justice of the Court of Appeal, to give them further advice relevant to the design of their proposed scheme. We have contacted Sir John Chadwick to offer our support on making progress as quickly as possible.

Governance

The Society's member relations strategy (published in the corporate governance section of the Society's website) aims to help members take an interest in its governance. Questions from members in respect of corporate issues can be addressed to the member relations function through a dedicated email address: member.relations@equitable.co.uk and through a special postal address: Member relations, Equitable Life Assurance Society, 2-4 Wendover Road, Aylesbury HP21 9LB. Questions relating to members' policies continue to be addressed by customer services staff in Aylesbury.

The Society produces a guide on how we manage the with-profits fund. This is a simpler, easier to follow version of the Principles and Practices of Financial Management ("PPFM"). Also, each year we produce reports by the Board and by the With-profits Actuary on how the with-profits fund has been managed. In the interests of keeping costs down, we make these documents available on the corporate governance section of the Society's website. They are also available to members on request. If there are material changes in these documents we will, of course, draw them to your attention.

Customer service

During 2008, we issued 245,000 annual statements to inform policyholders of the progress of their policies. We issued around 466,000 letters to policyholders and former policyholders regarding the Parliamentary Ombudsman's report and we also issued 198,000 letters regarding the possible sale process.

Our customer services staff dealt with 261,000 telephone calls (2007: 330,000) and 273,000 letters (2007: 316,000).

Business outlook

The Society's business objectives continue to include:

- Treating policyholders fairly, including leavers, and ensuring we meet the guarantees provided to policyholders by pursuing an appropriate investment strategy;

- Reducing expenses and ensuring an efficient and effective administration; and

- Resolving outstanding claims against the fund.

The Society's financial position is achieved, in part, by investing predominantly in fixed-income investments (with only around 20% of the fund in equities and property). We are satisfied that the expected cashflow from investments is more than sufficient to meet the expected policy payments year by year, but we will monitor the position in detail as necessary through these exceptional financial times.

Looking forward: run-off

During 2008, the Board decided that although various proposals were received from third parties, none would necessarily provide improved prospects for policyholders. Consequently, the Board is now pursuing the best possible run-off strategy, looking in detail at the company, people, structure and costs.

A key concern in run-off is expenses. Over time, as policies continue to mature, the relative management costs of the Society will increase and the cost of that increase will fall on the remaining policyholders. We have modelled this and made allowances in our management of the business, but some uncertainty remains. For that reason we are investigating long-term agreements with a number of companies who can provide administration services to the Society (known as 'third party administrators' or TPAs). The TPAs are in competition with each other and with HBOS (now part of the Lloyds Banking Group) who currently act as a TPA for the Society. We expect to complete a long-term agreement during 2009 and this should give both cost reductions in the short term and considerably greater certainty over future expense levels for policyholders in the long term.

Also, in run-off, we will require a smaller Board of Directors going forward and the role of Chief Executive will also be less challenging than before and are taking the following steps:

- We are currently in the process of recruiting a new Chief Executive who will take over from Charles Thomson who will step down in the autumn;

- We plan to reduce the number of non-executive Directors on the Board; and

- As a first step on that road, Fred Shedden and Andrew Threadgold will retire from the Board at the AGM and will not be seeking re-election.

To allow for the retirement of our other longer serving Directors, we are seeking two new non-executive Directors; one with an accounting or other finance background and the other with experience of outsourced administration. The Society has appointed search consultants, The Zygos Partnership, to help to identify suitable candidates. Anyone who believes that he or she has the skills and experience we are seeking and can add substantial value to the Board is encouraged to put his or her name forward for consideration. If you wish to be considered, please send your c.v. to The Zygos Partnership, 15 Sloane Square, London SW1W 8ER (or by e-mail to Toni@zygos.com) quoting reference 1017.

Further consideration is being given to the core organisation which will need to remain to give appropriate cost-effective control over the business on behalf of policyholders. We have already closed our London offices and relocated those operations to cheaper premises in Aylesbury. Also, to save costs and reflecting the Society's more stable position, we have decided to issue the interim review for the period to 30 June 2009 only on request – it will continue to be available to all on the Society's website.

Since 2001, the Society has had to face a wide range of extremely challenging circumstances ranging from the instability caused by the guaranteed annuity rates ("GARs"), various schemes to address problems of the past, the rising cost of annuities and financial markets in crisis. The Society has addressed those challenges successfully and we hope for calmer waters in the future, though we recognise the risk posed by the current uncertainty of financial markets.

In spite of the global economic crisis, we are pleased to report steady progress at Equitable Life and a clear plan for the future.

As always, you may rest assured that your Board will continue to do everything it possibly can 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

Vanni Treves **Chairman**	Charles Thomson **Chief Executive**

Personal message from the Chairman:

Our Corporate review explains that Charles Thomson has decided to leave the Society.

Charles joined in 2001 and took over as Chief Executive with the objective of leading a highly unstable company to a stable and secure future. That job has been well done.

As a result of Charles' success, the range and depth of challenges facing management will reduce significantly and that is why Charles has decided to move on.

On behalf of the Board, I would like to take this opportunity to express our thanks to Charles for his achievements over the last eight years. There was an intimidating number of complex issues to be addressed and the relentless arrival of new hurdles year after year as progress was being made would have drained lesser men. Yet, Charles' resourcefulness and commitment have contributed greatly to a number of innovative solutions including major deals the nature of which has been unprecedented.

The Board is grateful to Charles for the work he has done and the leadership he has shown on behalf of policyholders and wishes Charles all the best for the future.

We would also like to put on record our thanks to Fred Shedden and Andrew Threadgold for their outstanding contributions to the Society over the last eight years. They have been exemplary non-executive Directors: wise, committed, tolerant and strong friends, especially in adversity. The Society could not have hoped for more from them, and I count myself lucky to have been their colleague.

Vanni Treves
Chairman

Financial review

Excess Realistic Assets and regulatory solvency

The key measure of the Society's net resources is the excess of realistic assets over liabilities before deduction of the estimate of the value of future discretionary enhancements to policy values ("ERA"). This amount, which is reported as a policy-related liability in the technical provisions, 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 31 December 2008, ERA were £414m, a decrease of £207m over the prior year. The analysis of the with-profits assets and liabilities is as follows:

	2008 £m	2007 £m
Realistic value of with-profits assets	5,951	6,775
less:		
Policy values	4,552	5,383
Future charges	(300)	(206)
Impact of early surrenders	(34)	(31)
Cost of guarantees	814	442
Other long-term liabilities	287	384
Other liabilities	218	182
	5,537	6,154
Excess Realistic Assets	**414**	**621**

A description of the above liabilities is set out in Note 15g on page 49.

The key movements in the ERA during 2008 are shown in the following table:

	2008 £m	2007 £m
Opening Excess Realistic Assets	**621**	**884**
Investment performance net of the benefit of reduction in policy values and effect of bonuses	(311)	(112)
Mortality experience and assumption changes	3	(22)
Surrender experience and assumption changes	52	19
Changes in other valuation assumptions	26	28
Variances in provisions and expenses	(7)	(13)
Transfer of with-profit annuities to Prudential	(3)	(188)
Other movements	33	25
Closing Excess Realistic Assets	**414**	**621**

The principal changes in the ERA are explained in more detail in later sections of this review.

The Society seeks to maintain the ERA balance at a level that protects solvency while treating continuing and exiting policyholders fairly. The balance at 31 December 2008 represents 7.0% of with-profits realistic assets, a decrease from the equivalent figure of 9.2% at 31 December 2007.

The policy value attributable to with-profits policies may include an element of non-guaranteed final bonus. An 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 provision in these financial statements. Any enhancements to the bonuses assumed would be met from the ERA.

Investment performance and capacity to pay bonuses

The turbulence in the financial markets that began in 2007 continued to escalate during 2008. The Society continues to operate a cautious investment strategy of retaining a relatively low proportion of the with-profits fund in equities and property, in order that its assets match closely its realistic liabilities. This provides the assurance that asset proceeds will be available to meet anticipated policyholder payments as they fall due. The Society's assets are presented in the accounts at fair value which is the price achievable between a willing buyer and seller. Current market conditions have depressed prices as recessionary fears have grown.

Using these valuations the assets backing UK with-profits policies produced a gross return of 0.1% during the year. Falls in Government bond yields increased the value of fixed-income securities. However, this was almost entirely offset by the decrease in the value of corporate bonds as a result of the 'credit crunch', severe falls in property and, to a lesser degree, falls in equity values during the year. The return adjusted for Government bond yield movements (which affect both assets and liabilities) was -6.1%, reducing to -7.7%, after allowing for the impact of expenses, a 0.5% charge for guarantees, tax and the effect of changes in provisions and technical provisions. The changes above together with changes in bonus rates detailed below reduced the ERA by £311m.

Of particular note is the low value placed on corporate bonds, as a result of the re-evaluation of risk of default and illiquid markets. Allowing for the movements in Government bond yields over 2008 the Society's corporate bond holdings have reduced in value by £380m. Provided the Society's experience of defaults on corporate bonds does not reach historically very high levels and liquidity returns to the market, some of this £380m should be recovered in market prices. This would positively impact both the Society's ERA and bonus rates in due course.

The cash flows from the Society's assets and liabilities are well matched, so these depressed asset values do not directly affect our ability to pay guaranteed policy benefits as they are assumed to fall due. These values do, however, limit the Society's ability to declare further bonuses.

The Society considers the appropriate composition of the with-profits fund and seeks to manage its property and equity holdings in line with the run-off of business and its need to meet regulatory capital requirements. In particular, the use of derivatives will be considered where they can protect the with-profits fund from adverse financial conditions.

In determining bonus policy, the Society needs to consider the longer term picture and aims to balance the objectives of retaining sufficient capital to meet its obligations to policyholders and other creditors as they fall due, and of distributing the Society's assets over the lifetime of its policies as fairly as possible. The ability to increase policy values depends to a considerable extent on the returns achieved on, and the outlook for, the Society's corporate bond, property and equity-related portfolios, whose value and liquidity have been affected by adverse market conditions. It is also dependent on actual and expected expense levels, the expected cost of guarantees, costs of meeting commitments in respect of non-profit annuities, miscellaneous profits and losses, possible changes in the level of provisions and further changes to the regulatory environment.

As reported in previous financial statements, a charge is held back from the investment return to meet the cost of guarantees. In 2008 the charge against investment returns was 0.5% p.a. We expect the future charge against investment returns for 2009 onwards to be 1.0% p.a. The revised charge is in accordance with the range of values stated in the Society's Principles and Practices of Financial Management ("PPFM"). This charge can be reduced or increased depending on the financial position of the Society.

At 31 December 2008, and after consideration of all risks, reserving and capital matters, the Board decreased policy values by 3.0% for applicable with-profits pension policies and by 2.4% for life assurance policies (2007: increased by 5.0% p.a. and by 4.0% p.a. respectively) compared with an adjusted return of -7.7%. Reducing policy values by less than the reduction implied by the adjusted return (as happened in 2008) resulted in a distribution of excess assets to policies of £222m (2007: £157m). The Board will keep the level of capital available under review, in order that further bonus declarations reflect the circumstances and the risks facing the Society.

Subsequently, as a result of continuing poor investment returns in early 2009, the Board decreased policy values by a further 2.0% effective from 1 March 2009 for applicable with-profits pension policies and by 1.6% for life assurance policies to give an overall effect since 1 January 2008 of a 5.0% reduction for applicable with-profits pension policies and a 4.0% reduction for life assurance policies. Interim bonus for 2008 was initially set so that pension policies increased by 5.0% p.a. and life assurance policies increased by 4.0% p.a. However, during the year these bonuses were progressively reduced as investment conditions deteriorated and all interim bonus for 2008 was removed in October 2008. Until further notice, no interim bonus will be added for either pension policies or life assurance policies. The Board will keep this evolving situation under close scrutiny during the year.

As previously advised, policyholders should note that, in order to meet all its future contractual liabilities for the foreseeable future, any new distributions of surplus will be made in non-guaranteed form and there is no expectation of any further reversionary bonus being awarded in the near to medium term. Accordingly, there will be no reversionary bonuses for 2008. However, for those policies with Guaranteed Investment Returns ("GIR"), the value of the guaranteed benefit is not affected by a change in policy values, but is increased instead at the rate set out in the policy conditions, typically being 3.5% p.a.

Expenses and provisions

Overall, expenses have decreased in the year to £104m (2007: £166m). This excludes £85m of realised investment losses (2007: £nil) which is included in Investment expenses including interest (see Note 4b). Savings on all other expense categories were achieved. There was, however, an increase in pension provisions following a review of pension commitments in the year.

Incurred exceptional expenses reduced in the year to £54m (2007: £98m) and included the cost of the search for a possible buyer for the Society and a review of pension commitments. The triennial valuation of the pension scheme as at 31 December 2007 concluded later in 2008. Following consultation with our advisors on the most appropriate valuation assumptions to be used as at the end of 2008, the provision has been increased by £22m from the December 2007 level. This reflects the significant impact of the continuing financial turbulence and changes in the underlying assumptions.

As shown in Note 15h to the financial statements, balance sheet provisions, included as part of the technical provisions, have reduced over the year. The miscellaneous provisions (including Managed Pension mis-selling and the Rectification Scheme) have reduced by a combined £102m. The provision for exceptional expenses of £70m includes provision for future pension contributions which is also affected by the pension scheme assumption changes noted above.

The cost of administration and investment management at 0.8% of policy values for 2008 (2007: 0.6%) is an indicator of expense levels. In order to take account of the uncertainty of future costs and the challenge of reducing costs as policies mature or transfer, administration expenses as a percentage of policy values are allowed for at a rate of 1.0% p.a., and underruns (as occurred in 2008) below this level are held in reserve to cover expected future higher costs.

Overall, the ERA reconciliation table shows an adverse variance in provisions and expenses, taken together, of £7m.

During 2008, the Society was able to reach agreement with HBOS over the initial premium payable in respect of the 2001 reassurance arrangement resulting in a further payment, equal to the provision made at the end of 2007.

There remain uncertainties in establishing appropriate values relating to certain provisions and there continues to exist the possibility of changes in provisions arising from regulatory interpretations or requirements. Although the Society, in undertaking its responsibility to be fair to all members, adopts a robust procedure for dealing with mis–selling claims, there remains the risk of exposure to other claims and the possibility that provisions prove insufficient. There also remains the possibility of a return in the future to a situation of volatility in the number of policy exits, with related increases in costs.

Protection of the fund and policyholder behaviour

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. The financial adjustment was maintained at 5.0% throughout 2008. 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.

If the Society were to be forced to sell fixed-interest securities to its disadvantage before their relevant maturity dates, or became forced sellers of property or equity holdings in order to make payments to surrendering policyholders, assets and liabilities cease to be matched. In such circumstances, those policyholders would be expected to bear the related costs incurred, by way of a higher financial adjustment.

Although the Society experienced a stable level of claims during the year, with figures broadly in line with last year, changes in the pattern of surrenders have been reflected in the realistic assumptions which, together with favourable actual experience in the year, result in a gain of £52m (2007: £19m) in ERA, as shown in the reconciliation table on page 6.

Allowance has been made in realistic liabilities for future discretionary non-guaranteed bonuses. As noted previously, it is the Society's intention that any future bonuses will be in a non-guaranteed form. Allowance is made for continuing contractual commitments, such as the GIR of 3.5% p.a. that is applicable to many policies. If the Society's investment return is expected to fall below a rate which covers the guarantees and its expenses and the assumed retirement profile ceases to be appropriate as a result of significant numbers of policyholders deferring their retirement dates, substantially higher technical provisions may be required, as described in Note 15g to the financial statements.

Financial Services Authority capital requirements

In assessing the Society's ability to meet its obligations as they fall due, the amount of ERA is more relevant than the excess of net assets over the regulatory or realistic capital requirements, as reported in the separate set of financial returns sent to the Financial Services Authority ("FSA"). The FSA have established the Capital Resources Requirement ("CRR") which represents the minimum level of regulatory capital which the Society is required to establish. As a mutual company the ERA surplus is deemed to be part of policyholder liabilities, and therefore the Society does not report a capital surplus.

The table below details the principal reconciling items between the ERA and the excess of net assets over the CRR for the Society.

	2008 £m	2007 £m
Excess Realistic Assets	414	621
Reserving adjustments and disallowed assets (1)	35	119
Regulatory net assets	449	740
Capital Resources Requirement (CRR)	(449)	(740)
Net assets in excess of CRR	-	-

Note:
(1) Certain balances are required to be held in the FSA returns at values that are measured on bases different from those adopted for the financial statements.

In addition to the requirement to prepare financial statements on a realistic basis, the Society's particular risks are quantified for the preparation of an annual confidential assessment of its capital needs as required by FSA rules, introduced under the Individual Capital Assessment ("ICA") 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. The continuing uncertainty in the financial markets has led to a steady dialogue with the FSA in these rapidly changing circumstances. The FSA have been regularly apprised of the Society's position.

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 these 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; impact of discretionary bonus payments; effect of lower interest rates on the behaviour of policyholders with GIR; future expense levels (including the costs of the continuing pension obligations to former staff); persistency risks (the age or duration at which benefits are taken); and mortality risks.

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

The financial position of the Society has been projected under a range of economic scenarios. The Board has also considered the level of contingent liabilities (that is, liabilities not recorded in the financial statements but which could conceivably arise, as referred to in Note 23 to the financial statements, entitled 'Contingent liabilities and uncertainties') in its analysis of the Society's financial position. 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 all the potential risks and possible actions available to it and has concluded that it remains appropriate to prepare these financial statements on a going concern basis.

Profit and Loss Account

For the year ended 31 December 2008

Technical account — long-term business

	Notes	Society 2008 £m	£m	Group 2007 £m	£m
Earned premiums, net of reinsurance					
Gross premiums written	2a	103		124	
Outward reinsurance premiums	3				
— Continuing operations		(36)		(26)	
			67		98
Investment Income	4a		370		790
Other technical income	5a		4		41
Total technical income			**441**		**929**
Claims incurred, net of reinsurance					
Claims paid — gross amount	6	940		1,185	
Reinsurers' share	3	(66)		(124)	
			874		1,061
Change in provision for claims — gross amount	6		(2)		(12)
			872		1,049
Changes in other technical provisions, net of reinsurance					
Long-term business provision — gross amount	15a	(782)		(6,086)	
Reinsurers' share	3,15c	(28)		3,607	
			(810)		(2,479)
Comprising – Continuing operations			*(810)*		*(539)*
– Discontinued operations	*15d*		*-*		*(1,940)*
Technical provisions for linked liabilities — gross amount	15b	(529)		(526)	
Reinsurers' share	3,15c	526		516	
			(3)		(10)
Comprising – Continuing operations			*(3)*		*(10)*
– Discontinued operations	*15d*		*-*		*-*
Net operating expenses — non-exceptional	7a	40		45	
Net operating expenses — exceptional	7b	54		98	
Net operating expenses			94		143
Investment expenses including interest	4b		94		21
Other technical charges	5b		4		1,757
Unrealised losses on investments	4c		191		445
Taxation attributable to the long-term business	9a		(1)		2
Transfer to the Fund for Future Appropriations	14		-		1
			382		2,369
Total technical charges			**441**		**929**
Balance on the Technical Account			-		-

The results for 2008 are not consolidated as explained in Note 1a. The 2007 comparatives are Group results as previously published, but the results of the Society and Group for 2007 were materially the same. All significant recognised gains and losses are dealt with in the Profit and Loss Account. The Notes on pages 32 to 61 form an integral part of these financial statements.

Balance Sheet

As at 31 December 2008

Assets

	Notes	Society 2008 £m	2007 £m
Investments			
Land and buildings	10a	442	625
Investments in Group undertakings	10b	30	16
Shares and other variable yield securities and units in unit trusts	10c	430	466
Debt and other fixed-income securities	10c	5,203	5,661
Deposits and other investments	10c	264	337
		6,369	**7,105**
Assets held to cover linked liabilities	11	**74**	**76**
Reinsurers' share of technical provisions			
Long-term business provision	15c	343	315
Technical provisions for linked liabilities	15c	1,770	2,477
		2,113	**2,792**
Debtors	12		
Debtors arising out of direct insurance operations		5	5
Debtors arising out of reinsurance operations		2	-
Other debtors		30	36
		37	**41**
Other assets			
Cash at bank and in hand		**6**	**14**
Prepayments and accrued income			
Accrued interest and rent		113	111
Other prepayments and accrued income	13	42	70
		155	**181**
Total assets		**8,754**	**10,209**

The Notes on pages 32 to 61 form an integral part of these financial statements.

Balance Sheet

As at 31 December 2008

Liabilities

	Notes	Society 2008 £m	Society 2007 £m
Technical provisions	15a & 15g		
Long-term business technical provision - gross amount		6,692	7,474
Claims outstanding		1	3
		6,693	7,477
Linked liabilities	15b	1,844	2,553
		8,537	**10,030**
Provision for other risks and charges	18	**46**	**53**
Creditors			
Creditors arising out of direct insurance operations		40	43
Creditors arising out of reinsurance operations		-	1
Amounts owed to credit institutions	19a	12	16
Other creditors including taxation and social security	19b	102	41
		154	**101**
Accruals and deferred income		**17**	**25**
Total liabilities		**8,754**	**10,209**

These financial statements were approved by the Board on 26 March 2009 and were signed on its behalf by:

Vanni Treves
Chairman

Charles Thomson
Chief Executive

The Notes on pages 32 to 61 form an integral part of these financial statements.

Notes on the financial statements

1. Accounting policies

a. Basis of presentation

The financial statements have been prepared in accordance with sections 255 and 229(2) and (3) of, and Schedule 9A to, the Companies Act 1985 and in accordance with applicable accounting standards and the Association of British Insurers' Statement of Recommended Practice ("SORP") on Accounting for Insurance Business dated December 2005 and revised in December 2006, which, inter alia, incorporates the requirements of 'FRS 27 Life Assurance'. The true and fair override provisions of the Companies Act 1985 have been invoked.

The Directors have considered the appropriateness of the going concern basis used in the preparation of these financial statements, having regard to the ability of the Society to be able to meet its liabilities as and when they fall due, and the adequacy of available assets to meet liabilities. In the opinion of the Directors, the going concern basis adopted in the preparation of these financial statements continues to be appropriate. A more detailed explanation is provided in the Financial review on page 10.

Where relevant, Profit and Loss Account line items are analysed separately between continuing and discontinued operations. An explanation of the discontinued operations is provided in Note 5.

Certain administrative expenses were incurred in respect of customer support services provided by HBOS. For the purposes of these accounts, references to HBOS relate to various HBOS group companies.

University Life Assurance Society ("ULAS") was sold to Reliance Mutual Insurance Society Ltd. on 31 May 2007 and so its results to that date are consolidated in the 2007 Group Profit and Loss Account.

Equitable Life Finance plc ("ELF") passed a resolution for voluntary winding up on 30 October 2007 following the redemption of the Bonds in August. The results to the date of liquidation are consolidated in the 2007 Group Profit and Loss Account. The dissolution was completed on 7 January 2009.

The sale and liquidation of these two subsidiary companies has resulted in the aggregate size of the remaining subsidiary companies becoming immaterial from the point of providing true and fair view of the affairs of the Group. Therefore, these accounts represent the results and position of the Society only. The 2007 Profit and Loss account has not been restated as the results of the Society and Group were materially the same.

b. Change in accounting policies

The Directors have reviewed the accounting policies and satisfied themselves as to their appropriateness. There are no changes in accounting policy from the prior year.

c. Accounting for Part VII Transfers

During 2007 the Society completed two transfers of business under Part VII of the Financial Services and Markets Act 2000. The Part VII transactions involved transferring technical provisions and corresponding net assets to the counterparty. The value of assets transferred is reported in 'Other technical charges' in the Profit and Loss Account. The transfer of technical provisions is reported in 'Changes in other technical provisions'.

The transfer of with-profit annuities to The Prudential Assurance Company Ltd. ("Prudential") involved assets and liabilities of £1.75bn transferring on 31 December 2007, and a further £11m in June 2008, of which £8m had been accrued at 31 December 2007.

The transfer of non-profit annuities to Canada Life Ltd. ("Canada Life") involved an initial reassurance phase. Assets valued at £4.6bn were transferred to Canada Life to settle the initial premium. The assets were deposited back with the Society until the Part VII Transfer on 9 February 2007 when £4.23bn of assets and £4.13bn of liabilities were transferred to Canada Life. The technical provisions were fully reassured at the transfer, and the net assets were £nil.

d. Contract classification

The Group has classified its Long Term Assurance business in accordance with 'FRS 26 Financial Instruments: Recognition and Measurement'. Insurance contracts are contracts that transfer significant insurance risk such as non unit-linked non-profit contracts. Investment contracts are those contracts where no significant insurance risk is transferred. Investment contracts that contain a discretionary participation feature entitling the policyholder to receive additional bonuses or benefits, such as with-profit contracts, are classified as investment contracts with discretionary participation feature. Those investment contracts that do not have this feature are classified as investment contracts without discretionary participation feature.

Hybrid policies that include both discretionary participation features and unit-linked components have been unbundled and the two components have been accounted for separately.

Reassurance contracts have been classified in the same manner as direct contracts, with those reinsurance contracts which do not transfer significant insurance risk classified as financial assets.

A major treaty with HBOS reinsures unit-linked and non-profit business. Some of the reinsured policies are classified as insurance and others as investment. Rather than classifying the reinsurance treaty as a whole, the underlying policies have been considered and classified.

e. Insurance contracts and investment contracts with discretionary participation feature

Earned premiums

Premiums earned are accounted for on a cash basis, in respect of single premium business and recurrent single premium pension business, and on an accruals basis in respect of all other business.

All pension policies contain an open market option under which, in lieu of the benefits that must be taken on retirement, the equivalent lump sum can be transferred to another provider. All such lump sums, arising from policies within the Society, are included in claims paid. Where such lump sums are used to purchase annuities from the Society, these are included in premium income.

Claims

Death claims are recorded on the basis of notifications received. Surrenders are recorded when notified; maturities and annuity payments are recorded when due. Claims on participating business include bonuses payable and interest. Claims payable include direct costs of settlement.

Reassurance contracts

Outward reassurance premiums are recognised when payable. Reassurance recoveries are credited to match the relevant gross claims.

Liabilities

Liabilities for insurance contracts and investment contracts with discretionary participation feature are measured on an amortised cost basis as described in section m. on page 35.

f. Investment contracts without discretionary participation feature

Contracts classified as investment without discretionary participation feature are classified as financial instruments under FRS 26 and have been accounted for using the principles of deposit accounting. Deposits are no longer accounted through the Profit and Loss Account, but accounted for directly in the Balance Sheet as an adjustment to technical provisions. Fees receivable from investment contracts without discretionary participation features are reported in 'Other technical income'.

Withdrawals notified have been accounted for directly in the Balance Sheet as an adjustment to technical provisions and not through the Profit and Loss Account as claims.

Liabilities for contracts classified as investment without discretionary participation feature are measured on an amortised cost basis. The amortised cost of these financial liabilities is equivalent to the amount payable on demand without penalty.

g. Investment return

Investment return comprises all investment income, realised gains and losses, movements in unrealised gains and losses, net of investment expenses, including interest payable on financial liabilities.

All income from listed stocks and shares is included in the accounts when the security becomes ex-dividend. Other investment income, including interest income from fixed-interest investments and rent, is accrued up to the balance sheet date.

Property rental income arising under operating leases is recognised in equal instalments over the period of the lease.

Realised gains and losses on investments are calculated as the difference between net sales proceeds and the original cost.

Unrealised gains and losses on investments represent the difference between the valuation of investments at the balance sheet date and their purchase price or, if they have been previously valued, their valuation at the last balance sheet date. The movement in unrealised gains and losses recognised in the year also includes the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

h. Bonuses

The Society declares bonuses annually. Guaranteed bonuses are included in the long-term business provision. Non-guaranteed final bonuses are payable when a claim is made and an estimate of these non-guaranteed benefits, including any future discretionary increases to policy values, is included in the long-term business provision. Non-guaranteed final bonuses, payable when a claim is made, are included in claims paid.

i. Valuation of investments

All financial assets are initially recognised at cost, being the fair value at the date of acquisition. Subsequently all financial assets are valued at fair value through the Profit and Loss Account. Fair value is determined on either bid market prices for listed investments, if readily available, broker or dealer quotations, or market values of another instrument that is substantially the same. If prices are not readily available, the fair value is based on appropriate valuation techniques, supported by observable market data, where available.

A financial asset is recognised when the Society commits to purchase the asset, and is derecognised when the contractual right to receive cash flows expires or when the asset is transferred.

Financial assets at fair value through the Profit and Loss Account have two sub categories: financial assets held for trading; and those designated at fair value through the Profit and Loss Account at inception. Derivative instruments have been classified as held for trading. All other financial assets have been classified as fair value through profit and loss category. No material financial assets have been classified as held to maturity or as available for sale under FRS 26 classification.

The Society's derivatives are primarily concentrated in interest rate swaptions and FTSE 100 Futures. Hedge accounting has not been used for these Instruments. Collateral received to back derivative positions is recognised on the Balance Sheet as cash, with a corresponding liability in ‘Other creditors’.

Securities lent, where substantially all the risks and rewards of ownership remain with the Society, are retained on the Balance Sheet at their current value. Collateral received in respect of securities lent is not recorded on the Balance Sheet.

j. Property

Freehold and leasehold properties are valued individually by the qualified surveyors Jones Lang LaSalle on the basis of open market value, less the estimated costs of disposal.

No depreciation is provided in respect of investment properties. The Directors consider that this accounting policy is appropriate for the financial statements to give a true and fair view as required by 'SSAP 19 Accounting for Investment Properties'. Depreciation is only one of the factors reflected in the annual valuations and the amount which might otherwise have been shown cannot be separately identified or quantified.

k. Impairment policy

The Society reviews the carrying value of its assets (other than those held at fair value through profit and loss) at each balance sheet date. If the carrying value of a financial asset is impaired, the carrying value is reduced through a charge to the income statement. Impairment is only recognised if the loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

l. Technical provisions - long-term business provision and provision for linked liabilities

The long-term business provision is determined for the Society, following an investigation of the long-term funds, and is calculated in accordance with the rules contained in The FSA Handbook of Rules and Guidance. The investigation is carried out as at 31 December. For the with-profits business of the Society, the liabilities to policyholders are determined in accordance with the FSA realistic capital regime and in accordance with the requirements of FRS 27. These liabilities include an estimate of non-guaranteed benefits, including future discretionary increases to policy values, and provision for any guaranteed values which are in excess of policy values. Also included in the liability is an amount representing the excess of assets over other realistic liabilities. This amount is referred to as Excess Realistic Assets ("ERA") in these financial statements and is a key measure of the Society's resources, representing the amount 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.

The calculation of the long-term business provision for all non-profit business is calculated using the gross premium valuation method.

The technical provision in respect of index-linked annuities in payment is equal to the discounted value of the annuity benefits which allows for indexation.

The provisions in respect of with-profits investment contracts are not at fair value as there is no active market for such instruments and the basis to measure future supplementary discretionary returns is unreliable.

The Society's investment contracts without discretionary participation feature consist almost entirely of unit-linked contracts. The liability in respect of unit-linked contracts is equal to the value of assets to which the contracts are linked, and is included in 'Technical provisions' in the Balance Sheet.

m. Other financial liabilities

Borrowings are initially recognised at fair value and subsequently stated at amortised cost, using the effective interest method where appropriate.

n. Taxation

The charge for taxation in the Profit and Loss Account is based on the method of assessing taxation for long-term funds. Provision has been made for deferred tax assets and liabilities using the liability method, on all material timing differences, including revaluation gains and losses on investments recognised in the Profit and Loss Account. Deferred tax is calculated at the rates at which it is expected that the tax will arise and has not been discounted.

o. Foreign currency translation

Assets and liabilities in foreign currencies are expressed in Pounds Sterling at the exchange rates ruling at the balance sheet date. Revenue transactions have been translated at rates of exchange ruling at the time of the transactions.

p. Segmental reporting

In the opinion of the Directors, the Society operates in one business segment, being that of long-term insurance business.

2. Earned premiums

	Society 2008 Premiums £m	Group 2007 Premiums £m
a. Analyses of gross premiums written are as follows:		
Individual premiums	99	121
Premiums under group contracts	4	3
	103	**124**
Regular premiums	49	55
Single premiums	54	69
	103	**124**
Premiums from non-profit contracts	49	55
Premiums from with-profits contracts	46	58
Premiums from linked contracts	8	11
	103	**124**
Premiums from life business	27	34
Premiums from annuity business	1	2
Premiums from pension business	75	88
	103	**124**
Premiums from UK business	100	121
Premiums from overseas business	3	3
	103	**124**
b. Gross new business premiums		
Individual premiums	54	69
Premiums under group contracts	1	1
	55	**70**
Regular premiums	1	1
Single premiums	54	69
	55	**70**
Premiums from non-profit contracts	23	27
Premiums from with-profits contracts	26	35
Premiums from linked contracts	6	8
	55	**70**
Premiums from life business	-	-
Premiums from annuity business	-	1
Premiums from pension business	55	69
	55	**70**
Premiums from UK business	55	70
Premiums from overseas business	-	-
	55	**70**

Annual equivalent premiums in respect of new business received during the year were £6m (2007: £8m). New premiums in respect of reassured business during the year were £6m (2007: £8m).

Following the adoption of FRS 26, deposits received in respect of investment contracts without discretionary participation feature are not included in the Technical Account or in the tables opposite. Total deposits received in 2008 were £34m (2007: £45m) and new premium deposits were £6m (2007: £11m).

Classification of new business

The Society closed to new business on 8 December 2000. However, the Society continues to recognise new business premiums and deposits in the following instances:

- Recurrent single premiums are classified as regular where they are deemed likely to renew at or above the amount of initial premium or deposit. Incremental increases on existing policies are classified as new business premiums;

- Department for Work and Pensions rebates are classified as new single premiums;

- Unless classified as investment without discretionary participation feature, funds at retirement under individual pension contracts reinvested with the Society and transfers from group to individual contracts are classified as new business single premiums and, for accounting purposes, are included in both claims incurred and as single premiums within gross premiums written. Such amounts constitute the majority of premiums from non-profit contracts. Where an amount of fund under a managed pension is applied to secure an immediate annuity, that amount is included in both claims incurred and as a single premium within gross premiums written;

- Increments under existing group pension schemes are classified as new business premiums; and

- Where regular premiums are received other than annually, the regular new business premiums are stated on an annualised basis.

3. Outward reinsurance premiums

On 1 March 2001, the Society entered into reinsurance contracts with HBOS in respect of certain of its unit-linked and non-profit business. The establishment of the reinsurance contracts effectively transferred the risks and rewards in respect of the reinsured business to HBOS.

Premiums and deposits received from policyholders in respect of reinsured business are immediately forwarded to HBOS. HBOS reimburse the Society for any claims and withdrawals the Society has paid to policyholders in respect of reinsured business. As a result of these processes, after allowing for special features of the reinsurance contracts, the impact to the Society of these contracts is minimal.

Under the terms of the reinsurance contracts with HBOS, if the Society were to become insolvent, or reasonably likely to become insolvent in the opinion of the reinsurer's board, HBOS can then make payments directly to policyholders whose policies have been reassured.

The Society has several other outward reinsurance contracts under which relatively small volumes of business are reinsured.

The reinsurance balance, as required to be disclosed by the Companies Act 1985, and as defined by the Statement of Recommended Practice ("SORP"), which represents the aggregate total of all those items included in the Technical Account which relate to reassurance transactions, net of related losses of £286m (2007: gains of £195m), is a net debit of £2m (2007: £2m debit).

4. Total investment return

	Society 2008 £m	Group 2007 £m
a. Investment income comprises income from:		
Land and buildings	32	32
Other investments	338	498
	370	530
Net gains on realisation of investments	-	260
Investment income and net realised gains at fair value through the Profit and Loss Account	**370**	**790**
b. Investment expenses including interest comprise:		
Investment management expenses	9	12
Interest charges on loans	-	9
Net losses on realisation of investments	85	-
	94	**21**
c. Investment activity account		
Investment income	370	530
Realised investment gains/(losses)	(85)	260
Unrealised investment losses	(191)	(445)
Total fair value investment income and net gains at fair value through the Profit and Loss Account	94	345
Investment management expenses and charges	(9)	(21)
Investment return for the year	**85**	**324**

Included within the tables above is £10m (2007: £5m) of net gain in respect of derivative instruments designated as held for trading, and £48m (2007: £16m) of unrealised gain resulting from the retranslation of balances in connection with overseas business.

Interest charges on loans in 2007 was primarily interest payable on subordinated loan stock issued by Equitable Life Finance plc and redeemed in 2007.

There have been no material gains or losses arising on the disposal of subsidiary companies.

d. Interest income and expense not included in the investment return

Contracts classified as investment with discretionary participation feature are measured at amortised cost. The interest income and expense in respect of such contracts is included within the Technical Account under the heading 'Change in long-term business provision'.

5. Other technical income and charges

	Society 2008 £m	Group 2007 £m
a. Other technical income comprises:		
Income from non-insurance business	-	2
Investment return on secured assets deposited with the Society by Canada Life	-	35
Other income	4	4
	4	**41**
b. Other technical charges comprise:		
Transfer of assets to Prudential	3	1,754
Expenses of non life subsidiary companies	-	3
Other charges	1	-
	4	**1,757**

On 15 March 2007, the Society entered into an agreement with Prudential for the transfer of its with-profits annuity policies. Following the completion of the High Court process, this business was subsequently transferred to Prudential on 31 December 2007 as a Part VII Transfer under the Financial Services and Markets Act 2000. The final value of assets to be transferred was £1.76bn. The value of assets transferred and accrued is reported in the Profit and Loss Account, in table b. above and the assets are described in Note 10d.

On 11 May 2006, the Society entered into an agreement where a substantial proportion of the Society's non-profit pension annuity business was reassured with Canada Life. Following the completion of the High Court process, this business was subsequently transferred to Canada Life on 9 February 2007 as a Part VII Transfer under the Financial Services and Markets Act 2000. Until that date, this business was subject to a reassurance arrangement, under which Canada Life bore substantially all the risks and rewards from this business with effect from 1 January 2006. The initial premium of £4,608m for the reassurance of this business was included in 'Outward reinsurance premiums – discontinued operations' in 2006.

As part of the reassurance between the Society and Canada Life, the initial premium was deposited back with the Society. There existed a charge over investments of the Society equal to the value of the deposit. The investment returns from those secured assets were attributed to Canada Life and payments of related annuities deducted from the deposited assets.

In 2007, the secured assets earned a negative return in the period and the attribution to Canada Life is reported as 'Other technical income'.

Following Court approval of the Part VII Scheme of Arrangement, the charged assets were transferred to Canada Life. This resulted in a £nil charge to the Profit and Loss Account as the value of charged assets was equal to the value of deposits received from Canada Life as at the date of the transfer. The reassurance agreement was unwound when the business was transferred. Limited liability warranties were established as is normal for these forms of transactions.

6. Claims incurred – gross

	Society 2008 Claims £m	Group 2007 Claims £m
Claims paid – gross amount	940	1,185
Change in provision for claims – gross amount	(2)	(12)
Gross claims	**938**	**1,173**

Gross claims incurred comprise gross claims paid and the change in provision for claims outstanding.

	Society 2008 Claims £m	Group 2007 Claims £m
Gross claims paid comprise:		
On death	40	38
On maturity	504	519
On surrender	294	310
By way of periodic payments	99	304
Claims handling expenses	1	2
	938	**1,173**
Life and annuity business	146	175
Pension business	791	996
Claims handling expenses	1	2
	938	**1,173**
Linked business	48	66
Non-profit business	64	110
With-profits business	825	995
Claims handling expenses	1	2
	938	**1,173**
UK business	914	1,143
Overseas business	23	28
Claims handling expenses	1	2
	938	**1,173**

Included in the above payments are attributable final and interim bonuses for the Society and in 2007 for ULAS of £49m (2007: £50m).

Following the adoption of FRS 26, withdrawals made in respect of investment contracts without discretionary participation feature are not included in the Technical Account or in the tables above. Total withdrawals in 2008 were £214m (2007: £292m).

Gross claims incurred in 2008 relating to discontinued operations were £nil. Gross claims incurred for 2007 relating to discontinued operations were £42m for operations transferred to Canada Life on 9 February 2007, and £178m for operations transferred to Prudential on 31 December 2007, as described in Note 5.

7. Net operating expenses

	Society 2008 £m	Group 2007 £m
a. Non-exceptional		
Administrative expenses	**40**	**45**

b. Exceptional

The Society incurred the following exceptional expenses during the year:

	Society 2008 £m	Group 2007 £m
Rectification and other GAR-related expenses	1	1
Pension costs for former staff	22	44
Costs of strategic initiatives	27	51
Other projects	4	2
	54	**98**

As explained in the Financial review on page 8, exceptional expenses reduced in the year and included the cost of the search for a possible buyer for the Society and a review of pension commitments.

c. Services from auditors

PricewaterhouseCoopers LLP ("PwC") is one of a number of professional firms that undertake advisory work for the Society. Where PwC has been engaged to perform such non-audit work, in circumstances where it is to the Society's advantage that it does so, the Society's regular commitments procedures are followed and the Audit Committee reviews them to ensure that auditor independence is preserved.

During the year, the Society received the following services from the Society's auditor as detailed below:

	Society 2008 £m	Group 2007 £m
Fees payable for the audit of the Society accounts	0.6	0.7
Fees payable to the Society's auditor and its associates for other services:		
Other services pursuant to legislation	0.1	0.1
Tax services	-	0.1
All other services	0.4	0.6
	1.1	**1.5**

8. Directors and employees

	Society 2008 £m	Group 2007 £m
a. Staff costs		
Wages and salaries	4	5
Social security costs	1	1
	5	**6**

The monthly average number of employees employed by the Society during the year, including Executive Directors, required to be disclosed in accordance with the Companies Act 1985, was 25 (2007: 26). In addition, the Society employs a number of contractors and, under its agreement with HBOS, uses the services of HBOS staff.

b. Emoluments of Directors

Full details of Directors' emoluments, pensions and interests, as required by the Companies Act 1985, are included in the Remuneration report on pages 22 to 24.

c. Former staff pension arrangements

As a result of contractual commitments arising as part of the agreement entered into with HBOS in March 2001, when the Society sold its administrative and sales operations, the Society meets the major part of the funding in respect of the pension schemes for those staff that transferred to the employment of HBOS as a result of the sale transaction. An amount of £63m (2007: £59m) is provided in respect of the contractual commitment to HBOS in relation to the defined benefit scheme, following the triennial actuarial valuation performed as at 31 December 2007, as modified for relevant changes to the balance sheet date. An additional provision of £45m (2007: £46m), representing an estimate of the current value of the contractual commitment to HBOS in respect of future service costs over the next eight years (2007: nine years), and a provision for pension augmentations of £2m (2007: £2m) are included within 'Technical provisions: long-term business'.

9. Taxation

	Society 2008 £m	Group 2007 £m
a. Taxation charged to the Technical Account		
UK corporation tax		
Current tax on income for the period	4	9
Adjustments in respect of previous years	(2)	(6)
	2	3
Foreign tax		
Current tax on income for the period	-	-
Deferred tax		
Unrealised gains on investments	(3)	(1)
Total charge	**(1)**	**2**

The UK corporation tax charge is provided at 20% (2007: 20%), computed in accordance with the rules applicable to life assurance companies, whereby no tax is charged on pension business profits.

	Society 2008 £m	Group 2007 £m
b. Deferred taxation		
Provided in the financial statements:		
Deferred tax of the long-term fund		
Unrealised depreciation/(appreciation) in investments	**1**	**(2)**

Deferred taxation not provided for in the accounts relates to immaterial unrealised losses on the reassured book.

10. Non-linked investments

	Current value 2008 £m	Current value 2007 £m	Cost 2008 £m	Cost 2007 £m
a. Land and buildings				
Society				
Leasehold	118	177	129	129
Freehold	324	448	396	396
	442	**625**	**525**	**525**

The Society invests indirectly in property through specialised unit trusts, which are classified as 'Other financial investments' (see Note 10c). Total property-related investments at 31 December 2008 are £528m (2007: £766m).

	Current value 2008 £m	Current value 2007 £m	Cost 2008 £m	Cost 2007 £m
b. Investments in Group undertakings				
Shares	**30**	**16**	**23**	**18**

The Society has a wholly-owned subsidiary Basinghall Street Real Estate Inc. ("BSRE"). BSRE is an American incorporated property vehicle with a value as at 31 December 2008 of £6m (2007: £4m). BSRE's principal investment is cash and its loss for 2008 was £0.9m ($1.4m) (2007: £1.4m ($2.8m)).

The Society holds a majority investment in Equitable Private Equity Holdings Limited ("EPEHL") a Guernsey registered company with a value as at 31 December 2008 of £24m (2007: £12m). EPEHL's investment is Knightsbridge Integrated Holdings V.L.P. which invests in equity and venture capital projects. EPEHL made a loss in 2008 of £34k ($62k) (2007: £30k ($61k)) and its total capital value is £24m ($33m) (2007: £16m ($31m)).

	Current value 2008 £m	Current value 2007 £m	Cost 2008 £m	Cost 2007 £m
c. Other financial investments held at fair value through the Profit and Loss Account				
Society				
Shares and other variable yield securities and units in unit trusts				
Shares and units in unit trusts (1)	342	432	432	459
Other variable income securities (2)	88	34	29	29
	430	**466**	**461**	**488**
Debt securities and other fixed-income securities (3)	**5,203**	**5,661**	**5,260**	**5,703**
Deposits and other investments				
Loans secured by mortgages and policies	1	2	1	2
Deposits with credit institutions	263	335	263	334
	264	**337**	**264**	**336**
	5,897	**6,464**	**5,985**	**6,527**

Notes:
(1) Includes listed investments of £138m (2007: £199m) for the Society at fair value.
(2) Comprise derivatives including FTSE 100 Futures and interest rate swaptions. The interest rate swaption is valued on a mark-to-model basis. Both categories are classified as held for trading.
(3) Includes listed investments of £5,199m (2007: £5,198m) for the Society at fair value.

Investments of £649m (2007: £2,134m), which were lent in the normal course of business to authorised money brokers on a secured basis, are included in 'Other financial investments'. Cash and similar investments of £661m (2007: £2,154m) were received as collateral from brokers. Income earned on stock lending during the year, net of fees paid, was £2m (2007: £2m).

The Society closely monitors the valuation of assets in markets that have become less liquid. Determining whether a market is active requires the exercise of judgement and is determined based upon the facts and circumstances of the market for the instrument being measured. Where it is determined that there is no active market, fair value is established using a valuation technique as described in the Accounting Policies Note 1i above. The techniques applied incorporate relevant observable market information available.

For corporate bonds for which there is no active market, the fair value is based on broker/dealer price quotations. Where possible the Society seeks at least two quotations for each bond and considers whether these are representative of fair value. Where this information is not available the fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

	Assets transferred to Prudential on		Assets transferred to Canada Life on
	25 June 2008 £m	31 December 2007 £m	9 February 2007 £m
d. Assets transferred under Part VII Transfer in 2007			
Society			
Leasehold property		65	-
Freehold property		7	-
		72	**nil**
Shares and other variable yield securities and units in unit trusts		133	
Debt and other fixed-income securities	11	1,371	4,122
Deposits with credit institutions		150	43
Accrued interest		20	69
Accrued transfer of assets	(8)	8	nil
Total transferred and accrued	**3**	**1,754**	**4,234**

The total value of assets transferred to Prudential is reported in the Profit and Loss Account within 'Other technical charges' and in Note 5.

The total value of assets transferred to Canada Life was equal to the value of secured deposits received from Canada Life at the date of the transfer, and so net to nil within 'Other technical charges' and in Note 5.

11. Assets held to cover linked liabilities

	Society	
	2008 £m	2007 £m
Current value of linked assets held at fair value through the Profit and Loss Account	**74**	**76**

The cost of assets held to cover linked liabilities is £63m (2007: £56m) for the Society.

12. Debtors

	Society 2008 £m	2007 £m
Debtors arising out of direct insurance		
Amounts owed by policyholders	5	5
Debtors arising out of reinsurance insurance	2	-
Other debtors		
Debtors other than Group and related companies	30	36
	37	**41**

The carrying values of these items equate closely to fair values and are expected to be realised within a year of the balance sheet date.

Amounts in Debtors other than Group and related companies include an entitlement for the return of the variation margin associated with the FTSE futures investment from Goldman Sachs (2008: £17.5m, 2007: £2m), an assigned account owned by HSBC (2008: £7m, 2007: £17m), and policy related balances owed by Prudential in respect of the transfer as outlined in Note 5 (2008: £nil, 2007: £15m).

13. Other prepayments and accrued income

	Society 2008 £m	2007 £m
Prepayments	**42**	**70**

The prepayments include an interest-bearing advance payment made to a service provider.

14. Fund for Future Appropriations (FFA)

	Society 2008 £m	Group 2007 £m
At 1 January	-	10
Transfer from the Profit and Loss Account	-	1
University Life Assurance Society sold from Group	-	(11)
At 31 December	-	-

ULAS was sold to Reliance Mutual Insurance Society Ltd. during 2007, as described in Note 1.

15. Technical provisions

a. Gross long-term business technical provisions

	Society			
	2008		2007	
With-profits technical provisions	£m		£m	
With-profits insurance technical provisions				
Policy values	405		486	
Future charges	(35)		(35)	
Impact of early surrenders	(1)		(1)	
Cost of guarantees	77		65	
Other long-term liabilities	74		99	
		520		**614**
With-profits investment technical provisions				
Policy values	4,147		4,897	
Future charges	(265)		(171)	
Impact of early surrenders	(33)		(30)	
Cost of guarantees	737		377	
Other long-term liabilities	213		285	
		4,799		**5,358**
Excess Realistic Assets		**414**		**621**
		5,733		**6,593**
Non-profit technical provisions				
Non-profit insurance technical provisions	954		876	
Non-profit investment technical provisions	5		5	
		959		**881**
Total long-term business technical provisions		**6,692**		**7,474**

b. Gross linked liabilities

	Society			
	2008		2007	
	£m		£m	
Index-linked annuities	78		80	
Other linked insurance liabilities	140		225	
Other linked investment liabilities	1,626		2,248	
Total linked liabilities		**1,844**		**2,553**

c. Reinsurers' share of technical provisions: insurance and investment contracts

	Society			
	2008		2007	
	£m		£m	
Non-profit insurance technical provisions	338		310	
Non-profit investment technical provisions	5		5	
		343		**315**
With-profits insurance technical provisions	-		-	
With-profits investment technical provisions	-		-	
Index-linked annuities	4		4	
Other linked insurance liabilities	140		225	
Other linked investment liabilities	1,626		2,248	
		1,770		**2,477**
Total reinsurers' share		**2,113**		**2,792**

d. Discontinued operations

The Part VII Transfer of policies to Canada Life on 9 February 2007 and to Prudential on 31 December 2007 described in Note 5, resulted in the following movements to long-term business technical provisions:

	Society 2008 £m	Society 2007 £m
Gross provisions – transfer to Canada Life	-	(4,133)
Gross provisions – change during 2007 re Prudential	-	(186)
Gross provisions – transfer to Prudential	-	(1,754)
Gross provisions – all discontinued operations	**-**	**(6,073)**
Reinsurer's share of provisions – transfer to Canada Life	**-**	**4,133**
Net provisions – all discontinued operations	**-**	**(1,940)**

e. Movement of gross technical provisions investment contracts without discretionary participation feature

	Society	
	2008	2007
	£m	£m
At 1 January	2,253	2,370
Change arising from new deposits	34	45
Change arising from withdrawals	(214)	(292)
Other changes	(442)	130
At 31 December	**1,631**	**2,253**

f. The long-term business provision – non-profit and index-linked annuities

The long-term business provisions for the Society's non-profit and index-linked annuities have been calculated using the gross premium method. The principal assumptions and their comparatives are shown in the table below. Actuarial bases have been modified in respect of valuation interest rates, mortality assumptions and future expense allowances. Explanations of the effect of those changes are set out in notes (1) and (2) below.

The principal assumptions used in valuing the non-profit and index-linked annuities in payment were as follows:

Class of business	Interest rate % 2008	Interest rate % 2007	Future expense allowance 2008	Future expense allowance 2007
Non-profit annuities in payment				
Basic Life and General Annuity business – pre 1992	4.63	4.80	£20 p.a.	£24 p.a.
Basic Life and General Annuity business – post 1991	4.17	4.32	£20 p.a.	£24 p.a.
Pension business	4.63	4.80	£20 p.a.	£24 p.a.
Index-linked annuities in payment				
Basic Life and General Annuity business – pre 1992	1.79	1.38	£20 p.a.	£24 p.a.
Basic Life and General Annuity business – post 1991	1.61	1.24	£20 p.a.	£24 p.a.
Pension business	1.79	1.38	£20 p.a.	£24 p.a.

Notes:

(1) Valuation interest rates are based on the yields on the assets held, reduced for risk. Reductions from the yield for risk for corporate fixed-interest securities are based on credit ratings. Fixed-interest yields have fallen and index-linked yields have risen compared to those at the end of 2007. The changes to the valuation interest rates in aggregate have decreased the index-linked annuity provision by £3m and increased the non-profit technical provisions by £10m. Similarly, the market value of the backing assets has changed as yields have changed and this in part offsets the change in technical provisions. The change in asset values and technical provisions are not equal at this valuation due to the increased allowance for the risk of bond defaults allowed for in the valuation interest rates. Future expenses in respect of non-profit and index-linked annuities in payment are allowed for in two ways - an explicit per policy allowance, increasing by 3.15% p.a. (2007: 3.0% p.a.) and an expense allowance for fund management, expressed as a percentage of the value of the fund, of 0.06% p.a. (2007: 0.06% p.a.). The amount allowed for expenses has been assumed to increase by an additional 5.75% p.a. (2007: 4.6% p.a.) to allow for diseconomies of scale as the size of the business declines. The amount included for each successive year allows for the effect of inflation throughout the expected future lifetime of the policies.

(2) The Society continues to make allowance for future improvements in longevity of annuitants. The Society's valuation has been carried out using recently published mortality tables and an investigation into the Society's actual mortality experience. The overall effect of this review has been to decrease index-linked annuity and non-profit annuity technical provisions by £4m (2007: increased by £4m).

A sensitivity analysis, carried out in connection with the effect of a change in mortality basis on the technical provisions, has demonstrated that an assumed 10% improvement in the mortality rates would result in a £24m (2007: £22m) increase in the non-profit and index-linked annuity technical provisions. This change is equivalent to the life expectancy of a 65-year-old male increasing by an additional 12 months (2007: 12 months).

Mortality assumptions by class of business	2008	2007
Non-profit and index-linked annuities in payment		
Basic Life and General Annuity business	82.5% IML00 ult (U=2008)* for males 82.5% IFL00 ult (U=2008) * for females	70.0% IML00 ult (U=2007)* for males 75.0% IFL00 ult (U=2007) * for females
Pension business (both reassured and retained business)	90.0% PNMA00MC (U=2011) ** for males 97.5% PNFA00MC (U=2011) ** for females	90.0% PNMA00MC (U=2010) ** for males 97.5% PNFA00MC (U=2010) ** for females

Notes:
* The allowance for future mortality improvements is based on implied mortality improvements as per IML92/IFL92 (subject to a minimum improvement of 1.5% p.a.).
** The allowance for future mortality improvements is based on the implied future improvements as per PMA/PFA92 MC tables (subject to a minimum improvement of 1.5% p.a.).

g. The long-term business provision – with-profits business

The long-term business provisions for the Society's with-profits business have been calculated in accordance with the FSA realistic capital regime. The principal assumptions used to calculate these provisions and the comparatives are described below.

The calculation of realistic liabilities for the Society is based upon the projection of 5,000 different scenarios and includes an estimate of any future non-guaranteed bonuses that may be payable. The value of the liabilities is made up of the following components:

- Policy values – the total of policy values for all with-profits policies (or their equivalents for with-profits annuities and conventional with-profits contracts);
- Future charges – the margin assumed to be retained each year before making future increases to policy values;
- Impact of early surrenders – the value of the financial adjustment assumed to be deducted on non-contractual surrenders;
- Cost of guarantees – the cost of meeting contractual guarantees in excess of the policy values; and
- Other long-term liabilities include miscellaneous provisions (as described in Note 15h), with-profits reassured business, less a deduction for the present value of future profits from non-profit business as described below.

The present value of future profits from non-profit business represents the future profits expected from cash flows of the in-force non-profit and index-linked annuity business, less an amount to meet the cost of holding capital in respect of this business. These profits have been deducted as a capitalised amount from the technical provisions in accordance with the requirements of FRS 27. The resulting anticipated present value of future profits is a loss of £26m (2007: £17m).

(i.) Options and guarantees

Options and guarantees are features of life assurance contracts that confer potentially valuable benefits to policyholders. They expose the Society to two types of risk: insurance (such as mortality and morbidity) and financial (such as market prices and interest rates). The value of an option or guarantee comprises two elements: the intrinsic value and the time value. The intrinsic value is the amount that would be payable if the option or guarantee was exercised immediately. The time value is the additional value that reflects the possibility of the intrinsic value increasing in future, before the expiry of the option or guarantee. In adopting FRS 27, the intrinsic and time values of all options and guarantees are included in policyholder liabilities.

The Society now has in issue two principal types of with-profits policy: Recurrent Single Premium ("RSP") policies and Conventional With-Profits ("CWP") policies. These policies represented 97% and 3%, respectively, of the total policy values at 31 December 2008 (97% and 3% of the total policy values at 31 December 2007). For the majority of RSP policies issued before 1 July 1996, each premium (after charges) secures a Guaranteed Investment Return ("GIR"), typically at the rate of 3.5% p.a. For the majority of RSP policies issued after 1 July 1996, the GIR is nil%. For CWP policies, guarantees are payable at specified dates or on the occurrence of specified events.

The options and guarantees in respect of the Society's with-profits business relate to a guarantee on contractual termination (for example, on retirement, maturity, death or on payment of an annuity). The terms of the guarantee vary by contract. For the Society's RSP contracts where there is a GIR, the value of that guaranteed return is assessed based on assumed retirement ages of policyholders. Certain policies also contain a guaranteed minimum level of pension as part of the condition of the original transfer of state benefits to the policy.

For CWP business, there is a guarantee that the amount payable on death or at maturity (where appropriate) will not be less than the sum assured and any declared reversionary bonuses.

All the Society's material options and guarantees are valued on a market-consistent stochastic basis. The valuation involves constructing 5,000 scenarios, aggregating the results under each scenario and then calculating the average liability.

For policies where the guaranteed value at contractual termination exceeds the policy value at that date, the excess would be paid and estimates of such excess form part of the realistic liabilities. In calculating the amount payable to policyholders, account is taken of any management actions such as making changes to policy values in response to changes in market conditions. The cost of these guarantees has increased from £442m in 2007 to £814m at 31 December 2008 principally as a result of falling Government bond yields and the decreases made in policy values for 2008. This amount is included within 'Technical provisions' (see Note 15a).

There is inherent uncertainty in calculating the cost of these guarantees and options, as the value depends on future economic conditions, policyholder actions (such as early or late retirement and surrenders) and mortality. In calculating the value of the guarantees, account has been taken of actual experience to date, in addition to industry benchmarks and trends. For economic assumptions, prices for relevant quoted and non-quoted derivatives are used to confirm market consistency.

(ii.) Assumptions — with-profits business

Mortality

Using the results of an investigation into the Society's actual mortality experience, mortality assumptions have been derived for the with-profits business as detailed in the table below:

Mortality assumptions by class of business	2008	2007
Endowment assurances (with-profits)		
Basic Life and General Annuity business	90.0% AMC00 ultimate for males 97.5% AFC00 ultimate for females	90.0% AMC00 ultimate for males 97.5% AFC00 ultimate for females
Pension business	90.0% AMC00 ultimate for males 97.5% AFC00 ultimate for females	90.0% AMC00 ultimate for males 97.5% AFC00 ultimate for females

Mortality assumptions for other classes of business are not material and, for this reason, are not shown above.

Future charges

A charge of 1.0% p.a. (2007: 0.5% p.a.) is assumed to be retained before making future increases to policy values. This charge provides capital to meet the expected cost of guarantees (the additional cost where a policy's guaranteed benefits exceed its policy value, now or expected in the future).

Expenses

A further charge of 1.0% p.a.(2007: 1.0% p.a.), is assumed to be deducted each year before making future increases to policy values. In addition, an expense provision of £147m for expenses (2007: £142m) has been incorporated with the aim of maintaining a stable expense charge as the business declines. Taken together, these allowances are intended to provide for future expenses in respect of with-profits business. A 10% increase in future expenses would decrease the ERA by £43m (2007: £50m).

Retirement and surrender assumptions

For the majority of RSP contracts, benefits can be taken on contractual terms at a range of ages. For example, benefits from Retirement Annuity policies can be taken at any age between 60 and 75, whereas benefits from Group Pension policies are expected to be taken at the scheme's normal retirement age. This date is referred to as the Earliest Contractual Date ("ECD"). A proportion of policyholders take their benefits before the earliest expected retirement date.

An investigation of the actual retirement ages for the Society's with-profits policyholders, analysed by type of contract, has been carried out based on actual experience during 2007 and 2008. The results of that investigation have been used to set the assumed retirement ages for the valuation.

The retirement assumptions vary between different product types. The range of retirement dates assumed varies between policyholders being assumed to retire 2 years (2007: 2 years) earlier than ECD and up to 13 years (2007: 13 years) later than ECD.

A sensitivity analysis has been carried out to illustrate the potential impact on ERA, at 31 December 2008, of GIR on RSP business under certain scenarios modelled on a stochastic basis, where the results are aggregated and the average liability is calculated. If interest rates fall below a given level, it is possible that policyholders with policies that have a guaranteed return (usually 3.5% p.a.) and variable retirement dates may choose to defer retirement. If policyholders wait until interest rates fall below 2.5% and defer their retirement by up to five years (from that previously assumed), while the interest rate in the scenario is below 2.5%, ERA would reduce by £95m (2007: £40m). If the level of interest rates at which behaviour changes is 3.5% and the same period of deferment is assumed, the reduction is £135m (2007: £70m). If the deferral were for a period of up to 10 years, the reduction is £135m (2007: £65m) at 2.5% and £205m (2007: £115m) at 3.5% respectively.

The Society holds a series of receiver swaptions with a range of terms. The purpose of these swaptions is to provide additional capital when interest rates on similar fixed-interest securities fall. These swaptions are designed to partially mitigate any increase in liabilities for RSP policies with a non-zero GIR, if policyholders defer their retirement plans. A fall in interest rates of 1.0% at all terms would increase the value of the swaptions by £67m (2007: £44m) and a similar increase would decrease the value by £37m (2007: £19m).

An investigation of the actual surrender rates for the Society's with-profits business, analysed by type of contract, has been carried out based on actual experience during 2007 and 2008. The results of that investigation have been used to set the assumed surrender rates for the valuation.

Non-contractual surrender rates are assumed to fall steadily over the next few years to a long-term rate of 1.5% p.a. (2007: 1.5% p.a.) The effect of the change in the surrender rates has been to increase the ERA by £23m (2007: increase by £10m).

A financial adjustment of 5.0% (2007: 5.0%) of policy values is assumed as a deduction on surrender prior to contractual termination.

Economic assumptions

In order to produce many projections of different scenarios of the business, an economic model is required. The economic model used by the Society in the valuation was supplied by Barrie & Hibbert. The model has been calibrated to the gilt yield curve at the valuation date and this determines the risk-free rates used in the projections. The effect of the change in yield curve from 2007 to 2008 was to increase the ERA by £48m (2007: reduce by £2m). Assumptions are also required for the volatility of the asset values for different asset categories. Bond volatilities vary by term and duration and are calibrated to those implied by swap option volatilities obtained from Bloomberg. For equity values, the model produces a 10 year volatility of 34% (2007: 26%). For property values, the model uses an assumed volatility of 15% (2007: 15%).

h. The long-term business provision – miscellaneous provisions

Technical provisions include amounts in respect of specific provisions:

- Anticipated additional exceptional expenses of £70m (2007: £82m) over future years, including contractual commitments to HBOS in respect of pension scheme future service costs and anticipated additional costs associated with servicing policies in the medium term; and

- An amount of £34m (2007: £136m) for other miscellaneous liabilities including, inter alia, potential mis-selling liabilities. The principal components are provisions for potential mis-selling claims such as managed pensions, a provision for other legal claims against the Society, and provisions relating to residual reassurance balances in respect of the linked and part of the non-profit book and other items.

i. Technical provision for other linked liabilities (excluding index-linked annuities)

The technical provision in respect of other linked business (excluding index-linked annuities) is equal to the value of the assets to which the contracts are linked. This business is wholly reassured to HBOS (see Note 3).

A provision in respect of future expenses and mortality risks on other linked insurance business is included in the long-term business provision. The future expenses on other linked business are wholly reassured.

16. Capital statement

a. Analysis of capital

The capital statement in respect of the Society's life assurance business at 31 December 2008 is set out below. These figures are calculated in accordance with the regulations set out in The FSA Handbook of Rules and Guidance.

	2008 Society £m	2007 Society £m
Available capital resources		
Adjustments onto a regulatory basis – valuation differences (1)	451	742
Adjustments onto a regulatory basis – inadmissible assets	(2)	(2)
Total available capital resources	**449**	**740**
Long-term Insurance Capital Requirement (LTICR)	(251)	(273)
With-profits Insurance Capital Component (WPICC)	(198)	(467)
Total regulatory Capital Resource Requirements (CRR)	**(449)**	**(740)**
Excess of available capital resources over CRR	-	-

Note:
(1) Valuation differences represent any difference placed on the valuation of liabilities in the financial statements compared with those reported in the regulatory return to the FSA.

b. Available capital resources

The total available capital resources show the capital, calculated in accordance with regulations set out in The FSA Handbook of Rules and Guidance, that is available to meet the capital requirements of the business. The available capital resources for the Society amount to £449m (31 December 2007: £740m).

The table below shows the effect of movements in the total amount of available capital of the Society during the year:

Available capital resources	2008 £m	2007 £m
At 1 January	740	1,183
Investment return and interest rate movements	(321)	147
Mortality assumption change	4	(2)
Transfer of with-profits annuities to Prudential	(3)	(372)
Repayment of Subordinated Debt	-	(167)
Other movements	29	(49)
At 31 December	**449**	**740**

c. Restrictions on available capital resources

It is the Society's aim to manage its business in a sound and prudent manner for the benefit of all policyholders. The Society closed to new business in 2000 and new policies are only issued where there is a regulatory or contractual obligation to do so. The Society has no shareholders and all surpluses and deficits belong to the with-profits policyholders. The Society seeks to ensure that it can meet its contractual obligations to both policyholders and creditors as they fall due. Any new distributions of surplus will be made in non-guaranteed form.

The Society had guaranteed £171m (par value) of 8% Undated Subordinated Bonds which were issued by ELF (a subsidiary company). These were redeemed at par on 6 August 2007.

d. Capital requirements

Each life assurance company must retain sufficient capital to meet the capital requirements specified by the FSA. The minimum level of capital required is represented by the CRR.

For the Society, the CRR comprises the Long Term Insurance Capital Requirement ("LTICR") and any additional capital requirement over LTICR, which results from consideration of realistic liabilities. This additional amount of capital required is referred to as the With-Profits Insurance Capital Component ("WPICC").

In order to derive the value of the WPICC, it is necessary to compare the excess available capital resources over LTICR with the amount of the FFA (representing the balance of realistic capital), after deduction of a risk capital margin as required by FSA regulations (Adjusted FFA). A value for the WPICC is required where the excess capital resources, as so calculated, are greater than the Adjusted FFA and comprises that difference. Where the excess capital resources, as so calculated, are less than the Adjusted FFA, there is a nil value for the WPICC.

Actuarial guidance for closed with-profits funds issued in 2006 following the introduction by the FSA in 2004 of new rules for the determination of capital requirement, results in a requirement to anticipate the distribution of all assets to policyholders. For this reason, the realistic capital for the Society is a nil balance in 2008 and is lower than the excess capital resources over LTICR and, as a result, a WPICC applies.

e. Sensitivity to market conditions of liabilities and components of capital

The with-profits realistic liabilities are sensitive to both market conditions and changes to a number of non-economic assumptions that affect the valuation of the liabilities of the fund. The available capital resources (and capital requirements) are most sensitive to the level of fixed-interest yields and the values of equities and property, with the reduction in capital resources being more pronounced at lower levels of yields, as a result of the guarantees to policyholders increasing in value. Reductions in the value of property and equities directly reduce the available capital resources. The Board may take actions, such as changes to policy values, to mitigate reductions in capital resulting from an adverse change in market conditions.

The principal non-economic assumptions are the level of future mortality rates, level of future expenses, changes in future retirement ages and future surrender rates.

17. Management of financial risk

a. Risk management framework

As described in the Corporate governance section, the Society has established a comprehensive risk management framework. Through this framework, the Society seeks to manage and monitor the various risks to which the Society is exposed. These include other risks such as operational risk and insurance risk.

Also included within this process are the various financial risks, namely:

- Market risk: covering interest rate risk, equity and property price risk, derivative risk and currency risk;
- Credit risk; and
- Liquidity risk.

These risks are discussed in more detail below, and form part of the FRS 29 disclosures.

The Society uses a number of tools to manage the above risks. In addition to the regulatory testing described in Notes 15 and 16, the Society prepares an Individual Capital Assessment ("ICA") report in accordance with FSA requirements on an annual basis where a number of scenarios are tested to assess the potential effect on capital. Other tools more specific to managing an individual risk are included below.

b. Market risk

The Society holds a portfolio of investments which are subject to movements in market price. Market risk is the risk of adverse financial changes in fair values or future cash flows of financial instruments from fluctuations in interest rates, equity and property prices, and foreign currency exchange rates. The main responsibility for monitoring this risk lies with the Investment Committee of the Society. The majority of these assets are held to support contractual liabilities arising from both with-profits and non-profit classes of business.

For these long-term business classes, the Society's asset liability management framework aims to hold assets whose values will, as far as possible, move in line with the corresponding guaranteed liabilities to limit the overall impact of market risk on capital.

In line with the Society's with-profits investment policy, investments are mainly in fixed–interest securities, gilts (39%: 2008, 46%: 2007) and corporate bonds (39%: 2008, 30%: 2007).

With regard to unit–linked business, liabilities are reinsured with HBOS and no market risk is considered to arise on this class of business.

As an overall indication of the sensitivity of the Society to changes in market price, consideration is given to the impact on the ERA as a consequence of a number of adverse changes simultaneously occurring. These changes are detailed in the table below and include: reductions in the market price of key asset categories; adverse changes on the yields of corporate bond relative to government backed fixed-interest securities; and adverse changes in the assumed level of future policy surrenders. These adverse changes are consistent with the requirements for the Society's regulatory risk capital margin tests. The adverse changes used are detailed in the following table:

Adverse Changes	2008	2007
Reduction in market price of equities	20.0%	20.0%
Reduction in market price of properties	12.5%	12.5%
Percentage change in long-term gilt yields	17.5%	17.5%
Widening of spread of corporate bonds relative to gilts	0.8%	0.7%
Reduction in surrender rates	32.5%	32.5%

In such adverse investment conditions, the Society could make appropriate reductions to with-profits policy values. These reductions would mitigate market risk, but do not remove the risk entirely for with-profits policies because of the guarantees provided. After adjusting for the reductions, the adverse impact on the ERA of the Society would be as follows:

Adverse Changes	2008 £m	2007 £m
Above adverse changes – including where long-term gilt yields rise	306	191
Above adverse changes – including where long-term gilt yields fall	232	164

In the scenario where long-term gilt yields are assumed to fall, the figures above exclude the gain in the value of the Society's swaptions. However, where long-term gilt yields are assumed to rise the corresponding loss has been included. In both scenarios, any potential impact in policy liabilities as a result of changes to flexible retirement dates assumptions has been excluded.

(i.) Interest rate risk

Interest rate risk is the risk that the value or future cash flows of a financial instrument will fluctuate because of changes in interest rates.

The Society's exposure to changes in interest rates is concentrated in the investment portfolio. However, changes in investment values attributable to interest rate changes are mitigated by corresponding and partially offsetting changes in the economic value of the insurance provisions, and investment contracts liabilities. A potential market risk for the Society is in respect of GIR on with-profits policies, which are typically 3.5% p.a. When the market returns are below this rate, the cost of providing these guarantees is correspondingly higher. To mitigate this risk the Society holds a series of interest rate swaptions.

The Society monitors this exposure to changes in interest rates through regular periodic reviews of the asset and liability position. Estimates of cash flows, as well as the impact of interest rate fluctuations relating to the investment portfolio and insurance provisions, are modelled and reviewed periodically.

The Society is also exposed to the risk of changes in future cash flows from variable income securities arising from the changes in interest rates.

The Society's sensitivity to interest rate risk is included in the overall market risk sensitivity included in the stress scenario table above, excluding the impact of the Society's swaptions.

(ii.) Equity and property price risk

The Society invests in equity and property assets, whose market values are typically more volatile than other classes of asset held by the Society, but which we believe provide long-term benefits for the Society's members. To mitigate the risk of changes in the market price of these asset classes, the Society limits the proportion of the total assets invested in these categories. In addition, as indicated in section (i.) above, further mitigation takes place by partially offsetting changes in the liabilities of the Society.

The Society's sensitivity to equity and property price risk is included in the overall sensitivity to market risk described above.

(iii.) Derivative risk

The Society invests in derivatives within strict guidelines agreed by the Board of Directors and overseen by the Investment Committee. Derivatives are used for efficient investment management, particularly FTSE 100 Futures to increase exposure to the equity markets as part of a strategy to increase the Society's equity backing ratio. Interest rate swaption derivatives are also used to mitigate interest rate risk. Derivative transactions are fully covered by cash or corresponding assets and liabilities. Derivative contracts are entered into only with approved counterparties, thereby reducing the risk of credit loss.

(iv.) Currency risk

The Society's principal transactions are carried out in Pounds Sterling and its exposure to the risk of movements in foreign exchange rates is limited. The risk arises primarily with respect to the US Dollar.

The Society's financial assets are primarily denominated in the same currencies as its insurance and investment liabilities, which mitigate the foreign currency exchange rate risk for any overseas operations.

Therefore the main foreign exchange risk arises from recognised assets and liabilities denominated in currencies other than those in which insurance and investment liabilities are expected to be settled.

The relative exposure of the Society to currency risk is shown in the table below.

	2008				2007			
	Assets		Liabilities		Assets		Liabilities	
	£m	%	£m	%	£m	%	£m	%
Currency								
Sterling	8,331	95	8,134	98	9,861	97	9,407	98
Euro	258	3	200	2	222	2	174	2
US Dollar	163	2	6		120	1	7	
Other	2				6			
Total	**8,754**	**100**	**8,340**	**100**	**10,209**	**100**	**9,588**	**100**

The excess of the total value of assets over the total value of liabilities represents the Society's ERA. A change of 10% in Pounds Sterling to Euro/US Dollar exchange rates at the reporting date would have changed the ERA by £22m (2007: £16m).

c. Credit risk

Credit risk is the risk that a counterparty will fail to pay amounts in full when due. The main credit risks faced by the Society are:

- The risk of default on its portfolio of fixed-interest securities, especially corporate bonds;

- The risk of default by any of its reinsurers.

These risks are monitored by the Society's Investment Committee. A key aspect of this is the Society's policy of investing predominantly in high-quality corporate bonds and government issued debts.

The Society's objective is to earn competitive relative returns by investing in a diversified portfolio of securities. The Society manages this risk by up-front stringent underwriting analysis, reviews by the Investment Committee and regular meetings to review credit developments. Watch lists are maintained for exposures requiring additional review and all credit exposures are reviewed at least annually.

With regard to reinsurance, wherever possible, steps are taken to limit counterparty risk. The major reinsurance treaties are with companies in the HBOS Group. Because reinsurance does not remove the primary liability of the Society to its policyholders, the credit rating of these companies is monitored closely.

The Society's exposure to credit risk is summarised below according to the lowest of the external credit ratings supplied by Moody, Standard & Poor, and Fitch:

2008

Credit ratings	AAA £m	AA £m	A £m	BBB £m	Other £m	Total £m
Debt and other fixed-income securities	3,228	442	1,123	354	27	5,174
Other variable yield securities	84	1	18			103
Total of fixed and variable yield securities	**3,312**	**443**	**1,141**	**354**	**27**	**5,277**
Deposits with credit institutions	-	-	192	-	72	264
Cash at bank and in hand	-	-	6	-	-	6
Other financial assets	55	10	74	9	44	192
Reinsurers' share of technical provisions and liabilities (Note 15c)	-	2,113	-	-	-	2,113
	3,367	**2,566**	**1,413**	**363**	**143**	**7,852**

2007

Credit ratings	AAA £m	AA £m	A £m	BBB £m	Other £m	Total £m
Debt and other fixed-income securities	4,184	377	954	88	37	5,640
Other variable yield securities	81		16			97
Total of fixed and variable yield securities	**4,265**	**377**	**970**	**88**	**37**	**5,737**
Deposits with credit institutions	-	-	337	-	-	337
Cash at bank and in hand	-	-	14	-	-	14
Other financial assets	73	6	19	3	121	222
Reinsurers' share of technical provisions and liabilities (Note 15c)	-	2,792	-	-	-	2,792
	4,338	**3,175**	**1,340**	**91**	**158**	**9,102**

The total of fixed and variable yield securities includes assets held to back linked liabilities. Other financial assets comprise debtors and prepayments and accrued income.

When calculating technical provisions in respect of non-profit business, when deriving the discount rate to be used, reductions based on credit risk are made to the published yields of invested assets exposed to credit risk. This reduction to the discount rate results in an increase to the assessed technical provision, thereby providing an implicit margin against the risk of default by the counterparties.

The potential credit risk exposure from default by swaption counterparties is mitigated by the receiving of collateral. Collateral of £70.2m (2007: £14.8m) has been received in cash and has been invested in assets similar in nature to cash. The value of these assets at the year end was £70.4m and is included in 'Deposits with credit institutions' in Note 10c.

The largest single credit risk exposure amounts to £2,115m for HBOS reinsurance (2007: £2,972m for HBOS reinsurance). The Society holds a further £60m of investments (credit ratings of A: £19m and AA: £41m) with the Lloyds Banking Group, of which HBOS became part in January 2009.

At the reporting date, no material financial assets were past due nor impaired (2007: £nil) and management expects no significant losses from non-performance by these counterparties.

d. Liquidity risk

An important aspect of the Society's management of assets and liabilities is ensuring that cash is available to settle liabilities as they fall due. Monitoring of this risk is undertaken by the Investment Committee. The Society maintains cash and liquid deposits to meet these demands on a daily basis, thereby mitigating liquidity risk. The ratio of illiquid assets to total invested assets is monitored monthly.

Over the longer term, the Society monitors its forecast liquidity position by estimating both the guaranteed and expected cash outflows from its insurance and investment contracts and purchasing assets with similar durations to meet these obligations. The sensitivity of these outflows to changes in policyholder behaviour is also monitored.

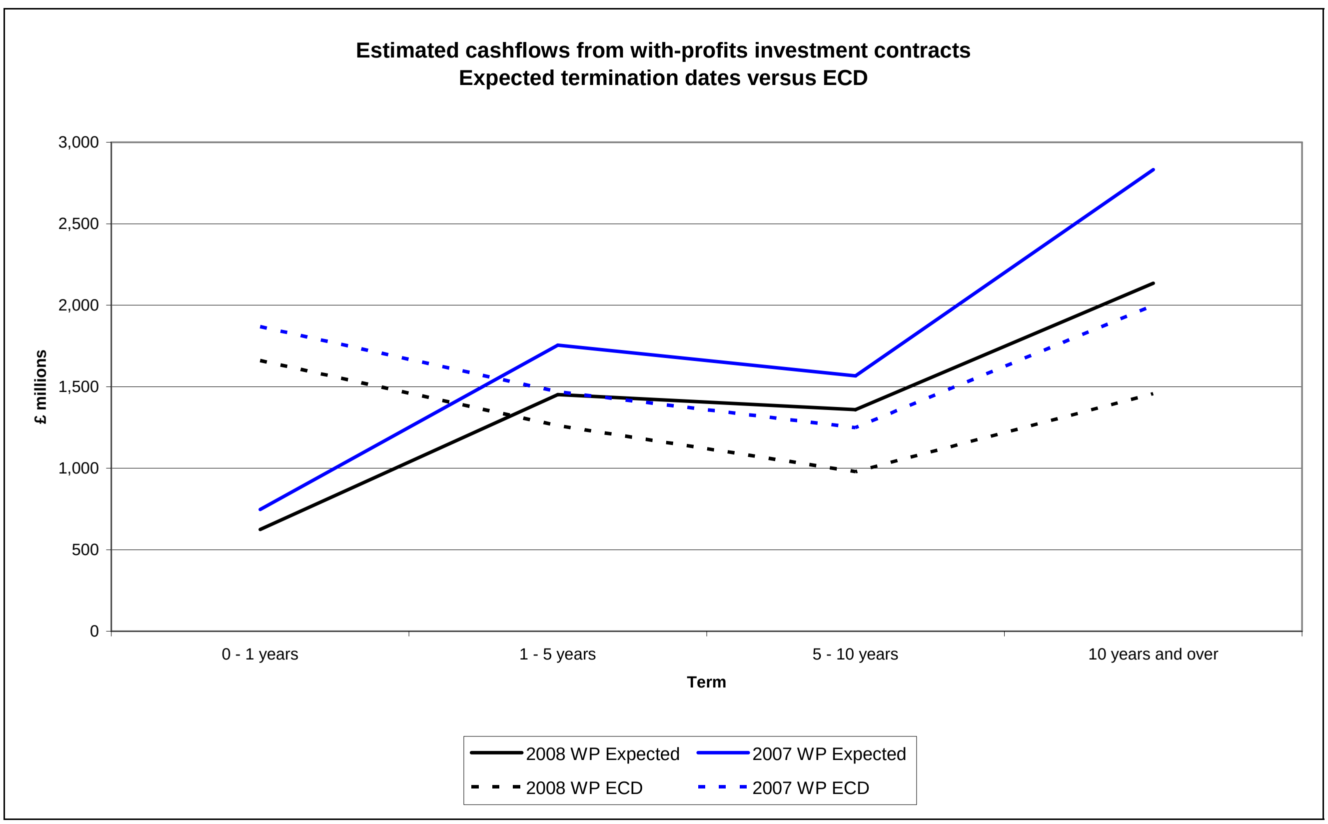
The Society's liquidity exposure is relatively limited even in an extreme scenario such as all corporate bonds becoming illiquid, over 45% of investment assets held backing insurance and investment liabilities are held in liquid assets such as gilts and cash, which can normally be quickly realised. Also, in times of market uncertainty and potentially poorer liquidity, market value adjustments may be borne by those with-profits insurance and investment contract customers who decide to transfer or withdraw their benefits.

As noted in Note 15g (ii.), the majority of RSP benefits can be taken on contractual terms at a range of ages. The table below details the cash flows using retirement assumptions based on recent experience, that vary between different product types. The range of retirement dates assumed varies between policyholders being assumed to retire 2 years (2006: 2 years) earlier than ECD and up to 13 years (2006: 13 years) later than ECD.

2008 Estimated cash flows (undiscounted)	0-1 year £m	1-5 years £m	5-10 years £m	10 years and over £m	Total £m	Carrying value £m
Unit-linked investment contracts	145	613	541	1,028	2,327	1,626
Other non-profit investment contracts	5	-	-	-	5	5
With-profits investment contracts	622	1,452	1,359	2,135	5,568	4,799
Other financial liabilities	154	-	-	-	154	154
	926	**2,065**	**1,900**	**3,163**	**8,054**	**6,584**

2007 Estimated cash flows (undiscounted)	0-1 year £m	1-5 years £m	5-10 years £m	10 years and over £m	Total £m	Carrying value £m
Unit-linked investment contracts	180	836	764	1,625	3,405	2,248
Other non-profit investment contracts	5	-	-	-	5	5
With-profits investment contracts	747	1,755	1,567	2,832	6,901	5,358
Other financial liabilities	101	-	-	-	101	101
	1,033	**2,591**	**2,331**	**4,457**	**10,412**	**7,712**

The cash flows assuming policies are terminated on ECD would vary from those detailed above as policies past the ECD would result in a cash flow in the category '0-1 year' and policies yet to reach ECD would be earlier than shown. The graph below indicates how the estimated cash flows for with-profits investment contracts above (solid graph lines) would vary from those at ECD (broken graph lines).



With-profits policies with an ECD prior to 31 December 2008 have a contractual value no lower than total guaranteed benefits, and equalled £1.3bn at 31 December 2008 (2007: £1.4bn).

Unit-linked contracts, with the exception of unit-linked annuities, can be terminated at any time resulting in a cash flow in the category '0-1 year'. All liabilities relating to unit-linked and other non-profit investment contracts are reassured so that, in practice, the Group is not exposed to any liquidity risk in respect of such contracts.

Part of the Society's assets is invested in property (including property unit trusts) and unlisted equity, amounting to £735m at year end 2008 (2007: £1,430m). In adverse market conditions, it may not be possible to realise these investments without delay.

18. Provision for other risks and charges

	Society	
	2008	2007
	£m	£m
Provisions for deferred taxation	-	2
Pension commitments for former staff	46	51
	46	**53**

The movement in the provisions for deferred taxation assets and liabilities is included in Note 9b.

The provision for pension commitments for former staff of £46.2m is in addition to a creditor to HBOS for payments during 2009 totalling £16.8m (2007: £7.8m). Pension payments for former staff relate to the contractual agreement with HBOS (described in Note 8c) under which £17.7m (2007: £18.7m) was paid during the year. The balance of the movements is due to changes in economic assumptions.

19. Creditors

	Society	
	2008	2007
	£m	£m
a. Amounts owed to credit institutions	**12**	**16**

Amounts owed to credit institutions represent uncleared payments to policyholders. An amount of £7m (2007: £17m) placed in an assigned account owned by HSBC is included in 'Debtors' in Note 12.

	Society	
	2008	2007
	£m	£m
b. Other creditors including taxation and social security		
Balances with Group companies	9	-
Corporation tax	3	5
Other creditors	90	36
	102	**41**

Amounts in Other creditors include an obligation to return to the variation margin associated with the swaption investment to Morgan Stanley (2008: £70.2m, 2007: £14.7m) and the contractual commitment to HBOS in relation to the defined benefit pension scheme (2008: £16.8m, 2007: £7.8m).

20. Subsidiary and associated undertakings

a. Principal subsidiary undertakings

The Society has no material subsidiary undertakings as outlined in Notes 1 and 10.

b. Significant holdings

At 31 December 2008, the Society held more than 20% of the nominal value of a class of equity shares in 11 companies with a value of £18m (2007: 11 companies, value £20m).

At 31 December 2008, the Society held more than 20% of the partnership interests in 1 limited partnership investing in properties with a value of £18m (2007: 1, value £29m).

At 31 December 2008, the Society held more than 20% of the partnership interest in 6 portfolios investing in private equity investment companies included in shares and other variable yield securities, with a value of £7m (2007: 10, value £7m).

None of the above holdings are regarded by the Directors as associated undertakings as the Society does not exert significant influence. None of the holdings materially affects the results or net assets of the Society. These investments are included in the Balance Sheet at current value, which is based upon the Society's share of relevant net assets.

Full information on subsidiary undertakings and companies and limited partnerships, in which the Society hold more than 20% of the nominal value of a class of equity share or ownership interests, will be annexed to the Society's next statutory annual return submitted to the Registrar of Companies.

21. Related party transactions

There were no material related party transactions during 2008 (2007: £nil).

22. Commitments

The Society has no material operating lease commitments.

There are no property investment commitments provided for in the financial statements (2007: £nil) for the Society.

Commitments in respect of uncalled capital on private equity fund interests, not provided for in the financial statements, amounted to £23.9m (2007: £21.9m) for the Society.

In line with usual business practice, warranties have been provided for the strategic transactions completed in the year.

23. Contingent liabilities and uncertainties

As noted in the Financial review on page 10 and in the following sections of this Note, there exist some uncertainties that, in the event they were to materialise, could adversely impact on the propriety of preparing these financial statements on an ongoing concern basis. Over the last few years these uncertainties have been resolved to a very significant extent and those that remain are referred to below. In the light of this, the Board has assessed the possibility of these uncertainties arising and their potential impact upon the financial situation of the Society and has concluded that, on the basis of current information and, having taken legal and actuarial advice, it is right to prepare these financial statements on a going concern basis.

- The Society has contractual commitments in respect of two pension schemes for which HBOS is the principal employer, as noted in Note 8c to the financial statements. Although full provision is made for estimated contractual liabilities calculated on a basis consistent with that adopted by the Scheme Actuary in his triennial valuations, there remains the possibility that it may be necessary for a more conservative basis to be adopted in future in calculating the Society's obligations.

- As noted in the Financial review on page 8, it is the Society's intention that any future bonuses will be in a non-guaranteed form. Allowance is made for continuing contractual commitments, such as the GIR of 3.5% p.a. that is applicable to many policies. In valuing policy liabilities, guarantees are valued under a range of economic scenarios. The calculation of the technical provisions is based on a projection of current market conditions, allowing for current retirement experience. There remains a risk to the Society that investment conditions change or that policyholders defer their retirement. To mitigate this risk the Society continues to invest in a series of interest rate swaptions.

- Following publication of the report of the Equitable Life inquiry by Lord Penrose in March 2004, the Parliamentary Ombudsman ("PO") announced in July 2004 her decision to open a new investigation. Her final report was laid before Parliament on 16 July 2008, and published on 17 July 2008. The report found ten determinations of maladministration on the part of the Department of Trade and Industry ("DTI"), Government Actuary's Department ("GAD"), and the Financial Services Authority ("FSA") in relation to their regulation of the Society in the period before 1 December 2001.

The Society has responded to the Government's proposed "ex gratia" payment scheme and generally in relation to the Government's response to the report and will continue to liaise with the Parliamentary Ombudsman's team, the Public Administration Select Committee, the Government and Sir John Chadwick as appropriate.

In view of the findings in the report and the Government's response, the Society has concluded that the likelihood of successful claims being brought against the Society is now extremely limited.

- Ninety-one claims have been issued against the Society in District courts across Germany. The Society is continuing to challenge these claims and a significant number of them have been determined in its favour. The Society has not lost a single case to date and in light of this the Society now believes the costs associated with this group of claims are unlikely to be significant.

The Society has made appropriate provisions for future expenses, alleged mis-selling and other risks based on currently available information. Over time, as more information becomes available, the range of possible outcomes in relation to these issues can be expected to continue to narrow, and the degree of confidence around the levels of the individual provisions can be expected to increase. The Society now considers that the potential impact of the uncertainties referred to on page 10 of the Financial review and in this note have diminished to a significant degree over the past few years. However, the potential impact of the range of uncertainties relating to provisions could be significant.

As discussed in the Financial review, even though subject to close management scrutiny, because of the volatility in investment and property markets, the uncertain nature of provisions and the other potential strains on the Society's finances, the Board recognises the possibility that the Society may not meet regulatory capital requirements at all times in the future. Any such failure does not, of itself, cause the Society to become insolvent.

The financial position of the Society has been projected under a range of economic scenarios. The Board has also considered the level of contingent liabilities in its analysis of the Society's financial position. 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.