

Equitable Life

Annual Report and Accounts 2005

The Equitable Life Assurance Society

Registered office

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

Policyholder administration

Walton Street
Aylesbury
Buckinghamshire
HP21 7QW

Board of Directors

Vanni Treves, Chairman

Peter Smith, Deputy Chairman

Charles Thomson, Chief Executive

David Adams OBE, Non-executive Director

Ron Bullen, Non-executive Director

Michael Pickard, Non-executive Director

Fred Shedden, Non-executive Director

Andrew Threadgold, Non-executive Director

Jean Wood, Non-executive Director

With-profits Actuary and Head of Actuarial Function

Tim Bateman

Legal Advisers

Lovells
Atlantic House
Holburn Viaduct
London
EC1A 2FG

Auditors

PricewaterhouseCoopers LLP
Southwark Towers
32 London Bridge Street
London
SE1 9SY

Corporate Review	2
Changes to Financial Reporting Regime	7
Financial Review	10
Board of Directors	16
Directors' Report	18
Corporate Governance	20
Directors' responsibilities in respect of the financial statements	27
Independent Auditors' Report to the members of The Equitable Life Assurance Society	28
Profit and Loss Account	29
Balance Sheets	30
Notes on the Financial Statements	32

Dear Members,

We are pleased to report another year of solid progress in bringing stability back to the Society. We remain confident that, with careful management, the Society can operate securely as a closed fund, paying policy benefits as they fall due.

This year's report shows:

- Our key measure of solvency, "Excess Realistic Assets", is £669 million (2004: £455 million), representing 6.6% of the with-profits fund (2004: 4.3%);
- With-profits pension policy values have been increased by up to 4.5% in respect of 2005;
- The major policyholder reviews are essentially complete, removing a major area of uncertainty;
- Surrenders have continued to fall and in 2005 totalled £482 million (2004: £835 million); and
- We have significantly strengthened our reserves.

New financial reporting rules, known as "realistic reporting", have been introduced in these accounts (see explanatory box). Under this new method, Excess Realistic Assets is the most important measure of the amount available to enhance bonuses in future

and to meet any unforeseen liabilities.

On this measure, our financial position has strengthened in the year by £214 million. As explained in more detail in the

Financial Review on pages 10 to 15, this result reflects good investment returns offset by a significant strengthening of reserves, particularly mortality reserves.

Realistic reporting

As we mentioned in last year's Report and Accounts, new accounting standards have changed the way the Society's financial position is reported. This new UK accounting standard, Financial Reporting Standard 27 "Life Assurance", is also known as the "realistic reporting basis". Full details are given on pages 7 to 9.

Realistic assets

Realistic assets are valued on a basis that reflects what they might be traded for in the market place.

Realistic liabilities

Realistic liabilities include an estimate of non-guaranteed benefits like final bonuses. For policies where the policy value at maturity is likely to exceed the guaranteed value, the

non-guaranteed payments would be paid at maturity and those amounts form part of the realistic liabilities.

In determining the underlying assumptions by which realistic liabilities are calculated, reference is made to detailed analyses of past experience, together with any factors which might affect the position in future.

Excess Realistic Assets

Our key measure of solvency on the new basis is the "Excess Realistic Assets". This is the amount available to meet any unforeseen liabilities and liabilities in excess of those already provided for at the balance sheet date and to enhance bonuses in the future. During 2005, the Excess Realistic Assets increased to £669 million from £455 million.

2005 Bonus declaration

Although the Society has had to adopt a cautious investment strategy, the with-profits fund achieved a gross return of 10.1%. After adjusting for gains in fixed interest securities, which are matched by similar increases in liabilities, and other deductions such as expenses, tax and changes to provisions and technical provisions, the net return was 5.6%. Details of the factors the Board considered in reaching its bonus decisions are given in the Financial Review.

The key highlights are:

- Policy values (or their equivalents) will be increased for UK with-profits pensions policies at a non-guaranteed accrual rate of 4.5% p.a. (2004: 3.5% p.a.) for the whole of 2005 (3.6% p.a. for UK life policies - 2004: 2.8% p.a.). This applies equally to policies with guaranteed investment returns (GIRs) and those without;
- A non-guaranteed interim bonus of 3.5% p.a. for UK with-profits pensions policies (2.8% p.a. for UK life policies) will continue to be added to policy values (or their equivalents); and
- Consistent with previous years, there is no reversionary bonus for 2005.

As we have previously stated, of the with-profits annuitants' share of the cost of Guaranteed Annuity Rates (GARs), 3% of policy value remains unrecovered. The majority of with-profits annuity policies have anticipated a higher level of bonus

than is achievable by a predominantly fixed interest fund in the current low inflation environment and, accordingly, income can be expected to fall year-on-year. In the light of this, the Board has decided that it will recover the with-profits annuitants' remaining share of the cost of GARs over a period of six years by withholding 0.5% p.a., commencing with the 2005 uplift in policy values.

Where a policy payment is due and the guaranteed benefit exceeds the policy value (or its equivalent), it is the guaranteed benefit which will be paid. For this reason, increases in policy values (or their equivalents) described above will not affect the benefit payable under a policy unless the policy value exceeds the guaranteed benefit at the due date.

As announced at the interim stage, and after consideration of the Society's improved financial circumstances, it was decided to reduce the financial adjustment applied to the surrender proceeds of with-profits policies from 11.1% to 8% with effect from 1 October 2005. This adjustment can be varied at any time.

Policyholder reviews

All of the major reviews have now been completed with only a few cases still considering offers. These reviews dealt with past retirements of policies which had GARs, other GAR-related complaints, and the suitability of Managed Pensions (income drawdown) policies.

The uncertain outcome of these reviews has been a considerable concern for several years. The level of provisioning is now substantially lower following settlements reached and the scale of the uncertainty is no longer disproportionate to the size of the Society's available funds.

Parliamentary Ombudsman and European Parliamentary Inquiry

In 2004, the Society called on the Parliamentary Ombudsman (PO) to reopen her independent inquiry into the regulation of Equitable Life following strong criticisms of the regulators in Lord Penrose's report. We have had lengthy and confidential discussions with her inquiry team and continue to give all possible assistance. If the PO finds maladministration on the part of the regulators, she has the power to recommend government compensation. We look forward to publication of the report, which is currently expected to be towards the end of this year and which should, in any event, bring finality to this matter.

In January 2006, the European Parliament set up a Committee of Inquiry into the regulation of Equitable Life. In particular, it will consider alleged contraventions of Community law and allegations of maladministration in the application of Community law in respect of Equitable Life. The Committee has been asked to present its final report within 12 months, with an interim report within 4 months. We will give all possible

assistance to the Committee. The inquiry is not seeking to investigate the conduct of the Society's affairs but, rather, its regulation and the status of any claims by non-UK European citizens.

Litigation

As we explained in detailed letters to policyholders in September and December 2005, the Society settled its legal claims against the former auditors, Ernst & Young, and the former directors. After considering expert audit and actuarial guidance and legal advice, we believed that we had credible and cost effective claims against the defendants and a duty to pursue them in the interests of policyholders. However, litigation always carries risk and it was with sadness and frustration that we concluded that we could not realise any material compensation for policyholders.

Following the end of the litigation, the Serious Fraud Office (SFO) announced that it had found nothing to justify a full criminal investigation into the affairs of Equitable Life – both Lord Penrose and the Treasury had asked the SFO to consider certain issues in Lord Penrose's report. The SFO's conclusion may reassure some members who have made allegations of fraud from time to time. As we have previously stated, your Board has found no evidence that could lead to a sustainable case of fraud against the Society.

In 2004, a group of 873 with-profits annuitants commenced proceedings

against the Society. There are now 413 annuitants who are still part of this action, the others having dropped out. There will be a further pre-trial hearing in the summer and the trial itself will probably take place towards the end of 2007. We continue to resist this attempt by a small group of annuitants to obtain additional monies at the expense of all other with-profits policyholders.

New pensions legislation

On 6 April 2006, new rules in relation to pensions come into force. The new rules affect anyone who is making provision for their retirement. We have written to relevant policyholders setting out the major changes and the actions that they may wish to consider. Although the aim of the legislation is simplification, the need to change many aspects of how we operate pension policies required our undertaking a major project at substantial cost. All the changes necessary are in place to ensure a smooth transition to the new framework.

Summary financial statements

After consulting with policyholders, we have this year introduced summary financial statements for the first time. Many members have indicated that they would prefer a simpler presentation of the financial statements, which also achieves a considerable saving in printing and postage. The full Report and Accounts continues to be available on our website and on request.

Governance

On 13 July 2005, the annotated Combined Code for mutual life offices was published by the Association of Mutual Insurers. For a number of years the Society has followed strictly the Combined Code, applicable to public companies, or made relevant disclosures, so this new Code requires little more from us.

The Association of Mutual Insurers also published guidance for mutual insurers in December 2005. We are undertaking a review of that detailed guidance.

The Society has produced a guide to how we manage the with-profits fund. This is a simpler, easier to follow version of the Principles and Practices of Financial Management (PPFM) document which the Society has had in place since 2004. We will issue the guide to all with-profits policyholders with their annual statements this year (both documents are also available on our website). With their annual statements we will also send to with-profits policyholders reports by the Board and by the With-profits Actuary on compliance with the PPFM. (Again, both documents will be added to the Society's website as soon as they are completed.)

Policyholder suggestions

Following comments from a number of with-profits annuitants regarding late notification of the change in the amounts of their annuity payment each year, we are developing a new system which will

calculate the annual change to annuitants' income in advance of that change taking place. This will enable the statements to be issued about three weeks in advance of the first payment of the new amount. The new system will be operating from July. It is taking longer than we would have wished to develop because the system resources available to us have been heavily committed during 2005 to deliver necessary changes for the new pensions rules mentioned above.

We have also followed up a number of suggestions from policyholders regarding the general servicing helpline telephone number. The new and cheaper local rate number, which is 0845 603 6771, is now available and we are updating our literature to reflect the change as opportunities arise.

Strategic objectives

The Society's business objectives continue to be to:

- Resolve outstanding claims against the fund;
- Stabilise the with-profits fund to ensure its continued solvency and maintain an appropriate level of free assets;
- Treat policyholders fairly, including leavers, and ensure we meet the guarantees provided to policyholders by pursuing an appropriate investment strategy; and
- Reduce expenses and restore an efficient business model.

After five challenging years, the major reviews have been completed reducing valid outstanding claims against the fund to levels that are much more normal in relation to the scale of the business. The fund is also now more stable and secure, though some uncertainties remain. We continue to make progress in reducing operating expenses year-on-year. We are also exploring strategic options which might improve the longer term prospects for policyholders.

Your Board

As this report demonstrates, the Society has made huge progress since the current Board took over in 2001. We have overcome the fundamental instability resulting from the GAR issue and addressed a host of other problems from the past during a mainly hostile economic climate. Your Board felt that it was important to remain as a single team throughout these troublesome times. Of the nine current Directors, seven have served throughout the last five years.

With new stability for the Society, it is the appropriate time for the Board to start to evolve. Later this year, the intention is that two of our non-executive Directors will stand down. We will be using a search consultancy as before to interview candidates and make suitable recommendations. Anyone who believes that he or she can add substantial value to the Board is encouraged to put his or her name

forward for consideration in that process. Details can be obtained from the Company Secretary or from the Society's website.

Looking forward

Through these five years of tough decisions, policyholders have had to suffer a great deal of uncertainty and to face reduced prospects. Although we are not entirely out of the woods, we have achieved much greater clarity and certainty regarding the Society's current position and prospects and the outlook for a stable run-off of the Society is, at last, looking far more secure.

As we have explained before, our improving stability allows us to consider whether any strategic options could improve longer term prospects for policyholders. One particular area of risk (which is not unique to Equitable Life) is the potential cost of paying pensions to annuitants if they live longer than we currently expect. Like some other funds, we are exploring the possibility of transferring the bulk of our non-profit annuities to another provider in order to remove that risk. This step could make sense for Equitable Life provided that the financial terms are satisfactory.

Also, we recognise that even with our greater stability, a limited outlook is implied for policy returns because the fund remains primarily in fixed interest investments. We are, therefore, exploring options relating to our with-profits policies that could improve

longer term prospects for with-profits policyholders. Essentially, these could involve the sale or transfer of some or all of the business. In considering such approaches, our challenge is “Can this approach deliver improved benefits to our policyholders?”. It is by no means certain that any such discussions would lead to a positive answer to this fundamental question but, if they do, we will present that option to policyholders. It is, of course, policyholders who would ultimately decide whether to accept such a strategic change.

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

**Vanni Treves and Charles Thomson on behalf of
the Society’s Board of Directors.**



Vanni Treves
Chairman



Charles Thomson
Chief Executive

As noted in last year's Annual Report, the Society's financial statements have been revised to comply with a new UK accounting standard, Financial Reporting Standard 27 "Life Assurance". The standard introduces "realistic" reporting, which was required in the previous financial year for reporting to the Financial Services Authority (FSA) only, though the Society provided voluntary disclosures in the Financial Review section of its Annual Report for 2004.

The key elements and changes created by the new regime are summarised below with further details shown in the notes to the financial statements.

Previous reporting basis

In previous years, the Society has prepared its financial statements on the modified statutory solvency basis. This basis did not recognise certain matters, such as terminal bonuses. The Accounting Standards Board introduced the new accounting standard to address the perceived shortcomings of accounting for with-profits business, including the criticisms detailed in the Penrose Report, against a background of development by the FSA of the regulatory solvency regime.

Realistic reporting basis

The realistic reporting basis requires values to be attributed to assets and liabilities on a basis that reflects what they might be traded for in the market place.

The new basis requires accounting for liabilities (including options and guarantees) to be "realistic". Unlike previous statutory reporting, realistic liabilities incorporate an estimate of non-guaranteed benefits, including future discretionary increases to policy values, and provision for any shortfall in policy values relative to guaranteed values in adverse financial conditions.

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 were to be 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. For policies where the guaranteed value at maturity is likely to exceed the policy value, the excess would be paid at maturity and such payments form part of the realistic liabilities. The measurement basis to be adopted for options and guarantees is fair value or stochastically modelled value, the latter being a methodology that derives an

expected or average value from aggregating the results of modelling projections based on a large number of scenarios.

Realistic assumptions

The realistic reporting basis values assets and liabilities consistently, using assumptions which are closer to those expected in practice than the more prudent assumptions that have been required to be used hitherto in financial statements.

The principal assumptions which are important in determining the realistic balance sheet position include the following: experience in respect of the performance of the portfolios, equity market volatility, interest rate trends and the amounts at which provisions are settled. In particular, in calculating realistic liabilities, reference is made to the detailed analyses of past experience, together with any factors that might affect the position in the future, to determine the underlying assumptions. Examples include those assumptions relating to mortality, expenses, surrender rates and expected policyholder choice of retirement date.

In deciding the assumptions to be used for annuitant mortality experience, a reduced margin is applied in the realistic valuation compared with the assumptions used for regulatory reporting. In considering expense assumptions, different methodologies are applied for regulatory and realistic

reporting, which result in realistic expenses being less than those calculated for regulatory reporting. In realistic reporting, analyses of the expected retirement dates and surrender rates are undertaken to generate a realistic run-off profile.

For the realistic balance sheet, the expected interest rates on risk-free assets are key assumptions that are used rather than the rate expected to be earned on the actual assets held to meet those liabilities.

In addition, it is assumed that the Society will apply an annual charge to policy values in order to retain an appropriate level of capital and that, in adverse conditions, the Board will act to cut policy values to the extent required to maintain solvency.

Details of all key assumptions adopted by the Society are set out in Note 16 on pages 44 to 48.

Impact of the new reporting basis

The change in reporting basis is a change of accounting policy for the Society and as such requires a restatement of the opening position.

However, FRS 27 does not require any restatement of the profit and loss account. A reconciliation of the changes to the opening balance sheet is set out in Note 16 on pages 44 to 48.

Furthermore, actuarial guidance on this new regime indicates that closed with-profits funds should anticipate the

eventual distribution of all assets which, in the Society's case as a mutual insurer, would be by way of distribution to policyholders. As a result, in these financial statements, the new reporting basis requires the adoption of this assumption, thereby leaving no balance on the Fund for Future Appropriations. However, the Society closely monitors the level of its future distribution capacity, which is represented by the "Excess Realistic Assets", as explained in the Financial Review, and the key movements in that amount. The Board's decisions on the timing of the distribution of this excess are based upon consideration of the remaining risks facing the Society, which are expected to reduce over time.

It should be noted that realistic reporting applies only to large with-profits funds. Accordingly, the Society's subsidiary company, University Life Assurance Society, continues to report on the modified statutory solvency basis and is consolidated as such in the Group accounts.

Excess Realistic Assets and regulatory solvency

As explained above, the Society's net resources, under the new financial reporting regime, are represented by Excess Realistic Assets, being the excess of realistic assets over liabilities. This amount 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.

Regulatory capital

In assessing the Society's ability to meet its obligations as they fall due, for the reasons detailed below, the Excess Realistic Assets remain more relevant than the excess of net assets over the Capital Resources Requirement (CRR), which forms part of the separate set of financial returns sent to the FSA. The CRR represents a minimum level of required regulatory capital.

The CRR subsumes the previous regulatory measure, the Long Term Insurance Capital Requirement (LTICR), and requires any additional capital requirement over LTICR, resulting from consideration of realistic liabilities, to be taken into account, under a test known as the "twin peaks" test. The result of this test is to require that the capital to be held for regulatory purposes (CRR) is the higher of the amounts calculated under the regulatory and realistic peaks, the former broadly representing the test applied in previous years and the latter reflecting the new realistic valuations of assets and liabilities.

For the Society, in situations where the regulatory excess of assets over liabilities is a positive value before bringing subordinated debt into account, the realistic peak will apply and, accordingly, the CRR is represented by the LTICR plus the With-profits Insurance Capital Component (WPICC),

where the latter represents the difference between the realistic and the regulatory peaks. In the absence of subordinated debt, the CRR would equal available capital resources when the realistic peak is applicable. Subordinated debt provides additional capital and results in an excess over CRR.

Risk Assessment

The Board assesses the risks that the Society faces as part of its consideration of the appropriateness of its assumption of a going concern basis for the preparation of its financial statements.

In addition to the requirement to prepare financial statements on a realistic basis, the Society's particular risks require to be quantified for the preparation of a confidential assessment of its capital needs as required by new FSA rules, introduced under the Individual Capital Adequacy (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 has reported its preliminary ICA figures to the FSA. The FSA process is that, after review, it may issue a confidential Individual Capital Guidance (ICG), which may result in a requirement that a particular level of capital be held by the Society and this amount may be in excess of the ICA reported by the Society. If it receives such an ICG, the Society may have to

consider taking specific actions to lower its capital needs by reducing or transforming the risks it faces, thereby altering its asset and/or liability profiles with a consequent effect on its income and expenses. In such circumstances, the Society might need to modify its published Principles and Practices of Financial Management (PPFM).

Excess Realistic Assets and regulatory solvency

Under the new financial reporting regime, the Society's net resources are represented by the excess of realistic assets over liabilities before deduction of the estimate of the value of future discretionary increases to policy values ("Excess Realistic Assets"). 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 2005, Excess Realistic Assets were £669m, an increase of £214m over the prior year. The analysis of the with-profits assets and liabilities is as follows:

	2005 £m	2004 £m
Realistic value of with-profits assets	10,185	10,678
less:		
Policy values	8,181	8,682
Future charges	(300)	(305)
Impact of early surrenders	(46)	(91)
Cost of guarantees	847	706
Other long-term liabilities	482	661
Other liabilities	352	570
	9,516	10,223
Excess Realistic Assets	669	455

A description of the above liabilities is set out in Note 16e on page 46.

The figures for 2004 have been restated to reflect new guidance and best practice in reporting on a realistic basis. There is no requirement to restate the profit and loss account for 2004.

The key movements in the Excess Realistic Assets during 2005 are shown in the following table:

	2005 £m
Opening Excess Realistic Assets	455
Favourable investment performance	465
Mortality assumption change	(275)
Surrender assumption change	(55)
Changes in other valuation assumptions	66
Variances in provisions and expenses	(3)
Other movements	16
Closing Excess Realistic Assets	669

The principal changes in the Excess Realistic Assets are explained in more detail in later sections of this Review.

The Society seeks to maintain the Excess Realistic Assets balance at a level that protects solvency whilst treating continuing and exiting policyholders fairly. The balance at 31 December 2005 represents 6.6% of with-profits realistic assets, an increase from the equivalent figure of 4.3% at 31 December 2004.

The policy value attributable to with-profits policies may include an element of non-guaranteed final bonus. Estimated final bonus, sometimes referred to as terminal bonus, included in the policy value, is not guaranteed and, under the previous reporting regime, this bonus was not included in the long-term business technical provision. However, for realistic reporting, a prudent allowance for future bonuses, based on assumed future net investment returns that take account of deductions for potential risks, is now 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 Excess Realistic Assets.

At the balance sheet date, the discounted value of aggregate guaranteed with-profits liabilities included within the realistic liabilities totalled £8,302m (2004: £8,595m). Discretionary amounts which, as noted above, are assumed to be distributed when contractual benefits are taken, are £480m (2004: £548m) and are included in the technical provisions.

In assessing the Society's ability to meet its obligations as they fall due, the amount of Excess Realistic Assets 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 FSA. The Capital Resources Requirement (CRR) represents a minimum level of regulatory capital which the Society is required to maintain. If the Society's net assets fall below CRR, the FSA has powers to require that certain information and plans be prepared to demonstrate how the Society would correct the position. However, if the Society has a positive balance of Excess Realistic Assets, and can meet its liabilities as they fall due, it will remain solvent even if the CRR is not met.

As noted in "Changes to Financial Reporting Regime", the Society is required to hold the higher of regulatory and realistic capital under the twin peaks test. Since Excess Realistic Assets are now treated as a liability (being amounts held to meet any unforeseen liabilities and liabilities in excess of those provided at the balance sheet date and to

enhance bonuses in future), the CRR is increased to a level that results in the figure for net assets in excess of CRR becoming zero, but for the existence of subordinated debt, which now forms the excess. If the Society were to repay its subordinated debt, the figure for net assets in excess of CRR would normally be zero.

Accordingly, the relevant figures for excess capital over that required for regulatory purposes are not directly comparable because, for 2005, the realistic balance sheet is the relevant measure whereas, for 2004, it is the regulatory figure which satisfies the twin peaks test. The table below details the principal reconciling items between the Excess Realistic Assets and the excess of net assets over the CRR for the Society.

Accounting changes resulting from the convergence of UK accounting

standards with international accounting standards will result in some differences in presentation and in the measurement of assets and liabilities in future financial statements.

Transactions with HBOS

As announced in the interim report, under the terms of the 2001 transactions with HBOS, when the administrative and sales operations, systems and certain subsidiary undertakings were sold by the Society, the final and contingent tranche of consideration, of up to £250m, was receivable on 31 March 2005 if certain thresholds of new business and profitability were achieved by the Society's former salesforce up to 31 December 2004. HBOS has confirmed that neither threshold, relevant for calculation of this consideration, was achieved.

Accordingly, no further consideration is due to the Society from HBOS in this regard.

	2005 £m	2004 £m
Excess Realistic Assets	669	455
Subordinated debt (note 1)	167	167
Reserving adjustments and disallowed assets (note 2)	52	81
Regulatory net assets	888	703
Capital Resources Requirement (CRR)	(721)	(599)
Net assets in excess of CRR	167	104

Notes:

- (1) For the purposes of regulatory reporting, the carrying value of the subordinated debt can be treated as capital. For 2005, the net assets in excess of CRR are represented by the subordinated debt balance.
- (2) 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.
- (3) The figures in the above table relate to regulatory amounts for the Society. Its FSA returns aggregate certain data for University Life Assurance Society, a subsidiary undertaking of the Society.

Protection of the fund and policy surrenders

Where a policyholder surrenders his or her with-profits policy (or switches to a unit-linked fund) before maturity, contractual obligations in respect of payouts under the policy generally do not apply. The Society takes account of the interests of all policyholders in these circumstances by paying the policy value (or equivalent), less a financial adjustment. In setting the financial adjustment, the aim is for the amounts paid to surrendering policies to be fair, but not to disadvantage continuing policyholders. In particular, the amounts paid to surrendering policyholders should not reduce the payout prospects of the continuing policyholders. As a result of the improved financial position and reduced financial uncertainty, the financial adjustment was reduced from 11.1% to 8% in October 2005.

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. In particular, any reduction in values of property or assets other than fixed-interest securities is not offset by a reduction in guaranteed liabilities, so that any future adverse change in the Society's financial circumstances resulting from a significant fall in net asset values or increase in provisions or non-matched liabilities would necessitate policy value reductions. Where the Society is forced

to sell fixed-interest securities to its disadvantage before their relevant maturity dates, 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.

Investment performance and capacity to pay bonuses

During 2005, the Society continued 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. The weighting in favour of fixed-interest securities and bonds within the investment portfolio results in there being limited scope for growth of the fund. The assets backing UK with-profits policies produced a gross return of 10.1% during the year. However, the return adjusted for bond yield movements (which affect both assets and liabilities) was 8.8%, reducing to 5.6%, after allowing for the impact of expenses, tax and adjustments to provisions and technical provisions.

In determining bonus policy, the Society needs to consider the longer-term picture and aims to balance the objectives of continuing 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 property and private equity portfolios, whose value and liquidity could be 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 and possible changes in the level of provisions.

As reported in last year's financial statements, a margin was held back from the investment return to meet the cost of guarantees and provide additional risk capital. After consideration of all risks, reserving and capital matters, the Board has increased, for applicable with-profits pension policies for 2005, policy values at the rate of 4.5% p.a. (3.5% p.a. in 2004) and 3.6% p.a. (2.8% p.a. in 2004) for life assurance policies. The assumption for the future margin against investment returns has been maintained at 0.5% p.a., in accordance with the range of values stated in the Society's Principles and Practices of Financial Management. The Board will keep this percentage under review – the margin can be reduced or increased, depending on the financial position of the Society. A non-guaranteed interim bonus will continue to be added to policy values (or their equivalents) in 2006 at a rate of

3.5% p.a., for pension policies, having been increased from 2.5% p.a. on 1 October 2005, and 2.8% p.a. for life policies (increased from 2% p.a. on 1 October 2005). These interim bonus rates will apply until further notice. The Board may change interim bonus rates 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 2005. However, for those policies with guaranteed investment returns (GIRs), the value of the guaranteed benefit is not changed by the increase in policy values, but is increased instead at the rate set out in the policy conditions, typically being 3.5% p.a.

As noted in the Corporate Review, the outstanding amount of the cost of GARs allocated to with-profits annuities is to be recovered over a period of six years by withholding 0.5% p.a., commencing with a deduction from the 2005 uplift in policy values.

Expenses and provisions

Expenses shown in the Profit and Loss Account, incorporating administration, exceptional, claims, investment expenses and interest costs, have decreased significantly to £128m in

2005 from £174m in 2004. Exceptional expenses have decreased, principally reflecting the completion of the rectification and managed pension reviews, partially offset by the costs of the litigation against the Society's former auditors and directors, including payment of £10m of the latter's litigation costs. Lower administration and claims costs reflect reduced levels of activity as the with-profits fund reduces in size, set against the backdrop of an increase in costs resulting from preparation for the introduction of new pensions legislation in 2006. Investment expenses have continued to decline as the funds invested have reduced and interest costs have fallen as a result of the reduction in January 2005 in the principal outstanding of subordinated debt.

As shown in Note 16f to the financial statements, balance sheet provisions, included as part of the technical provisions, have reduced over the year. The rectification and managed pension provision has reduced by £142m, as a result of settlements made or finalised. The provision for exceptional expenses of £129m includes a continuing increase in the provision for future pension contributions as well as funding past service entitlements for those former employees of the Society who transferred to HBOS in 2001.

The Excess Realistic Assets reconciliation table on page 10 shows an adverse variance in provisions and expenses, taken together, of £3m. Reference has

been made above to the reduction in the rectification and managed pension provision. This reduction is offset by a further strengthening of expense assumptions incorporated in the technical provisions in recognition of the outsourcing arrangements in place for administration services. Although the volume of transactions per policy is declining, the complexity of the Society's affairs and related uncertainties continue to result in a requirement for provision of an organisational infrastructure substantially greater than would be normal in run-off situations, with resultant higher costs.

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.

Actuarial assumptions and asset values

The Excess Realistic Assets reconciliation table on page 10 shows a net figure of £465m for favourable investment performance, representing the return in excess of the expected investment

return assumed at the beginning of the year, incorporating the beneficial effect of the change in the yield curve over the year, and includes total gains in equities, unit trusts and properties of £326m.

Following further analysis during the year of actual experience and following consideration of expected future experience, including assessment of the latest industry information published by Continuous Mortality Investigation, the Society has further strengthened its mortality assumptions in response to continuing concerns that future mortality improvements may be greater than previously expected, with a resultant increase of £275m in technical provisions.

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% per annum that is applicable to many policies. If the Society's investment return falls below a rate which covers the guarantees and its expenses, and the assumed retirement profile ceased 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 16e to the financial statements. In addition, further provisions would

be required if greater premium income were to be received in such circumstances. For this reason, a letter was sent to policyholders advising that additional investments into the with-profits fund would not be accepted for policies where policyholders have already ceased or who in future cease to comply with their policy conditions.

Maturities and surrenders

During the year, the Society experienced further reductions in the level of both maturities and surrenders. Surrenders in 2005 were £482m (2004: £835m). Maturities and other claims totalled £1,152m (2004: £1,373m). The changing surrender pattern has been reflected in the realistic assumptions which, together with the reduction in the financial adjustment referred to above in the section entitled "Protection of the fund and policy surrenders", results in a reduction of £55m in Excess Realistic Assets, as shown in the reconciliation table on page 10.

Equitable Life Finance plc ("ELF")

The payment of principal and interest and all other monies payable by ELF, a wholly owned subsidiary of the Society, in respect of the 8% undated subordinated guaranteed bonds, issued in 1997, has been irrevocably and unconditionally guaranteed on a subordinated basis by the Society. In December 2004, the Society made an

offer to Bondholders to repurchase bonds at £920 per £1,000 of principal, subsequently increased to £980. Acceptances were received for £179m of bonds and settlement was made on 4 January 2005. As a result, there are now subordinated bonds with a principal value of £171m outstanding. The transaction resulted in a profit, net of expenses, of £3m in 2005, which is included in the investment return. The resultant gross interest saving in 2005 was £14m.

If, when payment of interest in relation to the Bonds becomes due, the Society does not meet Required Minimum Margin (RMM), the capital required to be held under the previous regulatory regime, as defined under the issue terms, as of the date of its latest actuarial valuation, then the payment will be deferred by ELF unless FSA consent to such payment is obtained. As at 31 December 2005, the Society's net assets are in excess of RMM. However, there exists the possibility that the Society may not meet RMM at all times in the future. There is, therefore, uncertainty in respect of the payment of the interest on and principal of the Bonds, because Bondholders' interests are subordinated to those of the Society's policyholders and other creditors in the event of a winding up of the Society.

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.

Considerable time has again been spent by the Board in examining the issues relevant to the going concern basis which, in summary, are mainly the exposure to: increases in provisions, investment losses, impact of discretionary bonus payments, effect of lower interest rates on the behaviour of policyholders with GIRs, 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.

The financial position of the Society has been projected under a very wide 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) in its analysis of the Society's financial position. The results of

this work show that the probability, over the foreseeable future, of the Society being unable to meet its guaranteed obligations to policyholders is not significant. The Board is confident of its ability to manage adverse scenarios that may arise, but there cannot be absolute assurance. In such circumstances, as with any other long-term fund, painful actions could be necessary to adjust maturity values, with-profits annuity payments and surrender values.

In addition, the Board has considered the potential additional claims referred to in Note 23 to the financial statements, entitled "Contingent liabilities and uncertainties". The Board has assessed the probability of these uncertainties arising and on the basis of current information and having taken legal and actuarial advice, has concluded that it is highly unlikely they will result in any material adverse financial consequences. Certain of those risks, in extremely adverse scenarios, could prejudice the continuing solvency of the Society.

The Board has given due consideration to all the potential risks and possible actions set out above and has concluded that it remains appropriate to prepare these financial statements on a going concern basis.

Because of volatility in investment and property markets, the uncertain nature of provisions and the other potential strains on the Society's finances, and even though all these issues are subject to close management scrutiny, the Board

recognises the possibility that the Society may not meet regulatory capital requirements at all times in the future. As noted above, any such failure does not, of itself, cause the Society to become insolvent.

The Board will not hesitate to take appropriate action in any circumstances which jeopardise the fund's ability to meet guaranteed obligations to policyholders.



Vanni Treves (a) (b) (c) (e)
Chairman

Vanni Treves was appointed non-executive Chairman in February 2001. He chairs the Nominations Committee. He has been a solicitor for nearly 40 years, specialising in corporate law. He was 30 years a partner, for 12 of them Senior Partner, at the leading law firm, Macfarlanes. He has extensive experience on Boards, having been a Director (in the majority of cases as Chairman) of six public companies, a statutory corporation and two common investment funds. Vanni is presently Chairman of Intertek Group Plc and the National College of School Leadership and a director of a number of other companies. He retires from London Business School, where he served as Chairman for 8 years, in April 2006. Age 65.



Peter Smith (a) (b) (c) (e)
Deputy Chairman

Peter Smith joined the Board in April 2001. He chairs the Audit Committee. He is Chairman of Savills plc and a non-executive Director of N M Rothschild & Sons Limited and Templeton Emerging Markets Investment Trust plc. He was Senior Partner of PricewaterhouseCoopers until June 2000. In June 2005, following completion of the acquisition by Aviva, he retired from the chairmanship and the board of RAC plc. Age 59.



Charles Thomson (b) (d) (e)
Chief Executive

Charles Thomson was appointed Chief Executive of the Society and joined the Board in March 2001. With a career in the management and leadership of mutual societies spanning some 30 years and extensive knowledge of corporate transformation within the life and pensions industry, he was formerly Deputy Chief Executive at Scottish Widows and Chairman of the Life Board of the actuarial profession. He has also been a director of a further five life and pension companies. Since 2001, he has steered the Society to a more stable footing and is leading the strategic review of the options for the future of the Society. Age 57.



Michael Pickard (a) (d)

Michael Pickard joined the Board in April 2001. He was a Director of the mutual insurance company, Royal London, for 22 years and among the positions he occupied were Appointed Actuary, Chief Executive and Chairman. He has been Deputy Chairman of the Association of British Insurers and a Director of the Personal Investment Authority. He is currently the part-time independent Chairman of Mirror Group Pension Scheme. Age 66.



Fred Shedden (b) (d)

Fred Shedden joined the Board in May 2002. He chairs the Legal Audit Committee. He retired as senior partner of McGrigors, a leading Scottish law firm, in 2002 having spent his entire professional career with that firm. Between 1992 and 1999, Fred was a non-executive Director of Standard Life Assurance Company. He is currently Chairman of Halladale Group plc and is also a non-executive Director of Murray International Trust plc and Iomart Group plc. He is also vice-chair of Glasgow School of Art. Age 61.



Andrew Threadgold (d)

Andrew Threadgold joined the Board in April 2001. He chairs the Investment Committee. He started his career as a professional economist, holding positions at a range of organisations including the Bank of England. He subsequently moved into investment management, and has been Chief Executive of PosTel (now named Hermes), the Investment Manager for the British Telecom and Post Office pension funds, and Chief Investment Officer for the large Australian life company, AMP. He now holds a number of advisory, consultancy and non-executive directorship positions. Age 62.



David Adams OBE (a) (d)

David Adams joined the Board in April 2001. He was Finance Director from 1974 and Chief Executive from 1979 of Harrow Council. In 1987 he became Finance Director of the Railways Pension Scheme and was appointed Chief Executive four years later. From 1997 to 2000 he was Chief Executive of CIPFA. He is a non-executive Director of the Keystone Investment Trust plc. He is honorary chair of trustees of the Mencap Pension Plan Trustees and two other charities' pension trustee bodies. Age 66.



Ron Bullen (a)

Ron Bullen joined the Board in May 2002. He is a qualified Chartered Engineer who has spent his entire career in the manufacturing industry, primarily within the paper sector. From September 2000 until his co-option to the Board of Equitable Life, Ron was the Chairman of EPHAG, then the largest of the Equitable Life policyholder groups. Age 66.



Jean Wood (c) (d)

Jean Wood joined the Board in April 2001. She chairs the Remuneration Committee. She has worked for 25 years in the life insurance and pensions industry, in the UK, Ireland and Canada. Jean's work ranged from staff and management development to management of sales and marketing functions, leading to a position as Managing Director of a medium-sized life company, from which she retired in 1998. She is a Director of The Chelsea Building Society. Age 63.

Key to membership of principal Board Committees

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

Principal activities and business review

The Equitable Life Assurance Society (the Society) is the ultimate holding company of the Equitable group of companies (the Group). The principal activity of the Group during 2005 was the transaction of life assurance, annuity and pension business in the form of guaranteed, participating and unit-linked contracts. The Society closed to new business on 8 December 2000. The results of the Group are presented in the Profit and Loss Account on page 29. The operations of the Group are described in the Corporate Review and Financial Review on pages 2 to 6 and 10 to 15 respectively.

Valuation and bonus declaration

In accordance with the Society's Articles of Association and insurance company legislation, a valuation of the assets and liabilities of the Society has been carried out as at 31 December 2005. There is no guaranteed bonus for 2005, although those policies containing a Guaranteed Investment Return (typically 3.5% p.a.) will have this added to the guaranteed value of their policies as usual. The Board has increased policy values, or their equivalent, for UK with-profits pensions policies at an accrual rate of 4.5% p.a. for 2005 (3.6% p.a. for UK life policies and 4.1% p.a. for the Personal Pension 2000 product). The 2005 bonus decision is dealt with in greater detail in the Corporate Review on page 3.

Directors

The Directors shown on pages 16 and 17 were Directors throughout the year. The three Directors retiring at the Annual General Meeting (AGM) by rotation are David Adams, Charles Thomson and Andrew Threadgold, who offer themselves for re-election. There is one other candidate, John Newman, seeking election as a Director at the AGM.

Subordinated debt

In 1997, the Society's wholly-owned subsidiary, Equitable Life Finance plc, issued £350 million 8% Undated Subordinated Guaranteed Bonds, the proceeds of which were lent to the Society. Following an invitation by the Society to holders of the Bonds, an amount of £175.5 million was paid on 4 January 2005 as settlement of accepted, tendered Bonds, representing a principal value of £179.1 million at a price of £980 per £1,000 of Bonds tendered. Accordingly, the loan from Equitable Life Finance plc to the Society was reduced by £179.1 million.

Financial instruments

Financial instruments such as gilts, corporate bonds and equities form a significant proportion of the assets held by the Society to enable it to fulfil its obligations to its policyholders. The Society is exposed to some risks in relation to certain of these assets and has specific objectives and policies for managing these risks.

The key risks affecting the financial instruments are market risk (equity price), credit risk (bond default) and liquidity risk (cash flow). The Society's risk management processes are described in the Corporate Governance section of the Annual Report and Accounts on page 23 and the mechanisms for managing these risks relating to financial instruments are set out in more detail in Note 17f to the financial statements.

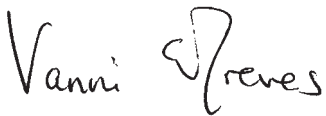
Employees

The majority of staff transferred to HBOS group companies at 1 March 2001. Employees of the Society have been regularly informed of and consulted with on matters of concern to them. It is the Society's policy to give equal consideration to disabled people as to others regarding applications for employment, continuation of employment, training, career development and promotion – having regard to their particular aptitudes and abilities. In relation to employment opportunities, the Society treats applications from all sectors of the community fairly and consistently. All applications for employment, consideration for continued employment, training opportunities, career development and promotion are fully considered with regard to an individual's particular aptitudes and abilities. As a mutual company, the Society has no employee share scheme.

Auditors

PricewaterhouseCoopers LLP have expressed their willingness to continue in office and a resolution to reappoint them as auditors to the Society will be proposed at the Annual General Meeting.

Signed on behalf of the Board

A handwritten signature in black ink that reads "Vanni Treves". The signature is written in a cursive style with a large, stylized 'V' and 'T'.

Vanni Treves

Chairman

30 March 2006

1. Introduction

The Society continues to aim to meet the highest standards in corporate governance and voluntarily adopts the relevant provisions of the Principles of Good Corporate Governance and Code of Best Practice (The Combined Code). The Board is responsible to the Society's policyholders for good corporate governance.

In July 2003, the Financial Reporting Council issued a revised Combined Code on Corporate Governance to come into effect for reporting years beginning on or after 1 November 2003. The Board has adopted the relevant provisions of the revised code for the Society's reporting years from 1 January 2004 onwards.

This report summarises the Society's governance arrangements and continued enhancements.

2. Governance by Directors

The Board

The Board meets regularly to lead, control and monitor the overall performance of the Society. Senior management supply the Board with appropriate and timely information and are available to attend meetings and answer questions. The Directors are free to seek any further information they consider necessary and advice from the Company Secretary or independent professional advisers. Authority is delegated to the Chief Executive for implementing strategy and managing the Society. There is a formal schedule of matters reserved for the Board's decision.

The roles of Chairman and Chief Executive are separated and the Chairman has primary responsibility for the effective functioning of the Board.

Directors

The Board has one executive Director, the Chief Executive.

There are eight non-executive Directors on the Board, whose diverse experience, skills and independent perspective provide an effective review and challenge of the Society's activities.

The Chairman, Vanni Treves, and the Deputy Chairman, Peter Smith, are elected by the Board. Peter Smith has been nominated as the Senior Independent non-executive Director. The Board members are described on pages 16 and 17.

Most of the Directors hold policies with the Society. In the opinion of the Board, in no instance do these interests interfere with the independence of the relevant Director. All the non-executive Directors are considered to be independent.

The Remuneration Report on pages 24 to 26 explains the basis of remuneration of the executive and non-executive Directors.

Performance evaluation

During 2005, the Board reviewed its own performance and that of its committees. With assistance from the Nominations Committee, it also reviewed the performance of individual Directors. The non-executive Directors met under the leadership of the Senior Independent non-executive Director to review the performance of the Chairman. In conducting these reviews, the Board had regard to the guidance on performance evaluation accompanying the Combined Code.

The Board considers that it has the appropriate balance of skills and experience to meet the requirements of the Society's business.

Appointments to the Board

Directors must retire and seek re-election at the first Annual General Meeting following appointment. The

Society's Articles require one-third of the Directors who are subject to retirement by rotation to retire at each Annual General Meeting and also that all Directors must submit themselves for re-election by rotation at an Annual General Meeting at least every three years. All appointments are subject to review by the Board, as advised by the Nominations Committee, at intervals not exceeding three years. The Board policy on remuneration is set out in the Remuneration Report.

Board Committees

The Board formally delegates specific responsibilities to five Board Committees, supported by senior management, which are established by the Board. The Terms of Reference of these committees are available on the Society's website (www.equitable.co.uk) or on request.

The Audit Committee

Peter Smith chairs the Audit Committee, currently comprising five non-executive Directors. It meets at least four times a year. The duties of the Audit Committee include reviewing the Society's compliance with the Smith Guidance (accompanying the Combined Code) on financial reporting, internal controls and risk management systems, the internal and external audit processes and procedures for handling allegations from whistleblowers. The Committee receives and reviews reports on these matters during the year. The Committee assists the Board in fulfilling its responsibilities in respect of the Annual and Interim Financial Statements and Annual Regulatory Returns to the FSA and reviews these items before their submission to the Board. The minutes of the Audit Committee meetings are circulated to the Board.

The Committee has a meeting at least once a year solely with the external auditors and with the internal auditors.

The external auditors attend key meetings and have direct access to the Chairman of the Committee. The Committee keeps the relationship between the Society and its auditors under review and considers their independence, including the extent of their fees from non-audit services. As part of the review, the Audit Committee obtains confirmation from PricewaterhouseCoopers LLP that, in their opinion, their independence as auditors has not been compromised. The Combined Code states that the Board should satisfy itself that at least one member of the Audit Committee has recent and relevant financial experience. The Board takes the view that, rather than an individual or individuals, the Audit Committee as a whole should be considered and has concluded that it does have the requisite skills and experience.

The Combined Code states that no one other than the committee chairman and members should be entitled to be present at a meeting of the Audit Committee, but others may attend at the invitation of the committee. The Board takes the view that any Director should have the right to attend meetings of the Audit Committee.

The Investment Committee

Andrew Threadgold chairs the Investment Committee, currently comprising five non-executive Directors and the Chief Executive. It normally meets bi-monthly. It is responsible for managing credit, market and liquidity risk in accordance with the risk policies set by the Board. It sets policy for strategic asset allocation for the with-profits, non-profit and index-linked funds, delegating implementation to management. It also oversees the activities of the Society's investment managers. The Committee receives advice from the Head of Actuarial Function.

The Legal Audit Committee

Fred Shedden chairs the Legal Audit Committee, currently comprising three non-executive Directors and the Chief Executive. It considers significant legal matters affecting the Society, which have included claims by the Society against previous professional advisers, Directors and management of the Society which were settled during 2005. The Committee meets as required by the demands of the business. The Chairman invites management and professional advisers to attend as appropriate.

The Remuneration Committee

Jean Wood chairs the Remuneration Committee, currently comprising three non-executive Directors. The Committee is responsible for recommending to the Board the terms of remuneration for executive Directors, including incentive arrangements for bonus payments, and for the terms of remuneration for non-executive Directors. More information on the work of the Remuneration Committee is given in the Remuneration Report on pages 24 to 26.

The Combined Code states that the Remuneration Committee should have delegated responsibility for setting the remuneration for executive Directors and the Chairman. The Remuneration Committee makes recommendations to the Board on such matters but the decisions are taken by the Board.

The Nominations Committee

Vanni Treves chairs the Nominations Committee, comprising two non-executive Directors and the Chief Executive. The Committee meets as necessary to consider and make recommendations to the Board regarding the appointment of Directors and the continuing suitability of the Society's Directors.

There were no new appointments to the Board during 2005.

	Board	Audit Committee	Investment Committee	Legal Audit Committee	Nominations Committee	Remuneration Committee
Number of meetings during 2005	14	7	6	8	1	5
Attendance by directors*						
Vanni Treves	14	5	–	8	1	5
Peter Smith	12	6	–	8	1	5
Charles Thomson	13	–	5	8	1	–
David Adams	14	7	6	–	–	–
Ron Bullen	14	7	–	–	–	–
Michael Pickard	14	7	6	–	–	–
Fred Shedden	14	–	5	8	–	–
Andrew Threadgold	13	–	6	–	–	–
Jean Wood	14	–	6	–	–	5

*see pages 16 and 17 for details of committee membership

Board and Committee meetings

Details of the number of meetings of the Board and attendance by Directors are given on page 21. Details of the number of meetings of committees of the Board and attendance by members of those committees are also given on page 21.

Taking advice

The Board and its Committees, subject to defined procedures and parameters, take advice from professional advisers, enabling them to manage the risks and issues arising from the Society's affairs.

Each Director has access to the Company Secretary. They may also obtain independent professional advice, at the Society's expense, about any matter concerning the Society relevant to their duties, subject to defined procedures and parameters.

Subsidiary company governance

The Society's main subsidiaries throughout the year were University Life Assurance Society and Equitable Life Finance plc.

University Life, a life assurance and annuity business, has been closed to new business since 1976. It has a separate Court of Directors (two of whom are Directors of the Society) and its Chairman is Michael Pickard.

Equitable Life Finance plc issued and manages £350 million 8% Undated Subordinated Guaranteed Bonds, the proceeds of which are lent to the Society. In December 2004, the Society made an offer to Bondholders to repurchase bonds at £920 per £1,000 of principal, subsequently increased to £980. Acceptances were received for £179m of bonds and settlement was made on 4 January 2005. As a result there are now subordinated bonds with a principal value of £171m outstanding. The company has a separate Board comprising two Directors (who are Directors of the Society). Its Chairman is Charles Thomson.

The Court of University Life meets at least quarterly and the Board of Equitable Life Finance plc meets as necessary to consider all matters relevant to the effective operation of the respective companies' continuing business, including governance.

Each of the other subsidiary companies has a Board of Directors that meets as appropriate to consider the matters relevant to those companies.

3. Management of the Society

The Executive Team meets regularly, usually weekly, to manage business activities. Papers are prepared and presented to the Board and its Committees by the Executive Team.

David Murray, who was not an employee of the Society, held the roles of With-profits Actuary and Head of Actuarial Function from 1 January 2005 to 31 March 2005. Tim Bateman became With-profits Actuary and Head of Actuarial Function from 1 April 2005.

The Head of Actuarial Function advises on the Society's ability to meet obligations to policyholders, the risks that could have a material impact on this, and the capital needed to support the business. He also advises the Board on the methods and assumptions to be used for the assessment of the value of the Society's assets and liabilities, and reports on the results. The With-profits Actuary advises the Board on key aspects of the discretion to be exercised in the treatment of with-profits policyholders, including advice on bonus rates.

The Society retains responsibility for investment strategy and policy, instructing independent investment managers and advisers to implement desired changes to asset allocations within the portfolio. The Society's Executive Team, taking advice from the Head of Actuarial Function, liaises with the investment advisers to oversee

day-to-day investment matters. This year, for the first time, the With-profits Actuary has prepared a report to policyholders confirming that the Board has taken into account the interests of policyholders in a reasonable and proportionate manner in exercising its discretion in 2005. A copy of this report will be issued to with-profits policyholders together with the Board's report on compliance with the Principles and Practices of Financial Management (PPFM) document, with their annual statements.

4. Accountability and Audit

The Directors are ultimately responsible for the Society's system of internal control and for reviewing its effectiveness, including any outsourced activities. This system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, not absolute, assurance against material loss or misstatement. The Directors actively seek to minimise the exposure to risks and, in doing so, take into consideration the materiality of the risks to be managed and the cost effectiveness of the relevant aspects of internal control in light of the particular environment in which the Society operates.

The Society has outsourced its administration activities to HBOS and it liaises with HBOS to review the appropriateness of the internal control environment and to consider specific needs or requirements of the Society. On an ongoing basis, the Society and HBOS review the appropriateness of the current arrangements for the provision of these services.

The effectiveness of the Society's system of internal control, including financial, operational and compliance controls and risk management, is reviewed by the Audit Committee on behalf of the Board and the Audit Committee has reported on the outcome of its review to the

Board. The principal components of the Society's system of internal control and developments in 2005 are detailed below.

Control environment

The Society is committed to the highest standards of business ethics and conduct, and seeks to maintain these standards across all of its operations.

The Society regularly reviews its governance manual confirming the governance structure for the business and the guiding policies for the organisation.

An appropriate organisational structure for planning, executing, controlling and monitoring business operations is in place in order to achieve the Society's objectives. The structure is reviewed and updated on a regular basis, taking into account the pressures on and conflicting priorities of the Society's business, to ensure that it provides clear responsibilities and control for key areas. Separate internal functions have been established for risk management, internal audit and programme management.

Control procedures

The Society operates a number of control procedures to safeguard the policyholders' assets and investments, including:

- Physical controls, segregation of duties and reviews by management
- Forums for the Executive Team and HBOS to monitor controls and other matters in relation to (i) finance, (ii) operations, (iii) human resources, (iv) information technology, (v) projects and (vi) risk, audit and compliance
- The Investment Committee provides oversight and monitoring of the Society's investment managers
- The Society's Compliance Officer monitors the HBOS compliance function as it relates to the Society on a day-to-day basis in accordance with the Society's compliance strategy

- The contractual arrangement with HBOS dated 1 March 2001 that establishes operational delegations and outline service levels
- Implementation and testing of an appropriate Business Continuity Plan
- Preparation and monitoring of detailed budgets for functional business segments
- A programme management function to structure, co-ordinate, monitor and report on the very significant projects within the programme management function.

Information and communication

Monthly management information in respect of financial performance, customer service, complaints handling and investment performance is prepared and reviewed by senior management, the Executive Team and the Board. Additionally, projects have their own management information processes.

The Society prepares an annual business plan and budget to assist in the monitoring of results, assets, liabilities and investment performance. Actual performance against these plans is actively monitored and, where appropriate, corrective action is agreed and implemented.

Risk management

The Audit Committee has delegated authority from the Board for the review of the Society's internal control and risk management systems.

A Risk Committee, consisting of all members of the Executive Team, meets monthly. Significant internal and external risks are identified and evaluated and accountability for their management is allocated to appropriate individuals. The Risk Committee determines the actions required and their adequacy and monitors progress.

There is a clear risk management framework and methodology, which includes:

- The approval of risk policies by the Board covering each of the key risk categories of credit, market, liquidity, operational and insurance risks
- The agreement by the Board of risk tolerance for each of the key risks facing the Society and key risk indicators for the monitoring of these risks
- Risk identification and management procedures for major projects
- The detailed reporting and review of material risks, including operational risks and those that impact the solvency of the Society
- The application of detailed modelling to assess the sensitivity of the Society's position to economic and business scenarios.

The framework described above is designed to comply with the regime for prudential management of insurance companies contained in FSA's Prudential Source Book.

There is a discussion in the Financial Review on pages 10 to 15 of significant risks the Society faces.

Internal audit

The Society has an internal audit capability to provide assurance over the operation of the system of internal control. The programme of internal audit reviews is based on the Society's risk register and the internal audit programme is designed to provide assurance that the risk-mitigating actions identified by management and the risk register are working effectively. The internal audit plan and activities are reviewed by the Risk Committee and are reported to the Audit Committee.

The Society also receives regular reports from HBOS in relation to the findings of internal audit reviews HBOS has conducted that are relevant to the Society.

Monitoring and corrective action

The risk management function reports to the Risk Committee, Audit Committee, Investment Committee and the Board the results of the risk assessment and other significant changes to risks, including specific reports as required.

Assurance is provided to the Audit Committee and the Board on the effectiveness of the key controls through:

- Monthly consideration by the Risk Committee of key risks, controls effectiveness and adequacy of mitigating actions
- Annual review of effectiveness of key internal controls by the Executive Team
- Reporting by the Society's internal audit function on the key controls reviewed. In performing this work, reliance is placed where possible on the HBOS risk management and internal audit functions that review systems and controls operated by HBOS on behalf of the Society and on information received from and appropriate disclosures having been made by HBOS to the Society
- Reporting on the compliance environment and the management of significant regulatory risks by the Society's Compliance Officer
- Reports received from the Society's risk management function on specific elements of risk and their management
- Reporting by the forums (referred to on page 23 – Control procedures), comprising representatives from the Society and HBOS, of key risks, controls and mitigating actions arising from the processes operated by HBOS on behalf of the Society. This includes tracking the implementation of agreed actions from Internal Audit and Compliance reviews
- The work of other independent advisers commissioned to report on specific aspects of internal control.

The Audit Committee monitors the status of corrective actions for the improvement of effectiveness of the system of internal control.

5. Policyholder communications

The Board is committed to a policy of openness in its communications with policyholders.

In order to understand the views of members, the Board has during the year commissioned market research among members. The Board has sought to keep all relevant stakeholders informed on all major issues and, during the year, letters were sent to all members covering key issues.

At its Annual General Meeting, the members of the Board are available to answer questions. Separate resolutions are proposed on each issue so that they can be given proper consideration. Resolutions are dealt with on a show of hands unless a poll is called. The Society counts all proxy votes and will indicate the level of proxies lodged on each resolution, after it has been dealt with on a show of hands. Since the 2005 AGM, the proxy form has specifically provided for members to be able to abstain on a resolution or resolutions if they wish. All policyholders can gain access to the Society's Annual Report and Accounts and further information on its website.

6. Going concern

As noted in Note 1 to the financial statements on page 32, the Directors consider the adoption of the going concern basis to be appropriate in the preparation of the financial statements. A detailed assessment of the going concern basis is provided in the Financial Review on page 15.

7. Remuneration Report

The composition and responsibilities of the Society's Remuneration Committee are set out on page 21. The Remuneration Committee's recommendations are made

on the basis of rewarding individuals for the scope of their responsibilities and their performance. Where possible, the Committee seeks to meet the standards set out in the Combined Code applicable to listed companies.

Proper regard is paid to the need to retain good quality, highly motivated staff and the remuneration being paid by competitors of the Society is taken into consideration. In this respect, the Committee has received information and advice from remuneration consultants, KPMG and Towers Perrin.

The total emoluments of the Directors, excluding pension benefits, comprise:

Non-executive Directors	Notes	2005 £	2004 £
V E Treves, Chairman	1	140,000	132,500
Other non-executive Directors	2		
P A Smith		38,000	34,000
D H Adams OBE		33,000	30,729
R Bullen		28,000	26,500
M J Pickard		33,000	31,500
F Shedden		33,000	31,500
A R Threadgold		33,000	31,500
J Wood		33,000	31,500
		231,000	217,229
Total for non-executive Directors		371,000	349,729

Notes:

(1) The Chairman's fees have been £140,000 p.a. since 1 July 2004.

(2) From 1 July 2004 the non-executive Directors (other than the Chairman) have received fees at the rate of £28,000 p.a. The following non-executive Directors have also received additional fees of £5,000 p.a. in relation to specific services: M J Pickard (Chairman, University Life) from 1 June 2002; A R Threadgold (Chairman, Investment Committee) from 1 June 2002; F Shedden (Chairman, Legal Audit Committee) from 1 January 2004; J Wood (Chairman, Remuneration Committee) from 1 January 2004 and D H Adams (Deputy Chairman, Audit Committee) from 25 February 2004. P A Smith (Deputy Chairman and Chairman of Audit Committee) has received an additional fee of £10,000 p.a. from 1 July 2004.

Executive Directors

Salary and bonuses

	Salary		Performance Related Bonus		Benefits		Total	
	2005 £	2004 £	2005 £	2004 £	2005 £	2004 £	2005 £	2004 £
Charles Thomson	419,662	399,575	184,196	155,930	102,544	104,308	706,402	659,813
Nigel Brinn (resigned 1 August 2004)	–	141,000	–	97,200	–	41,148	–	279,348
Total for executive Directors	419,662	540,575	184,196	253,130	102,544	145,456	706,402	939,161

C G Thomson's annual rate of salary for the period 1 January to 30 June 2005 was £409,325 plus annual benefits of £88,050. His annual rate of salary was increased to £430,000 with effect from 1 July 2005, with annual benefits remaining at the same level. In addition, benefits in kind received in 2005 totalled £14,494.

The maximum potential annual discretionary bonus award he may receive is 50% of his salary. For 2005/2006 the Remuneration Committee has recommended to the Board that the amount of C G Thomson's discretionary bonus award should be £129,000 and be paid in June 2006.

Long-term retention scheme

	2005 £	2004 £
Charles Thomson	281,250	–

C G Thomson participated in an annual retention bonus scheme. Under this scheme, a retention bonus of £68,750 vested on 31 March in each year of 2003, 2004 and 2005 and was paid in full on 1 April 2005. The scheme was extended to 31 December 2005 and a bonus of £75,000 was paid as due. The scheme has been further extended to 30 June 2006 and, provided that C G Thomson continues in service until that date, he will be entitled to a further bonus of £50,000 payable on 30 June 2006.

Benefits

Executive Directors' benefits include a car allowance and payments in lieu of pension contributions. The executive Director has no accrued pension entitlements (2004 – no accrued entitlements).

No benefits are paid to non-executive Directors.

Service contracts

C G Thomson has a service contract with a six-month notice period. No non-executive Director has a service contract.

Long-term benefits

No share options are available. Other than a retention bonus scheme, the Society does not operate any other long-term benefits scheme.

Directors' remuneration

Non-executive Directors' remuneration comprises a specified fee, which includes extra amounts for specific additional responsibilities, as set out on page 25.

Executive bonus entitlements

The Society operates an annual discretionary bonus scheme for executive Directors. The Society's policy is to ensure that executive Directors are appropriately incentivised to meet the objectives of the business. In particular, significant objectives against which targets are set and approved by the Remuneration Committee include the maintenance of solvency, the achievement of business stability, the management of significant regulatory reviews and litigation issues and the maintenance of effective service delivery.

Directors' pension entitlement

The Society does not provide an occupational scheme for Directors. Executive Directors are provided with a specific allowance in lieu of direct contributions.

8. Statement of compliance with the Code of Best Practice

The Society confirms it complied with all the relevant provisions of the Combined Code throughout the year except for the matters explained in this report, summarised below:

The Board continues to seek to adopt the relevant provisions of the Combined Code, including formalisation of service level agreements with outsourced providers.

Non-executive Directors are not appointed for a specific term. However, each Director's continued appointment is subject to periodic review by the Board, assisted by the Nominations Committee, at least annually. The Society's Articles of Association require that all Directors must seek re-election at the AGM at least every three years.

Decisions regarding the remuneration of executive Directors and the Chairman are taken by the Board, following recommendations from the Remuneration Committee.

All Directors have the right to attend meetings of the Audit Committee.

The Board considers that, rather than an individual or individuals needing to have recent and relevant financial experience, the Audit Committee as a whole should be considered as having the requisite skills and experience.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Society and of the Group and of the results for the Group for that period. In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business (see page 15 of the Financial Review above).

The Directors have complied with the above requirements. The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Society and the Group, and enable them to ensure that the financial statements comply with the Companies Act 1985 as described above. They also have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The financial statements are published on www.equitable.co.uk website. The maintenance and integrity of this website is the responsibility of the Directors. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent Auditors' Report to the members of The Equitable Life Assurance Society

We have audited the group and parent company financial statements (the "financial statements") of The Equitable Life Assurance Society which comprise the Group Profit and Loss Account, the Group and Society Balance Sheets and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Society has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the other information contained in the Annual Report and consider

whether it is consistent with the audited financial statements. The other information comprises only the Corporate Review, the Financial Review, the Corporate Governance report, the Directors' Report and the Statement of Directors' Responsibilities in respect of the financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and Society's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements:

- give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the group's and the Society's affairs as at 31 December 2005 and of the group's result for the year then ended; and

- have been properly prepared in accordance with the Companies Act 1985.

Emphasis of matter – contingent liabilities and uncertainties

In arriving at our opinion we have considered the adequacy of the disclosures made in relation to contingent liabilities and uncertainties in Note 23 and under the heading "The Board's conclusions on provisions and going concern" in the Financial Review, 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 GIR policyholder behaviour. If the uncertainties prevail, further obligations would arise in respect of mis-selling and other claims, which in extreme circumstances may also have consequences for the going concern preparation of the financial statements.

Our opinion is not qualified in respect of this emphasis of matter.

PricewaterhouseCoopers LLP
Chartered Accountants and
Registered Auditors
London
30 March 2006

Technical account – long-term business

	Notes	Group	
		2005	2004
		£m	£m
Earned premiums, net of reinsurance			
Gross premiums written	2a	210.4	274.3
Outward reinsurance premiums	3	(98.3)	(128.7)
		112.1	145.6
Investment income	4a	989.9	947.1
Unrealised gains on investments	4c	458.9	339.6
Other technical income	5a	8.4	7.5
		1,569.3	1,439.8
Claims incurred, net of reinsurance			
Claims paid – gross amount	6	1,643.0	2,206.0
Reinsurers' share	3	(268.3)	(372.5)
		1,374.7	1,833.5
Change in provision for claims – gross amount	6, 16b	(5.0)	6.0
		1,369.7	1,839.5
Changes in other technical provisions, net of reinsurance			
Long-term business provision – gross amount	16b	72.0	(602.6)
Reinsurers' share	3	(45.3)	(5.2)
		26.7	(607.8)
Technical provisions for linked liabilities – gross amount	16b	299.6	(18.0)
Reinsurers' share	3	(254.9)	34.3
		71.4	(591.5)
Net operating expenses – non-exceptional	7a	51.2	54.0
Net operating expenses – exceptional	7b	46.0	71.8
Net operating expenses		97.2	125.8
Investment expenses including interest	4b	27.0	44.4
Other technical charges	5b	1.5	5.6
Taxation attributable to the long-term business	9a	2.2	11.4
Transfer to the fund for future appropriations	15	0.3	4.6
		128.2	191.8
		1,569.3	1,439.8
Balance on the Technical Account		-	-

All significant recognised gains and losses are dealt with in the Profit and Loss Account. All the amounts above are in respect of continuing operations. A change in accounting policy in respect of FRS 27 was made as at 31 December 2004, as permitted. As a result, the profit and loss comparatives are not on an equivalent basis.

The notes on pages 32 to 55 form an integral part of these financial statements.

30 Balance Sheets

As at 31 December 2005

Assets


	Notes	2005 £m	Group Restated 2004 £m	2005 £m	Society Restated 2004 £m
Investments					
Land and buildings	10a	714.3	813.6	710.2	806.5
Investments in group undertakings	10b	–	–	16.8	19.2
Other financial investments	10c	13,642.0	13,678.0	13,596.1	13,625.5
		14,356.3	14,491.6	14,323.1	14,451.2
Assets held to cover linked liabilities	11	741.3	696.6	741.1	696.4
Reinsurers' share of technical provisions					
Long-term business provision		419.9	374.6	419.9	374.6
Technical provisions for unit-linked liabilities		2,568.7	2,313.8	2,568.7	2,313.8
		2,988.6	2,688.4	2,988.6	2,688.4
Debtors					
	12				
Debtors arising out of direct insurance operations		30.3	33.1	30.3	33.1
Debtors arising out of reinsurance operations		–	10.1	–	10.1
Other debtors		32.1	203.4	34.1	238.7
		62.4	246.6	64.4	281.9
Other assets					
Cash at bank and in hand		13.1	32.6	9.3	15.8
		13.1	32.6	9.3	15.8
Prepayments and accrued income					
Accrued interest and rent		208.9	202.4	208.4	202.0
Other prepayments and accrued income	13	142.8	1.2	142.8	1.2
		351.7	203.6	351.2	203.2
Total assets		18,513.4	18,359.4	18,477.7	18,336.9

The notes on pages 32 to 55 form an integral part of these financial statements.

Liabilities

	Notes	Group		Society	
		2005 £m	Restated 2004 £m	2005 £m	Restated 2004 £m
Subordinated liabilities	14	170.5	170.3	167.1	167.1
Fund for Future Appropriations	15	9.3	9.0	–	–
Technical provisions	16a				
Long-term business provision – gross amount		14,851.1	14,779.1	14,826.2	14,754.2
Claims outstanding		2.0	7.0	2.0	7.0
Linked liabilities		3,310.0	3,010.4	3,309.8	3,010.2
		18,163.1	17,796.5	18,138.0	17,771.4
Provisions for other risks and charges	18	49.7	64.2	49.3	64.0
Creditors					
Creditors arising out of direct insurance operations		42.0	54.5	40.8	53.7
Creditors arising out of reinsurance operations		2.3	–	2.3	–
Amounts owed to credit institutions	19a	19.6	25.6	19.6	25.6
Other creditors including taxation and social security	19b	26.7	200.9	36.1	228.1
		90.6	281.0	98.8	307.4
Accruals and deferred income		30.2	38.4	24.5	27.0
Total liabilities		18,513.4	18,359.4	18,477.7	18,336.9

These financial statements were approved by the Board on 30 March 2006 and were signed on its behalf by:



Vanni Treves
Chairman



Charles Thomson
Chief Executive

The notes on pages 32 to 55 form an integral part of these financial statements.

1. Accounting policies

Basis of presentation

The financial statements have been prepared in accordance with sections 255 and 255A 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 which, inter alia, incorporates the requirements of FRS 27, Life Assurance. Further details are given in subsequent notes to these financial statements. The true and fair override provisions of the Companies Act have been invoked; see valuation of investments below.

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 15.

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 plc group companies.

Change in accounting policies

In adopting FRS 27, the Group has amended its accounting policies and has consequently restated prior periods in accordance with FRS 3, Reporting Financial Performance. The Group has taken advantage of the allowance made in FRS 27 that the prior period profit and

loss account need not be restated on the grounds that it would be impractical to do so.

The Directors have reviewed the accounting policies and satisfied themselves as to their appropriateness. Other than as a result of the adoption of FRS 27, referred to above, there are no material changes from the prior year.

Basis of consolidation

The financial statements for the Group consolidate the financial statements of the Society and all its subsidiary undertakings, drawn up to 31 December each year.

The Society, as permitted under Section 230 of the Companies Act 1985, has not presented its own profit and loss account.

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 Group, are included in claims paid. Where such lump sums are used to purchase annuities from the Group, these are included in premium income.

Reassurance contracts

Outward reinsurance premiums are recognised when payable. Reinsurance recoveries are credited to match the relevant gross claims.

Investment income

Interest income is included on an accruals basis.

Dividends are included by reference to ex-dividend dates.

Income on fixed-interest investments is adjusted for purchased accrued interest.

Property rental income arising under

operating leases is recognised in equal instalments over the period of the lease.

Realised gains and losses on investments

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

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.

Claims incurred

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.

Bonuses

The Society declares bonuses annually and the Society's subsidiary, University Life, declares bonuses triennially. 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. The inclusion of an estimate of non-guaranteed benefits within the long-term business provision is a change in accounting policy to comply with FRS 27. Non-guaranteed final bonuses, payable when a claim is made, are included in claims paid.

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.

Valuation of investments

Investments, including assets held to cover linked liabilities, are stated at current value at the balance sheet date, calculated as follows:

- Freehold and leasehold properties are valued individually by qualified surveyors on the basis of open market value, less the estimated costs of disposal.
- Investments in limited partnerships are held at net asset value.
- 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.
- Listed securities are stated at the middle market value.
- Unit trust units are stated at bid value.
- Short-term deposits are included at cost.
- Unlisted investments, stated at Directors' valuation, are generally valued using local industry valuation guidelines.
- Investments in subsidiaries are held at net asset value.

- 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.

Certain valuations are adjusted, where appropriate, to reflect liquidity considerations.

Technical provisions – Long-term business provision and provision for linked liabilities

The long-term business provision is determined separately for each insurance company in the Group following an investigation of the long-term funds and is calculated in accordance with the FSA rules contained in its Integrated Prudential Sourcebook for Insurers. The investigations are 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 which, in the event that they are not needed for other purposes, are available to enhance policyholder benefits. The amount is referred to as "Excess Realistic Assets" 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 conventional with-profits business of University Life and all non-profit business is calculated using the gross premium valuation method. For such business, the technical provisions represent the amounts needed to meet the guaranteed benefits under contracts, including any declared reversionary bonuses (where appropriate) added up to and including the date of the financial statements, and make allowance, in accordance with the assumptions adopted, for specific levels of future contractually-guaranteed bonuses and are discounted where appropriate.

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 technical provision in respect of other linked business is equal to the value of the assets to which the contracts are linked.

Fund for Future Appropriations (FFA)

The Society's FFA is presented as a nil balance, because the amounts available to enhance bonuses in the future are now included in the technical provisions. This represents a change of accounting policy to comply with FRS 27.

For University Life, which is not affected by the FSA realistic capital regime, the FFA represents amounts which are available for future bonuses of various kinds in excess of levels allowed for in the technical provisions and for transfer to shareholder's funds. The introduction of FRS 27 has no effect on the measurement of the FFA for University Life and, for this reason, the FFA for University Life represents the balance shown in the Group accounts.

1. Accounting policies (continued)

Foreign currency translation

Assets and liabilities in foreign currencies are expressed in sterling at the exchange rates ruling at the balance sheet date. Revenue transactions and those relating to the acquisition and realisation of investments have been translated at rates of exchange ruling at the time of the respective transactions.

Segmental reporting

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

2. Earned premiums

Classification of new business

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

- Recurrent single premium contracts are classified as regular where they are deemed likely to renew at or above the amount of initial premium. Incremental increases on existing policies are classified as new business premiums.
- Department for Work and Pensions rebates are classified as new single premiums.
- 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.

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

	2005 £m	Group 2004 £m
a. Analyses of gross premiums written are as follows:		
Individual premiums	183.9	236.4
Premiums under group contracts	26.5	37.9
	210.4	274.3
Regular premiums	122.7	149.2
Single premiums	87.7	125.1
	210.4	274.3
Premiums from non-profit contracts	50.3	56.2
Premiums from with-profits contracts	78.8	116.3
Premiums from linked contracts	81.3	101.8
	210.4	274.3
Premiums from life business	51.9	59.5
Premiums from annuity business	3.1	3.9
Premiums from pension business	154.3	209.8
Premiums from permanent health business	1.1	1.1
	210.4	274.3
Premiums from UK business	205.2	268.5
Premiums from overseas business	5.2	5.8
	210.4	274.3
b. Gross new business premiums		
Individual premiums	94.4	132.8
Premiums under group contracts	6.0	9.3
	100.4	142.1
Regular premiums	12.7	17.0
Single premiums	87.7	125.1
	100.4	142.1
Premiums from non-profit contracts	23.4	25.7
Premiums from with-profits contracts	46.1	76.1
Premiums from linked contracts	30.9	40.3
	100.4	142.1
Premiums from life business	0.2	0.8
Premiums from annuity business	2.2	0.4
Premiums from pension business	98.0	140.9
	100.4	142.1
Premiums from UK business	100.4	142.1
Premiums from overseas business	–	–
	100.4	142.1

Annual equivalent premiums in respect of new business received during the year were £21.4m (2004: £29.5m). New premiums in respect of reassured business during the year were £30.9m (2004: £40.3m).

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 has effectively transferred the risks and rewards in respect of the reinsured business to HBOS.

Premiums received from policyholders in respect of reinsured business are immediately forwarded to HBOS. HBOS reimburse the Society for any claims 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.

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

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 reinsurers' board, then HBOS can make payments directly to policyholders whose policies have been reassured.

Ongoing outward reinsurance premiums paid under the contracts during 2005 were £98.3m (2004: £128.7m).

The reinsurance balance, as required to be disclosed by the Companies Act 1985, and as defined by the SORP, which represents the aggregate total of all those items included in the technical account which relate to reinsurance transactions, net of related gains of £465.0m (2004: £213.2m), is a net credit of £5.2m (2004: £1.5m).

4. Total investment return

	Group	
	2005 £m	2004 £m
a. Investment income comprises income from:		
Land and buildings	40.6	58.5
Other investments	770.0	813.5
	810.6	872.0
Gains on realisation of investments	179.3	75.1
	989.9	947.1
b. Investment expenses including interest comprise:		
Investment management expenses	15.9	16.0
Interest charges		
Bank loans and overdrafts	–	0.4
Other loans	14.1	28.0
Gain on the repurchase of subordinated bonds	(3.0)	–
	27.0	44.4
c. Investment activity account		
Investment income	810.6	872.0
Realised investment gains	179.3	75.1
Unrealised investment gains	458.9	339.6
	1,448.8	1,286.7
Investment management expenses and charges	(27.0)	(44.4)
Investment return for the year	1,421.8	1,242.3

5. Other technical income and charges

	Group	
	2005	2004
	£m	£m
a. Other technical income comprises:		
Income from non-insurance business	5.0	5.4
Other income	3.4	2.1
	8.4	7.5

b. Other technical charges:

Other technical charges of £1.5m (2004: £5.6m) comprise expenses for non-insurance business of subsidiary companies.

6. Claims incurred – gross

	Group	
	2005	2004
	£m	£m
Claims paid – gross amount	1,643.0	2,206.0
Change in provision for claims	(5.0)	6.0
Gross claims	1,638.0	2,212.0

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

	Group	
	2005	2004
	£m	£m
Gross claims paid comprise:		
On death	48.9	45.9
On maturity	508.7	683.6
On surrender	482.1	834.9
By way of periodic payments	594.7	643.7
Claims handling expenses	3.6	3.9
	1,638.0	2,212.0
Life and annuity business	180.0	246.6
Pension business	1,454.4	1,961.5
Claims handling expenses	3.6	3.9
	1,638.0	2,212.0
Linked business	284.7	392.4
Non-profit business	352.7	364.4
With-profits business	997.0	1,451.3
Claims handling expenses	3.6	3.9
	1,638.0	2,212.0
UK business	1,591.0	2,147.1
Overseas business	43.4	61.0
Claims handling expenses	3.6	3.9
	1,638.0	2,212.0

Included in the above payments are attributable final and interim bonuses for the Society and University Life of £39.3m (2004: £58.6m).

7. Net operating expenses

	Group	
	2005 £m	2004 £m
a. Non-exceptional		
Acquisition costs	0.5	0.5
Administrative expenses	50.7	53.5
	51.2	54.0

Acquisition costs reflect the expenses incurred in processing new business and drawing up insurance documents. The Society has been closed to new business since 8 December 2000 and continues to administer existing policies.

b. Exceptional

The Group incurred the following exceptional expenses during the year:

	Group	
	2005 £m	2004 £m
Rectification and other GAR-related expenses	14.2	34.7
Costs of pursuing litigation against third parties	22.9	8.4
Administration and legal costs of non-GAR leavers review	0.5	0.6
Pension costs for former staff	2.7	20.7
Other projects	5.7	7.4
	46.0	71.8

The litigation costs of £22.9m (2004: £8.4m) include an amount of £1.4m (2004: £2.5m) for litigation support services shown in Note 7c, within the table of non-audit fees payable to PricewaterhouseCoopers LLP (PwC).

The expense of £20.7m in 2004 for the pension costs of former staff principally relates to the impact of changes to mortality expectations of the scheme's members following the introduction of revised mortality tables.

c. Expenses include:

The Group audit fees and expenses, inclusive of VAT, of £1,474,000 (2004: £1,343,000) comprised £1,301,000 (2004: £988,000) in respect of statutory audit and £173,000 (2004: £355,000) in respect of regulatory matters, including costs relating to the introduction of new regulatory reporting requirements. The element of the total fees and expenses relating to the Society was £1,406,000 (2004: £1,259,000).

The fees payable to PwC in respect of non-audit fees, inclusive of VAT and expenses, were £1.9m (2004: £3.2m), all of which related to the Society.

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 ensures that auditor independence is preserved.

The non-audit fees, including VAT and expenses, related to services in the following areas:

	Group	
	2005	2004
	£m	£m
Review of interim accounts and other accounting advice	0.2	0.2
Tax advisory services	0.1	0.2
Other non-audit services:		
Governance and compliance work	0.1	–
Services to support litigation against third parties	1.4	2.5
Advice on new regulatory requirements	0.1	0.3
	1.9	3.2

8. Directors and employees

	Group	
	2005	2004
	£m	£m
a. Staff costs		
Wages and salaries	4.0	3.2
Social security costs	0.5	0.4
	4.5	3.6

The monthly average number of employees employed by the Group during the year, including executive Directors, required to be disclosed in accordance with the Companies Act 1985, was 26 (2004: 23).

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 24 to 26.

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 £47.9m (2004: £64.0m) has been 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 2004, as modified for relevant changes to the balance sheet date. An additional provision of £58.5m (2004: £48.3m), representing an estimate of the current value of the contractual commitment to HBOS in respect of future service costs over the next 11 years (2004: 12 years), is included within technical provisions for long-term business.

continued

9. Taxation

	Group	
	2005 £m	2004 £m
a. Taxation charged to the technical account		
UK corporation tax		
Current tax on income for the period	11.7	6.5
Adjustments in respect of previous years	(11.9)	2.4
	(0.2)	8.9
Foreign tax		
Current tax on income for the period	0.1	0.2
Deferred tax		
Unrealised gains on investments	1.2	0.5
Accelerated capital allowances	(0.2)	–
Deferred expenses carried forward	1.3	1.8
	2.3	2.3
Total charge	2.2	11.4

The UK corporation tax charge is provided at rates between 20% and 22% (2004: 20% and 22%), computed in accordance with the rules applicable to life assurance companies, whereby no tax is charged on pension business profits.

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
b. Deferred taxation				
Provided in the financial statements:				
Deferred tax of the long-term fund				
Accelerated capital allowances	(0.4)	(0.6)	(0.4)	(0.6)
Unrealised appreciation in investments	(2.1)	(0.8)	(1.7)	(0.6)
Deferred expenses carried forward	0.7	2.0	0.7	2.0
	(1.8)	0.6	(1.4)	0.8

10. Non-linked investments

	Current Value		Cost	
	2005 £m	2004 £m	2005 £m	2004 £m
a. Land and buildings				
Group				
Leasehold	169.9	214.1	113.7	192.3
Freehold	544.4	599.5	403.2	518.4
	714.3	813.6	516.9	710.7
Society				
Leasehold	169.9	214.1	113.7	192.3
Freehold	540.3	592.4	399.2	511.3
	710.2	806.5	512.9	703.6

Independent professional valuers have valued the Group's and the Society's properties individually. The properties are included in these financial statements at those valuations. The valuations of commercial properties were carried out by Jones Lang Lasalle. During 2004, a number of the Society's property limited partnerships, with a value of £420m, were converted to property unit trusts. In addition, £63m of property limited partnerships were reclassified to reflect the nature of the investments. There was, as a result, a switch in asset value of £483m from "Land and buildings" to "Shares and other variable yield securities and units in unit trusts". In 2005, two further properties, held as "Land and buildings" in 2004, were converted to unit trusts. As a result, there has been a switch of a further £74m from "Land and buildings" to "Shares and other variable yield securities and units in unit trusts". Total property-related investments at 31 December 2005 are £1,511m (2004: £1,482m).

	Current Value		Cost	
	2005 £m	2004 £m	2005 £m	2004 £m
b. Investment in Group undertakings				
<i>Society</i>				
Shares	16.8	14.2	19.0	16.7
Loans	–	5.0	–	5.0
	16.8	19.2	19.0	21.7

	Current Value		Cost	
	2005 £m	2004 £m	2005 £m	2004 £m
c. Other financial investments				
<i>Group</i>				
Shares and other variable yield securities and units in unit trusts ⁽¹⁾	1,194.4	1,075.5	1,001.0	974.6
Debt and other fixed-income securities ⁽²⁾	12,095.8	12,077.4	11,466.7	11,672.6
Loans secured by mortgages	1.6	2.1	1.6	2.1
Loans secured by policies	1.0	1.5	1.0	1.5
Deposits with credit institutions	348.8	521.1	354.9	533.0
Other investments	0.4	0.4	0.4	0.4
	13,642.0	13,678.0	12,825.6	13,184.2

	Current Value		Cost	
	2005 £m	2004 £m	2005 £m	2004 £m
<i>Society</i>				
Shares and other variable yield securities and units in unit trusts ⁽¹⁾	1,171.7	1,056.2	980.0	955.7
Debt and other fixed-income securities ⁽²⁾	12,073.3	12,055.4	11,444.7	11,650.6
Loans secured by mortgages	1.6	2.1	1.6	2.1
Loans secured by policies	1.0	1.5	1.0	1.5
Deposits with credit institutions	348.1	509.9	354.0	521.6
Other investments	0.4	0.4	0.4	0.4
	13,596.1	13,625.5	12,781.7	13,131.9

Investments of £3,716.7m (2004: £3,663.4m), which have been lent in the normal course of business to authorised money brokers on a secured basis, are included in other financial investments. Similar investments of £3,906.1m (2004: £3,846.4m) were received as collateral from brokers. Income earned on stock lending during the year, net of fees paid, was £1.7m (2004: £1.8m).

Notes:

⁽¹⁾ Includes listed investments of £179.4m (2004: £194.6m) for the Group and £167.3m (2004: £183.0m) for the Society at current value.

⁽²⁾ Includes listed investments of £12,070.0m (2004: £12,021.7m) for the Group and £12,047.7m (2004: £11,999.7m) for the Society at current value.

11. Assets held to cover linked liabilities

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
Current value of linked assets	741.3	696.6	741.1	696.4

The cost of assets held to cover linked liabilities is £523.0m (2004: £520.1m) for the Group and £523.0m (2004: £520.1m) for the Society. For the Society, assets relate to index linked business only.

12. Debtors

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
Debtors arising out of direct insurance operations				
Amounts owed by policyholders	30.3	33.1	30.3	33.1
Debtors arising out of reinsurance operations	–	10.1	–	10.1
Other debtors				
Debtors other than Group and related companies	31.1	202.2	30.0	202.9
Deferred tax	–	0.8	–	0.8
Outstanding sales of investments	1.0	0.4	1.0	0.4
Balances with group companies	–	–	3.1	34.6
	32.1	203.4	34.1	238.7
	62.4	246.6	64.4	281.9

Included within other debtors in 2004 is an amount of £175.5m transferred to the Society's tender agent for the settlement of the invitation to purchase subordinated guaranteed bonds (see Note 14).

13. Other prepayments and accrued income

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
Prepayments	142.8	1.2	142.8	1.2

The increase in prepayments relates to interest-bearing advance payments made to a service provider during 2005.

14. Subordinated liabilities

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
Amounts falling due after more than five years	170.5	170.3	167.1	167.1

On 6 August 1997, Equitable Life Finance plc ("ELF"), a wholly-owned subsidiary of the Society, issued £350m 8.0% undated subordinated guaranteed bonds ("the Bonds"), which are guaranteed by the Society. The proceeds, after deduction of costs associated with the issue, were loaned to the Society on similar terms as to interest, repayment and subordination as to those applicable to the Bonds. All (but not some only) of the Bonds are repayable at the option of ELF on 6 August 2007 and each fifth anniversary thereafter, so long as the Bonds are outstanding.

The payment of principal and interest in respect of the Bonds has been irrevocably and unconditionally guaranteed by the Society. The obligations of the Society under the guarantee constitute direct and unsecured obligations of the Society. In the event of a winding up of the Society, the claims of the bondholders under the guarantee will be subordinated in right of payment to the claims of all creditors of the Society.

In accordance with the Trust Deed, where the payment of any amount in relation to the Bonds is due and the Society cannot meet the Required Minimum Margin (RMM) of assets over liabilities required under the Trust Deed, by reference to the Insurance Companies Act 1982, on the due date (or would not be able to meet RMM immediately after such payment), then the payment (or an appropriate part thereof) will be deferred unless the FSA's consent is obtained. The measure of RMM is in accordance with previous FSA regulatory rules and continues to be applicable to the Group's ability to make payments under the Trust Deed.

Following an invitation by the Society to holders of the Bonds, an amount of £175.5m was paid on 4 January 2005 as settlement of accepted, tendered Bonds, representing a principal value of £179.1m at a price of £980 per £1,000 of Bonds tendered. Accordingly, the amount payable for the cancelled Bonds is shown as other creditors at the balance sheet date in 2004 (see Note 19). The gain, net of expenses, resulting from this transaction, of £3m, has been included in the investment return (see Note 4b).

15. Fund for Future Appropriations

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
At 1 January	9.0	552.0	–	542.2
Transfer from the Profit and Loss Account	0.3	4.6	–	5.4
Exchange loss on retranslation of overseas operations	–	(0.2)	–	(0.2)
At 31 December (as reported)	9.3	556.4	–	547.4
FRS 27 restatement (see Note 16c)	–	(547.4)	–	(547.4)
At 31 December (as restated)	9.3	9.0	–	–

In adopting FRS 27, the Group has amended its accounting policies and has consequently restated the opening balance sheet. The analysis of the restatement amount of £547.4m is shown in Note 16c.

For the Society, all future surplus not required to meet any unforeseen liabilities and liabilities in excess of provisions will be distributed over time to policyholders as increases to policy values. For this reason, the Fund for Future Appropriations (FFA) is presented as a nil balance.

For University Life, which, because of its size, is not affected by the FSA realistic capital regime, the FFA represents amounts which are available for future bonuses of various kinds in excess of levels allowed for in the technical provisions and for transfer to shareholder's funds. Similarly, the introduction of FRS 27 has no effect on the measurement of the FFA for University Life and, for this reason, the FFA for University Life represents the balance shown in the Group accounts.

16. Technical provisions**a. Gross technical provisions**

	Group		Society	
	2005 £m	Restated 2004 £m	2005 £m	Restated 2004 £m
Non-profit technical provisions	5,018.3	4,671.3	5,005.7	4,659.7
With-profits technical provisions				
Policy values	8,181.4	8,682.0	8,181.4	8,682.0
Future charges	(299.7)	(305.5)	(299.7)	(305.5)
Impact of early surrenders	(46.2)	(90.8)	(46.2)	(90.8)
Cost of guarantees	846.9	705.8	846.9	705.8
Other long-term liabilities	481.6	661.5	469.3	648.2
	9,164.0	9,653.0	9,151.7	9,639.7
Excess Realistic Assets	668.8	454.8	668.8	454.8
Total with-profits technical provisions	9,832.8	10,107.8	9,820.5	10,094.5
Long-term business provision	14,851.1	14,779.1	14,826.2	14,754.2
Claims outstanding	2.0	7.0	2.0	7.0
Index-linked annuities	742.8	697.7	742.8	697.7
Other linked business	2,567.2	2,312.7	2,567.0	2,312.5
Linked liabilities	3,310.0	3,010.4	3,309.8	3,010.2
	18,163.1	17,796.5	18,138.0	17,771.4

The Excess Realistic Assets is a key measure of the Society's resources and represents 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.

b. Gross technical provisions movement

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
At 1 January	17,796.5	17,863.2	17,771.4	17,837.7
Retranslation of opening foreign branch technical provisions	–	0.5	–	0.5
Change in long-term business provision	72.0	(602.6)	72.0	(602.2)
Change in provision for claims	(5.0)	6.0	(5.0)	6.0
Change in technical provisions for linked liabilities	299.6	(18.0)	299.6	(18.0)
At 31 December (as reported)	18,163.1	17,249.1	18,138.0	17,224.0
FRS 27 restatement (see Note 16c)	–	547.4	–	547.4
At 31 December (as restated)	18,163.1	17,796.5	18,138.0	17,771.4

c. Impact of adoption of FRS 27, Life Assurance with effect from 31 December 2004

	Group 2004 £m	Society 2004 £m
Excess Realistic Assets	454.8	454.8
Effect of other realistic assumptions on with-profits liabilities	77.2	77.2
Other adjustments	15.4	15.4
FRS 27 restatement	547.4	547.4

The adoption of amended accounting policies results in amounts previously included in the FFA for the Society to be recognised as liabilities as shown above. These amounts have been reclassified as Excess Realistic Assets.

In addition, with-profits benefits are now required to be valued in accordance with the FSA realistic capital regime rather than the gross premium valuation method that was used previously. This new method includes an estimate of the value of any non-guaranteed future discretionary benefits and allows for the value of options and guarantees using a market-consistent, stochastic basis.

Other adjustments include the value of future payments of interest in respect of the subordinated debt.

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

The technical provisions in respect of some non-profit business are wholly reassured with HBOS. The long-term business provisions for the Society's non-profit and index-linked annuities and University Life's non-profit 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 i and ii below. The principal assumptions used in valuing the non-profit and index-linked annuities in payment were as follows:

Class of business	Interest rate %		Future expense allowance	
	2005	2004	2005	2004
Non-profit annuities in payment				
Basic Life and General Annuity business – pre 1992	4.20	4.60	£24 p.a.	£20 p.a.
Basic Life and General Annuity business – post 1991	3.70	4.10	£24 p.a.	£20 p.a.
Pension business	4.20	4.60	£24 p.a.	£20 p.a.
Index-linked annuities in payment				
Basic Life and General Annuity business – pre 1992	1.50	1.70	£24 p.a.	£20 p.a.
Basic Life and General Annuity business – post 1991	1.25	1.45	£24 p.a.	£20 p.a.
Pension business	1.50	1.70	£24 p.a.	£20 p.a.

- i. 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. In general, fixed-interest and index-linked yields decreased during 2005 and the valuation interest rates have also decreased. The changes to the valuation interest rates in aggregate have increased the index-linked annuity and non-profit technical provisions by £202m. Similarly, the market value of the backing assets has increased as yields have fallen and this offsets a large proportion of the increase in technical provisions. Future expenses in respect of non-profit and index-linked annuities in payment are allowed for in two ways – an explicit allowance per policy increasing by 2.75% p.a. (2004: 3.00% p.a.) and an expense allowance for fund management, expressed as a percentage of the value of the fund, of 0.06% p.a. (2004: 0.06% p.a.). The amount allowed for expenses has been assumed to increase by an extra 2.75% p.a. (2004: 2.50% 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.
- ii. Using the results of an investigation into the Society's actual mortality experience and making additional allowance for future improvements in the longevity of annuitants, mortality assumptions have been determined for the non-profit and index-linked annuities as detailed in the table below. The effect of the change in mortality assumptions has been to increase the index-linked annuity and non-profit technical provisions by £240m.

A sensitivity analysis, carried out in connection with the effect of a change in mortality basis on the technical provisions, has demonstrated that a 10% change in the mortality basis would result in a £171m increase in the index-linked annuity and non-profit technical provisions. This change is equivalent to the life expectancy of a 65-year-old male increasing by an additional 10 months.

Mortality assumptions by class of business

	2005	2004
Non-profit and index-linked annuities in payment		
Basic Life and General Annuity business	77.5% IMA92 (U=2005) for males	85% IMA92 (U=2004) for males
	82.5% IFA92 (U=2005) for females	100% IFA92 (U=2004) for females
Pension business	82.5% PMA92MC (U=2008) for males	100% PMA92MC (U=2013) for males
	82.5% PFA92MC (U=2008) for females	100% PFA92MC (U=2011) for females

16. Technical provisions (continued)

e. 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 long-term business provisions for University Life have been calculated using the gross premium method.

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 16f), 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 present value of future profits deducted is £9.9m. In 2004, the corresponding amount was £17.4m, following clarification by the FSA in 2005 of the assumptions required for the investment return and discount rates.

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 has in issue three principal types of with-profits policy: Recurrent Single Premium (RSP) policies, With-Profits Annuity (WPA) policies and Conventional With-Profits (CWP) policies. These policies represented 75%, 23% and 2%, respectively, of the total policy values at 31 December 2005 (75%, 23% and 2% at 31 December 2004). For the majority of RSP policies issued before 1 July 1996, each premium (after charges) secures a guaranteed investment return, typically at the rate of 3.5% pa. For the majority of RSP policies issued after 1 July 1996, the guaranteed investment return is 0%. For WPA policies, there are similar guarantees but these are expressed as a minimum annual income for each policy. 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 guaranteed investment return, 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 WPA policies, there is a guarantee that the annuity payable in any year will not be less than a guaranteed amount. This guaranteed amount reduces each year by the anticipated bonus rate that was selected at outset by the policyholder.

For CWP business, there is a guarantee that the amount payable on death and on 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 £705.8m in 2004 to £846.9m at 31 December 2005, principally as a result of changes in interest rate assumptions. This amount is included within technical provisions (see Note 16a).

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.

There are also some guarantees and options in University Life policies. These are not considered to be material to the Group's future cash flows and provisions have been established using deterministic scenarios on prudent assumptions.

ii. Assumptions – with-profits business

Mortality

Using the results of an investigation into the Society's actual mortality experience and making additional allowance for future improvements in the longevity of annuitants (where appropriate), mortality assumptions have been derived for the with-profits business as detailed in the table below:

<i>Mortality assumptions by class of business</i>	2005	2004
Endowment assurances (with-profits)		
Basic Life and General Annuity business	65% AM92 ultimate for males	65% AM92 ultimate for males
	90% AF92 ultimate for females	90% AF92 ultimate for females
Pension business	65% AM92 ultimate for males	65% AM92 ultimate for males
	90% AF92 ultimate for females	90% AF92 ultimate for females
Recurrent single premium (RSP) (with-profits)		
Basic Life and General Annuities in payment	80% IMA92 (U=2005) for males	85% IMA92 (U=2004) for males
	85% IFA92 (U=2005) for females	100% IFA92 (U=2004) for females
Pension Annuities in payment	75% PMA92MC (U=2008) for males	85% PMA92MC (U=2013) for males
	70% PFA92MC (U=2008) for females	80% PFA92MC (U=2011) for females

The effect of the change in the mortality assumptions in 2005 has been to decrease the Excess Realistic Assets by £35m.

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

Future charges

A margin of 0.5% p.a. (2004: 0.5% p.a.) is assumed to be retained before making future increases to policy values. This margin 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) and to provide some additional capital to act as a buffer against risks and adverse experience.

Expenses

A further margin of 1.05% p.a. (2004: 0.85% p.a.) is assumed to be deducted each year before making future increases to policy values. This margin is intended to provide for future expenses in respect of with-profits business. The increase in 2005 includes the result of a change in the classification of the provision for VAT. A further 0.1% increase in the expense assumption would decrease the Excess Realistic Assets by £28m.

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 2004 and 2005. 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 3 years earlier than ECD and up to 10 years later than ECD. The retirement dates used are up to a year later than those used in 2004.

16. Technical provisions (continued)**e. The long-term business provision – with-profits business (continued)****ii. Assumptions – with-profits business (continued)**

A sensitivity analysis has been carried out to illustrate the potential impact on Excess Realistic Assets, at 31 December 2005, of GIRs on RSP business under certain scenarios modelled on a stochastic basis, where the results are aggregated and the average liability is calculated. If investment returns fall below a given level, it is possible that policyholders may defer their retirement. If policyholders defer their retirement by up to 5 years (from that previously assumed), while the interest rate in the scenario is below 2.5%, then the Excess Realistic Assets would reduce by £95m. If the level of interest rates at which behaviour changes is 3.5% and the same period of deferment is assumed, the amount is £145m. If the deferral were for a period of up to 10 years, the amounts are £150m at 2.5% and £250m at 3.5% respectively.

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 2004 and 2005. 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. (2004: 2% p.a.). The effect of the change in the surrender rates has been to reduce the Excess Realistic Assets by £30m.

A financial adjustment of 8% (2004: 11.1%) of policy values is assumed as a deduction on surrender prior to contractual termination. The effect of the change in the rate of the financial adjustment on surrender has been to reduce the Excess Realistic Assets by £25m.

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 is The Smith Model. 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 2004 to 2005 was to increase the Excess Realistic Assets by £62m. 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 swaption volatilities obtained from Bloomberg. For equity values the model produces a 10 year volatility of 21% (2004: 18%). Property (including property-related assets) is modelled using a proxy index with a volatility of 15% and a correlation with equities of 30%.

f. The long-term business provision – miscellaneous provisions

Technical provisions include amounts in respect of specific provisions:

- An amount of £85m (2004: £227m), which is the current estimate of the compensation or adjustments to future benefits which may be payable under the Rectification Scheme to policyholders who had policies with guaranteed annuity options which matured prior to the House of Lords' decision, and compensation and other costs which may be payable under the review of managed pensions sales. This provision is based on an assessment of the likely level of claims, the level of current interest rates and the possible form of compensation which may be payable on individual cases, if a claim is found to be appropriate. The principal reduction in the provision is as a result of further assessment and settlements during the year.
- Anticipated additional exceptional expenses of £129m (2004: £123m) over future years, including contractual commitments to HBOS in respect of pension scheme future service costs, the costs associated with implementing new regulations and anticipated additional costs associated with servicing policies in the medium term.
- An amount of £182m (2004: £208m) for other miscellaneous liabilities including, inter alia, potential mis-selling liabilities. The principal components are provisions for potential mis-selling claims, a provision for other legal claims against the Society, and provisions relating to the reinsurance of the linked and part of the non-profit book to HBOS in 2001 and other items.

g. 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 business is included in the long-term business provision. The future expenses on other linked business are wholly reassured.

17. Capital statement

a. Analysis of capital

The capital statement in respect of the Group's life assurance business at 31 December 2005 (and 2004) is set out below. These figures are calculated in accordance with the regulations set out in the FSA Handbook of Rules and Guidance. The Group has two with-profits funds as follows:

	Notes	Equitable Life £m	University Life £m	2005 Total £m
Available capital resources:				
Fund for future appropriations		–	9.3	9.3
Subordinated debt	14	167.1	–	167.1
Regulatory adjustments				
Valuation differences ⁽¹⁾		722.1	(1.8)	720.3
Inadmissible assets		(1.0)	–	(1.0)
Total available capital resources		888.2	7.5	895.7
Long-term Insurance Capital Requirement (LTICR) ⁽²⁾		(592.6)	(2.0)	(594.6)
With-profits Insurance Capital Component (WPICC)		(128.5)	–	(128.5)
Total regulatory Capital Resource Requirement (CRR)		(721.1)	(2.0)	(723.1)
Excess of available capital resources over CRR		167.1	5.5	172.6

	Notes	Equitable Life £m	University Life £m	2004 Total £m
Available capital resources:				
Fund for future appropriations		–	9.0	9.0
Subordinated debt	14	167.1	–	167.1
Regulatory adjustments				
Valuation differences ⁽¹⁾		547.4	(1.9)	545.5
Inadmissible assets		(11.4)	–	(11.4)
Total available capital resources		703.1	7.1	710.2
Long-term Insurance Capital Requirement (LTICR) ⁽²⁾		(598.7)	(2.1)	(600.8)
With-profits Insurance Capital Component (WPICC)		–	–	–
Total regulatory Capital Resource Requirement (CRR)		(598.7)	(2.1)	(600.8)
Excess of available capital resources over CRR		104.4	5.0	109.4

Notes:

⁽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.

⁽²⁾ For University Life, the regulatory capital requirement is the minimum amount defined by the regulations.

The tables above show the regulatory capital position for Equitable Life and University Life separately. Equitable Life's actual FSA return presents the figures on an adjusted solo basis where University Life is incorporated on a different basis. The surplus capital for 2005 on this basis is £167.1m (2004: £104.4m).

17. Capital statement (continued)**b. Available capital resources**

The total available capital resources show the capital, calculated on a regulatory, rather than a realistic basis, 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 Group amount to £895.7m (31 December 2004: £710.2m).

The table below shows the effect of movements in the total amount of available capital of the Society during 2005:

Available capital resources:	£m
At 1 January 2005	703.1
Investment return and interest rate movements	491.1
Mortality assumption change	(269.0)
Other movements	(37.0)
At 31 December 2005	888.2

The available capital of the University Life's UK with-profits fund has been calculated under the regulatory basis. The surplus capital of University Life is not available at this time, nor in full, to the Society.

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 has guaranteed £171m (par value) of 8% undated subordinated bonds which were issued by Equitable Life Finance plc (a subsidiary company). The Society has the option, subject to certain conditions, to repurchase the Bonds in 2007. Payments of interest and repayment of the Bonds are subject to certain conditions (see Note 14).

University Life is closed to new business and all surpluses belong to its with-profits policyholders and its shareholder, which is the Society. The expenses of running University Life's business are restricted to an amount calculated annually in accordance with an agreement signed in 1919. Any excess of expenses above that amount is met by the Society.

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 Capital Resources Requirement.

For the Society, the CRR comprises the Long-term Insurance Capital Requirement 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 (after deducting the value of subordinated debt) 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 2005 following the introduction by the FSA in 2004 of new rules for the determination of capital requirements, 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 2005 and is lower than the excess capital resources over LTICR and, as a result, a WPICC applies.

For University Life, the CRR is the minimum amount defined by the regulations.

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.

f. Capital and risk management

The Society is exposed to particular risks, including those resulting from its past business operations. Note 23 sets out contingent liabilities and uncertainties.

In order to have sufficient capital to satisfy regulatory and other capital requirements, the Society retains a margin before applying any increases to policy values. In addition, financial adjustments continue to be applied to policies that surrender. In setting the level of financial adjustment, the intention is that the amount paid to surrendering policies should be fair but that it should not disadvantage continuing policyholders.

A potential market risk for the Society is in respect of GIRs, which are typically 3.5% p.a. If market returns fall below this rate, the rate of policy value growth could reduce and the future expected cost of GIRs would increase. It is also possible that policyholders could defer their retirement, leading to further increases in the cost of these guarantees.

In order to protect with-profits policyholders from the effects of falling stock markets and property values, the Society operates a relatively conservative investment policy as a result of its solvency position and to satisfy any requirement for liquidity. Accordingly, the Society invests mainly in fixed interest securities (both gilts and corporate bonds). This policy also limits the returns that will be achieved in rising markets. The asset mix at 31 December 2005 was gilts 49% (2004: 50%), corporate bonds 25% (2004: 23%), property (including property unit trusts) 15% (2004: 14%), cash 6% (2004: 8%) and equities 5% (2004: 5%). The Society did not have any material derivative holdings in either year.

There are risks in the investment portfolio, particularly relating to counterparty defaults in respect of corporate bonds. The Society has a policy of limiting the exposure to lower quality corporate bonds and limiting concentration with individual counterparties. In addition, although the Society aims to match closely the expected maturity of assets with liabilities, an exact match is not possible as, for certain assets (such as property), there are no redemption dates and, for certain liabilities (such as annuity mortality risks), the duration can change. In the case of assets backing the non-profit policies (mainly non-profit and index-linked annuities), a separate set of assets has been notionally hypothecated and invested in fixed interest and index-linked assets to match the liabilities.

g. Analysis of policyholder liabilities

An analysis of policyholder liabilities is as follows:

	2005			2004		
	Equitable Life £m	University Life £m	Total £m	Equitable Life £m	University Life £m	Total £m
Non-profit	5,005.7	12.6	5,018.3	4,659.7	11.6	4,671.3
With-profits	9,822.5	12.3	9,834.8	10,101.5	13.3	10,114.8
Linked	3,309.8	0.2	3,310.0	3,010.2	0.2	3,010.4
	18,138.0	25.1	18,163.1	17,771.4	25.1	17,796.5

18. Provision for other risks and charges

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m
Provisions for deferred taxation	1.8	0.2	1.4	–
Pension commitments for former staff	47.9	64.0	47.9	64.0
	49.7	64.2	49.3	64.0

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

Pension payments for former staff relate to the contractual agreement with HBOS (described in Note 8c) under which £18.7m (2004: £18.7m) has been paid during the year. The balance of the movements is due to changes in economic assumptions.

19. Creditors

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m

a. Amounts owed to credit institutions

Bank overdrafts	19.6	25.6	19.6	25.6
------------------------	-------------	-------------	-------------	-------------

Bank overdrafts were partly matched by an amount of £16.3m (2004: £16.5m) placed in an assigned account owned by HSBC. The amount is included in debtors in Note 12.

	Group		Society	
	2005 £m	2004 £m	2005 £m	2004 £m

b. Other creditors including taxation and social security

Outstanding purchases of investments	1.9	1.6	1.9	1.6
Balances with group companies	–	–	10.9	29.2
Corporation tax	15.0	13.6	14.6	13.6
Other creditors	9.8	185.7	8.7	183.7
	26.7	200.9	36.1	228.1

In 2004, an amount is included within other creditors of £175.5m, payable for the cancelled subordinated guaranteed bonds, which was settled on 4 January 2005 (see Note 14).

20. Subsidiary and associated undertakings**a. Principal subsidiary undertakings**

The principal subsidiary undertakings, all of which are wholly and directly owned, are as follows:

	Nature of business
Equitable Life Finance plc	Arranging and managing loan finance
University Life Assurance Society	Life assurance and annuity business. Closed to new business

The above holdings are of ordinary shares. Both companies are incorporated in the UK.

b. Significant holdings

At 31 December 2005, the Group and the Society held more than 20% of the nominal value of a class of equity shares in 14 (2004: 16) companies.

At 31 December 2005, the Group and the Society held more than 20% of the partnership interests in 1 (2004: 1) limited partnership investing in properties.

At 31 December 2005, the Group and Society held more than 20% of the partnership interest in 10 (2004: 10) portfolios investing in private equity investment companies included in shares and other variable yield securities.

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 Group or of the Society. These investments are included in the balance sheet at current value which is based upon the Group and Society's share of the net assets.

Full information on subsidiary undertakings and companies and limited partnerships in which the Group and 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 2005 (2004: nil).

22. Commitments

The Society has no material operating lease commitments.

Property investment commitments, not provided for in the financial statements, amounted to £16.9m (2004: £65.8m) for the Group and for the Society. The commitment is to finance the estimated costs of developments to completion and final costs may be more than currently expected.

Commitments in respect of uncalled capital on private equity fund interests, not provided for in the financial statements, amounted to £42.6m (2004: £56.8m) for the Group and for the Society.

23. Contingent liabilities and uncertainties

As noted in the Financial Review on page 15 and in the following sections of this Note, there exist certain uncertainties that, in the event they materialised, could adversely impact on the appropriateness of the going concern basis of preparation of these financial statements. Certain of those risks, in extremely adverse scenarios, could prejudice the continuing solvency of the Society. The Board has assessed the probability of these uncertainties arising and, on the basis of current information and having taken legal and actuarial advice, has concluded that it remains appropriate to prepare these financial statements on a going concern basis.

These uncertainties and potential additional claims are as follows:

- As reported previously, the report of the Equitable Life inquiry, led by Lord Penrose, was published in March 2004. Lord Penrose commented upon several aspects of the Society's affairs in a way that may impact on the likelihood of further claims being made against the Society for breach of statutory duty, or in tort or contract. The FSA has undertaken a review of the report by Lord Penrose and has concluded that generic claims against the Society regarding its basis for allocating bonuses during the 1990s are unlikely to succeed. The Board has also been advised that any claims regarding alleged "over-allocation" of bonus, relative to the relationship between aggregate policy values and aggregate assets, would face very significant difficulties and that a claim effectively seeking to recover losses relating to investment conditions would be highly unlikely to succeed. The Financial Ombudsman Service (FOS) announced on 22 March 2005 that it will not investigate such complaints.
- Although some complaints have been received by the Society that have included matters commented upon by Lord Penrose, including the claim by certain with-profits annuitants referred to below, there has only been a small number of complaints received arising directly out of the report by Lord Penrose.
- Following publication of the report by Lord Penrose, the Parliamentary Ombudsman announced in July 2004 her decision to open a new investigation. It is an inquiry that is independent of the government and can recommend to Parliament compensation payable by the government, but cannot require the Society to take any particular action. However, the terms of reference of the inquiry's report may result in consideration of some of the issues commented upon by Lord Penrose and may result in findings that could result in policyholders trying to assert claims against the Society. The Society has had lengthy and confidential discussions with representatives of the Parliamentary Ombudsman, who plans to publish her report before the end of 2006.
- In January 2006, in response to petitions by a policyholder and a policyholder action group, the European Parliament established an EU Parliamentary Committee of Inquiry into Equitable Life to carry out a formal investigation into "alleged contraventions of Community law and alleged maladministration in the application of Community law related to the demise" of the Society. Although the investigation relates to the actions of the UK government, the process may result in findings that could result in claims being asserted against the Society.

23. Contingent liabilities and uncertainties (continued)

- The Institute of Chartered Accountants in England and Wales has initiated disciplinary proceedings against Ernst & Young in respect of its conduct in certain of its audits of the Society. The Institute of Actuaries has also initiated disciplinary proceedings against certain of the Society's actuaries, who were also directors of the Society, for their actions during varying periods of time up to February 2000. Both disciplinary proceedings were deferred until completion of the Society's litigation against its former directors and former auditors. Although these proceedings and investigations cannot result in a requirement for the Society to take any particular action, they may make findings that could influence the way in which claims are presented against the Society.
- As previously reported, in relation to with-profits annuities, there has been a number of complaints made to the FOS and to date there has been a very limited number upheld on the basis of their respective facts. The FOS approach to these complaints has not been on the basis of generic mis-selling. However, an action has been brought by 413 with-profits annuity policy claimants, who allege, inter alia, generic mis-selling and over-allocation of bonus. Having taken legal advice, the Society believes that any generic claims are not well-founded and is defending the action.
- As noted in the Financial Review on pages 12 and 13, 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. The potential additional costs associated with these guarantees if interest rates fall from assumed levels, under certain specified scenarios, have been disclosed in Note 16e. In addition, further provisions would be required if greater premium income were to be received in such circumstances.
- The Society is required to submit to the FSA a confidential report assessing its capital requirements under the Individual Capital Adequacy (ICA) framework. The FSA process is that, after review, it may issue a confidential Individual Capital Guidance (ICG), which may result in a requirement that a particular level of capital be held by the Society and this amount may be in excess of the ICA reported by the Society. If it receives such an ICG, the Board may have to consider taking specific actions to lower the Society's capital needs by reducing or transforming the risks it faces, thereby altering its asset and/or liability profiles with a consequent effect on its income and expenses. Discussions as to the appropriate level of capital to be held by the Society have commenced with the FSA, but are unlikely to be completed for some months.
- The Society holds provisions for various guarantees and options arising under certain policies, including options to surrender early, GARs for certain classes of policies and Guaranteed Minimum Pension entitlements for other policies. Although technical provisions are held for all material guarantees or options, there exists the possibility that those provisions may require to be adjusted as a result of an analysis of benefits arising in the case of less commonly occurring policies or where special practices apply or where investigation of past events results in a requirement for corrective action to be taken.
- Having taken legal advice in respect of allegations of fraud made by former non-GAR policyholders in respect of the non-disclosure of GAR risks after 1998, the Board believes that there is no sustainable case of fraud and, in the event that any proceedings were issued, they would be defended vigorously. There exists the possibility that further claims could be made against the Society, alleging fraud or mis-selling not addressed hitherto or otherwise seeking compensation.
- As noted in the Corporate Review, new rules in respect of pensions come into force in April 2006. The tax treatment for policyholders of payments which result from policyholder reviews relating to pensions products remains unclear in the regulations introduced to date and, accordingly, there remains the possibility of additional liabilities for the Society.
- As previously reported, in March 2001 the Society entered into a reinsurance arrangement with a subsidiary undertaking of HBOS in respect of all of the Society's insurance policies except with-profits policies and immediate annuities. Assets were transferred by the Society following a provisional calculation of the initial premium payable under the agreement. After discussions, the parties failed to agree the final amount of assets transferable in respect of this initial premium. The Society has provided in its financial statements an amount considered appropriate to satisfy its estimated liability for any balance of assets to be transferred. As the Society was unable to reach agreement with HBOS as to the relevant amount of the initial premium, it was agreed in March 2004 that the matter be referred to an umpire for resolution, as contemplated by the reinsurance arrangement in the event of a dispute arising. The umpire has not yet completed his deliberations.

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. However, the potential impact of the range of uncertainties relating to provisions may be significant.

The uncertain nature of the provisions, the incidence of other uncertainties and risks, the possible volatility of asset values and potential strains arising from surrenders and maturities could, in adverse outcomes, result in the possibility that CRR (which is a measure of the capital that the FSA requires life assurance companies to hold) may not be satisfied at all times in the future. Attention is also drawn to the implications of these uncertainties on the ability of the Society to meet payments of interest and principal in relation to the subordinated debt as explained in Note 14 to the financial statements.

Equitable Life