Equitable Life

Annual Report and Accounts 2006

The Equitable Life Assurance Society

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Peter Smith, Deputy Chairman

Charles Thomson, Chief Executive

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Ian Brimecome, Non-executive Director

Ian Reynolds, Non-executive Director

Fred Shedden, Non-executive Director

Andrew Threadgold, Non-executive Director

Jean Wood, Non-executive Director

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Corporate Review

The Society's Chairman, Vanni Treves, and Chief Executive, Charles Thomson, on behalf of the Board, review 2006

Dear Members

We are pleased to tell you that, during the last twelve months, we have taken major strategic steps. In addition, we have continued our steady improvement in the financial security of the Society and this has allowed us to increase bonuses.

This year's report shows:

- Completion in February 2007 of the transfer of the bulk of our non-profit pension annuities to Canada Life, largely removing a significant risk from the with-profits fund;
- Agreement in March 2007 with Prudential, subject to policyholder and Court approval, to transfer £1.8 billion of with-profits annuity policies, enabling the annuitants to join an actively managed with-profits fund in a large and growing organisation;
- A further improvement in the Society's strength – our key measure of solvency, "Excess Realistic Assets", has improved to £884 million (2005: £669 million), representing 9.4% of the with-profits fund (2005: 6.6%);
- The continued improvement in the Society's financial position and the reduction in the risks that it faces have allowed an enhancement to the bonus that would otherwise have been payable;
- With-profits pension policy values have been increased by up to 5.0% p.a. in respect of 2006 (2005: 4.5% p.a.); and
- The interim bonus for 2007 on with-profits pension policies will be at the rate of up to 5.0% p.a. (2006: 3.5% p.a.).

Transfer of non-profit pension annuities to Canada Life

We wrote to members in May and October 2006 to explain the agreement we reached to transfer most of our non-profits pension annuity business to Canada Life Limited ("Canada Life"). The final transfer of about £4.2 billion of assets in February 2007 makes this the largest transfer of its kind in the UK to date. This was the first major step flowing from our review of strategic options for the future.

The competitive process we used enabled us to secure attractive terms for the transfer. The transfer was approved by the High Court in London on 1 February 2007 and the policies were transferred on 9 February 2007.

The transfer has greatly reduced exposure of the with-profits fund to the risk of unexpected and unquantifiable improvements in life expectancy. Consequently, we have been able to reduce the additional capital we are required to retain for that risk.

Transfer of with-profits annuity policies to Prudential

We wrote to members on 15 March 2007 to describe the agreement we have reached with The Prudential Assurance Company Limited ("Prudential").

The agreement represents another major phase in our strategic development, allowing with-profits annuitants to join Prudential's large, strong and actively managed long-term investment fund.

This will enable with-profits annuitants to benefit from a fund with much greater bonus earning potential than the Society can provide.

If members approve the transfer of with-profits annuities to Prudential, the Society's business will be simpler and the Board will be able to focus all its attention on the 80% of policyholders who remain. Our prospects of finding an attractive strategy for the benefit of the remaining policyholders will be significantly improved.

We plan to write again in September with more information about the proposal including the Independent Expert's report and details of the voting arrangements. In the meantime, we will put new information regarding the agreement to transfer with-profits annuities to Prudential on our website (www.equitable.co.uk) as it becomes available.

If it is approved by members, we expect to complete the transfer at the end of this year.

2006 Bonus declaration

During 2006, the Society achieved a gross return on the with-profits fund of 2.6%. This return reflects the rise in interest rates during the year which reduces the value of fixed-interest investments. However, the rise in interest rates also reduces the value of our liabilities. After adjusting for reductions in the value of the liabilities corresponding to the rise in interest rates, and also making allowances for expenses, tax and changes to provisions, the effective net return on the with-profits fund was 3.9%.

Throughout the past six years, the Society has, as you know, had a significant level of uncertainty in its provisions and, consequently, has had to hold substantial capital against the risks associated with that uncertainty. As an example of the Society's increased strength, our key measure of solvency, Excess Realistic Assets, has improved to £884 million at 31 December 2006 (2005: £669 million), representing 9.4% of the with-profits fund (2005: 6.6%). As a result of the removal of some risks and the reduction in others, the Board has enhanced the bonus figures, shown below, above those that would have been appropriate based on investment performance alone.

Further details of the factors affecting the Board's bonus decisions are given in the Financial Review.

The key decisions are:

- Policy values (or their equivalents) will be increased for UK with-profits pensions policies at a non-guaranteed accrual rate of 5.0% p.a. (2005: 4.5% p.a.) for the whole of 2006 (4.0% p.a. for UK life policies – 2005: 3.6% p.a.);
- A non-guaranteed interim bonus in 2007 of 5.0% p.a. for UK with-profits pensions policies (4.0% 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 2006.

As you are aware, part of the with-profits annuitants' share of the cost of Guaranteed Annuity Rates ("GARs") from 2000 remains unrecovered. The majority of with-profits annuity policies has a higher level of anticipated bonus than is achievable by a predominantly fixed-interest fund in the current low inflation environment so that, regrettably, income can be expected to fall year on year. The balance of the cost of the GARs allocated in 2000 to with-profits annuitants continues to be recovered by withholding 0.5% p.a.. This will apply to both the final bonus for 2006 and the interim bonus for 2007. This process continues as planned. For example, the non-guaranteed accrual rate of 5.0% p.a. mentioned above for 2006 will be applied as 4.5% p.a. for relevant with-profits annuities.

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

The financial adjustment applied to the early surrender of with-profits policies is 8.0%. This adjustment can be varied at any time and is kept under regular review.

Parliamentary Ombudsman and European Parliamentary Inquiry

In 2004, following strong criticisms of the regulators in Lord Penrose's report, the Society called on the Parliamentary Ombudsman ("PO") to reopen her independent inquiry into the regulation of Equitable Life. We have had lengthy and numerous 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 should, in any event, bring finality to this matter. Following a delay announced in the autumn, the report is currently expected to be published this year, before Parliament's summer recess.

In January 2006, the European Parliament set up a Committee of Inquiry into the regulation of Equitable Life. In particular, it is considering alleged contraventions of Community law and allegations of maladministration in the application of that law to Equitable Life. We have given all possible assistance to the Committee and your Chief Executive has attended the Committee on two occasions to give evidence and answer questions. The inquiry is not seeking to investigate the conduct of the Society's affairs but, rather, its UK regulation and the status of any claims by non-UK European citizens. The Committee plans to present its report to the European Parliament in July 2007.

University Life Assurance Society

University Life Assurance Society ("University Life") has been a subsidiary of Equitable Life since 1919. It has been closed to new business since 1976. It now has fewer than 2,000 policyholders and around £30 million in assets. We have agreed to sell University Life to Reliance Mutual Insurance Society Limited and the sale is expected to complete in the summer.

This is another step flowing from our strategic review – simplifying the business makes it easier to assess and implement strategic options.

Litigation

In 2004, a group of 873 with-profits annuitants commenced proceedings against the Society. 406 annuitants are still part of this action, the others having withdrawn. The trial itself is scheduled to take place early in 2008. Some of the claimants may have legitimate complaints that could be compensated under our normal procedures. However, we continue to resist any attempts by policyholders to obtain an unfair financial advantage at the expense of all other with-profits policyholders.

Governance

The Association of Mutual Insurers ("AMI") published guidance for mutual insurers in December 2005. Much of the guidance was already covered in the Society's practices, but we have published (in the corporate section of the Society's website) a member relations strategy which aims to help members of the Society to take an interest in its governance.

The member relations strategy is implemented by a member relations function, which provides answers to members in respect of corporate issues (whereas the customer services staff answer questions relating to members' policies) through a dedicated email address: member.relations@equitable.co.uk and through a special postal address: Member relations, Equitable Life Assurance Society, Warwick Court, Paternoster Square, London EC4M 7DX.

We will also propose amendments to the Society's Articles at the Annual General Meeting (AGM) in May 2007. These reflect changes in relevant legislation and developments in good practice in corporate governance (including the AMI's guidance). The proposals include reducing to 500 (from 1,000) the number of members needed to requisition a resolution to an AGM or to requisition an Extraordinary General Meeting.

During 2006, we issued to with-profits policyholders, together with their annual statements, a guide on how we manage the with-profits fund. This is a simpler, easier to follow version of the Principles and Practices of Financial Management ("PPFM") document which the Society has had in place since 2004. We also issued to with-profits policyholders reports by the Board and by the With-profits Actuary on compliance with the PPFM. In the interests of keeping costs down, we do not propose to issue these documents again unless there are material changes in them. However, the latest versions of all of these documents will continue to be available on the Society's website and, on request, to members.

Customer service

During 2006, we issued some 280,000 annual statements to inform policyholders of the progress of their policies and we also issued some 280,000 letters informing clients with pensions policies of the effects of the new rules for pensions, which came into force on 6 April 2006.

Our customer services staff dealt with around 400,000 telephone calls (2005: 340,000) and 550,000 letters (2005: 520,000) – many as a result of the new rules for pensions.

Strategic objectives

Particularly since the completion of the transfer of non-profit pension annuities to Canada Life, the fund is more stable and secure than it has been for many years. We continue to make progress in reducing operating expenses year on year. However, new regulations require the fund to remain predominantly invested in fixed-interest investments with limited potential to earn higher bonuses. We, therefore, continue to explore strategic options which might further improve the longer term prospects for policyholders. Our success in this area is demonstrated by the agreement reached with Prudential which will allow with-profits annuitants to move to a fund which has much greater investment freedom and higher bonus earning potential.

The Society's business objectives continue to include:

- Treating policyholders fairly, including leavers, and ensuring we meet the guarantees provided to policyholders by pursuing an appropriate investment strategy;
- Reducing expenses and restoring an efficient business model; and
- Resolving outstanding claims against the fund.

Your Board

As we reported last year, the greatly improved stability of the Society has allowed the Board to start to evolve – because of the turbulence of earlier years, it had largely been unchanged since 2001.

During the year, Ron Bullen and Michael Pickard, who between them served as Directors for a total of nine years, retired from the Board and we thank them for their outstanding contribution to the Society's development.

We are glad to welcome Ian Reynolds and Ian Brimecome who were appointed to the Board as non-executive Directors with effect from 1 October 2006 and 12 January 2007 respectively.

Ian Reynolds has over forty years' experience in the insurance industry and is currently a non-executive Director of HSBC Life Assurance and also a member of the Council of the Institute of Actuaries.

Ian Brimecome, formerly a non-executive Director of Winterthur UK Financial Services Group Limited, has over thirty years' experience in the financial services industry and is currently Chairman of Fox-Pitt Kelton Limited's Advisory Board. He has also recently been appointed a non-executive Director of AXA UK plc.

Looking forward

This review emphasises two things: the Society has continued to improve substantially its financial position and the security of policyholders; and we have delivered strategic opportunities with the potential for significantly improved prospects for policyholders.

The transfer of non-profit pension annuities to Canada Life much reduced a major mortality risk to the with-profits fund and the agreement with Prudential, if approved by members, would allow with-profits annuitants to join an actively managed with-profits fund in a large, strong organisation.

Once the transfer of with-profits annuity policies to Prudential is completed, we believe that there will be greater opportunities for further strategic options which can improve the outlook for the remaining policyholders.

As always, you may rest assured that your Board will continue to do everything it possibly can to improve the stability and the security of your Society and the prospects for all policyholders.

On behalf of the Society's Board of Directors.

Vanni Treves
Chairman

Charles Thomson
Chief Executive

Excess Realistic Assets and regulatory solvency

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

At 31 December 2006, Excess Realistic Assets were £884m, an increase of £215m over the prior year. The analysis of the with-profits assets and liabilities is as follows:

	2006 £m	2005 £m
Realistic value of with-profits assets	9,453	10,185
less:		
Policy values	7,559	8,181
Future charges	(288)	(300)
Impact of early surrenders	(50)	(46)
Cost of guarantees	566	847
Other long-term liabilities	406	482
Other liabilities	376	352
	8,569	9,516
Excess Realistic Assets	**884**	**669**

Notes:

The above analysis excludes the matching assets and liabilities of the Canada Life "deposit back" arrangement, as explained further on page 49.

A description of the above liabilities is set out in Note 16d on page 42.

The key movements in the Excess Realistic Assets during 2006 are shown in the following table:

	2006 £m	2005 £m
Opening Excess Realistic Assets	**669**	**455**
Favourable investment performance	69	465
Mortality experience and assumption changes	97	(275)
Surrender experience and assumption changes	28	(55)
Changes in other valuation assumptions	(12)	66
Variances in provisions and expenses	13	(3)
Other movements	20	16
Closing Excess Realistic Assets	**884**	**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 2006 represents 9.4% of with-profits realistic assets, an increase from the equivalent figure of 6.6% at 31 December 2005.

The policy value attributable to with-profits policies may include an element of non-guaranteed final bonus. A prudent allowance for future bonuses, based on assumed future net investment returns that take account of deductions for potential risks, is included in the valuation of the long-term business technical provision in these financial statements. Any enhancements to the bonuses assumed would be met from the Excess Realistic Assets.

In the first of the tables, the amount of £566m shown as the cost of guarantees relates to policy liabilities where the guarantees exceed policy values. At the balance sheet date, the total discounted value of aggregate guaranteed with-profits liabilities included within the realistic liabilities totalled £7,270m (2005: £8,302m). Discretionary amounts, which are assumed to be distributed along with the guaranteed amounts when contractual benefits are taken, are £586m (2005: £480m) 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.

The Society is required to hold the higher of regulatory and realistic capital. 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 accordingly 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. If the Society were to repay its subordinated debt, the CRR would equal available capital resources and the figure for net assets in excess of CRR would normally be zero. Subordinated debt provides additional capital and results in an excess over CRR. In situations where the regulatory excess of assets over liabilities is a positive value before bringing subordinated debt into account, the amount of realistic capital will be the relevant amount for the purposes of the FSA returns.

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.

	2006 £m	2005 £m
Excess Realistic Assets	884	669
Subordinated debt (note 1)	167	167
Reserving adjustments and disallowed assets (note 2)	132	52
Regulatory net assets	1,183	888
Capital Resources Requirement (CRR)	(1,016)	(721)
Net assets in excess of CRR	**167**	**167**

Notes:

1. For the purposes of regulatory reporting, the carrying value of the subordinated debt can be treated as capital. 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.

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.

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 an annual confidential assessment of its capital needs as required by 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 FSA has the power to require that a particular level of capital be held by the Society which could result in the Society considering 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.

Transfer of the bulk of the non-profit pension annuities

On 11 May 2006, the Society entered into various agreements with Canada Life, which led to the transfer of around 90% of the Society's non-profit pension annuities in payment. The actual transfer of those policies took place on 9 February 2007, following High Court approval of a Part VII scheme of arrangement. From 11 May 2006 to 9 February 2007, relevant annuities were subject to a reassurance arrangement under which Canada Life bore substantially all the risks and rewards from this business with effect from 1 January 2006. This transfer is reflected as "Outward reinsurance premiums – Discontinued operations" in the Profit and Loss Account and as an increase within the "Reinsurers' share of technical provisions" asset on the Group and Society Balance Sheets.

In order to protect the policyholders from a large counterparty credit exposure, the initial premium was deposited back with the Society until the transfer was approved by the High Court and completed. This deposit was held in assets with a similar investment mix to that previously held by the Society. Canada Life held a secured charge over those assets. The investment returns from those secured assets were attributed to Canada Life and payments of related annuities were deducted from the deposited assets. The net balance due to Canada Life at 31 December 2006, of £4,316m, is shown within "Deposits received from reinsurer – secured" as a new category of liability on the Group and Society Balance Sheets. This deposit back had the effect of increasing total assets and total liabilities of the Society and the Group by the deposited amount.

The transfer, together with expected related costs of £36m (including 2006 costs shown in Note 7b to the financial statements), does not reduce the amount of the Society's Excess Realistic Assets. In these financial statements, the business transferred is treated as discontinued operations within the Profit and Loss Account. Further details are provided in Notes 3 and 19 on pages 33 and 49 respectively.

Investment performance and capacity to pay bonuses

During 2006, 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-income securities 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 2.6% during the year, being impacted adversely by the rise in interest rates during the year, which reduced the value of fixed-income securities. The return adjusted for bond yield movements (which affect both assets and liabilities) was 5.2%, reducing to 3.9%, 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.

The Society sold £609m of indirect property holdings during the year. This action was taken to improve the liquidity of the property portfolio. Some of these proceeds have been re-invested in direct property investments and the Society continues to seek attractive opportunities to invest.

As reported in previous financial statements, a margin is held back from the investment return to meet the cost of guarantees and provide additional risk capital. 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. This margin can be reduced or increased depending on the financial position of the Society.

After consideration of all risks, reserving and capital matters, the Board has increased, for applicable with-profits pension policies for 2006, policy values at the rate of 5.0% p.a. (2005: 4.5% p.a.) and 4.0% p.a. (2005: 3.6% p.a.) for life assurance policies. This bonus includes a partial distribution of excess assets following the Society's continued improved financial strength and reduction of risks. The Board will keep the level of capital available under review, in order that further distributions reflect the circumstances and the risks facing the Society.

A non-guaranteed interim bonus will continue to be added to policy values (or their equivalents) in 2007 at a rate of 5.0% p.a. for pension policies (2006: 3.5% p.a.), and 4.0% p.a. for life policies (2006: 2.8% p.a.). 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 2006. 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..

The outstanding balance of the cost of GARs allocated in 2000 to with-profits annuities continues to be recovered by withholding 0.5% p.a.. This will apply to both the increase in policy values for 2006 and the interim bonus for 2007.

Expenses and provisions

Expenses shown in the Profit and Loss Account, incorporating administration, exceptional, claims, investment expenses and interest costs, have continued to reduce, from £127m in 2005 to £116m in 2006. Within non-exceptional expenses, lower administration and claims costs, reflecting reduced levels of activity as the with-profits fund reduces in size, were more than offset by the one-off costs of implementing the new pensions legislation in April 2006. Investment management expenses have continued to decline as the funds invested have reduced. Exceptional expenses have decreased significantly in 2006, principally reflecting the wind-down of the rectification and managed pension reviews and the third party litigation, partially offset by the costs incurred in implementing the strategic initiatives.

As shown in Note 16e 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 a further £17m, as a result of settlements made or finalised. The provision for exceptional expenses of £115m includes provision for future pension contributions in addition to the cost of 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 7 shows a favourable variance in provisions and expenses, taken together, of £13m. This reflects reductions in certain provisions, which offset the costs of pursuing alternative strategic solutions. Although the volume of transactions per policy is now more stable, 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. The cost of administration and investment management at 0.7% of realistic with-profits assets for 2006 is a key indicator of expenses. In order to take account of the uncertainty of future costs and the challenge of reducing costs as policies mature or transfer, administration expenses as a percentage of fund assets are allowed for at a rate of 1.0% p.a., and underruns below this level are held in reserve to cover expected future higher costs.

As previously reported, the Society was unable to reach agreement with HBOS over the initial premium payable in respect of the 2001 reassurance arrangement and the matter was referred to an independent umpire for resolution. The umpire issued his determination during the year, the resultant amount due and paid to HBOS being within the provision held by the Society for this matter. The matter has been subject to a further claim by HBOS which is pending judicial decision and could result in a further determination being necessary.

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 7 shows a net figure of £69m for favourable investment performance, representing the return in excess of the expected investment return assumed at the beginning of the year and includes total gains in equities, unit trusts and properties of £141m. This figure is stated after allowing for the impact of the distribution of capital made this year which is referred to in the section above, entitled "Investment performance and capacity to pay bonuses".

To remain consistent with a change to the valuation treatment which was required to be adopted in its regulatory reports, the Society has changed its accounting policy to value investments on a "bid-market" basis, rather than a "mid-market" basis. This has generated a one-off reduction in the value of investments and the balance of Excess Realistic Assets of £12m at 31 December 2006.

Following further analysis during the year of actual experience and following consideration of expected future experience, the Society has further modified its mortality assumptions, principally relating to the with-profits annuity business. Combined with actual experience of longevity being less than allowed for, these factors generated a resultant decrease of £97m in technical provisions, with a corresponding increase in Excess Realistic Assets.

Allowance has been made in realistic liabilities for future discretionary non-guaranteed bonuses. As noted previously, it is the Society's intention that any future bonuses will be in a non-guaranteed form. Allowance is made for continuing contractual commitments, such as the GIR of 3.5% p.a. that is applicable to many policies. If the Society's investment return falls below a rate which covers the guarantees and its expenses and the assumed retirement profile ceases to be appropriate as a result of significant numbers of policyholders deferring their retirement dates, substantially higher technical provisions may be required, as described in Note 16d to the financial statements.

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. The financial adjustment has remained at 8% since 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.

Although the Society experienced a stable level of claims during the year, with figures broadly in line with last year, changes in the pattern of surrenders have been reflected in the realistic assumptions which, together with favourable actual experience in the year, result in a gain of £28m in Excess Realistic Assets, as shown in the reconciliation table on page 7.

Proposed transfer of with-profits annuity policies to Prudential

Since the balance sheet date, the Society has announced it has entered into an agreement with The Prudential Assurance Company Limited for the transfer of all its with-profits annuity policies. On completion, expected to be by the end of 2007, approximately 62,000 with-profits annuities (representing some 50,000 annuitants) would be transferred. These policies represent about 20% of the with-profits liabilities with an estimated value of £1.8 billion as at 31 December 2006. The transfer is conditional on certain matters, including the approval of members and the High Court. The amount of assets to be transferred will be determined by reference to the Society's financial position at the date of transfer, after deducting the costs to implement the transfer and allowing for an allocation of the with-profits annuitants' share of the Excess Realistic Assets.

Equitable Life Finance plc

The payment of principal and interest and all other monies payable by Equitable Life Finance plc ("ELF"), a wholly owned subsidiary of the Society, in respect of the 8% Undated Subordinated Guaranteed Bonds ("the 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 and acceptances were received for £179m of bonds. As a result, there are now subordinated bonds with a principal value of £171m outstanding. ELF has the option to repay all (but not some only) of the Bonds on 6 August 2007 and each fifth anniversary thereafter.

If, when payment of interest in relation to the Bonds becomes due, the Society does not meet the 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 2006, 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.

University Life Assurance Society

On 20 December 2006, the Society agreed to sell the share capital of its subsidiary company, University Life Assurance Society ("ULAS") to Reliance Mutual Insurance Society Limited. The sale is expected to complete on 31 May 2007. At the year-end, ULAS had total assets of £36m, including shareholders' funds of £0.1m and the sale does not reduce the amount of the Society's Excess Realistic Assets.

The Board's conclusions on provisions and going concern

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

The Board has examined the issues relevant to the going concern basis which, 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 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, appropriate actions could be necessary to adjust maturity values, with-profits annuity payments and surrender values in order that policy guarantees can be met.

In addition, the Board has considered the potential additional claims referred to in Note 25 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.

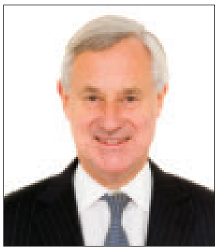
The Board has given due consideration to all the potential risks and possible actions set out above and has concluded that it remains appropriate to prepare these financial statements on a going concern basis.

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.

Board of Directors

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, Chairman) of six public companies, a statutory corporation and London Business School. Vanni is presently Chairman of Intertek Group plc and the National College of School Leadership and a Director of a number of other companies. Age 66.



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

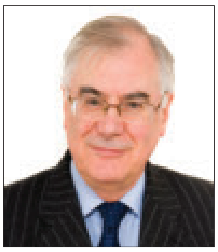
Peter Smith joined the Board in April 2001. He chairs the Audit Committee. He is Chairman of Savills plc and a non-executive Director of N M Rothschild & Sons Limited, Templeton Emerging Markets Investment Trust plc and Associated British Foods plc. He was Senior Partner of PricewaterhouseCoopers until June 2000. In June 2005, following completion of the acquisition by Aviva, he retired from the chairmanship and the board of RAC plc. Age 60.

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 58.

Ian Reynolds (a) (d)

Ian Reynolds, a Chartered Director, joined the Board in October 2006. He is a non-executive Director of HSBC Life Assurance and of Alternative Assets Opportunities, and is a Member of the Council of the Institute of Actuaries. He has over 40 years of experience in the insurance industry. He held the roles of UK Divisional Director and then General Manager Life at Commercial Union plc and a variety of posts at Royal Insurance. He has also worked as a special advisor at the Financial Services Authority and, since 2003, as a senior consultant at Beachcroft Regulatory Consulting. Age 63.



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 62.

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 63.

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 67.

Ian Brimecome (d)

Ian Brimecome joined the Board in January 2007. He is Chairman of Fox-Pitt Kelton Limited's Advisory Board and a non-executive Director of AXA UK plc. He was a non-executive Director of Winterthur UK Financial Services Group Limited until December 2006. He has over 30 years of experience of the financial services industry in a wide variety of roles. He has advised on more than eighty merger and acquisition transactions in the insurance and asset management industries in more than twenty countries. He is an Associate of the Institute of Financial Services and a Member of the Institute of Management. Age 53.

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 64.

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 2006 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 27. The operations of the Group are described in the Corporate Review and Financial Review on pages 2 to 6 and 7 to 13 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 2006. There is no guaranteed bonus for 2006, 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 5.0% p.a. for 2006 (4.0% p.a. for UK life policies and 4.6% p.a. for the Personal Pension 2000 product). The 2006 bonus decision is dealt with in greater detail in the Corporate Review on page 3.

Directors

The Directors shown on pages 14 and 15 were Directors throughout the year, except for Ian Reynolds (appointed 1 October 2006) and Ian Brimecome (appointed 12 January 2007). In addition, Ron Bullen and Michael Pickard were Directors until their resignations on 31 October 2006. The Directors retiring at the Annual General Meeting (AGM) by rotation are Fred Shedden and Jean Wood, who offer themselves for re-election. As Ian Reynolds and Ian Brimecome have been appointed as Directors of the Society since the last AGM, in accordance with Regulation 40 of the Articles of Association, they will both retire at the AGM and seek re-election.

Subordinated debt

In 1997, the Society's wholly-owned subsidiary, Equitable Life Finance plc, issued £350m 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, the Society repurchased Bonds in January 2005, representing a principal value of £179m 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 £179m.

Subject to certain conditions, Equitable Life Finance plc has the right to redeem the remaining Bonds, at par, on 6 August 2007. Were this redemption to take place, the Society would repay the remaining loan to Equitable Life Finance plc.

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 pages 20 and 21 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

Vanni Treves

Vanni Treves
Chairman
28 March 2007

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.

The Myners Review of the Governance of Life Mutuals, which reported in December 2004, recommended that an annotated version of the Combined Code suitable for life mutuals should be produced. This was taken forward by the Association of Mutual Insurers ("AMI") and the Association of Friendly Societies ("AFS") and The Combined Code on Corporate Governance – An Annotated Version for Mutual Insurers ("The Annotated Code") was published in July 2005. Mutual insurers who are members of the AMI, as is the Society, are required to adhere to this Annotated Code for all financial years beginning on or after 1 April 2005. The Society has adopted the relevant provisions of the Annotated Code.

Reference is made in this report to the provisions of the Combined Code and of the Annotated Code, where the latter extends the relevant provisions of the Combined Code.

This report summarises the Society's governance arrangements.

2. Governance by Directors

The Board

The Board meets regularly to lead, control and monitor the overall performance of the Society. The Board's principal functions are to determine the strategy and policies of the Society, to set out guidelines within which the business is managed and to review business performance. The Board considers and decides on all major matters of Group corporate strategy. There is a formal schedule of matters reserved for the Board's decision. 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.

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 14 and 15.

Some 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 22 to 24 explains the basis of remuneration of the executive and non-executive Directors.

Performance evaluation

During 2006, 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's 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 four 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 Audit Committee has indicated that any Director may attend its meetings if he or she wishes, and this opportunity has been taken up.

The Investment Committee

Andrew Threadgold chairs the Investment Committee, currently comprising six 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. 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 22 to 24.

The Combined Code states that the Remuneration Committee should have

	Board	Audit Committee	Investment Committee	Legal Audit Committee	Nominations Committee	Remuneration Committee
Number of meetings during 2006	11	6	6	5	2	5
Attendance by directors†						
Vanni Treves	11	5	–	5	2	5
Peter Smith	10	6	–	5	2	4
Charles Thomson	11	–	6	5	2	–
David Adams	9	6	5	–	–	–
Ron Bullen*	9	5	–	–	–	–
Michael Pickard*	9	6	5	–	–	–
Ian Reynolds**	3	1	1	–	–	–
Fred Shedden	11	–	6	5	–	–
Andrew Threadgold	11	–	5	–	–	–
Jean Wood	10	–	6	–	–	5

†see pages 14 and 15 for details of committee membership.

* Ron Bullen and Michael Pickard resigned as Directors of the Society on 31 October 2006.

** Ian Reynolds was appointed a Director of the Society with effect from 1 October 2006.

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 assists the Board in ensuring that the composition of the Board is appropriate to govern the Society effectively, that suitable candidates are identified to fill vacancies or to add to the strength of the Board and that the Society, wherever possible, meets the relevant principles and provisions of the Combined Code and the Annotated Code. The Committee also reviews, on an ongoing basis, the appropriateness and suitability of each Director for continuing membership of the Board. 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.

The Board appointed Ian Reynolds as a non-executive Director with effect from 1 October 2006 and Ian Brimecome as a non-executive Director with effect from 12 January 2007. The Board's intention to make appointments of new non-executive Directors was announced in the Annual Report and Accounts/Summary Financial Statements 2005 issued to members in April 2006. It included the Board's intention to use a search consultancy to interview candidates and make suitable recommendations. It also included an invitation to anyone who believed he or she could add substantial value to the Board to put his or her name forward for consideration in the process.

Board and Committee meetings

Details of the number of meetings of the Board and attendance by Directors are given on page 18. Details of the number of meetings of committees of the Board and attendance by members of those committees are also on page 18.

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 (one of whom is a Director of the Society) and its Chairman is Michael Pickard (who is a former Director of the Society).

The Society announced on 20 December 2006 that it has agreed to sell University Life to Reliance Mutual Insurance Society Limited. This sale is expected to complete on 31 May 2007.

Equitable Life Finance plc issued and manages £350m 8% Undated Subordinated Guaranteed Bonds, the proceeds of which are lent to the Society. In January 2005, following offers to Bondholders, the Society repurchased £179m of the bonds. As a result there are now subordinated bonds with a principal value of £171m outstanding. Subject to certain conditions, Equitable Life Finance plc has the right to redeem the remaining bonds, at par, on 6 August 2007. 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. Tim Bateman holds the roles of With-profits Actuary and Head of Actuarial Function.

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. 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 2006. A copy of this report will be available on the Society's website and, on request, to members.

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.

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 2006 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; and
- 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; and
- 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 the FSA's Handbook.

There is a discussion in the Financial Review on pages 7 to 13 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 the results of the risk assessment and other significant changes to risks to the Risk Committee, Audit Committee, Investment Committee and the Board.

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 20 – 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; and
- 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.

At the 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.

During 2006, the Board adopted a member relations strategy. The purpose of this strategy is to help members of the Society to take an interest in its governance. The strategy is available in the Corporate Governance section of the Society's website.

The member relations function within the Society implements the member relations strategy on behalf of the Chairman and the Chief Executive.

The member relations function is responsible for the provision of realistic, appropriate and proportionate information to members and for organising the Annual General Meeting.

The member relations function provides answers to members in respect of corporate issues (whereas the customer services staff answer questions relating to members' policies). The member relations function is accessible to members through a dedicated e-mail address: member.relations@equitable.co.uk and through a special postal address: Member Relations, The Equitable Life Assurance Society, Warwick Court, Paternoster Square, London EC4M 7DX.

In order to understand the views of members, the Board has during the year commissioned market research among members. The Board has always sought to keep all relevant stakeholders informed on all major issues and, during the year, letters were sent to all members covering key issues – for example, the Interim Review, the agreement with Canada Life, and Pensions Simplification.

The member relations strategy is reviewed annually by the Board who also receive reports on issues raised, feedback from members and recommendations for improvement.

6. Going concern

As noted in Note 1 to the financial statements on page 30, 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 13.

7. Remuneration Report

The composition and responsibilities of the Society's Remuneration Committee are set out on pages 18 and 19. 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 Annotated Code. 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. KPMG has undertaken additional engagements for the Society, including advice on accounting standards and providing an Independent Expert in respect of the transfer of most of the Society's non-profit annuity business to Canada Life. The Committee considers both KPMG and Towers Perrin to be independent. KPMG and Towers Perrin had no other connections with the Society.

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

Non-executive Directors	Notes	2006 £	2005 £
V E Treves, Chairman	1	140,000	140,000
Other non-executive Directors	2		
P A Smith		38,000	38,000
D H Adams OBE		33,000	33,000
R Bullen	3	23,333	28,000
M J Pickard	3	27,500	33,000
D I W Reynolds	4	7,000	–
F Shedden		33,000	33,000
A R Threadgold		33,000	33,000
J Wood		33,000	33,000
		227,833	231,000
Total for non-executive Directors		**367,833**	**371,000**

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); A R Threadgold (Chairman, Investment Committee); F Shedden (Chairman, Legal Audit Committee); J Wood (Chairman, Remuneration Committee) and D H Adams (Deputy Chairman, Audit Committee). P A Smith (Deputy Chairman and Chairman of Audit Committee) has received an additional fee of £10,000 p.a..
3. R Bullen and M J Pickard resigned as Directors on 31 October 2006.
4. D I W Reynolds was appointed a Director with effect from 1 October 2006.

Executive Directors

Salary and bonuses

	Salary		Performance Related Bonus		Benefits		Total	
	2006	2005	2006	2005	2006	2005	2006	2005
	£	£	£	£	£	£	£	£
Charles Thomson	436,450	419,662	129,000	184,196	107,101	102,544	672,551	706,402
Total for executive Directors	**436,450**	**419,662**	**129,000**	**184,196**	**107,101**	**102,544**	**672,551**	**706,402**

C G Thomson's annual rate of salary for the period 1 January to 30 June 2006 was £430,000 plus annual benefits of £88,050. His annual rate of salary was increased to £442,900 with effect from 1 July 2006, with annual benefits remaining at the same level. In addition, benefits in kind received in 2006 totalled £19,051.

The maximum potential annual discretionary bonus award he may receive is 50% of his salary. For 2006/2007 the Remuneration Committee has recommended to the Board that the amount of C G Thomson's discretionary bonus award should be £199,305 and be paid in June 2007.

Long-term retention scheme

	2006	2005
	£	£
Charles Thomson	149,653	281,250

C G Thomson participated in an annual retention bonus scheme for senior staff. 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. Under extensions to that scheme, further amounts of £75,000 and £50,000 were payable provided C G Thomson remained in the service of the Society on 31 December 2005 and 30 June 2006 respectively. These amounts were paid as due.

A new retention bonus scheme for senior staff was introduced in September 2006 under which C G Thomson is eligible to receive payments equal to the following percentages of his then prevailing salary on the dates below, provided he remains in the Society's employment on the relevant date:

- 22.5% on 31 December 2006;
- 22.5% on 30 June 2007;
- 30% on 31 December 2007; and
- up to 75% on 31 December 2008.

The amount of the final bonus entitlement accruing on 31 December 2008 will be at the discretion of the Remuneration Committee (who will determine the amount of the final payment depending on the prevailing financial and operational conditions and strategy of the Society).

In accordance with the new scheme, C G Thomson received a bonus of £99,653 in December 2006.

Benefits

Executive Directors' benefits include a car allowance and payments in lieu of pension contributions. The executive Director has no accrued pension entitlements (2005 – 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 22.

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 Combined and Annotated Codes and AMI guidance

Combined and Annotated Codes

The Board considers the Society has applied the relevant principles and has complied with all the relevant provisions of the Combined Code and the Annotated Code (and associated guidance) throughout the year except for the matters explained in this report and summarised below. The Board does not regard the exceptions as a material departure from the principles and provisions of the Combined Code and the Annotated Code:

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.

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.

AMI guidance

The Society has, in some instances, not complied with the guidance on the Annotated Code issued by the AMI in December 2005, or in some cases not throughout the year in question. These instances are as follows:

The Society's Articles of Association currently require at least 1,000 members (eligible to vote at General Meetings) to requisition a resolution to be put to an AGM or to requisition a General Meeting, whereas the AMI guidance specifies 500 members as a reasonable requirement. Changes to the Articles to bring them in line with the AMI guidance are being proposed at the AGM.

The Board did not consider it appropriate or practical to hold a vote of members on the sale of most of its non-profit annuity book of business to Canada Life. The non-profit annuitants' benefits were not affected by the transfer and the annuitants were not members of the Society (in respect of those benefits). Furthermore, reassurance arrangements needed to be in place before the transaction was announced. The transfer was subject to the scrutiny of an Independent Expert and the FSA together with the approval of the High Court – where members and other policyholders were able to lodge any objections to the transaction with the Court.

A specimen letter of appointment of non-executive directors now appears on the Society's website but it did not appear throughout the year in question.

The Society's member relations strategy now appears on the Society's website but the member relations function and the member relations strategy were not fully in place and the member relations strategy did not appear on the website throughout the year in question.

Directors' responsibilities in respect of the financial statements

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 result of 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; and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business (see page 13 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 enable them to ensure 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 Society and to prevent and detect fraud and other irregularities.

The financial statements are published on the Society's website (www.equitable.co.uk). 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 the legislation in other jurisdictions.

Statement of disclosure of information to auditors

As far as the Directors are aware, there is no relevant audit information of which the Group's auditors are unaware. The Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

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 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.

We also, at the request of the Directors, review whether the Corporate Governance Statement reflects the Society's compliance with the eight provisions of the Annotated Combined Code for Mutual Insurers (2005) specified for our review by the Association of Mutual Insurers, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

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 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 2006 and of the Group's result for the year then ended;
- have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

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 25 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
28 March 2007

Technical account – long-term business

	Notes	Group 2006 £m	Group 2005 £m
Earned premiums, net of reinsurance			
Gross premiums written	2a	177	210
Outward reinsurance premiums	3		
– Continuing operations		(109)	(98)
– Discontinued operations		(4,608)	–
		(4,540)	112
Investment income	4a	1,060	990
Unrealised gains on investments	4c	–	459
Other technical income	5a	9	9
		(3,471)	1,570
Claims incurred, net of reinsurance			
Claims paid – gross amount	6	1,676	1,643
Reinsurers' share	3	(626)	(268)
		1,050	1,375
Change in provision for claims – gross amount	6, 16b	13	(5)
		1,063	1,370
Changes in other technical provisions, net of reinsurance			
Long-term business provision – gross amount	16b	(1,240)	72
Reinsurers' share	3	(3,530)	(45)
		(4,770)	27
Comprising – Continuing operations		*(798)*	*(275)*
– Discontinued operations		*(3,972)*	*302*
Technical provisions for linked liabilities – gross amount	16b	17	300
Reinsurers' share	3	(671)	(255)
		(654)	45
Comprising – Continuing operations		*(4)*	*4*
– Discontinued operations		*(650)*	*41*
Net operating expenses – non-exceptional	7a	55	51
Net operating expenses – exceptional	7b	28	46
Net operating expenses		83	97
Investment expenses including interest	4b	30	27
Other technical charges	5b	19	2
Unrealised losses on investments	4c	744	–
Taxation attributable to the long-term business	9a	13	2
Transfer to the fund for future appropriations	15	1	–
		890	128
		(3,471)	1,570
Balance on the Technical Account		**–**	**–**

All significant recognised gains and losses are dealt with in the Profit and Loss Account. The Notes on pages 30 to 52 form an integral part of these financial statements.

Balance Sheets

As at 31 December 2006

Assets

	Notes	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Investments					
Land and buildings	10a	840	714	837	710
Investments in group undertakings	10b	–	–	19	17
Other financial investments	10c	13,099	13,642	13,051	13,596
		13,939	14,356	13,907	14,323
Assets held to cover linked liabilities	11	87	741	87	741
Reinsurers' share of technical provisions					
Long-term business provision		3,950	420	3,950	420
Technical provisions for linked liabilities		3,240	2,569	3,240	2,569
		7,190	2,989	7,190	2,989
Debtors	12				
Debtors arising out of direct insurance operations		31	30	31	30
Other debtors		48	32	47	34
		79	62	78	64
Other assets					
Cash at bank and in hand		16	13	11	9
Prepayments and accrued income					
Accrued interest and rent		208	209	207	209
Other prepayments and accrued income	13	111	143	111	143
		319	352	318	352
Total assets		**21,630**	**18,513**	**21,591**	**18,478**

The Notes on pages 30 to 52 form an integral part of these financial statements.

Liabilities

	Notes	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Subordinated liabilities	14	171	171	167	167
Fund for Future Appropriations	15	10	9	–	–
Technical provisions					
Long-term business provision – gross amount		13,611	14,851	13,587	14,826
Claims outstanding		15	2	15	2
		13,626	14,853	13,602	14,828
Linked liabilities		3,327	3,310	3,326	3,310
	16a, 17g	16,953	18,163	16,928	18,138
Provisions for other risks and charges	18	37	50	36	50
Creditors					
Creditors arising out of direct insurance operations		47	42	47	41
Deposits received from reinsurer – secured	19	4,316	–	4,316	–
Creditors arising out of reinsurance operations		25	2	25	2
Amounts owed to credit institutions	20a	19	19	19	19
Other creditors including taxation and social security	20b	20	27	27	36
		4,427	90	4,434	98
Accruals and deferred income		32	30	26	25
Total liabilities		**21,630**	**18,513**	**21,591**	**18,478**

These financial statements were approved by the Board on 28 March 2007 and were signed on its behalf by:

Vanni Treves
Chairman

Charles Thomson
Chief Executive

The Notes on pages 30 to 52 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. 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 13.

Where relevant, Profit and Loss Account line items are analysed separately between continuing and discontinued operations. An explanation of the discontinued operations is provided in Note 3.

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

The Group has modified the way in which investment assets are valued at the balance sheet date by using bid value market prices rather than mid-market prices. This change has been made in order to bring the basis of valuation into line with a similar change for the annual FSA regulatory returns. Due to the limited impact of this change, the Group has not restated the financial statements for 2005.

The Directors have reviewed the accounting policies and satisfied themselves as to their appropriateness. Other than the change in valuing investments, there are no other changes in accounting policy 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 reassurance premiums are recognised when payable. Reassurance recoveries are credited to match the relevant gross claims.

Investment income

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 Assurance Society, 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. 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 and units in unit trusts are valued 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; and
- 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 rules contained in The FSA Handbook of Rules and Guidance. 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. This 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.

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 the shareholder's funds. The FFA for University Life represents the balance shown in the Group financial statements.

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

	Group 2006 £m	Group 2005 £m
a. Analyses of gross premiums written are as follows:		
Individual premiums	152	184
Premiums under group contracts	25	26
	177	**210**
Regular premiums	116	123
Single premiums	61	87
	177	**210**
Premiums from non-profit contracts	49	50
Premiums from with-profits contracts	56	79
Premiums from linked contracts	72	81
	177	**210**
Premiums from life business	44	53
Premiums from annuity business	1	3
Premiums from pension business	132	154
	177	**210**
Premiums from UK business	173	205
Premiums from overseas business	4	5
	177	**210**
b. Gross new business premiums		
Individual premiums	77	94
Premiums under group contracts	6	6
	83	**100**
Regular premiums	22	12
Single premiums	61	88
	83	**100**
Premiums from non-profit contracts	23	23
Premiums from with-profits contracts	30	46
Premiums from linked contracts	30	31
	83	**100**
Premiums from life business	1	–
Premiums from annuity business	1	2
Premiums from pension business	81	98
	83	**100**
Premiums from UK business	83	100
Premiums from overseas business	–	–
	83	**100**

Annual equivalent premiums in respect of new business received during the year were £27m (2005: £21m). New premiums in respect of reassured business during the year were £30m (2005: £31m).

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

3. Outward reinsurance premiums

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

Premiums 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.

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

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

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

The reinsurance balance, as required to be disclosed by the Companies Act 1985, and as defined by the SORP, which represents the aggregate total of all those items included in the technical account which relate to reassurance transactions, net of related gains of £101m (2005: £465m), is a net credit of £9m (2005: £5m).

4. Total investment return

	Group	
	2006 £m	2005 £m
a. Investment income comprises income from:		
Land and buildings	33	41
Other investments	751	770
	784	811
Gains on realisation of investments	276	179
	1,060	**990**
b. Investment expenses including interest comprise:		
Investment management expenses	14	16
Interest charges on loans	16	14
Gain on the repurchase of subordinated bonds	–	(3)
	30	**27**
c. Investment activity account		
Investment income	784	811
Realised investment gains	276	179
Unrealised investment (losses)/gains	(744)	459
	316	1,449
Investment management expenses and charges	(30)	(27)
Investment return for the year	**286**	**1,422**

At 31 December 2006, the Group modified the basis used to value listed investments from a mid-market price basis to a bid price basis. This change has been made in order to maintain consistency between these financial statements and the FSA regulatory returns, where a similar change is required.

The effect of this change at 31 December 2006 was to reduce Balance Sheet investment values by £12m, which is reflected in unrealised losses. An equivalent reduction for 2005 would have been £13m.

5. Other technical income and charges

	Group 2006 £m	Group 2005 £m
a. Other technical income comprises:		
Income from non-insurance business	2	5
Other income	7	4
	9	**9**

b. Other technical charges:

Other technical charges of £19m (2005: £2m) comprise expenses for non-insurance business of subsidiary companies of £nil (2005: £2m) and the net return payable on a secured deposit received from Canada Life of £19m (2005: £nil).

6. Claims incurred – gross

	Group 2006 £m	Group 2005 £m
Claims paid – gross amount	1,676	1,643
Change in provision for claims	13	(5)
Gross claims	**1,689**	**1,638**

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

	Group 2006 £m	Group 2005 £m
Gross claims paid comprise:		
On death	45	49
On maturity	548	509
On surrender	514	482
By way of periodic payments	579	595
Claims handling expenses	3	3
	1,689	**1,638**
Life and annuity business	165	180
Pension business	1,521	1,455
Claims handling expenses	3	3
	1,689	**1,638**
Linked business	342	285
Non-profit business	336	353
With-profits business	1,008	997
Claims handling expenses	3	3
	1,689	**1,638**
UK business	1,655	1,591
Overseas business	31	44
Claims handling expenses	3	3
	1,689	**1,638**

Included in the above payments are attributable final and interim bonuses for the Society and University Life of £47m (2005: £39m). The gross claims incurred include £306m (2005: £310m) relating to the discontinued operations transferred to Canada Life on 9 February 2007 as described in Note 3.

7. Net operating expenses

	Group 2006 £m	Group 2005 £m
a. Non-exceptional		
Administrative expenses	**55**	**51**

b. Exceptional

The Group incurred the following exceptional expenses during the year:

	Group 2006 £m	Group 2005 £m
Rectification and other GAR-related expenses	2	14
Costs of pursuing litigation against third parties	–	23
Pension costs for former staff	5	3
Costs of strategic initiatives	18	–
Other projects	3	6
	28	**46**

As explained in the Financial Review on page 9, the greater part of the expenses of strategic initiatives incurred during the year represents the cost of implementing the arrangements with Canada Life. The litigation costs in 2005 include an amount of £1m for litigation support services as detailed in Note 7c, within the table of non-audit fees payable to PricewaterhouseCoopers LLP (PwC).

c. Services from auditors

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

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

	Group 2006 £m	Group 2005 £m
Fees payable for the audit of the Society and Group accounts	1.0	1.2
Fees payable to the Society's auditor and its associates for other services:		
Other services pursuant to legislation	0.2	0.2
Tax services	0.1	0.1
All other services, including litigation support	0.3	1.8
	1.6	**3.3**

8. Directors and employees

	Group 2006 £m	Group 2005 £m
a. Staff costs		
Wages and salaries	4	4
Social security costs	1	1
	5	**5**

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 28 (2005: 26). In addition, the Society employs a number of contractors and, under its agreement with HBOS, uses the services of HBOS staff.

b. Emoluments of Directors

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

c. Former staff pension arrangements

As a result of contractual commitments arising as part of the agreement entered into with HBOS in March 2001, when the Society sold its administrative and sales operations, the Society meets the major part of the funding in respect of the pension schemes for those staff that transferred to the employment of HBOS as a result of the sale transaction. An amount of £34m (2005: £48m) is provided in respect of the contractual commitment to HBOS in relation to the defined benefit scheme, following the triennial actuarial valuation performed as at 31 December 2004, as modified for relevant changes to the balance sheet date. An additional provision of £45m (2005: £59m), representing an estimate of the current value of the contractual commitment to HBOS in respect of future service costs over the next 10 years (2005: 11 years), is included within technical provisions for long-term business.

9. Taxation

	Group 2006 £m	Group 2005 £m
a. Taxation charged to the technical account		
UK corporation tax		
Current tax on income for the period	10	12
Adjustments in respect of previous years	(1)	(12)
	9	–
Foreign tax		
Current tax on income for the period	3	–
Deferred tax		
Unrealised gains on investments	1	1
Deferred expenses carried forward	–	1
	1	2
Total charge	**13**	**2**

The UK corporation tax charge is provided at rates between 20% and 22% (2005: 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	
	2006 £m	2005 £m	2006 £m	2005 £m
b. Deferred taxation				
Provided in the financial statements:				
Deferred tax of the long-term fund				
Unrealised appreciation in investments	**(3)**	**(2)**	**(3)**	**(2)**

10. Non-linked investments

	Current Value		Cost	
	2006 £m	2005 £m	2006 £m	2005 £m
a. Land and buildings				
Group				
Leasehold	203	170	136	114
Freehold	637	544	449	403
	840	**714**	**585**	**517**
Society				
Leasehold	203	170	136	114
Freehold	634	540	445	399
	837	**710**	**581**	**513**

Independent professional valuers have valued the Group's and the Society's properties individually at the balance sheet date. The properties are included in these financial statements at those valuations. The valuations of commercial properties were carried out by Jones Lang Lasalle. The Group also invests indirectly in property through specialised unit trusts, which are classified as other financial investments (see Note 10c). Total property-related investments at 31 December 2006 are £1,080m (2005: £1,511m).

	Current Value		Cost	
	2006 £m	2005 £m	2006 £m	2005 £m
b. Investments in Group undertakings				
Society				
Shares	**19**	**17**	**24**	**19**

	Current Value		Cost	
	2006 £m	2005 £m	2006 £m	2005 £m
c. Other financial investments				
Group				
Shares and other variable yield securities and units in unit trusts (1)	569	1,194	574	1,001
Debt and other fixed-income securities (2)	11,972	12,096	11,733	11,467
Loans secured by mortgages	2	2	2	2
Loans secured by policies	1	1	1	1
Deposits with credit institutions	555	349	562	355
	13,099	**13,642**	**12,872**	**12,826**

10. Non-linked investments (continued)

c. Other financial investments (continued)

Society

	Current Value		Cost	
	2006 £m	2005 £m	2006 £m	2005 £m
Shares and other variable yield securities and units in unit trusts [1]	544	1,172	548	980
Debt and other fixed-income securities [2]	11,952	12,073	11,712	11,445
Loans secured by mortgages	2	2	2	2
Loans secured by policies	1	1	1	1
Deposits with credit institutions	552	348	558	354
	13,051	**13,596**	**12,821**	**12,782**

Notes:

1. Includes listed investments of £194m (2005: £179m) for the Group and £182m (2005: £167m) for the Society at current value.
2. Includes listed investments of £11,326m (2005: £12,070m) for the Group and £11,306m (2005: £12,048m) for the Society at current value.

Investments of £2,204m (2005: £3,717m), which were lent in the normal course of business to authorised money brokers on a secured basis, are included in other financial investments. Similar investments of £2,256m (2005: £3,906m) were received as collateral from brokers. Income earned on stock lending during the year, net of fees paid, was £1m (2005: £2m).

The agreement entered into with Canada Life on 11 May 2006 included reassurance of non-profit annuities with a deposit back arrangement. The amount deposited with the Society was equal to the value of the non-profit annuity business ceded and was £4,316m at 31 December 2006. There was a charge over the Society's investments to the value of the deposit received from the reinsurer, at the balance sheet date. This charge was released after the transfer of assets following Court approval of the Part VII Transfer under the Financial Services and Markets Act 2000 in February 2007. This deposit back arrangement had the effect of increasing the Group's and Society's total assets and total liabilities by the deposited amount.

11. Assets held to cover linked liabilities

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
Current value of linked assets	**87**	**741**	**87**	**741**

The cost of assets held to cover linked liabilities is £80m (2005: £523m) for the Group and £80m (2005: £523m) for the Society. For the Society, assets relate to index-linked business only.

12. Debtors

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
Debtors arising out of direct insurance operations				
Amounts owed by policyholders	31	30	31	30
Other debtors				
Debtors other than Group and related companies	38	31	37	30
Outstanding sales of investments	10	1	10	1
Balances with Group companies	–	–	–	3
	48	32	47	34
	79	**62**	**78**	**64**

13. Other prepayments and accrued income

	Group		Society	
	2006	2005	2006	2005
	£m	£m	£m	£m
Prepayments	**111**	**143**	**111**	**143**

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

14. Subordinated liabilities

	Group		Society	
	2006	2005	2006	2005
	£m	£m	£m	£m
Amounts falling due after more than five years	**171**	**171**	**167**	**167**

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 and subject to satisfying certain conditions and obtaining regulatory approval.

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.

15. Fund for Future Appropriations

	Group		Society	
	2006	2005	2006	2005
	£m	£m	£m	£m
At 1 January	9	9	–	–
Transfer from the Profit and Loss Account	1	–	–	–
At 31 December	**10**	**9**	**–**	**–**

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. The FFA for University Life represents the balance shown in the Group accounts.

16. Technical provisions

a. Gross technical provisions	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Non-profit technical provisions	4,534	5,018	4,521	5,005
With-profits technical provisions				
Policy values	7,559	8,181	7,559	8,181
Future charges	(288)	(300)	(288)	(300)
Impact of early surrenders	(50)	(46)	(50)	(46)
Cost of guarantees	566	847	566	847
Other long-term liabilities	406	482	395	470
	8,193	9,164	8,182	9,152
Excess Realistic Assets	884	669	884	669
Total with-profits technical provisions	9,077	9,833	9,066	9,821
Long-term business provision	**13,611**	**14,851**	**13,587**	**14,826**
Claims outstanding	**15**	**2**	**15**	**2**
Index-linked annuities	707	743	707	743
Other linked business	2,620	2,567	2,619	2,567
Linked liabilities	**3,327**	**3,310**	**3,326**	**3,310**
	16,953	**18,163**	**16,928**	**18,138**

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 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At 1 January	18,163	17,796	18,138	17,771
Change in long-term business provision	(1,240)	72	(1,239)	72
Change in provision for claims	13	(5)	13	(5)
Change in technical provisions for linked liabilities	17	300	16	300
At 31 December	**16,953**	**18,163**	**16,928**	**18,138**

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

The technical provisions in respect of the majority of non-profit and index-linked annuities were wholly reassured with Canada Life prior to a Part VII Transfer. Some non-profit business (relating to business other than non-profit and index-linked annuities) is 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.

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

Class of business	Interest rate % 2006	Interest rate % 2005	Future expense allowance 2006	Future expense allowance 2005
Non-profit annuities in payment				
Basic Life and General Annuity business – pre 1992	4.70	4.20	£24 p.a.	£24 p.a.
Basic Life and General Annuity business – post 1991	4.20	3.70	£24 p.a.	£24 p.a.
Pension business reassured with Canada Life	4.75	4.20	£24 p.a.	£24 p.a.
Retained pension business	4.70	4.20	£24 p.a.	£24 p.a.
Index-linked annuities in payment				
Basic Life and General Annuity business – pre 1992	1.48	1.50	£24 p.a.	£24 p.a.
Basic Life and General Annuity business – post 1991	1.23	1.25	£24 p.a.	£24 p.a.
Pension business reassured with Canada Life	1.60	1.50	£24 p.a.	£24 p.a.
Retained pension business	1.48	1.50	£24 p.a.	£24 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 increased during 2006 and the valuation interest rates have also increased. The changes to the valuation interest rates in aggregate have reduced the index-linked annuity provision by £7m and decreased the non-profit technical provisions by £225m. Similarly, the market value of the backing assets has decreased as yields have changed and this offsets a large proportion of the change in technical provisions. Future expenses in respect of non-profit and index-linked annuities in payment are allowed for in two ways – an explicit per policy allowance, increasing by 3.0% p.a. (2005: 2.75% p.a.) and an expense allowance for fund management, expressed as a percentage of the value of the fund, of 0.06% p.a. (2005: 0.06% p.a.). The amount allowed for expenses has been assumed to increase by an additional 4.0% p.a. (2005: 2.75% p.a.) to allow for diseconomies of scale in respect of policies not reassured to Canada Life, 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. The Society continues to make allowance for future improvements in longevity of annuitants. The Society's valuation has been carried out using recently published mortality tables and an investigation into the Society's actual mortality experience. The overall effect of this review has been to decrease index-linked annuity and non-profit annuity technical provisions by £11m (2005: increase of £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 £152m (2005: £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 (2005: 10 months).

16. Technical provisions (continued)

c. The long-term business provision – index-linked annuities and non-profit business (continued)

Mortality assumptions by class of business	2006	2005
Non-profit and index-linked annuities in payment		
Basic Life and General Annuity business	75.0% IML00 ult (U=2006)* for males	77.5% IMA92 (U=2005) for males
	80.0% IFL00 ult (U=2006)* for females	82.5% IFA92 (U=2005) for females
Pension business	82.5% PNMA00MC (U=2009)** for males	82.5% PMA92MC (U=2008) for males
(both reassured and retained business)	82.5% PNFA00MC (U=2009)** for females	82.5% PFA92MC (U=2008) for females

Notes:

* the allowance for future mortality improvements for IML00/IFL00 ult (U=2006) is based on implied mortality improvements in the IML92/IFL92 tables.

** the allowance for future mortality improvements for PNMA00MC/PNFA00MC (U=2009) is based on the implied future improvements in the PMA/PFA92 MC tables.

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

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

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

- Policy values – the total of policy values for all with-profits policies (or their equivalents for with-profits annuities and conventional with-profits contracts);
- Future charges – the margin assumed to be retained each year before making future increases to policy values;
- Impact of early surrenders – the value of the financial adjustment assumed to be deducted on non-contractual surrenders;
- Cost of guarantees – the cost of meeting contractual guarantees in excess of the policy values; and
- Other long-term liabilities include miscellaneous provisions (as described in Note 16e), 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. Following the Canada Life transaction, the future profits expected have been reduced to reflect the lower level of retained non-profit business. However, there remains a requirement to hold capital in respect of the reassured non-profit business until the transfer is completed, which is in excess of the future profits expected for the retained non-profit business. The resulting anticipated present value of future profits is a loss of £11m (2005: a profit of £10m) before taking into account any release of capital subsequent to the balance sheet date.

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

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 value 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 Annuities (WPA) and Conventional With-Profits (CWP) policies. These policies represented 75%, 23% and 2%, respectively, of the total policy values at 31 December 2006 (75%, 23% and 2% at 31 December 2005). 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% p.a.. For the majority of RSP policies issued after 1 July 1996, the guaranteed investment return is 0% p.a.. 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 or at maturity (where appropriate) will not be less than the sum assured and any declared reversionary bonuses.

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

For policies where the guaranteed value at contractual termination exceeds the policy value at that date, the excess would be paid and estimates of such excess form part of the realistic liabilities. In calculating the amount payable to policyholders, account is taken of any management actions such as making changes to policy values in response to changes in market conditions. The cost of these guarantees has reduced from £847m in 2005 to £566m at 31 December 2006 principally as a result of changes to interest rate assumptions and the increases made in policy values for 2006. 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:

Mortality assumptions by class of business	2006	2005
Endowment assurances (with-profits)		
Basic Life and General Annuity business	87.5% AMC00 ultimate for males 92.5% AFC00 ultimate for females	65% AM92 ultimate for males 90% AF92 ultimate for females
Pension business	87.5% AMC00 ultimate for males 92.5% AFC00 ultimate for females	65% AM92 ultimate for males 90% AF92 ultimate for females
Recurrent Single Premium (RSP) (with-profits)		
Basic Life and General Annuities in payment	75% IML00 ult (U=2006)* for males 80% IFL00 ult (U=2006)* for females	80% IMA92 (U=2005) for males 85% IFA92 (U=2005) for females
Pension Annuities in payment	87.5% PNMA00MC (U=2009)** for males 77.5% PNFA00MC (U=2009)** for females	75% PMA92MC (U=2008) for males 70% PFA92MC (U=2008) for females

Notes:

* the allowance for future mortality improvements for IML00/IFL00 ult (U=2006) is based on the implied future improvements to mortality in the IML92/IFL92 tables.

** the allowance for future mortality improvements for PNMA00MC/PNFA00MC (U=2009) is based on the implied future mortality improvements in the PMA/PFA92 MC tables.

The effect of the change in the mortality assumptions in 2006 for with-profits annuities has been to increase the Excess Realistic Assets by £68m (2005: decrease by £35m).

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

16. Technical provisions (continued)

d. The long-term business provision – with-profits business (continued)

ii. Assumptions – with-profits business (continued)

Future charges

A margin of 0.5% p.a. (2005: 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 1.0% p.a. (2005: 1.05% p.a.), is assumed to be deducted each year before making future increases to policy values. In addition, an expense provision of £60m (2005: £nil) has been incorporated with the aim of maintaining a stable expense margin as the business declines. Taken together, these allowances are intended to provide for future expenses in respect of with-profits business. A 0.1% increase in the expense margin assumption would decrease the Excess Realistic Assets by £25m (2005: £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 2005 and 2006. The results of that investigation have been used to set the assumed retirement ages for the valuation.

The retirement assumptions vary between different product types. The range of retirement dates assumed varies between policyholders being assumed to retire 2 years (2005: 3 years) earlier than ECD and up to 13 years (2005: 10 years) later than ECD.

A sensitivity analysis has been carried out to illustrate the potential impact on Excess Realistic Assets, at 31 December 2006, 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%, Excess Realistic Assets would reduce by £75m (2005: £95m). If the level of interest rates at which behaviour changes is 3.5% and the same period of deferment is assumed, the reduction is £105m (2005: £145m). If the deferral were for a period of up to 10 years, the reduction is £140m (2005: £150m) at 2.5% and £210m (2005: £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 2005 and 2006. 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. (2005: 1.5% p.a.). The effect of the change in the surrender rates has been to increase the Excess Realistic Assets by £15m (2005: decrease by £30m).

A financial adjustment of 8.0% (2005: 8.0%) of policy values is assumed as a deduction on surrender prior to contractual termination.

Economic assumptions

In order to produce many projections of different scenarios of the business, an economic model is required. The economic model used by the Society in the valuation 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 2005 to 2006 was to reduce the Excess Realistic Assets by £58m (2005: increase 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 swap option volatilities obtained from Bloomberg. For equity values, the model produces a 10 year volatility of 21% (2005: 21%). Property (including property-related assets) is modelled using a proxy index with a volatility of 15% (2005: 15%) and a correlation with equities of 30% (2005: 30%).

e. The long-term business provision – miscellaneous provisions

Technical provisions include amounts in respect of specific provisions:

- An amount of £68m (2005: £85m), which is the current estimate of the compensation or adjustments to future benefits which may be payable under the review of managed pension sales and other costs 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. 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 reduction in the provision is principally as a result of further assessment and settlements during the year;
- Anticipated additional exceptional expenses of £115m (2005: £129m) over future years, including contractual commitments to HBOS in respect of pension scheme future service costs and anticipated additional costs associated with servicing policies in the medium term; and
- An amount of £128m (2005: £182m) 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 residual reassurance balances in respect of the linked and part of the non-profit book and other items.

f. 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 2006 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:

2006	Notes	Equitable Life £m	University Life £m	Total £m
Available capital resources:				
Fund for future appropriations		–	10	10
Subordinated debt	14	167	–	167
Regulatory adjustments				
Valuation differences(1)		1,017	(2)	1,015
Inadmissible assets		(1)	–	(1)
Total available capital resources		1,183	8	1,191
Long-term Insurance Capital Requirement (LTICR)(2)		(467)	(2)	(469)
With-profits Insurance Capital Component (WPICC)		(549)	–	(549)
Total regulatory Capital Resource Requirements (CRR)		(1,016)	(2)	(1,018)
Excess of available capital resources over CRR		**167**	**6**	**173**

2005	Notes	Equitable Life £m	University Life £m	Total £m
Available capital resources:				
Fund for future appropriations		–	9	9
Subordinated debt	14	167	–	167
Regulatory adjustments				
Valuation differences(1)		722	(2)	720
Inadmissible assets		(1)	–	(1)
Total available capital resources		888	7	895
Long-term Insurance Capital Requirement (LTICR)(2)		(593)	(2)	(595)
With-profits Insurance Capital Component (WPICC)		(128)	–	(128)
Total regulatory Capital Resource Requirements (CRR)		(721)	(2)	(723)
Excess of available capital resources over CRR		**167**	**5**	**172**

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 FSA return presents the figures on an adjusted solo basis where University Life is incorporated on a different basis. The surplus capital for 2006 on this basis is £167m (2005: £167m).

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 £1,191m (2005: £895m).

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

Available capital resources:	2006 £m	2005 £m
At 1 January	888	703
Investment return and interest rate movements	207	491
Mortality assumption change	56	(269)
Other movements	32	(37)
At 31 December	**1,183**	**888**

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 redeem 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 (CRR).

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

In order to derive the value of the WPICC, it is necessary to compare the excess available capital resources over LTICR (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 2006 following the introduction by the FSA in 2004 of new rules for the determination of capital requirement, results in a requirement to anticipate the distribution of all assets to policyholders. For this reason, the realistic capital for the Society is a nil balance in 2006 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.

17. Capital statement (continued)

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 25 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 2006 was: gilts 52% (2005: 49%); corporate bonds 24% (2005: 25%); property (including property unit trusts) 12% (2005: 15%); cash 8% (2005: 6%); and equities 4% (2005: 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 closely match 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:

			2006			2005
	Equitable Life £m	University Life £m	Total £m	Equitable Life £m	University Life £m	Total £m
Non-profit	4,521	13	4,534	5,005	13	5,018
With-profits	9,081	11	9,092	9,823	12	9,835
Linked	3,326	1	3,327	3,310	–	3,310
	16,928	**25**	**16,953**	**18,138**	**25**	**18,163**

18. Provision for other risks and charges

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Provisions for deferred taxation	3	2	3	2
Pension commitments for former staff	34	48	33	48
	37	**50**	**36**	**50**

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 £19m (2005: £19m) was paid during the year. The balance of the movements is due to changes in economic assumptions.

19. Deposits received from reinsurer – secured

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

In order to protect the policyholders from a large counterparty credit exposure, the initial premium was deposited back with the Society until the final transfer was approved by the High Court and completed. This deposit was held in assets with a similar investment mix to that previously held by the Society. Canada Life held a secured charge over these assets. The investment returns from those secured assets were attributed to Canada Life and payments of related annuities deducted from the deposited assets. The net balance due to Canada Life at 31 December 2006 was £4,316m. This deposit back arrangement had the effect of increasing the Group's and Society's total assets and total liabilities by the deposited amount.

20. Creditors

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
a. Amounts owed to credit institutions	**19**	**19**	**19**	**19**

Amounts owed to credit institutions represent bank overdrafts partly matched by an amount of £17m (2005: £16m) placed in an assigned account owned by HSBC. The amount is included in debtors in Note 12.

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
b. Other creditors including taxation and social security				
Outstanding purchases of investments	–	2	–	2
Balances with Group companies	–	–	10	11
Corporation tax	13	15	13	14
Other creditors	7	10	4	9
	20	**27**	**27**	**36**

21. 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.

On 20 December 2006, the Society announced that it had reached agreement to sell the share capital of University Life Assurance Society, a wholly owned subsidiary, to Reliance Mutual Insurance Society Limited. The Society expects to complete the sale on 31 May 2007.

b. Significant holdings

At 31 December 2006, the Group and the Society held more than 20% of the nominal value of a class of equity shares in 14 (2005: 14) companies.

At 31 December 2006, the Group and the Society held more than 20% of the partnership interests in 1 (2005: 1) limited partnership investing in properties.

At 31 December 2006, the Group and the Society held more than 20% of the partnership interest in 10 (2005: 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 relevant 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.

22. Related party transactions

There were no material related party transactions during 2006 (2005: nil).

23. Commitments

The Society has no material operating lease commitments.

Property investment commitments, not provided for in the financial statements, amounted to £4m (2005: £17m) 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 £28m (2005: £43m) for the Group and for the Society.

24. Post balance sheet events

- On 11 May 2006, the Society announced that it had reached agreement with Canada Life for the reassurance and subsequent transfer of most of its non-profit pension annuity business, comprising approximately 130,000 policies. The Society entered into a reassurance agreement with Canada Life on that date, paying an initial premium of £4,608m. Application was subsequently made to the High Court and the policies were transferred to Canada Life under a Part VII Transfer under the Financial Services and Markets Act 2000 on 9 February 2007. Investment assets to the value of £4,234m were transferred to Canada Life to match the liabilities of the business at that date. The Society no longer has a liability for these policies.

- On 15 March 2007, the Society announced that it had entered into an agreement with The Prudential Assurance Company Limited for the transfer of all its with-profits annuity policies. This transfer is conditional on certain matters, including the approval of members and the High Court. On completion, expected to be by the end of 2007, approximately 62,000 with-profits annuities (representing some 50,000 annuitants) would be transferred. These policies represent about 20% of the with-profits liabilities with an estimated value of £1.8 billion as at 31 December 2006. The amount of the assets to be transferred will be determined by reference to the Society's financial position at the date of transfer, after deducting the costs to implement the transfer and allowing for the with-profits annuitants' share of the Excess Realistic Assets.
- On 20 December 2006, the Society announced that it had reached agreement to sell University Life Assurance Society, a wholly owned subsidiary, to Reliance Mutual Insurance Society Limited. The Society expects to complete the sale on 31 May 2007.

25. Contingent liabilities and uncertainties

As noted in the Financial Review on page 13 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 Parliamentary recess in the summer of 2007.
- 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. Its report is expected to be published in the summer of 2007.
- 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 completed 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. One former director was expelled and two others admonished in respect of those charges on which misconduct was found. Although these proceedings and investigations cannot result in a requirement for the Society to take any particular action, their findings could influence the way in which claims are presented against the Society.

25. Contingent liabilities and uncertainties (continued)

- 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 406 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, which is expected to be considered by the court in 2008.
- As noted in the Financial Review on pages 9 and 10, 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 16d. 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 has the power to require that a particular level of capital be held by the Society which could result in the Society considering 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.
- 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.
- As previously reported, the Society was unable to reach agreement over the amount of the premium in respect of its 2001 reassurance arrangement with HBOS and the matter was referred to an independent umpire for resolution. On 22 September 2006, the umpire issued his determination, the resultant amount due and paid to HBOS being within the provision held by the Society for this matter. The determination is subject to a further claim by HBOS which is pending final judicial decision. There exists the possibility that the amount of the premium may be subject to further determination by another umpire.
- As noted in Note 8c to the financial statements, the Society has contractual commitments in respect of two pension schemes for which HBOS is the principal employer. Although full provision is made for estimated contractual liabilities calculated on a basis consistent with that adopted by the Scheme Actuary in his triennial valuations, there remains the possibility that it may be necessary for a more conservative basis to be adopted in future in calculating the Society's obligations.

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 Capital Resources Requirement (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