



An Independent association of Equitable Life Members & Policy-Holders funded by subscription

Equitable Members Action Group

Equitable Life – the Year of Decision

Briefing Note by the Equitable Members Action Group (EMAG)

February 2007

The Equitable Members Action Group (EMAG) represents the interests of about 1.5 million people (according to Equitable's own figure) and their dependents who lost a sizeable part of their retirement savings, in total around £4bn, following the closure of the Society and subsequent 16% devaluation of all of Equitable's policies in July 2001.

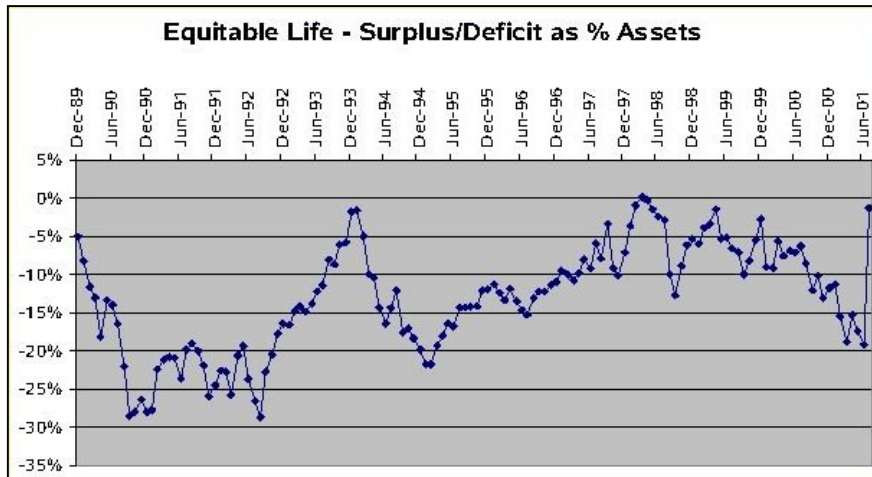
EMAG was formed when the problems at Equitable first became apparent. We represent ordinary people from all walks of life – savers past and present who have lost significant amounts of money and had their financial security undermined by the collapse of Equitable Life. With over 10,000 paying members, EMAG's purpose is to achieve payment of fair and reasonable compensation from the UK Government for what we maintain has been catastrophic and serial regulatory failure, dating back throughout the 1990s.

Equitable investors are, it is implied, undeserving "fat cats". But by 2001 the average Equitable customer's savings were less than £20,000 and it was largely the fat cats who actually got out first and on more favourable terms, leaving the most vulnerable members facing penury. Many locked-in annuitants have seen their annual income halved, leaving them unable to enjoy the retirement for which they had saved. Some have sold their homes to survive. Further, hundreds of thousands of Equitable's policyholders compounded their losses by incurring punitive additional penalties on non-contractual exit when they escaped the disaster that is Equitable.

The Equitable Story

In the 1970s Equitable Life, the world's oldest life insurance company, decided to go for growth by competing aggressively in the pensions savings market. By the late 1980s its reserves had been severely depleted by reckless over-distribution of the fund and it chose a risky new hybrid strategy. The idea was to run the Society almost like a unit trust, making a virtue out of not holding reserves and, uniquely, telling the policyholders annually the apparent total worth of their policies. In the early 1990s stock markets fell. According to the "unit trust" approach, Equitable should then have told its policyholders of their reduced fund values. But instead it continued to declare attractive but unearned (actually non-existent) increases in values for its policies, which no unit trust would have been allowed to do. It continued to announce bonuses even while the total of all policy values reported to policyholders actually far exceeded the Society's assets - by a breathtaking 28%.

The public had no knowledge of this deception, yet Government regulators were aware of what was happening and failed to act as insurance laws required, "to protect the reasonable expectations of the policyholders". As a result of these inflated valuations, policyholders who cashed in their policies from the late 1980s up until the policy value cuts in 2001 unknowingly took away far more than their share of Equitable's assets, leaving an even larger deficit not least for new policyholders who had been suckered into what had become in effect a pyramid selling or Ponzi scheme.



With its blue-chip reputation and competition-beating annual bonus declarations (which were not backed by performance), Equitable grew very rapidly during the 1990s from £6bn to £26bn invested within its with-profits pensions fund. Top management was aware of the growing problem of the “Guaranteed Annuity Rates” (GARs) which were embedded within all earlier policies issued in the 1970s and 1980s but - unwilling to rock the boat - they chose a secretive approach to deny these liabilities and not to reserve for them.

When, in the summer of 2000, Equitable's treatment of GAR liabilities was ruled inadmissible by the House of Lords, the historic and catastrophic financial “black hole” began to surface. The board put Equitable up for sale immediately but it continued to issue misleading statements about performance and the true state of the fund. Neither the Government nor the regulators, the FSA, did anything to protect the public from the ongoing deception that was perpetrated during this period. Owing to its concealed asset deficit and open-ended future liabilities, Equitable Life was, to the apparent surprise of the FSA, found to be completely unsaleable. In consequence, the mutual Society's policyholders were left to carry the can alone. **The Society closed its doors to new business and had to face a future with a multi-billion pound deficit, without any further influx of new investors to prop up its flimsy pyramid.**

What has happened since then?

Lord Penrose was asked by the Treasury in August 2001 to investigate the history of the Equitable, “to inquire into the circumstances ... to identify any lessons to be learnt for the conduct, administration and regulation of life insurance”. At the time, the Financial Secretary to the Treasury, Ruth Kelly, said it was “in the public interest to have a wider, independent review”. Penrose described a “picture of a Society that had deep-seated financial and management problems”. His report made clear that the former board of Equitable had recklessly pursued growth, locking the Society into a strategy that would inevitably fail, while Government regulators looked passively on. However, the explicit remit of the Penrose Report meant that he could not identify negligence or recommend compensation. The report was ignored by a Government unwilling to set a costly precedent or admit any complicity in the downfall of Equitable.

Presenting the report to Parliament in March 2004, Ruth Kelly invited policyholders to take their claims to the Financial Ombudsman Service (FOS) as a practical free and fast alternative to expensive and unpredictable litigation. But one year later, the FOS quietly announced a volte face, abandoning all ‘Penrose-related’ claims.

In February 2007 eminent academic Lord Neill of Bladen QC produced a rigorous report, commissioned by EMAG, on the performance of the FOS in responding to complaints from Equitable members. He found that the service provided by the FOS “fell short of the standards which [Equitable's policyholders] were entitled to expect” - standards that the Service had set itself. In addition, Lord Neill pointed out that claimants had “good reason to be dismayed” by the unilateral dismissal by the chief ombudsman, Walter Merricks, of all complaints relating to the Penrose Inquiry without any “consideration of their merits”.

Why does the collapse of Equitable Life matter?

Without vigilant regulation pensions policies can degenerate into pyramid schemes by paying out attractive returns to maturing policies while depleting the assets that support the remaining policies. This is what happened with Equitable. The management ruthlessly pursued growth with no apparent regard to the deficit of real assets required to cover their annually declared policy values. But this is why the Insurance Companies Act 1982 gave the regulatory authorities the duty to protect “the reasonable expectations of the policyholders” and gave them adequate powers to control life assurances companies, which they consistently failed to use.

Everyone agrees that having a healthy pensions and savings market is a good idea. Indeed, the Government is currently reconstructing our pensions systems and trying to convince more people to save more for their retirement. **But this will only happen if people have trust in a system that is buttressed by firm and effective regulation.** The Equitable saga has shown the dangers of light touch regulation: savers were told they were protected, while the regulators sat on their hands, thus producing a far worse result than would have been the case under “caveat emptor”. This has done immeasurable damage to public confidence in the financial services sector and those 1.5 million victims have spread the word of mistrust in pensions to their friends and families.

Government has a legal responsibility to regulate the UK financial services industry effectively. The DTI and latterly the Financial Services Authority (FSA) should have put a stop to Equitable's reckless and unsustainable business practices. For over a decade, lax regulators let Equitable get away with deceiving its policyholders and allowed it to use an imaginative variety of dubious accounting devices to embellish the Society's illusion of financial strength. **Regulation was tested and failed; restitution should follow.**

What now?

On 21st February, in a critical Judicial Review Judgement in the High Court, the PO's finding in favour of victims of failed Occupational Pension schemes was upheld. This quashed the rejection of the report by the Department of Work and Pensions (DWP) and the Secretary of State was directed by Judge Bean to reconsider the Ombudsman's recommendation. **Hopefully, this will be a tipping point, as it presents the opportunity for Parliament to reassert its political will and its faith in the office of the PO.**

Around about June we should see the publication of two defining reports into Equitable Life that have been many months in the making: one from the PO and the other from the European Parliament's Committee of Inquiry into Equitable Life (EQUI). These reports will examine whether there was maladministration warranting compensation and the role that the UK Government should have played in protecting consumers both in the UK and elsewhere in Europe.

It is crucial that MPs act upon the findings and the recommendations of the PO's report on Equitable. It is in the power of Parliament, if the PO deems it appropriate, to demand appropriate compensation for your constituents. Those families have had their futures marred by the failure of successive Governments properly to regulate. Paying proper compensation would also go a long way towards beginning to restore confidence in the FSA.

EMAG asks MPs to act decisively this year finally to redress the Equitable Life scandal, obtain justice for the victims and help restore faith in the UK's pensions providers and the UK regulators.

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Find up to date information about Equitable Life and the full Lord Neill report at: www.emag.org.uk