



**Annuity
& Life Re**

**UNAUDITED
CONDENSED
CONSOLIDATED**

FINANCIAL STATEMENTS

FOR THE THREE AND SIX MONTH PERIODS ENDED

JUNE 30, 2006

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ANNUITY AND LIFE RE (HOLDINGS), LTD.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in U.S. dollars)

	June 30, 2006	December 31, 2005
	(Unaudited)	
Assets		
Cash and cash equivalents	\$ 19,360,734	\$ 19,277,490
Fixed income investments at fair value (amortized cost of \$27,018,746 and \$66,104,138 at June 30, 2006 and December 31, 2005, respectively)	26,504,212	65,266,415
Accrued investment income	403,236	1,145,614
Receivable for reinsurance ceded.....	74,644,300	76,341,602
Other reinsurance receivables		104,135
Other assets.....	306,531	256,693
Total Assets.....	\$ 121,219,013	\$ 162,391,949
Liabilities		
Reserves for future policy benefits	\$ 75,647,865	\$ 77,476,039
Amounts due reinsurer	-	32,929,104
Other reinsurance liabilities.....	188,994	1,742,753
Accounts payable and accrued expenses	821,195	5,069,912
Total Liabilities.....	76,658,044	117,217,808
Stockholders' Equity		
Preferred shares (par value \$1.00; 50,000,000 shares authorized; no shares outstanding)	-	-
Common shares (par value \$1.00; 100,000,000 shares authorized; 24,808,811 and 24,793,811 shares outstanding at June 30, 2006 and December 31, 2005, respectively)	24,808,811	24,793,811
Additional paid-in capital	334,125,057	334,123,757
Stock warrants	1,350,000	1,350,000
Unamortized stock based compensation.....		(22,800)
Accumulated other comprehensive loss	(484,484)	(837,723)
Accumulated deficit	(315,238,415)	(314,232,904)
Total Stockholders' Equity	44,560,969	45,174,141
Total Liabilities and Stockholders' Equity	\$ 121,219,013	\$ 162,391,949

See accompanying notes to unaudited condensed consolidated financial statements

ANNUITY AND LIFE RE (HOLDINGS), LTD.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited and in U.S. dollars)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2006	2005	2006	2005
Revenues				
Net premiums	\$ -	\$ 2,927,917	\$ -	\$ 8,416,183
Investment income, net of related expenses	604,441	1,609,615	1,177,254	3,275,624
Net realized investment (losses) gains	(697,189)	(6)	(1,058,052)	401,144
Net change in fair value of embedded derivatives	-	(35,736)	-	451,409
Surrender fees and other revenues	-	30,677	-	61,313
Total Revenues	(92,748)	4,532,467	119,202	12,605,673
Benefits and Expenses				
Claim and policy benefits	(224,368)	1,587,086	(423,532)	6,189,529
Interest credited to interest sensitive products	-	257,075	-	626,253
Policy acquisition costs and other insurance expenses	22,046	1,008,209	(480,791)	2,364,446
Operating expenses	759,533	2,220,065	2,029,036	4,734,076
Total Benefits and Expenses	557,211	5,072,435	1,124,713	13,914,304
Net Loss	\$ (649,959)	\$ (539,968)	\$ (1,005,511)	\$ (1,308,631)
Net loss per common share				
Basic	\$ (0.03)	\$ (0.02)	\$ (0.04)	\$ (0.05)
Diluted	\$ (0.03)	\$ (0.02)	\$ (0.04)	\$ (0.05)

See accompanying notes to unaudited condensed consolidated financial statements

ANNUITY AND LIFE RE (HOLDINGS), LTD.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME
(Unaudited and in U.S. dollars)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2006	2005	2006	2005
Net loss for the period.....	\$ (649,989)	\$ (539,968)	\$ (1,005,511)	\$ (1,308,631)
Other comprehensive income (loss):				
Unrealized holding gains (loss) on securities arising during the period	(622,847)	787,616	(704,813)	58,559
Less reclassification adjustment for realized (loss) gains in net loss.....	<u>(696,189)</u>	<u>(6)</u>	<u>(1,058,052)</u>	<u>401,144</u>
Other comprehensive income (loss).....	<u>\$ 74,342</u>	<u>\$ 787,622</u>	<u>\$ 353,239</u>	<u>\$ (342,585)</u>
Total comprehensive income (loss)	<u><u>\$ (575,617)</u></u>	<u><u>\$ 247,654</u></u>	<u><u>\$ (652,272)</u></u>	<u><u>\$ (1,651,216)</u></u>

See accompanying notes to unaudited condensed consolidated financial statements

ANNUITY AND LIFE RE (HOLDINGS), LTD.
CONDENSED CONSOLIDATED STATEMENTS OF
CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited and in U.S. dollars)

	For the Six Months Ended June 30,	
	2006	2005
Preferred shares par value \$1.00		
Balance at beginning and end of period	\$ --	\$ --
Common shares par value \$1.00		
Balance at beginning of period.....	\$ 24,793,811	\$ 26,338,528
Issuance of shares	15,000	--
Cancellation of shares	--	(21,667)
Balance at end of period	<u>\$ 24,808,811</u>	<u>\$ 26,316,861</u>
Additional paid-in capital		
Balance at beginning of period.....	\$ 334,123,757	\$ 333,810,766
Issuance of shares.....	1,300	--
Cancellation of stock based compensation	--	(13,058)
Balance at end of period	<u>\$ 333,125,057</u>	<u>\$ 333,797,708</u>
Stock warrants		
Balance at beginning of period.....	\$ 1,350,000	\$ 1,350,000
Issuance of warrants.....	--	--
Balance at end of period	<u>\$ 1,350,000</u>	<u>\$ 1,350,000</u>
Unamortized stock based compensation		
Balance at beginning of period.....	\$ (22,800)	\$ (490,415)
Issuance of stock based compensation.....	--	--
Cancellation of stock based compensation	--	34,725
Amortization of stock based compensation.....	22,800	250,140
Balance at end of period	<u>\$ -</u>	<u>\$ (205,550)</u>
Accumulated other comprehensive income		
Balance at beginning of period.....	\$ (837,732)	\$ 1,016,260
Net unrealized losses on fixed maturity investments.....	353,239	(342,585)
Balance at end of period	<u>\$ (484,484)</u>	<u>\$ 673,675</u>
Accumulated deficit		
Balance at beginning of period.....	\$ (314,232,904)	\$ (295,607,926)
Net loss	(1,005,511)	(1,308,631)
Balance at end of period	<u>\$ (315,238,415)</u>	<u>\$ (296,916,557)</u>
Total Stockholders' Equity	<u>\$ 44,560,969</u>	<u>\$ 65,016,137</u>

See accompanying notes to unaudited condensed consolidated financial statements

ANNUITY AND LIFE RE (HOLDINGS), LTD.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited and in U.S. dollars)

	For the Six Months Ended June 30,	
	2006	2005
Cash flows from operating activities		
Net loss	\$ (1,005,511)	\$ (1,308,631)
Adjustments to reconcile net loss to cash used by operating activities:		
Net realized investment gains.....	1,058,052	(401,144)
Net change in fair value of embedded derivatives		(451,409)
Amortization of premiums on fixed maturity investments.....	67,795	532,821
Amortization of stock based compensation.....	22,800	250,140
Changes in:		
Accrued investment income	742,378	284,966
Receivable for investments sold.....		(309,525)
Deferred policy acquisition costs.....		401,316
Other reinsurance receivables	1,801,437	4,460,670
Other assets.....	(49,838)	(5,359)
Reserves for future policy benefits	(1,828,174)	(1,685,374)
Interest sensitive contracts, net of funds withheld		(382,390)
Other reinsurance liabilities.....	(1,553,769)	(38,715,213)
Accounts payable	(4,246,717)	(4,237,658)
Net cash used by operating activities	4,993,547	(41,566,790)
Cash flows from investing activities		
Proceeds from sales and maturity of fixed maturity investments	21,596,808	20,414,758
Purchase of fixed maturity investments.....	(16,535,0217)	(1,605,371)
Net cash provided by investing activities	5,061,791	18,809,387
Cash flows from financing activities		
Net proceeds from exercise of company stock options	15,000	-
Net cash provided by financing activities	15,000	-
Increase (decrease) in cash and cash equivalents.....	83,,244	(22,757,403)
Cash and cash equivalents, beginning of period	19,277,490	56,394,484
Cash and cash equivalents, end of period.....	\$ 19,360,734	\$ 33,637,082

See accompanying notes to unaudited condensed consolidated financial statements

ANNUITY AND LIFE RE (HOLDINGS), LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Description of Business

Annuity and Life Re (Holdings), Ltd. (“Holdings”) was incorporated on December 2, 1997 under the laws of Bermuda. Holdings provides annuity and life reinsurance to insurers and reinsurers through its wholly-owned subsidiaries: Annuity and Life Reassurance, Ltd., which is licensed under the laws of Bermuda as a long term insurer; and Annuity and Life Re America, Inc., an insurance holding company based in the United States, and Annuity and Life Reassurance America, Inc., a life insurance company domiciled in the United States. Holdings, Annuity and Life Reassurance, Ltd., Annuity and Life Re America, Inc. and Annuity and Life Reassurance America, Inc. are collectively referred to herein as the “Company.”

2. Significant Events

Wilton Re Transaction

On August 10, 2005, the Company entered into a Master Agreement (the “Master Agreement”) with Prudential Select Life Insurance Company of America (which has subsequently been renamed Wilton Reassurance Company) and Wilton Reinsurance Bermuda Limited (collectively, the “Wilton Subsidiaries”), each a direct or indirect wholly owned operating subsidiary of Wilton Re Holdings, Ltd. The Master Agreement provided for the novation to or 100% coinsurance (the “Coinsurance Agreements”) by the Wilton Subsidiaries of all of the Company’s life and annuity reinsurance treaties identified in the Master Agreement (the “Treaties”), effective as of June 30, 2005 (the “Effective Date”).

The transactions contemplated by the Master Agreement closed on January 17, 2006. Accordingly, the Company transferred the following assets and liabilities to the Wilton Subsidiaries at closing: cash and investments of \$32.9 million, funds withheld at interest of \$58.7 million, future policy benefits liabilities of \$38.3, and interest sensitive contracts liabilities of \$53.3 million. The Company recorded the transactions as of the Effective Date. As of December 31, 2005, the Company recorded a liability of \$32.9 million representing the cash and investments transferred to the Wilton Subsidiaries at closing. As a result of the execution of the Master Agreement, the Company recorded a \$15.2 million loss from operations for the year ended December 31, 2005.

As of the Effective Date, the Company had 28 Treaties in force, all of which were included in the Master Agreement. At the closing twenty (20) Treaties were novated as of the Effective Date. Because the consents of the counterparties to the remaining eight Treaties were not obtained prior to the closing, the Company executed Coinsurance Agreements covering those Treaties with the Wilton Subsidiaries pursuant to the terms of the Master Agreement. As such, approximately \$1.1 billion of the Company’s life insurance in force had been 100% reinsured to the Wilton Subsidiaries as of the effective date. As of June 30, 2006, all Treaties have been novated and no Treaties remain subject to the Coinsurance Agreements

For additional information on the effects of the Wilton Re transaction, please see Note 3 to the Company’s 2005 Audited GAAP Financial Statements.

Termination of Registration of Securities

On February 2, 2006, the Company announced that it was filing a Form 15 with the Securities and Exchange Commission (“SEC”). The effect of this filing was to terminate the Company’s reporting obligations under the Securities Exchange Act of 1934 and to terminate the registration of its common stock. Under the SEC’s rules, a company with fewer than 300 record holders may voluntarily terminate the registration of its securities by filing a Form 15 with the SEC. The Company currently has fewer than 300 record holders. The Company’s reporting obligations were terminated immediately upon the filing of the Form 15. The Company also anticipates, but cannot guarantee, that its shares will continue to trade on the over-the-counter market and be quoted in the Pink Sheets’ quotation system under the trading symbol ANNRF.PK.

3. Loss per Common Share

The following table sets forth the computation of basic and diluted (loss) income per common share for the three and six month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net loss	<u>\$ (649,959)</u>	<u>\$ (539,966)</u>	<u>\$ (1,005,511)</u>	<u>\$ (1,308,631)</u>
Basic and diluted:				
Weighted average number of common shares outstanding	24,808,811	26,107,695	24,801,311	26,054,011
Net loss per common share	<u>\$ (0.03)</u>	<u>\$ (0.02)</u>	<u>\$ (0.04)</u>	<u>\$ (0.05)</u>

At June 30, 2006, 5,556,318 warrants and 147,000 options were outstanding. The calculation of the diluted loss per common share for the three and six months ended June 30, 2006 does not include the incremental number of shares from the assumed exercise of options and warrants because the inclusion of these potential common shares would be considered antidilutive.

The following tables set forth the pro forma computation of basic and diluted income per share after accounting for stock option grants made prior to the Company’s January 1, 2003 adoption of the prospective method described in Statement of Financial Accounting Standards (“SFAS”) No. 148 for the three and six month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net loss - as reported	\$(649,959)	\$(539,966)	\$(1,005,511)	\$(1,308,631)
Stock option expense recognized.....	-	43,633	22,800	88,592
Pro forma effect on net income of applying fair value accounting to all stock option grants	<u>-</u>	<u>(43,633)</u>	<u>(22,800)</u>	<u>(88,592)</u>
Net loss - pro forma.....	<u>\$(649,959)</u>	<u>\$(539,966)</u>	<u>\$(1,005,511)</u>	<u>\$(1,308,631)</u>
Net loss per common share – as reported:				
Basic and diluted	\$(0.03)	\$(0.02)	\$ (0.04)	\$ (0.05)
Net loss income per common share - pro forma:				
Basic and diluted	\$(0.03)	\$(0.02)	\$ (0.04)	\$ (0.05)

The stock-based compensation expense, including restricted common stock issued to employees, for the three and six months ended June 30, 2006 and 2005 was \$22,800 and \$250,140, respectively.

4. Accounting Standards

Emerging Issues Task Force

The Emerging Issues Task Force (“EITF”) of the FASB issued EITF Issue No. 03-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments” in late 2003. It contains two aspects that impact the Company. First, it provides details regarding disclosures about unrealized losses on available-for-sale debt and equity securities accounted for under SFAS No. 115, “Accounting for Certain Investments in Debt and Equity Securities.” These disclosures were effective in annual financial statements for fiscal years ended after December 15, 2003. Second, it provides additional guidance for evaluating whether an investment is other-than-temporarily impaired. This guidance was scheduled to be effective for reporting periods beginning after June 30, 2004. However, the FASB has since determined that a delay in the effective date of these provisions was necessary until it can issue additional guidance on the application of EITF Issue No. 03-1. The Company will assess whether this guidance will have a material impact on the Company’s results of operations or financial condition once it is released.

Share-Based Payments

On December 16, 2004, the FASB issued SFAS No. 123 (revised 2004), “Share-Based Payment” (“SFAS No. 123R”). SFAS No. 123R replaces SFAS No. 123 “Accounting for Stock-Based Compensation” and supersedes APB opinion No. 25 “Accounting for Stock Issued to Employees”. SFAS No. 123R requires all entities to recognize compensation expense in an amount equal to the fair value of share-based payments granted to employees and is effective as of the beginning of the first annual reporting period that begins after June 15, 2005. Because the Company applies fair value accounting to all employee stock options granted or modified subsequent to December 31, 2002, the impact of this statement will be to record compensation expense utilizing fair value accounting for awards vesting on or after July 1, 2005 that were granted on or before December 31, 2002. The pro forma table in Note 3 illustrates the impact of SFAS 123 on the Company’s unaudited condensed consolidated statement of operations; SFAS No. 123R will have no impact on the Company’s financial position and results of operations.

5. Contingencies

Annuity and Life Reassurance. Ltd. and Transamerica entered into an Agreement to novate the Company’s reinsurance contracts with F&G and Scottish Re to Transamerica effective December 31, 2004. The Company is currently in a dispute with Transamerica concerning both the F&G and Scottish Re aspects of the novation.

With respect to F&G, Transamerica contends that there should be adjustments to the policy benefit reserves transferred to Transamerica. On March 30, 2005, the Company received a demand letter from Transamerica stating that \$7,000,000 was owed to Transamerica as an adjustment to the F&G policy benefit reserves. On June 14, 2005, the Company received an additional letter from Transamerica

revising its original demand to \$6,000,000. The Company and Transamerica were unable to resolve the issues through negotiations and the matter is now in arbitration-

In addition, Transamerica for the first time asserted claims relating to the Scottish Re contracts when it submitted its initial position statement to the arbitration panel on July 20, 2006. Specifically, Transamerica now alleges that it is entitled to damages of approximately \$45 million in connection with the Scottish Re novation. Transamerica also asserts that it is entitled to rescind the novations of both the Scottish Re and F&G books.

Additionally, Transamerica has requested that the arbitration panel award interim relief in the form of a trust fund, to be established by Annuity and Life Reassurance, Ltd., in the amount of \$51 million. (This amount is the total damages claimed by Transamerica in connection with both the F&G and Scottish Re books. Transamerica contends that the amount should be held in trust to secure payment of an ultimate award in the arbitration. (Importantly, Annuity and Life Reassurance, Ltd., the company that is party to the arbitration, has total assets of less than \$36 million at June 30, 2006.)

On July 27, 2006 the arbitration panel held its organizational meeting. At that meeting, the panel scheduled the arbitration hearing to take place during the week of April 16, 2007. The panel is expected to address the interim relief request in late September or October.

The Company believes Transamerica's position with respect to both the F&G and Scottish Re books is without merit. The Company is working with counsel in presenting its position to the arbitration panel. The Company cannot predict the outcome of the arbitration proceedings or the impact the arbitration may have on its financial position.

The Company has also learned that Scottish Re has made adjustments to its billing methodology for 2004 and 2005. These adjustments indicate that the Company may have received overpayments of premiums and / or may not have been billed for claims for which it is responsible. Scottish Re estimates the adjustments to be approximately \$9 million, most of which would be related to the period prior to the novation. The Company has not been provided any data or back-up in order to validate the adjustment and no additional liability has been established at this time. The Company cannot predict the timing or magnitude of any required adjustments related to the Scottish Re treaty, nor the impact these adjustments may have on its financial position.