Phoenix Group Holdings

Audited Results for the year ended 31 December 2009

STRONG CASH GENERATION FROM UK'S LARGEST CLOSED LIFE CONSOLIDATOR

Financial Highlights

- Holding company cash inflows £716m[1, 2]
- IGD capital surplus increased by over 70% to £1.2bn (2008: £0.7bn[3])
- Group MCEV up 75% to £1,827m (2008: £1,044m[1])
- IFRS operating profit £457m[1]
- Dividend per share Euro 0.17 (2008: Nil), in line with guidance of Euro 0.50 per share per annum (pro rata from the date of the acquisition of the Pearl businesses)
- Assets under management £66.9bn (2008: £68.2bn[1])
- Asset management operating profit £34m[1] (2008: £43m[1])

Operational Highlights

- Scottish Mutual and Scottish Provident funds merged into Phoenix Life Limited
- Consolidation of operations to Wythall substantially completed
- Consolidation and re-branding of asset management business under Ignis

Capital Structure and Corporate Developments

- Appointment of Ron Sandler as Chairman and four new independent non-executive directors
- Good progress in discussions with Tier 1 bondholders
- Successful exchange of almost 22m Public and all Insider Warrants to simplify the group capital structure
- Change of name to enhance brand recognition

Commenting on the results, Chief Executive Jonathan Moss said:

"These results demonstrate the strength and attraction of our business model. We have delivered on our promises regarding management actions, improved our capital position and generated strong cashflows. We are targeting £2.7 billion of cash generation over the next five years from our operating businesses. As a group, we are well placed to deliver improving service and investment outcomes for our policyholders.

We are on track to achieve a Premium Listing on the London Stock Exchange in the first half of this year and Phoenix Group is strongly placed to play an increasingly important role in the future consolidation and efficient management of the closed life sector."

Dividend

The ordinary shares will be quoted ex-dividend on the stock exchange of London and Amsterdam as of Tuesday 6 April, 2010. The record date for eligibility payment will be Thursday 8 April 2010 and the date of payment of the dividend shall be 15 April 2010.

Presentation

There will be a presentation for analysts and investors at 8.30am (BST) at JPMorganCazenove, 20 Moorgate, London, EC2R 6DA.

A live webcast of the presentation will be available at www.thephoenixgroup.com

Participants may also dial in as follows:

020 3059 5754 (UK)

+44 20 3059 5754 (outside UK)

Participant password: Results

The presentation slides will be available on www.thephoenixgroup.com before commencement of the presentation.

In addition, a further conference call will be hosted at 2.00pm (BST), primarily for the benefit of US investors, with the same dial in numbers as above.

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Notes

1. 2009 pro forma information includes the results of the Pearl businesses for the period from 1 January 2009 to 27 August 2009 in addition to the consolidated results of Phoenix Group Holdings from 1 January 2009 to 31 December 2009. 2008 pro forma information includes the Pearl businesses for the year to 31 December 2008.

2. UK holding company cash inflows are a measure of cash and cash equivalents remitted by the Group's operating subsidiaries to the UK holding companies and are available to cover dividends, bank interest and other items.

3. The 2008 IGD capital surplus reflects the position of the Pearl businesses at 1 January 2009 following the merger of Scottish Mutual Assurance and Scottish Provident funds into Phoenix Life Limited.

4. The financial information set out in this announcement has been extracted without material adjustment from the audited accounts of Phoenix Group Holdings for the year ended 31 December 2009. The E&Y audit opinion on the Phoenix Group Holdings accounts is unqualified. The accounts will be published on 15 April 2010, in line with statutory regulations, and will be presented for approval at the Annual General Meeting on 23 June 2010.

5. This announcement in relation to Phoenix Group Holdings and its subsidiaries (the "Group") contains forward looking statements concerning future events. Those forward looking statements are based on the current information and assumptions of the Group's management concerning known and unknown risks and uncertainties. Forward looking statements do not relate to definite facts and are subject to risks and uncertainty. The actual results and financial condition of the Group may differ considerably as a result of risks and uncertainties relating to events and circumstances beyond the Group's control, including among other things, domestic and global economic and business conditions, market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally; the policies and actions of regulatory authorities, the impact of competition, inflation, and deflation; experience in particular with regard to mortality and morbidity trends, and lapse rates; the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; and the impact of changes in capital, solvency or accounting standards, and tax and other legislation and regulations in the jurisdictions in which members of the Group operate. The Group cautions that expectations are only valid on the specified dates, and accepts no responsibility for the revision or updating of any information contained in this announcement.

Phoenix Group Holdings
A) Overview

Results Announcement

Business overview
Phoenix Group is the UK's largest closed life and pension fund consolidator. The Group has in excess of £66 billion of assets under management and over 6.5 million policyholders.

As a closed life business consolidator Phoenix Group focuses on the efficient run-off of existing policies, maximising economies of scale and generating capital efficiencies through operational improvements. The Group only writes annuity business for existing policyholders and therefore has limited new business capital strain.

The Group has implemented a business model which combines the use of in-house financial control and risk management, outsourced customer administration and in-house asset management – all of which combine to protect policyholders and maximise shareholder return.

Our mission
To improve returns for policyholders and deliver value for shareholders.

Our vision
To be recognised as "the industry solution" for the safe, innovative and profitable decommissioning of closed life funds in the UK.

Group transition

Liberty Acquisition Holdings (International) Company ("Liberty") was incorporated on 2 January 2008 under the laws of the Cayman Islands as an exempted company with limited liability. Liberty was formed as a non-operating Special Purpose Acquisition Company ("SPAC") to acquire one or more operating businesses with principal activities outside of North America. Liberty listed on Euronext Amsterdam on 6 February 2008.

Acquisition

On 29 June 2009, Liberty announced that it would acquire a group of businesses that specialise in the consolidation and management of closed life and pension funds, referred to in the Results Announcement as the "Pearl businesses". The acquisition completed on 2 September 2009* when Liberty became the ultimate parent of the Pearl businesses.

Following the acquisition, Liberty changed its legal name to Pearl Group and moved its principal place of business to Jersey. Subsequently, on 15 March 2010, Pearl Group further changed its name to Phoenix Group Holdings.

Throughout the Results Announcement, Phoenix Group Holdings and its subsidiaries are referred to as "Phoenix Group" or "the Group". When referring to Phoenix Group Holdings, the parent company, "Phoenix Group Holdings" or "the Company" is used.

Results Announcement

Acquisition of "Pearl businesses" – impact for Results Announcement 2009

The Results Announcement 2009 includes the consolidated results of Phoenix Group Holdings and its subsidiaries from 1 January to 31 December 2009 presented in accordance with International Financial Reporting Standards ("IFRS"). The results of the Pearl businesses are therefore included from 28 August 2009* to 31 December 2009.

To assist users and give shareholders a basis for future comparison, the Directors have provided additional financial information on a pro forma basis. This information includes the Pearl businesses for the period from 1 January 2009 to 27 August 2009 in addition to the consolidated results of Phoenix Group Holdings from 1 January 2009 to 31 December 2009. Pro forma information is separately referenced throughout the Results Announcement and is predominantly located within the sections covering Performance and the Market Consistent Embedded Value ("MCEV") supplementary information.

Certain commentary provided throughout the Results Announcement refers to the activities of the Pearl businesses prior to their acquisition. The Directors believe it is necessary to include this information in the context of the programmes of strategic and operational change that the Group is currently undertaking.

Additionally, although it is not necessary for the Company to comply with the UK Companies Act 2006 ("CA06"), or, by virtue of its secondary listing on the LSE, with the UK Combined Code on Corporate Governance ("the Combined Code") the Directors support the high standards of corporate governance and reporting they require. Accordingly the Results Announcement seeks to comply with certain of these provisions.

* The acquisition date for accounting purposes is deemed to be the date on which Phoenix Group Holdings effectively obtained control of the Pearl businesses. The point at which control passed and the acquisition became unconditional for accounting purposes is deemed to be the date on which the FSA confirmed their non-objection to the change of control of the Pearl businesses, 28 August 2009. The legal date of completion for the acquisition was five days later on 2 September 2009.

Highlights

Financial

– Pro forma UK holding company cash inflows of £716 million

– IGD capital surplus of £1.2 billion

– Group MCEV of £1,827 million

Corporate governance and capital structure

– Change of name to enhance brand recognition

– Appointment of Ron Sandler as Chairman and four new independent non-executive Directors

– Successful exchange of almost 22 million Public and all Insider warrants to simplify Group capital structure

Operational

– Scottish Mutual and Scottish Provident funds merged into Phoenix Life Limited

– Progressed closure of Glasgow and Peterborough life company offices and associated transfer of operations to Wythall

– Consolidation and rebranding of asset management business under Ignis

Key performance indicators

Pro forma UK holding company cash inflows

£716 million

IGD capital surplus

£1.2 billion

Group MCEV

£1,827 million

IFRS operating profit

£457 million (pro forma)

£282 million

Dividend per share

€0.17

Pro forma asset management operating profit

£34 million

Assets under management

£66.9 billion

Our goals

– Maximise business performance and value

– Improve customer outcomes

– Sustain a robust and scalable business model

– Be a place where people want to work

– Build an industry-wide reputation

– Pursue value adding acquisitions

Chairman's report

This has been a momentous year for Phoenix Group Holdings, with the acquisition of the Pearl businesses in September 2009. Against the backdrop of a global recession, these businesses required additional capital and, through a restructuring of debt obligations and an injection of new funds, their balance sheet has been strengthened by some £1 billion. The acquisition has also provided the Pearl businesses with access to public markets through the Company's listing on Euronext and secondary listing on the London Stock Exchange ("LSE").

The purchase and subsequent restructuring marks the start of an exciting phase for the newly formed Group and this is reflected in the Board's decision to develop the Phoenix name as the core brand for the Group. Since the majority of the Group's activities are within the Phoenix Life umbrella, there are synergies and value to be obtained by extending the Phoenix name and brand to the holding company.

The UK life insurance industry, our core marketplace, continues to adapt to changes in the market and regulatory environment. The disappointing returns and lack of transparency of traditional with profit products have led to a significant reduction in their attractiveness for providers and consumers alike. Taken together with a more onerous regulatory framework, it is clear that there will be an increasing number of life companies ceasing to write new capital intensive policies and disposing of books of business. The Group is well positioned to meet the growing need for providers capable of managing legacy policies safely and responsibly on behalf of millions of policyholders.

The business model of the Group is a very simple one. We operate closed life funds (funds that no longer write new life policies) in the UK, with an efficient, outsourced operating platform and a leading asset management capability. We combine sophisticated asset/liability matching techniques with a prudent approach to risk to ensure that the Group is capital efficient, and the predictable cash generative characteristics of closed life funds allow us to operate with higher leverage than life companies that are still writing new business. Our scale, with more than £66 billion of assets under management and over 6.5 million policyholders, positions us as the natural consolidator of closed life funds in the UK. This is reinforced by our proven expertise in extracting synergy value through the integration of acquisitions.

The Group's strategy is similarly straightforward. Financial and operational stability remain our near-term focus following the acquisition and restructuring in September. We are undertaking additional portfolio de-risking and further integration of our back offices and asset management activities to deliver greater efficiencies. We are also simplifying our capital structure and migrating our share register to best match the longer term ambitions of the Group. This process will be facilitated by moving our listing from Euronext to a Premium Listing on the LSE which we are on track to achieve in the first half of 2010. We will progressively turn our attention to creating further efficiencies from within our existing portfolio of life funds and the realisation of our consolidation ambitions for the UK closed life sector as a whole. This process is financially attractive for the Group and has considerable social merit, providing the potential to deliver improvements in the security, service and returns for policyholders.

Indeed, policyholder concerns remain at the heart of everything we do. With our proud heritage of life assurance brands such as Phoenix, Pearl, Scottish Mutual, London Life and NPI, we are acutely aware of the millions of our policyholders who rely on us for their long-term financial security. We are determined that our policyholders receive continually improving levels of service and investment performance, combined with demonstrable fair treatment.

The interests of our policyholders are closely aligned with those of our shareholders: both are well served by a Group that is financially robust, prudently managed and widely respected. Nonetheless, they are not always identical and therefore it is crucial that we have strong and effective governance arrangements.

The Board of Phoenix Group Holdings has been strengthened considerably since September and we are fortunate to have been joined recently by four new non-executive Directors: Alastair Lyons, Charles Clarke, Isabel Hudson and David Woods, who each bring significant relevant experience. Their contribution is already in evidence as we advance our strategic thinking and build a strong platform for the future. I look forward to working with them and the rest of the Board in achieving the Group's goals.

Looking ahead, we expect that economic conditions will remain very challenging for some time. The internal challenges faced by the Group are also not to be underestimated and much remains to be done: continuing to deliver synergies from combining the Group's operations; overcoming a number of structural complexities en route to achieving the

Premium Listing; integrating and realising value from the asset management businesses; simplifying our financial, legal and shareholding structures; creating sound long-term funding arrangements; and developing further the reputation and standing of the Group. These add up to a demanding agenda but I am confident that we are progressively putting in place the right policies and resources to realise the full potential of the Phoenix Group – for policyholders, shareholders, employees and, more widely, for the UK financial services sector and millions of consumers.

Ron Sandler

Chairman 30 March 2010

Group Chief Executive's report

I am pleased to present the first annual results of Phoenix Group Holdings since the acquisition of the Pearl businesses in September 2009. I believe this acquisition marks the beginning of an exciting phase in the Company's history and positions us strongly for the future.

As CEO of the Pearl businesses I was delighted to take on the additional responsibility of becoming the Group Chief Executive for Phoenix Group Holdings. Working closely with our Chairman, Ron Sandler, who joined the Group in September, I am committed to continuing the significant progress already made in developing the Group for the benefit of our policyholders, shareholders and employees.

Pearl businesses

The end of 2008 and early 2009 was a challenging period for all business sectors. But life insurers, including the Pearl businesses, were particularly impacted by widening corporate bond spreads and falling asset markets. As a result, although the underlying life companies had sufficient capital, the extreme market dislocation challenged the sustainability of the Pearl businesses' highly leveraged financial structure. This led to their acquisition by Phoenix Group Holdings, an injection of new capital and a significant restructuring of bank loans and other liabilities.

Overall, the restructuring strengthened the Group's balance sheet by some £1 billion and as a result we enter 2010 in a much improved financial position. This can be evidenced by the Insurance Group's Directive ("IGD") regulatory solvency calculation, where surplus capital amounted to £1.2 billion (or 132 percent of regulatory requirements) at the end of 2009 before allowing for the payment of the 2009 dividend, compared to a surplus of £0.7 billion at 1 January 2009.

Financial results

Despite the market volatility of the past 18 months, the Group produced a resilient performance in 2009. Our primary performance measure is pro forma UK holding company cash inflows which continues to exhibit strength with £716 million remitted during the year. This is well in excess of the Group's debt servicing obligations and ahead of our target for the year.

We achieved this strong cash flow by identifying and implementing a number of management actions during 2009, including the transfer of the Scottish Provident and Scottish Mutual life funds into Phoenix Life Limited, the restructuring of Phoenix & London Assurance, the renegotiation of certain outsourcer contracts and the resolution of other legacy issues. We are targeting £2.7 billion of cash generation over the next five years.

Our primary measure of long-term shareholder value is MCEV. We achieved a Group MCEV pro forma operating profit of £374 million for the year ended 31 December 2009 and Group MCEV of £1,827 million at 31 December 2009 (compared to a pro forma £1,044 million on a comparable basis at 31 December 2008). The change during the year reflects the positive impact of improved investment markets in the second half of 2009 and implemented management actions.

Phoenix Group has two core segments: Phoenix Life and Ignis Asset Management. Analysis of their results provides further evidence of a strong performance during the year.

Phoenix Life

Our life companies produced a creditable result for 2009 with improving returns across the underlying businesses. We achieved a full year pro forma IFRS operating profit of £469 million (£285 million which arose in the post acquisition period from 28 August 2009).

Ignis Asset Management

Our asset management business continued to perform well despite the market volatility. We achieved a pro forma IFRS operating profit of £34 million with assets under management also remaining broadly stable at £66.9 billion in spite of insurance policy maturities.

These are pleasing results for 2009 which provide a stable financial footing for the future.

Strategy for the future

The transition of the private Pearl businesses into a listed environment has brought about a short-term change in our priorities and one key objective is to obtain a Premium Listing during the first half of 2010 (a matter covered in more detail later). However, the strategies and operating models for Phoenix Life and Ignis Asset Management remain broadly unchanged as the Board continues to support the focus on closed life insurance funds.

Our Group goals are summarised below:

Maximise business performance and value

Deliver predictable long-term cash flow, drive increased value within Phoenix Life and increase the profits of Ignis Asset Management

Improve customer outcomes

Demonstrate an understanding of our customers' needs and a commitment to deliver consistent service that provides ease of access to information and communicate in a way our customers understand

Ensure the security of policyholders is protected whilst actively seeking opportunities for enhanced value

Sustain a robust and scalable business model

Ensure the Group is well placed to meet all its long-term obligations by delivering a structure that has optimal levels of leverage and efficient capital structuring while driving operational excellence within our underlying businesses

A place where people want to work

Ensure high levels of employee engagement driven by strong leadership, clear communication, fair reward and development practices

Build an industry-wide reputation

Ensure the Group is recognised as the industry leader in closed life fund consolidation and the safe delivery of customer outcomes

Pursue value-adding acquisitions

Maintain scale through selective acquisitions – execution and integration are a core competency of the Group.

Key 2009 achievements*

*All references to 2009 achievements are for the full year; encompassing the achievements of the Pearl businesses from 1 January 2009

It is of great credit to our employees that, despite the impact the acquisition and restructuring has had on the underlying businesses and employees during 2009, we continued to successfully deliver initiatives in line with our strategic goals. I therefore thank all employees for their hard work and energy during this period and recognise some significant achievements during the year:

- Completed the funds mergers of the Scottish Mutual and Scottish Provident businesses into Phoenix Life Limited which has simplified the structure of our life companies and achieved capital, cost and tax efficiencies
- Progressed the closure of Glasgow and Peterborough life company offices and associated transfer of operations to Wythall. This will simplify our operating model and creates operating synergies by consolidating our Phoenix Life business into one location
- Reorganised and rebranded our asset management business to operate under the Ignis brand. This has enhanced our third-party asset management offering and capability
- Implemented a plan to restructure National Provident Life's businesses – this was effected in early 2010
- Secured approval for the Guaranteed Annuity Option Compromise Scheme for Phoenix and London Assurance. This removes longevity risk from the business whilst providing immediate policyholder cash enhancements
- Successfully progressed the public and insider warrant exchange invitations to a conclusion. This has helped simplify the Group's capital structure ahead of our planned premium listing
- Achieved a secondary listing on the LSE in November, which has raised our profile with the UK investment market

We were also pleased to announce the appointment of Mike Merrick and Chris Samuel as Chief Executives for our Phoenix Life and Ignis Asset Management businesses respectively. In their new positions, Mike and Chris will assist me in delivering the strategic objectives of these businesses and the Group as a whole. Specifically Mike will continue to integrate the Group's closed life businesses and Chris will continue to build Ignis Asset Management's third-party offering.

Risk and capital management

Risk and capital management are an essential part of the Group's strategic agenda. The effective management of our risks and the efficient allocation of capital against them is crucial in allowing us to achieve our strategic and operating objectives regardless of prevailing market conditions.

We believe Phoenix Life and Ignis Asset Management manage our key risks effectively but recognise that we have further work ahead to both enhance and fully embed the Group-wide risk governance, monitoring and reporting framework. In support of this risk agenda we recruited as Group Chief Risk Officer, Jean Park, in November 2009 and have established a Board level Risk Committee that will assist the Group in driving this agenda forward. All our future governance, risk and capital management initiatives will be aligned to the Solvency II directive.

Solvency II

We fully endorse the principles underlying the Solvency II framework and expect its implementation to result in an improved understanding of the links between governance, risk and capital management. However, while I welcome the benefits that Solvency II brings to the insurance industry, a number of important issues concerning the development and implementation of the Solvency II proposals remain – and these will need to be resolved without inadvertently impacting policyholders or the industry as a whole.

We have developed our own programme of activities to ensure compliance and identify opportunities within the Solvency II framework. For details of the Group's internal programme for Solvency II please refer to our Capital management report.

Dividends

The Board has declared a dividend for 2009 of €0.17 per share which is expected to be paid on 15 April 2010. The 2009 dividend is in line with previous guidance of €0.50 per share per annum (pro rata from the date of the acquisition of the Pearl businesses to the year end).

In arriving at this dividend the Board has taken into account the conditions contained in the Group's credit agreements which include provisions restricting the distribution of profits by the Group. The dividend declaration reflects the maximum permitted pro-rated dividend payment in respect of 2009. Over time, we anticipate the Group's dividend policy to be more closely aligned with the underlying cash generation of our operating businesses.

Transition to Premium Listing

Achieving a Premium Listing on the LSE is an important objective for the Group. Over time we believe that it will help to develop a broader investor base and improve liquidity.

In order to achieve a Premium Listing we are required to satisfy certain UK Listing Authority ("UKLA") requirements. In particular we need to simplify our capital structure by reducing the number of outstanding warrants and contingent rights over the Group's shares to a maximum of 20 percent of the issued share capital. I was therefore pleased with the successful outcome of our public warrant and insider warrant exchange invitations.

Discussions with the holders of the contingent rights over shares have continued with a view to arriving at a solution which brings the proportion of dilutive instruments below the level required by the UKLA.

Outlook for the Phoenix Group

I believe the Group's business model is attractively differentiated from the rest of the UK life assurance sector. Our focus is on the consolidation of closed funds and our existing scale and previous experience makes us the natural home for these businesses. I expect the Group to play an increasingly important role in continuing to ensure the effective and

efficient management of closed life insurance funds while overseeing the safe decommissioning of the with profits sector.

Our analysis shows that many life insurance companies employ significant amounts of regulatory capital to support in-force policies which are no longer actively marketed or sold. Furthermore, continued market volatility and management of key business risks will bring the issue of capital allocation into sharper focus as the insurance industry heads towards Solvency II. We believe this will encourage companies to identify ways of releasing and reallocating capital currently tied up in closed or quasi-closed funds. Additionally, the operational management costs involved in administering run-off portfolios will become increasingly uneconomic, particularly for those insurers with inefficient legacy infrastructure. These factors play to our strengths and reinforce the importance of the Group's role within the industry as it enters a period of significant change.

Maintaining strict financial discipline, a prudent approach to risk management and a focus on service will protect and, over time, enhance the value of the Group and its reputation.

Jonathan Moss
Group Chief Executive

30 March 2010

B) Business and Strategy

Our business

Although the markets in which we operate are complex, our operating model is straightforward. We acquire and efficiently manage closed life insurance businesses that are in run-off.

We operate in two interdependent market sectors: UK life insurance and asset management. These sectors continue to face significant challenges driven by a combination of market volatility, regulatory change and shifts in customer product choice.

In order to efficiently manage the life businesses while the policies are in run-off, it is essential that we achieve a high level of variability in the cost base. This ensures that the Group is not exposed to high fixed costs in relation to the volume of policies under management. To fulfil this aim we have established a model within Phoenix Life of separating financial and risk management from policy administration. Financial and risk management are core skills and are retained in-house. Our management service operation is charged with all sourcing strategies including putting in place arrangements for third-party policy administration and having oversight of their performance. We use Ignis Asset Management, our in-house asset manager to manage the policyholders' investment portfolios.

To implement our model we have invested heavily in our employees, infrastructure and outsourcer partnerships, providing us with a scalable platform for acquisitions, their integration and hence the opportunity to benefit from synergies. This is key for the sustainability of our business, while providing policyholder protection and shareholder returns.

As a closed life business we do not need to allocate significant capital to support the writing and distribution of new insurance products. This means that the capital requirements of our operating businesses will decline as policies mature, thereby releasing excess capital as free cash flow. This emerging cash flow can be used to fund future acquisitions, reduce financial leverage and pay dividends to shareholders.

In operating this way the Group's management is able to focus its attention on financial control, risk management and customer outcomes.

Management team

Day-to-day direction of the UK operations is the responsibility of the Board of Phoenix Life Holdings Limited (“PLHL”) (a subsidiary of Phoenix Group Holdings) and its Executive Management Committee (“ExCo”). ExCo oversees matters relating to the implementation of the Group’s strategy and recommends the optimal operating structure.

The members of ExCo and their key roles and responsibilities are outlined below.

Jonathan Moss
Group Chief Executive and Director of PLHL
– Lead and direct the Group’s businesses in the delivery of the Group strategy and business plan

– Maximise shareholder value and improve returns for policyholders

– Embed a Group culture which recognises our policyholder obligations in terms of service and security

– Manage the Group’s key external stakeholders

Simon Smith
Group Finance Director and Director of PLHL
– Develop and deliver the Group’s financial business plan in line with the strategy

– Ensure that the Group’s finances and capital are managed and controlled

– Ensure that the Group has effective processes in place to ensure all reporting obligations are met

– Assist the Group Chief Executive in managing the Group’s key external stakeholders

Mike Merrick
Chief Executive, Phoenix Life
– Lead the development and delivery of the Phoenix Life business strategy, including the continued integration of life businesses

– Ensure the optimisation of outcomes for customers in terms of both value and security

– Ensure Phoenix Life deploys capital efficiently and effectively, while adhering to all regulatory requirements

Chris Samuel
Chief Executive, Ignis Asset Management
– Lead the development and delivery of the Ignis Asset Management business strategy including the growth of third-party offerings

– Maximise the value of Ignis Asset Management by delivering top quartile investment performance and a profitable service to all managed clients (including Phoenix Life)

– Ensure that the activities of Ignis are undertaken with due regard to regulatory requirements

Diarmuid Cummins
Managing Director, Corporate Office
– Support the Group Chief Executive and Finance Director in the development and delivery of Group strategies and plans

– Maximise shareholder value though clear, rigorous and innovative assessment of business opportunities

– Lead Group-wide change initiatives and provide administrative oversight of the Corporate Office

Jean Park
Chief Risk Officer
– Oversee and manage the Group’s risk framework in line with the risk strategy and appetite

– Lead the Group's risk management function, embracing changes in best practice and regulation including Solvency II

– Support the enhancement of the risk management framework at both Group and operating segment level

Alan Jones
Group Human Resources Director

– Deliver high quality Human Resources (HR) services to the Group Board, ExCo and operating companies

– Lead in the implementation of the Group's Employee Strategy in order to recruit, retain, motivate and develop employees

– Provide guidance and support on HR matters to the Group Chief Executive, ExCo and the Group Board

Jane MacLeod
General Counsel

– Oversee and coordinate the implementation of appropriate corporate governance procedures across the Group

– Lead the provision of legal advice to the Group Board, ExCo and other Group Company Boards and senior management

– Oversee statutory administration of Group companies, ensuring compliance by Companies and staff with relevant legal obligations

Operating structure

Our structure is aligned to the market sectors in which we operate. The Group has two core segments: life assurance (including management services) – Phoenix Life; and asset management – Ignis Asset Management. In addition, our Corporate Office provides functional support and coordination for the delivery of the Group's strategic initiatives.

Phoenix Group – Operating Structure

Phoenix Life

Phoenix Life is responsible for the financial and operational management of the closed life funds with the support of the management service companies and outsourced service providers. Phoenix Life is overseen by a management team, led by its Chief Executive, Mike Merrick.

Insurance business

The Group comprises eight regulated life companies including well-known brands such as Phoenix, Pearl, Scottish Mutual, London Life and NPI that have been acquired over a number of years. The Group is currently undertaking a programme of activity to integrate its life companies as far as possible in order to optimise economies of scale and capital allocation.

Although the life companies are closed and do not generally write new business, they do accept additional policyholder contributions on in-force policies and allow certain policies, such as pension savings plans, to be reinvested at maturity into annuities held by a Group life company. Writing annuities offers the Group a further opportunity to increase its embedded value through incremental investment returns, while also improving the management of the liquidity position of the individual life companies.

Certain of the Group's life insurance companies include a small amount of run-off general insurance business and Phoenix Group Holdings also owns Opal Re, a reinsurer based in Bermuda. Opal Re provides reinsurance solely to Phoenix Life to support the diversification of risk on the annuity books.

Management services

The management services operations ensure the life companies benefit from economies of scale, established outsourcer relationships and innovative integrated technology infrastructure.

Management services are charged with the efficient provision of financial and risk management services, sourcing strategies and delivery of all administrative services required by the Group's life companies. To facilitate this, management services operates a number of third-party contracts including outsourced policyholder administration and IT services.

Management services has approximately 700 employees in three operational centres. However, plans are well underway to centre operations in the Group's Wythall office near Birmingham.

Ignis Asset Management

Ignis Asset Management is the Group's asset management business providing services to the Group's life companies as well as third-party clients, including retail and institutional investors. Ignis Asset Management is overseen by a management Board led by its Chief Executive, Chris Samuel and offers investment, asset/liability and fund of funds management services and has recently combined its two in-house asset management businesses under the Ignis brand.

Whilst Ignis Asset Management primarily manages assets for the Group life companies, which provides the life companies with greater control over asset allocation and investment performance, it has also established and is further developing third-party distribution channels. Ignis Asset Management has its own sales and marketing division with some 70 employees who focus on developing relationships with independent financial advisers and global investment consultants to help access new clients and increase Ignis Asset Management's third-party asset base.

In addition, Ignis Asset Management has an innovative joint venture/partnership model and currently has three active joint ventures and one partnership arrangement. This provides Ignis Asset Management's clients with a wide range of

investment options and access to additional highly skilled, specialist fund management teams. Existing joint ventures include Argonaut, Cartesian and HEXAM, while Castle Hill is currently the only partnership arrangement. Ignis Asset Management provides marketing and distribution, access to research, compliance and administrative infrastructure functions on behalf of each of the joint ventures. This framework provides the joint ventures with access to the Ignis Asset Management platform and the related economies of scale, while allowing the investment managers to focus on maximising investment performance.

Ignis Asset Management has approximately 530 employees with offices in Glasgow and London.

Corporate Office

The Corporate Office brings together centralised functions that provide Group-wide services. Under the direction of its Managing Director, Diarmuid Cummins, the Corporate Office has four principal roles:

– To assist in the delivery of goals established by the Group Board

– To promote the Group's strategy and profile to stakeholders

– To monitor alignment of business unit plans and Group goals

– To co-ordinate Group-wide initiatives.

Corporate Office has approximately 40 employees based in London.

Our goals and strategies

Our mission is to improve returns for policyholders and deliver value for shareholders. We will do this by realising our vision to be recognised as “the industry solution” for the safe, innovative and profitable decommissioning of closed life funds in the UK.

Phoenix Group Holdings acquired the Pearl businesses in September 2009. Since then, the Group has undertaken a detailed review of its goals and strategies. The review concluded that the core business purpose, rationale and direction of the underlying Pearl businesses remain appropriate with the acquisition and restructuring providing the platform to execute these strategies.

In 2009*, the Group maintained its focus on delivering its goals despite market turbulence and the process of acquisition. In 2010 we expect that economic conditions will remain challenging and initially our focus will be on further developing the foundations of our business from which we can realise the full potential of the Group.

*All references to 2009 achievements are for the full year; encompassing the achievements of the Pearl businesses from 1 January 2009

Goals	Strategies	Key 2009 achievements	2010 priorities
Maximise business performance and value			
– Deliver predictable cash flows – Increase MCEV within Phoenix Life – Increase profits within Ignis Asset Management	– Implement single life company structure – Enhance Group-wide risk and capital management – Grow third-party asset management franchise	– Pro forma UK holding company cash inflows of £716 million – Management actions generated £155 million of added embedded value – First phase of life company fund mergers completed – Pro forma Ignis Asset Management third-party asset inflows of £1.3 billion – Agreed plans to repatriate life company asset management and to establish new fund structures within Ignis Asset Management	– Drive further cash flow acceleration and value creation within Phoenix Life – Continue programme to rationalise life companies – Enhance the Group-wide risk and capital management frameworks – Increase third-party asset management business

Goals	Strategies	Key 2009 achievements	2010 priorities
Improve customer outcomes			
– Demonstrate an understanding of customer needs – Deliver consistent industry-standard customer service – Provide easy access to information and communicate clearly – Ensure policyholder security – Improve policyholder returns and growth opportunities	– Extend customer research and improvement programmes – Optimise estate distribution – Extend product performance review programme – Maintain strong capital policies	– Overall service level maintained at above 90 percent and improved transaction times on high volume processes – Complaint volumes reduced from 2008 and speed of complaint-handling response improved – Increased speed of processing Open Market Options – 1st phase of Phoenix Life product review completed on target – Above benchmark fund performance	– Following continued customer research implement appropriate initiatives to enhance customer experience – Develop alternative solutions for low value products – Pursue management actions to enhance distributable with profit fund estate – Develop with profit fund restructure strategy

Goals	Strategies	Key 2009 achievements	2010 priorities
Sustain a robust and scalable business model			
– Ensure long-term ability to service debt – Optimise capital and debt structures – Operational excellence in Phoenix Life and Ignis Asset Management – Share register matched to long-term ambitions of the Group	– Increase share liquidity – Debt and capital simplification – Transform Phoenix Life operations – Integrate operating platforms within Ignis Asset Management	– Benefit of acquisition and restructuring of some £1 billion – Secondary listing on LSE – Further outsourced Phoenix Life operations and renegotiated improved terms on existing contracts – Closure of Phoenix Life Glasgow operations on track and the transition plans for the Peterborough operations accelerated – Integration of the businesses of Axial and Ignis Asset Management under the Ignis brand	– Achieve Premium Listing on LSE – Maintain strong financial position and further simplify capital structures – Continue life company and outsourcer transformation programmes – Complete Ignis Asset Management operational integration – Achieve all Solvency II programme 2010 milestones

Goals	Strategies	Key 2009 achievements	2010 priorities
Be a place where people want to work			
– High levels of employee engagement – Strong and effective leadership – Clear communication – Fair reward and development policies and practice	– Active employee engagement programme – Enhance support framework for staff impacted by organisational restructuring – Leadership development programme	– Established employee engagement survey and action plans agreed – Flexible benefits scheme implemented – Senior management leadership development programme initiated – "Next Steps" programme implemented to support exiting staff – Announced new people values – Launched employee share save scheme	– Embed recently announced people values – Implement and further develop action plans from 2009 engagement survey – Strengthen Group succession planning process – Expand the leadership development programme

Goals	Strategies	Key 2009 achievements	2010 priorities
Build an industry-wide reputation			
– Recognised as the industry leader in closed life fund consolidation – Safe delivery of customer outcomes – Stakeholder confidence in our business model and governance	– Defined and robust corporate governance – Proactive and open stakeholder engagement – Champion of closed life fund issues – Enhance relationships with key stakeholders	– Enhanced corporate governance structure implemented – Strengthened our non-executive and executive management teams – Established Investor Relations and Corporate Communication teams	– Develop Phoenix Group brand awareness – Strengthen investor relations capability – Increase market, industry and media engagement – Further strengthen corporate governance arrangements

Goals	Strategies	Key 2009 achievements	2010 priorities
Pursue value adding acquisitions			

- In-depth market awareness and open engagement with vendors
- Rigorous selection and evaluation
- Execution and integration are a core competency

- Proactive relationships with potential vendors
- Identification and evaluation of opportunities that offer significant value enhancement and synergy benefits
- Right skills and support

- Market analysis identified future acquisition opportunities

- Continued analysis and assessment of opportunities
- Discuss market opportunities with key market participants

C) Performance

Key performance indicators

The Group's financial key performance indicators ("KPIs") are those that demonstrate the financial performance and strength of the Group as a whole.

These KPIs comprise:

P	Pro forma UK holding company cash inflows	£716 million
	IGD capital surplus	£1.2 billion
	Group MCEV	£1,827 million
P	Pro forma IFRS operating profit	£457 million
	IFRS operating profit	£282 million
	Dividend per share	€0.17 per share
	Assets under management	£66.9 billion
P	Pro forma asset management operating profit	£34 million

P Pro forma - the Board has analysed the Group performance with reference to certain pro forma financial information.

Where pro forma financial information is presented it is clearly indicated as being pro forma.

The Group financial KPIs are set out below. Comparatives are not provided since Phoenix Group Holdings was a SPAC during 2008.

Certain KPIs are calculated on a pro forma basis for 2009. The pro forma KPIs are identified as such below.

(P) Pro forma UK holding company cash inflows - £716 million

The Board's intention is to build a long-term base of owners through the development of a progressive dividend policy. The Board seeks to achieve this through improving UK holding company cash inflows:

Analysis: Continued strong cash generation by the Group's operating subsidiaries has allowed the Group to exceed its full year target of more than £500 million in UK holding company cash inflows

As at 31 December 2009 the Group has achieved £275 million of its cash flow acceleration target of £500 million by the end of 2010

Definition and calculation: UK holding company cash inflows are a measure of cash and cash equivalents remitted by the Group's operating subsidiaries to the UK holding companies[1] and are available to cover dividends, bank interest and other items

The 2009 KPI is pro forma and includes the cash flows of the Pearl businesses for the full year

Quantified target: Annual UK holding company cash inflows target of £400 to £500 million. In addition, an accelerated UK holding company cash inflows target of over £500 million by the end of 2010

1 - UK holding companies are PLHL, Pearl Group Holdings (No.2) Limited, Impala Holdings Limited, Pearl Life Holdings Limited, Pearl Group Holdings (No.1) Limited, PGH (LC1) Limited, PGH (LC2) Limited, PGH (LCA) Limited and PGH (LCB) Limited.

Estimated IGD capital surplus as at 31 December 2009 - £1.2 billion

IGD surplus is a measure of the capital strength of the business:

Analysis: The estimated IGD surplus at 31 December 2009 has increased by over £500 million from the 1 January 2009 pro forma position of £673 million, primarily as a result of the cash injection from Phoenix Group Holdings and strong performance of the non-profit funds, partially offset by financing costs. The IGD surplus represents 132 percent coverage of regulatory requirements

Definition and calculation: The IGD surplus is a regulatory capital measure which calculates surplus capital at the highest EEA level insurance group holding company, which is PLHL. IGD surplus is defined as Group regulatory capital employed less the Group regulatory capital requirement

Quantified target: Group capital resources of 125 percent of the regulatory requirement

Group MCEV - £1,827 million

The Board considers that MCEV provides owners with the most relevant and consistent means of assessing the Group's ability to manage the closed book of business effectively:

Analysis: The Group continues to focus on improving the operating performance of its underlying businesses and the Group's embedded value remains in line with management's expectations

As at 31 December 2009 the Group has achieved £155 million of its £300 million increment to embedded value target by the end of 2010

Definition and calculation: MCEV supplementary information – basis of preparation within the Performance section explains the definition and calculation

Quantified target: the Group's target is to increase embedded value (before payment of interest, debt principal and dividends) by up to £300 million through management actions by December 2010 and £100 million per annum thereafter to 2014. This includes targeted benefits in respect of management services actions that will not be included in the MCEV under the Group's methodology

(P) Pro forma IFRS operating profit

IFRS operating profit - £457 million (pro forma)& £282 million

The Board considers that IFRS operating profit is a more representative measure of performance than profit before tax as it provides long-term performance information and gives an insight into the Group's ability to generate cash flows to support dividends:

Analysis: The IFRS operating profit of £282 million reflects a strong performance in continuing volatile economic conditions

Definition and calculation: The Group operating profit – IFRS section explains the definition and calculation of IFRS operating profit

Pro forma IFRS operating profit: To provide a basis for future comparison, a pro forma IFRS operating profit for the year ended 31 December 2009 of £457 million is disclosed

The pro forma IFRS operating profit is calculated as the operating profit of the Group plus the Pearl businesses for the period prior to their acquisition by Phoenix Group Holdings

Dividend per share in respect of the 4-month period to 31 December 2009 - €0.17 per share (€0.50 per share pro rata from the date of acquisition of the Pearl businesses)

This is a measure of owner return. In an environment of low interest rates, the Group recognises that dividends are important to owners[1]:

Analysis: Phoenix Group Holdings legally acquired the Pearl businesses on 2 September 2009 and therefore a final pro-rated dividend is intended to be paid in 2010 in respect of the period to 31 December 2009

Quantified target: Whilst it remains restricted by its credit agreements, the Group initially intends to pay a dividend of €0.50 per share per annum

1 Phoenix Group is subject to Cayman Islands Companies Law. Under Cayman Companies Law distributions can be made out of profits or share premium subject, in each case, to a solvency test. The solvency test is broadly consistent with the Group's going concern assessment criteria. Therefore distributions may also be made by Phoenix Group Holdings out of share premium.

Assets under management ("AUM")
£66.9 billion AUM

(P) Pro forma asset management IFRS operating profit
£34 million asset management IFRS operating profit

For the Ignis Asset Management segment, assets under management are a key driver of revenues and therefore impacts owner value:

Analysis: Total assets under management saw a small reduction from the pro forma position at 1 January 2009 of £1.3 billion (1.9 percent) to £66.9 billion as the net run-off of the closed life business was largely offset by positive changes in market values on in-house and third party assets under management

To provide a basis for future comparison, the pro forma asset management operating profit figure which includes 12 months of the Pearl businesses is £34 million

Definition and calculation: AUM represents all assets actively managed or administered by the asset management operations of the Group

The Group operating profit – IFRS section explains the definition and calculation of IFRS asset management operating profit

Group performance

Basis of preparation

This Group performance commentary provides a review of the Group's development and performance for the year and of its financial position at the year end on both an IFRS and an MCEV basis. Cash generation is a key measure of the Group's performance and the Cash generation section sets out an analysis of the UK holding company cash flows for a full year.

The Board considers that the MCEV methodology represents a more meaningful basis of reporting the value of the Group's life companies and the drivers of performance than IFRS.

Given the acquisition of the Pearl businesses part way during the year, the Board considers it helpful to present, on a pro forma basis, what would have been the 12 month result had the Pearl businesses been acquired from 1 January 2009. The pro forma results represent the results of the Group together with the results of the Pearl businesses prior to their acquisition by Phoenix Group Holdings.

Acquisition of the Pearl businesses

In July 2009 the owners of Phoenix Group Holdings voted in favour of the acquisition of the Pearl businesses. The total consideration for the acquisition was £493 million. The fair value of net assets acquired was £416 million, with the difference of £77 million representing goodwill. The goodwill is attributable to the Ignis Asset Management business and the management services operations within Phoenix Life.

The net assets acquired included acquired in-force business of £2.2 billion. This represents the present value of the estimated surpluses that should emerge on the purchased book of business over time. In addition, the net assets acquired include the value assigned to customer relationships and other intangibles of £476 million.

Information on the fair values of the assets and liabilities acquired is given in the consolidated IFRS financial statements.

Group performance – Cash generation

Cash generation

The Group's cash flows are generated from the interest earned on capital, the release of excess capital as the life funds run down, policyholder charges and management fees earned on assets under management. The Group's closed life funds provide predictable fund maturity and liability profiles, creating expected long-term cash flows for distribution to policyholders and owners and repayment of outstanding debt. Although investment returns are less predictable, investment risks are mainly borne by policyholders in accordance with the terms of the relevant policies.

Pro forma UK holding company cash flow

The statement of cash flows prepared in accordance with IFRS combines cash flows relating to policyholders and cash flows relating to owners, but the practical management of cash within the Group maintains a distinction between the two, as well as taking into account regulatory and other restrictions on availability and transferability of capital. For this reason, the following discussion of cash flows focuses on the UK holding company cash flows (i.e. the holding companies under Phoenix Group Holdings) for the year ended 31 December 2009, which reflect cash flows relating only to owners and which are, therefore, more representative of the cash that could potentially be distributed to the Group's owners.

This cash flow reflects the cash receipts from the operating subsidiaries to the Group's UK holding companies, as well as the uses of the cash receipts. The surplus owner cash will be used to fund inter alia the payment of Phoenix Group Holdings' dividend in April 2010.

Pro forma UK holding company cash inflows from the operating subsidiaries for the year were ahead of target at £716 million, compared to the 2009 target of £500 million.

The table below sets out the cash remittances to the UK holding companies and the uses of the cash remittances:

Pro forma UK holding company cash flow £m	Year ended 31 December 2009*
Cash receipts	
Cash receipts from life companies	466
Cash equivalents released from life companies	194
Cash receipts from Ignis Asset Management	21
Cash receipts from service companies	35
Total receipts of cash and cash equivalents[1]	716
Uses of cash	
Non-recurring cash outflows	
Settlement with Royal London	240
IT and other business transformation costs	67
Debt interest[2]	72
Transaction and restructuring costs	30
Pension scheme contributions	25
Other	10
Total non-recurring outflows	444
Recurring cash outflows	
Pension scheme contributions[3]	33
Other operating expenses	27
Debt interest	102
Total recurring expenses	162
Total uses of cash	606

* Includes 12 months results of the Pearl businesses

1. Amounts received by UK holding companies in respect of group relief are included within cash receipts from the relevant subsidiaries

2. Includes £7 million of interest on swaps

3 Certain contributions are made directly by service companies to the pension scheme

Cash receipts

£466 million of cash and £194 million of cash equivalents were remitted by Phoenix Life from the emergence of surplus and regulatory capital releases. In addition a number of management actions have contributed to these remittances including the benefit of fund mergers and the resolution of specific legacy issues.

Cash equivalents

As a result of resolving certain legacy issues, receipts from Phoenix Life in the year also included remittance of a £170 million receivable due from Royal London to one of the life companies. This receivable was used to offset amounts due to Royal London by other Group companies. Following a payment to Royal London in December 2009, the Group's true-up liabilities[1] to Royal London have now been settled.

1 In connection with their acquisition of Resolution plc in 2007, the Pearl businesses transferred certain assets of Resolution plc to Royal London for total consideration of £1.3 billion (subject to certain post-closing adjustments, or "true-ups").

IT and other business transformation costs

The Group's UK holding companies incurred IT and other business transformation costs of £67 million in 2009, including costs associated with the Group's transformation programme with its outsourcers. Known IT and other business transformation costs of the UK holding companies are expected to reduce by between 25 and 50 percent in 2010, and by a further 50 percent in 2011, when the current operational projects are expected to be completed.

Pension scheme contributions

During 2007 the Pearl businesses and the Trustees of the Pearl Group Staff Pension Scheme entered into a contract under which the Pearl businesses guaranteed returns on the defined benefit Pearl Scheme assets sufficient to ensure that there would be no funding shortfall by 30 June 2027. As an integral part of Phoenix Group Holdings' acquisition of the Pearl businesses, agreement was reached with the Trustees of the Pearl Group Staff Pension Scheme to replace the existing funding guarantee with a schedule of cash contributions of £50 million in 2009 followed by cash payments of £25 million per annum (subject to satisfaction of capital resource requirements) for a period of 10 years, commencing on 30 September 2010. The first cash payment from the holding companies to the Pearl Group Staff Pension Scheme of £50 million (included above as £25 million recurring and £25 million non-recurring) occurred in October 2009.

Debt interest

The UK holding companies paid interest to their lending banks and Royal London of £167 million in 2009. Annualising the £34 million post acquisition financing costs on this debt (as set out in the Group operating profit – IFRS section) provides a more representative indication of the Group's future debt financing commitments than the full year cash payments and forms the basis for the recurring, non recurring split as provided above.

Group performance – MCEV

Basis of preparation

Whilst the IFRS consolidated financial statements consolidate the results of the Pearl businesses for the period from acquisition on 28 August 2009 to 31 December 2009, the pro forma MCEV results include a full year's contribution for the acquired Pearl businesses. The pro forma MCEV results are therefore based on the results of the Group plus the Pearl businesses for the period prior to their acquisition by Phoenix Group Holdings.

The supplementary MCEV information reflects the financial position of the Group at 31 December 2009. The asset management and management service businesses are included in the Group MCEV at the value of IFRS net assets and do not include the future earnings from its existing business. This is because, in the opinion of the Directors, applying the CFO Forum MCEV principles and guidance published in October 2009 to these businesses would not provide a fair reflection of the Group's financial position as explained in the "Restatement of the 31 December 2008 Embedded Value" section.

The Phoenix Group Market Consistent Embedded Value methodology (referred to herein and in the supplementary information as MCEV) is in accordance with the MCEV principles and guidance published by the CFO Forum in October 2009, except that:

- risk-free rates have been defined as the annually compounded UK government nominal spot curve plus 10 basis points rather than as a swap rate curve
- no allowance for the costs of non-hedgeable risk has been made because, in the opinion of the Directors, the Group operates a robust outsourcer model in terms of operational risk, does not write new business, is focused entirely on the back book, and has succeeded in closing out significant legacy risks. The theoretical value of costs of residual non-hedgeable risk is disclosed separately in the Basis of preparation in the note 1 to the MCEV supplementary information
- the value of the asset management and management service companies are calculated on an IFRS basis

Group MCEV operating earnings

The Group generated pro forma MCEV operating earnings of £374 million before tax for the year ended 31 December 2009.

The Board is pleased to report that embedded value performance was strong in a challenging trading environment and reflects the resilient performance of Phoenix Life and Ignis Asset Management throughout the year.

Pro forma £ million	Year ended 31 December 2009*
MCEV operating earnings	
Life MCEV operating earnings	380
Management services operating profit	14
Ignis Asset Management operating profit	34
Corporate operating loss	(54)
Group MCEV operating earnings before tax	374
Tax on operating earnings	(105)
Group MCEV operating earnings after tax	269

* Includes 12 months of results of the Pearl businesses

Life MCEV operating earnings (after tax)

Other than vesting annuities, the Group's Life operations are closed to new business. The principal underlying components of the life MCEV earnings are therefore the expected existing business contribution together with non-economic experience variances and assumption changes.

Pro forma £ million		Year ended 31 December 2009*
Expected existing business contribution		95
New business value		22
Non-economic experience variances and assumption changes		
– Experience variances	62	
– Other operating variances	21	
– Assumption changes	73	
Total non-economic experience variances and assumption changes		156
Life MCEV operating earnings after tax[1]		273

* Includes 12 months of results of the Pearl businesses after tax

1 Life MCEV operating earnings is derived on an after tax basis. For presentational purposes Life MCEV operating earnings before tax has been calculated by grossing up the after tax Life MCEV operating earnings using a tax rate of 28 percent. Life MCEV operating earnings before tax of £380 million is therefore calculated as £273 million (as above) grossed up for tax at 28 percent

Expected existing business contribution

The expected contribution on the existing business for the year ended 31 December 2009 of £95 million after tax represents the expected return on the opening MCEV using a 1 year gilt forward rate plus the Group's short-term expectations of excess investment returns on equities, properties and bonds. This rate is expected to increase in line with the forward gilt yield curve.

New business value

New business profits generated during the year amounted to £22 million after tax and represent the value of vesting pension policies not reflected in the opening MCEV. These arise from pension policies which have no attaching annuity guarantees.

The new business margin is 5 percent after tax and represents the ratio of the net of tax new business value to the amount received as new single premiums.

Non-economic experience variances and assumption changes

The Life divisions' non-economic experience variances and assumption changes contributed £156 million to MCEV pro forma operating earnings after tax for the year ended 31 December 2009.

Favourable experience and other operating variances of £83 million primarily related to several management actions including the resolution of certain legacy issues, partially offset by the strengthening of regulatory capital requirements and capital policy in the life companies following the acquisition of the Pearl businesses by Phoenix Group Holdings. Favourable assumption changes of £73 million mainly relates to harmonisation of longevity assumptions across the Group and the results of an annuitant survival investigation.

Management services

The operating profit for management services comprises income from the life companies in accordance with the respective management service agreements less fees related to the outsourcing of services and other operating costs.

Management services generated an operating profit before tax of £14 million for the year ended 31 December 2009, reflecting a business as usual outsourcer average expense per policy of £24.[2]

Further on-going site rationalisation and staff reductions are expected to enhance annual cost savings, together with other initiatives related to the renegotiation of arrangements with outsourced service providers and aligning core business and administrative processes across the Group.

2 Recurring outsourcer expenses for the year divided by the average number of in-force policies for the year (7.4 million). The policy count is based on the Pearl businesses average policy count for the year.

Ignis Asset Management

In the face of volatile economic conditions the fund management business recorded a pro forma operating profit before tax of £34 million before tax for the year ended 31 December 2009.

Pro forma £ million	Year ended 31 December 2009*
Retail revenue	14
Institutional and international revenue	15
Life fund revenue	82
Total revenues[3]	111
Expenses[3]	(77)
Ignis Asset Management operating profit before tax	34

* Includes 12 months of results of the Pearl businesses

3 Revenues and expenses are stated net of rebates from collective investment schemes

Profits in the first half of the year were impacted by a number of factors, including significantly lower equity market levels and the depressed conditions of the commercial property market which resulted in a reduction in average funds under management and consequently lower fees. Equity markets improved significantly in the second half of the year and the commercial property market is also showing signs of recovery. The following diagram shows the development of assets under management during the year.

Pro forma £ billion	Year ended 31 December 2009*		
	Life companies	Third party	Total
Opening assets under management at 31 December 2008	61.0	7.2	68.2
Inflows	-	1.3	1.3
Outflows	(4.6)	(0.9)	(5.5)
Market movements	3.7	0.7	4.4
Transfer to Royal London	-	(1.5)	(1.5)
Closing assets under management at 31 December 2009	60.1	6.8	66.9

* Includes 12 months of results of the Pearl businesses

Internal funds under management reduced by £0.9 billion (1.5 percent) to £60.1 billion in the twelve month period as positive changes in market values of £3.7 billion offset the run-off of the closed life business of £4.6 billion.

In line with the Group strategy to consolidate fund management under Ignis Asset Management £1.3 billion of Phoenix Life assets currently managed by a third-party are due to be transferred to Ignis Asset Management in 2010. In addition, approximately £5.5 billion of Life funds managed by a third-party on a passive basis are being transferred to Ignis Asset Management in 2010 where they will be managed on an active basis. The Board is confident this will enhance policyholder returns, and will also benefit owners as the Group moves to managing the assets on a single platform on a consistent basis.

Third-party inflows were £1.3 billion in the year mainly reflecting strong sales in retail products and liquidity funds on the back of improving market sentiment and strong investment performance. The liquidity fund outperformed the IMMFA sector by 57 basis points achieving a gross total return of 1.63 percent over 2009.

Corporate

The Group's business structure includes a Corporate Office that provides a coordination and oversight function. The Corporate Office's operating loss of £54 million before tax for the year ended 31 December 2009 includes:

– corporate office costs and project spend of £14 million

– net expected charge on the Pearl Group Staff Pension Scheme of £22 million and a £17 million contribution to the PGL pension scheme. The £17 million contribution is an expense under the Group's MCEV basis as a deduction to the Group's MCEV is made for pension schemes in deficit, but no credit is taken for pension scheme surpluses

Reconciliation of Group MCEV operating earnings to Group MCEV earnings

Group MCEV operating earnings is reconciled to the Group MCEV earnings, as follows:

Pro forma £ million	Year ended 31 December 2009*
Group MCEV operating earnings after tax	269
Economic variances on covered business	701
Economic variances on non covered business	(245)
Non-recurring items	(78)
Gain on debt refinancing	491
Finance costs attributable to owners	(390)
Tax on non-operating earnings	(197)
Group MCEV earnings after tax	551

* Includes 12 months results of the Pearl businesses

Economic variances on covered business

Positive economic variances in 2009 of £504 million after tax reflect the benefit of the reduction in credit spreads on corporate bonds and favourable equity and yield movements, partially offset by an increase of £36 million in the market value of listed debt issued by Phoenix Life Limited (ex Scottish Mutual Assurance).

Economic variances on non covered business

The economic variances on non-covered business of £245 million before tax primarily relates to the increase in the market value of listed debt issued by the Group's subsidiary Pearl Group Holdings (No. 1) Limited and Phoenix Group Holdings warrants, which reduced MCEV earnings by £169 million and £51 million respectively. In addition, the economic variances include a £29 million foreign exchange loss incurred by Phoenix Group Holdings primarily related to its euro cash holdings prior to its capital injection into the Pearl businesses. Having reduced its euro cash holdings, Phoenix Group Holdings' exposure to foreign exchange fluctuations has reduced.

Non-recurring items

Non-recurring items reduced pro forma embedded value by £78 million before tax and primarily includes:

– £27 million of costs associated with the Phoenix Life site rationalisation and associated staff reductions and the Group's transformation programme with its outsourcers

– £44 million of acquisition related expenditure incurred by Phoenix Group Holdings subsidiaries

– A charge of £78 million after tax as a consequence of the restructuring of the Pearl businesses external debt which reduced the expected tax attributes available to the Group to relieve the tax on the emerging surpluses from the operating businesses

– A charge of £12 million after tax related to the court approved Guaranteed Annuity Option Compromise Scheme for Phoenix and London Assurance. This removed longevity risk from the business whilst providing policyholder benefit enhancements

– Offset by a profit of £102 million after tax as a result of reassessing the impairment of a loan made to the Phoenix & London Assurance long-term fund. The improved recoverability of the loan reflects the outcome of risk management activity within Phoenix & London Assurance and the improved financial position of the fund

Gain on debt refinancing

As part of their acquisition by Phoenix Group Holdings, the Pearl businesses successfully refinanced their external borrowings resulting in an overall reduction of £575 million in exchange for cash and an issue of warrants totalling £84 million.

Finance costs attributable to owners

Pro forma £ million	Year ended 31 December 2009*
Debt finance costs[1]	176
Debt issue costs	202
Other finance costs	12
Finance costs attributable to owners	390

* Includes 12 months results of the Pearl businesses

1 Finance costs on the Impala and Pearl facility agreements (and associated swap interest) and the Royal London PIK notes

Debt finance costs include interest of £142 million on the holding company debt for the 8 month period prior to the refinancing (as discussed above) and interest on the refinanced debt on amended terms thereafter of £34 million for the final 4 month period.

As part of Phoenix Group Holdings' acquisition of the Pearl businesses, fees of £202 million were paid to the banks as consideration to facilitate the transaction. The consideration was in the form of equity issued to the lenders by Phoenix Group Holdings and therefore resulted in a corresponding increase in capital. Under IFRS these debt issue costs are taken into account in determining the cost of acquisition of the Pearl businesses.

Tax on non-operating earnings

Tax on non-operating earnings includes £199 million of tax relating to economic variances and non-recurring items related to covered business.

31 December 2009 MCEV

The Group MCEV increased by £783 million over the year to £1,827 million at 31 December 2009. The increase was mainly due to MCEV profits generated in the year, as discussed above, of £551 million, capital movements of £290 million offset by other comprehensive income items of £58 million.

Restatement of the pro forma 31 December 2008 Embedded Value

Certain changes have been made to the previously reported embedded value of the Pearl businesses. These changes have been implemented to align the methodology more closely with the CFO Forum principles.

Pro forma £ million	Year ended 31 December 2008
	Total
Historical pro forma net EV as disclosed in the Proxy Statement as at 31 December 2008	1,265
Phoenix Group Holdings IFRS Net Assets at 31 December 2008	573
Inclusion of Opal Re MCEV at 31 December 2008	12
Pro forma Group MCEV before methodology changes	1,850
Methodology changes:	
Removal of PVFP of non-covered business	(630)

Liquidity premiums	(251)
Vesting annuities	65
Other changes	10
Pro forma Group MCEV at 31 December 2008	1,044

Inclusion of Opal Re MCEV at 31 December 2008

As Opal Re is now part of the Group it is included within covered business from 31 December 2008 and is valued on a basis consistent with the annuity business within the life companies.

Removal of PVFP on non-covered business

Asset management and management service companies have been excluded from the definition of covered business. Under CFO Forum principles and guidance productivity gains should not be recognised until achieved. This treatment is inconsistent with the cost profile of a closed fund where continual cost reductions are expected to maintain unit costs as the business runs off. In the opinion of the Directors, if the MCEV principles and guidance were to be applied to the asset management and the management services companies, it would not provide a fair reflection of the Group's financial position. These companies are therefore reported alongside the Group's other non-life Group companies at their IFRS net asset value.

Liquidity premiums

The allowance for default risk has been increased to include an explicit margin for unexpected default risk premium. This reduces the value of liquidity premiums within the MCEV. This change is to align the Group's methodology with the risk-neutral principles that form the basis of the CFO Forum's MCEV methodology.

Vesting annuities

The MCEV places a value on the profits expected to be earned on annuities arising from policies vesting with guaranteed annuity terms. These policies are excluded from the definition of new business on the basis that the annuity being provided is an obligation under an existing policy and the life companies are already reserving for the cost of these guarantees.

Group performance – IFRS

Group operating profit – IFRS

The Group has delivered a strong performance, which includes 4 months of the results of the Pearl businesses, despite the generally unstable economic and financial conditions.

The Group generated an IFRS operating profit[1] of £282 million for the year ended 31 December 2009. This operating profit represents 4 months of the results of the Pearl businesses which came under the control of Phoenix Group Holdings for accounting purposes from 28 August 2009. The pro forma IFRS operating profit for the year ended 31 December 2009 is £457 million.

This performance demonstrates the strength of the Group's run-off business model:

£ million	Year ended 31 December 2009	Year ended 31 December 2009 (pro forma)*
IFRS operating profit		
Phoenix Life	285	469
Ignis Asset Management	14	34
Corporate costs	(17)	(46)
Operating profit before tax	282[3]	457[3]

*Includes 12 months results of the Pearl businesses

Pro forma IFRS operating profit before tax

The pro forma IFRS operating profit before tax of £457 million reflects the positive performance of the Pearl businesses throughout the year. The post acquisition performance was relatively stronger than the year as a whole which is a reflection of the improved market conditions in that period relative to the first half of the year.

The life funds' performance benefited from improving market conditions, narrowing credit spreads, several planned management actions and improving non-economic experience throughout the year.

Ignis Asset Management's performance was favourable throughout the year generating a pro forma IFRS operating profit before tax of £34 million. The post acquisition period reflects the recovery in corporate bonds and equity markets.

The following commentary focuses on the reported results of the Group.

Phoenix Life[2] – reported operating profit before tax

£ million	Year ended 31 December 2009
With profit	20
With profit where internal capital support provided	30
Non-profit and unit-linked	201
Longer term return on owners' funds	17
Management services	17
Phoenix Life operating profit before tax	285[3]

1 Operating profit, a key metric used in both IFRS and MCEV reporting, reports the profit (or loss) in a financial year but excludes short-term fluctuations in investment returns and other items considered to be non-operating by management.

2 Operating profit for Phoenix Life is based on expected investment returns on financial investments backing owners and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities. Operating profit includes the effect of variances in experience for non-economic items, such as mortality, persistency and expenses, and the effect of changes in non-economic assumptions. Changes due to economic items, for example market value movements and interest rate changes, which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed separately outside operating profit. Phoenix Life operating profit is net of policyholder finance charges and policyholder tax.

3 Operating profit is presented before adjusting items

The owners' one-ninth share of policyholder with profit bonus of £20 million in the 4 month post-acquisition period reflects the impact of lower terminal bonuses in 2009 following difficult market conditions. The market recovery in the financial investments backing the with profit business experienced in the latter half of the year is expected to be considered in bonus rates in 2010 along with the market performance for the first half of 2010.

The operating profit on with profit funds where internal capital support has been provided was £30 million in the 4 month post-acquisition period. The operating profit benefited from the impact of several management actions and harmonisation of longevity improvement factors across the Group and using updated industry tables. These favourable impacts were partially offset by a reduction in assumed surrender rates in funds with valuable policyholder guarantees.

The operating profit on non-profit and unit linked funds was £201 million in the 4 month post-acquisition period. This includes margin emergence and return on surplus assets of £52 million. This return was supplemented with favourable non-economic experience variances as well as assumption changes related to longevity (as discussed above) which were only partially offset by increased provisions for expenses as some funds moved from being managed on a passive to an active basis.

The longer term return on owners' funds for 2009 of £17 million reflects the asset mix of owners' funds, primarily cash based assets and fixed interest securities.

The operating profit for management services of £17 million comprises income from the life companies in accordance with the respective management service agreements less fees payable in relation to the outsourcing of services and other operating costs.

Ignis Asset Management

The Group's two asset management businesses have recently been integrated under the Ignis brand, with the aim of enhancing the brand and revenue generation of the asset management businesses.

Continued improvements in market conditions in the second half of 2009 had a positive impact on the results of the combined asset management business. Ignis Asset Management recorded an operating profit of £14 million in the 4 month post-acquisition period.

Corporate costs

The Corporate Office costs and project spend amounted to £8 million. The balance of the charge relates primarily to the net expected return on the pension scheme and share-based payment charges on warrants issued.

Reconciliation of IFRS operating profit to profit after tax

IFRS operating profit is reconciled to profit after tax, as follows:

£ million	Year ended 31 December 2009
Operating profit before adjusting items	282
Investment return variances and economic assumption changes on long-term business	145
Variances on owners' funds	(70)
Amortisation of acquired in-force business and other intangibles	(52)
Non-recurring items	(105)
Profit before finance costs attributable to owners	200
Finance costs attributable to owners	(49)
Profit before tax attributable to owners	151
Tax attributable to owners	(16)
Profit for the year attributable to owners	135

Attributable to:	
Owners of the parent	95
Non-controlling interests	40

Investment return variances and economic assumption changes on long-term business

The expected return on investments for both policyholder and owners' funds is based on opening economic assumptions applied to the funds under management at the beginning of the reporting period. Expected investment return assumptions are derived based on market yields on risk-free fixed interest assets at the start of each financial year. Margins are applied on a consistent basis across the Group to gross risk-free yields, to obtain investment return assumptions for equities and properties. The principal assumptions underlying the calculation of the longer term investment return are set out in note 5 to the IFRS financial statements.

Overall, the Phoenix Life business had net favourable investment return variances and economic assumption changes of £145 million for the 4 months ended 31 December 2009, largely reflecting narrowing credit spreads, stronger performance on hedge funds and favourable property returns.

Variances on owners' funds

The unfavourable variances on owners' funds of £70 million for the 4 months ended 31 December 2009 primarily relates to the increase in the fair value of the Phoenix Group Holdings warrants which are accounted for as a financial liability. In addition the variances include £29 million foreign exchange loss incurred by Phoenix Group Holdings primarily related to its euro cash holdings prior to the acquisition of the Pearl businesses.

Amortisation of acquired in-force business and other intangibles

Acquired in-force business and other intangibles of £2.7 billion were recognised on the acquisition of the Pearl businesses.

The acquired in-force business is being amortised in line with the run-off of the acquired businesses. Amortisation of acquired in-force business during the period totalled £45 million. Amortisation of other intangible assets totalled £7 million in the period.

For further information on these intangible assets refer to notes 3 and 33 to the IFRS financial statements.

Non-recurring items

Non-recurring items include:

A charge of £78 million related to the court approved Guaranteed Annuity Option Compromise scheme for Phoenix and London Assurance. This removed longevity risk from the business whist providing policyholder benefit enhancements. This is higher than the charge recognised under MCEV due to the more prudent reserving basis. It is expected that this loss will unwind in future periods as margins of prudence in reserving for liabilities unwind

Costs associated with the Phoenix Life site rationalisation and associated staff reductions totalled £19 million and the Group's transformation programme with its outsourcers amounted to £13 million.

Finance costs attributable to owners

£ million	Year ended 31 December 2009
Debt finance costs[1]	34
Other finance costs	15
Finance costs attributable to owners	49

1 Finance costs on the Impala and Pearl facility agreements (and associated swap interest) and the Royal London PIK notes

Tax attributable to owners

The Group tax charge for the year attributable to owners is £16 million. This represents an effective tax rate of 11 percent on profits (after policyholder tax) of £151 million.

The Company is exempt from tax in the Cayman Islands on any profits, income and gains for a period of 20 years from 15 January 2008. Consequently no tax was due from the Company in 2008 or 2009.

With effect from the acquisition of the Pearl businesses the Company has been managed and controlled from Jersey, where its permanent office premises are located, and as a Jersey resident holding company the Company is expected to be subject to a zero percent tax rate on its income. Consequently tax charged in these Accounts primarily represents UK tax on profits earned in the UK, where the principal life companies, excluding Opal Re, have their centre of operations.

The effective tax rate for 2009 has been impacted by a number of one-off events. These include the restructuring of National Provident Limited ("NPL"), which crystallised operational losses incurred in prior years, but not previously recognised for tax purposes, of £250 million.

As a result of tax losses brought forward and further losses realised by NPL in the year, the Group is not expected to pay any shareholder tax in 2009 and has significant excess tax losses and expenses at the end of the year which have not been recognised in full.

Capital management

Capital management framework

The Group's Capital Management Framework is designed to achieve the following objectives:

– Provide appropriate security for policyholders and meet all regulatory capital requirements whilst not retaining unnecessary excess capital

– Ensure sufficient liquidity to meet obligations to policyholders and creditors

– Meet the dividend expectations of owners as set by the Group's dividend policy

The framework comprises a suite of capital management policies that govern the allocation of capital throughout the Group to achieve the objectives under a range of stress conditions. The policies are defined with reference to policyholder security, creditor obligations, owner dividend policy and regulatory capital requirements.

The capital policy of each Group holding company is set by the Board of Phoenix Group Holdings and monitored each month at both executive and Board level. The policies ensure sufficient liquidity to meet creditor obligations and dividend expectations through the combination of cash buffers and strong cash flows from the Group's operating companies. Volatility in the latter is monitored at the executive and Board level through stress and scenario testing. Where cash flow volatility is judged to be in excess of the Board's risk appetite, de-risking activities are undertaken.

The capital policy of each life company is set by each life company Board and monitored on a daily basis. These policies ensure there is sufficient capital within each life company to meet regulatory capital requirements under a range of stress conditions. The capital policy of each life company varies according to the risk profile and financial strength of the company.

Regulatory capital requirements

Each UK life company must retain sufficient capital at all times to meet the regulatory capital requirements mandated by the FSA. In addition to EU-directive-based "Pillar 1" and group capital requirements, the FSA has also stipulated a "Pillar 2" of risk-based capital requirements that have been implemented in the UK. A life company's actual capital requirement is based on whichever of the Pillar 1 or Pillar 2 requirement turns out to be more onerous for the company. Each life company generally holds an amount of capital that is greater than the minimum required amount to allow for adverse events in the future that may use capital and might otherwise cause the company to fail the minimum level of regulatory capital test.

Pillar 1

With the exception of with profit businesses, the regulatory capital requirement under Pillar 1 is the total amount held in respect of investment, expense and insurance risks (the long-term insurance capital component ("LTICR")) and any additional amounts required to cover the more onerous of two specified stress tests (the resilience capital requirement ("RCR")). The regulatory capital requirement is then deducted from the available capital resources to give the regulatory basis excess capital.

A further test is required under Pillar 1 in respect of with profit funds which may result in an additional capital requirement referred to as the With Profit Insurance Capital Component (WPICC).

Pillar 2

The Pillar 2 capital requirements are based on a self-assessment methodology, the Individual Capital Assessment ("ICA"). This methodology determines the capital requirement to ensure that the life company's realistic liabilities can be met in one year's time with a 99.5 percent confidence level, or a one in 200 year event. The FSA reviews each life company's ICA and may impose additional capital requirements if necessary in the form of Individual Capital Guidance.

Insurance Groups Directive ("IGD")

FSA regulated insurance groups (including their holding companies) are also required to provide an assessment of capital adequacy on a group-wide basis to enable the FSA to assess both the level of insurance and financial risk within

the group and the capital resources available to cover that risk. The assessment is known as the IGD and is the Group's primary capital and solvency measure.

The Group's IGD assessment is made at the highest EEA level insurance group holding company, which is PLHL. PLHL is a subsidiary of Phoenix Group Holdings.

The components of the estimated IGD calculation are shown below:

	£bn
Group capital resources ("GCR")	5.0
Group capital resource requirement ("GCRR")	3.8
IGD surplus	1.2

The estimated IGD surplus has increased by over £500 million from 1 January 2009 to £1.2 billion at 31 December 2009. The estimated IGD surplus at 31 December 2009 represents 132 percent coverage of regulatory requirements, compared to an operating target of 125 percent. The key drivers of the improved solvency position are:

- As a consequence of the acquisition of the Pearl businesses £0.45 billion of additional capital was provided to the business operations. This improved estimated IGD surplus by approximately £0.4 billion
- Surplus transfers from non profit funds and other capital generation items improved estimated IGD surplus by approximately £0.2 billion. Following individual guidance from the FSA, the IGD surplus includes established surpluses in the non profit funds of UK life and pensions business which are available for transfer to shareholders. This improved the estimated IGD surplus by approximately £52 million which is included within the £0.2 billion
- Financing costs of approximately £0.1 billion.

Estimated IGD capital surplus movement £ billion	Year ended 31 December 2009*
IGD capital surplus at 1 January 2009	0.7
Capital injection at acquisition by Phoenix Group Holdings	0.4
Capital generation	0.2
Financing costs	(0.1)
Estimated IGD capital surplus at 31 December 2009	1.2
Margin	132%

*Includes 12 months results of the Pearl businesses

Sensitivity analysis

As part of the Group's internal risk management processes the estimated IGD surplus is tested against a number of financial and non-financial scenarios to ensure it remains in excess of the 125 percent target in a range of reasonably foreseeable circumstances. The results of that stress testing are provided below:

	£bn
Estimated IGD surplus	£1.22 (132% margin)
Estimated IGD surplus following a 20 percent fall in equity markets	£1.21 (144% margin)
Estimated IGD surplus following a 15 percent fall in property values	£1.21 (134% margin)
Estimated IGD surplus following a 75bps parallel decrease in yields	£1.23 (131% margin)
Estimated IGD surplus following credit spread widening[1]	£1.12 (131% margin)
Estimated IGD surplus following a combined 20 percent fall in equity markets, 15 percent fall in property, 75 bps fall in yields and credit spreads widening[1]	£1.14 (144% margin)

1 AAA – 100bps, AA – 113bps, A – 120bps,

BBB – 153bps, BB – 370bps, B – 613bps.

The GCRR includes a WPICC which is matched by GCR in the with profit funds. In stress scenarios, as the value of GCR falls, it is broadly offset by a corresponding decrease in the WPICC within the GCRR. Therefore, although both GCR and GCRR decline, the IGD surplus is not impacted to the same extent, which can cause the percentage margin to increase in stress scenarios.

Capital resources

The primary sources of capital used by the Group covering individual life company and Group capital requirements are equity, perpetual reset capital securities, subordinated debt and other borrowings.

Liquidity management

Details on the Group's objectives and policies for the management of liquidity risk are included within the Risk management report and note 42.3.3 of the IFRS financial statements.

Solvency II

Solvency II represents a new solvency framework for EU insurers that will replace all existing prudential regulation including Solvency I, Realistic Balance Sheets, ICA and the IGD. It is expected to come into force on 31 October 2012 and comprises a three-pillar approach that includes a formulaic minimum capital requirement (similar to the current ICA regime), supervisory review of the Group's own risk assessment and prescribed disclosure requirements.

Solvency II was adopted in the European Parliament on 22 April 2009 and the high level principles agreed in the "Level 1 Framework Directive" on 5 May 2009. The Committee of European Insurance and Occupational Pensions Supervisors ("CEIOPS") is currently consulting with the industry on the technical specifications of the formulaic capital requirements.

The Group expects Solvency II to result in an improved understanding of the link between risk and capital management and welcomes the increased focus on risk management that Solvency II will bring. The Group is concerned however, that the recent final advice from CEIOPS is more prudent than the Level 1 Framework Directive and more onerous than the existing Pillar 2 regime, in particular for annuity business. As currently drafted, the technical specifications would result in a significant increase in the capital requirements of the industry and the Group is currently working with the Association of British Insurers ("ABI") and other UK insurers through membership of the ABI's Solvency II working group with a view to ensuring that the final specifications are appropriate for the UK insurance market.

The Group's Solvency II programme was started in 2008 with its involvement in the fourth Quantitative Impact Survey exercise. The programme spans all areas of the business with multi-discipline workstreams in place. Due to the complexity of the Group's insurance business and the number of smaller life companies within the Group, the Group will pursue a partial internal model approach to Solvency II and will seek approval from the FSA to utilise its own risk assessment models for the material insurance entities within the Group. The formulaic approach will be adopted for smaller insurance entities such as Scottish Mutual International and the Group's general insurance business. Regular dialogue continues with the FSA that is focused on ensuring the Group is well positioned to achieve Wave 1 approval for its own internal model application.

Risk management

Risk management is an essential part of the Group's strategic agenda. The Board seeks to ensure that the Group understands and manages its risks accordingly; to either create additional value for its stakeholders or to mitigate any potentially adverse effects.

A risk framework is in place which seeks to establish a coherent and interactive set of risk management arrangements comprising formal committees, risk review functions, risk management policies and risk assessment processes. This framework allows informed decisions to be made by the relevant statutory and regulated entity boards and senior management. The framework defines how risks taken by the Group are managed and mitigated ensuring that initiatives are not evaluated purely in terms of the potential returns, but also in terms of the range of potential outcomes which may arise and their relative likelihood. The framework provides assurance that risks are being appropriately identified and managed and that an independent assessment of management's approach to risk management is being performed.

Risk culture, oversight and governance

Overall responsibility for approving, establishing and maintaining the risk framework rests with the Group Board. The Board recognises the critical importance of having efficient and effective risk management systems and appropriate oversight of their output. A clear organisation structure with documented, delegated authorities and responsibilities from the Phoenix Group Holdings Board to the Board of PLHL and ExCo is in place.

A series of divisional management oversight committees covering financial and operational risks exists within the Group. These committees are responsible for ensuring the risks associated with the divisional business activities are identified, controlled, monitored and reported to the relevant boards and board committees.

Each committee has formal terms of reference which are approved by the relevant divisional group executive team. Overall reporting of risk management and escalation of emerging issues is undertaken through divisional management committees to ExCo and reported to the PLHL and Group Boards.

Risk management is an evolving landscape and developments to augment risk culture and governance across the Group will continue. Actions taken recently include the appointment of a Group Chief Risk Officer in November 2009, the establishment of a Phoenix Group Holdings Board Risk Committee in early 2010 and improvements in consolidated risk reporting in line with current best practice. The Group sees these enhancements as key to supporting further strengthening of the Group's risk culture and maintaining it in line with current best practice guidelines.

Risk management framework overview

The Group's risk management framework is underpinned by its governance model which includes statutory boards, management boards, risk policies, oversight committees and established governance functions.

Three Lines of Defence

The Group operates a Three Lines of Defence model:

– First line: management of risk is delegated from the Group Board to the Group Chief Executive, PLHL Board and its ExCo members and through to divisional business managers

– Second Line: risk oversight is provided by the Group's divisional risk and compliance functions and established oversight committees

– Third line: independent verification of the adequacy and effectiveness of the internal risk and control management systems is provided by Board Audit Committees. The Board Audit Committees are supported by the Group Internal Audit function.

Risk appetite

The Phoenix Group risk appetite framework consists of a set of statements that articulate the risk appetite of the Group Board with respect to policyholder security, earnings volatility, liquidity and regulatory compliance.

A range of high level metrics and reporting mechanisms is in place to monitor risk appetite across the Group. Breaches of appetite are corrected through management action when appropriate.

Further development work is underway to establish risk appetite limits and trigger points in terms of capital and earnings impact, and ensure that such limits are aligned with capital resources and owner expectations.

Risk assessment processes
The Group has a standardised assessment framework for the identification and assessment of the different types of risk it may be exposed to and how much capital should be held in relation to those exposures. This framework is applicable across the Group as a whole and establishes a basis of consistency not only for the approach to risk assessment, management and reporting processes but also for determining and embedding capital management at all levels of the Group.

Risk assessment activity is a continuous process and is performed on the basis of identifying and managing the significant risks to the achievement of the Group's objectives. Stress and scenario tests are used to support the assessment of risk and analysis of the financial impact. The Board Committees, ExCo, senior management and specialist functions (e.g. Finance, Risk and Actuarial) review the various outputs of the risk assessments. A Group-level risk assessment process determines the most significant risks to the Group and the options available for their management. An overview of the key risks and uncertainties facing the Group is provided below.

Risk review functions
Group and the divisional operating units' risk functions provide oversight of the risk management processes across the Group. A central risk function is being created with responsibility for the oversight of the risk management framework, policy and standards across the Group. Risk review functions in each of the business units manage the framework in line with these standards. Their responsibilities include the evaluation of changes in the business operating environment and business processes, the assessment of the impact of these changes on risks to business and the monitoring of the mitigating actions. The risk functions also ensure that divisional risk committees are provided with meaningful risk reports and that there is appropriate information to assess risks.

Risk policies and categorisation
A policy framework exists, which sets out the high level risk appetite of the Group, together with risk management, internal control and business conduct standards for the Group's operating units.

The policies define:

– The Group's methods for the identification of risk and its interpretation

– Required structures to ensure the appropriate quality and diversification of assets in the context of the liabilities

– The Group's approach to ensuring that its customers are treated fairly

– Reporting requirements

Each policy is the responsibility of a member of ExCo who is charged with overseeing compliance with the policy throughout the Group.

Principal risks and uncertainties facing the Group

Risk	Impact	Mitigation
In times of extreme market turbulence, the Group may not have sufficient liquid assets to meet its payment obligations or may suffer a loss in value.	The Group has ongoing obligations to meet payments to creditors which are funded by the release of capital and profits from the underlying operating companies. The emerging cash flows of the Group may be impacted during periods of extreme market turbulence by the need to maintain appropriate levels of regulatory capital. The impact of market turbulence may also result in a material adverse impact on the Group's embedded value, financial condition and prospects.	The Group undertakes regular monitoring activities in relation to market risk exposure, including the monitoring of asset mixes, cash flow forecasting and stress and scenario testing. In response to this, the Group may implement de-risking strategies to mitigate against unwanted outcomes. The Group also maintains cash buffers at the holding company level to reduce reliance on emerging cash flows.
The potential limitation on distributions from the Group's FSA regulated companies may impair the ability of the Group to service its existing debt commitments.	The Group has ongoing principal repayment and interest obligations to a syndicate of lenders. In the event that transfers from the Group's insurance and investment management subsidiaries are limited by any law or regulatory action, this may impair the Group's ability to service these obligations. The implementation of directives and other legislative changes such as Solvency II could have this effect and may therefore have a material adverse effect on the Group's results, financial condition and cash flows, including the exercise by the external finance providers of their security rights over shares in Group companies.	The Group puts considerable efforts into managing relationships with our regulators so that we are able to maintain a forward view regarding potential changes in the regulatory landscape. The Group assesses the risks of regulatory change and their impact on our operations and lobbies where appropriate.

Significant counterparty failure.	The Phoenix Life segment is exposed to deterioration in the actual or perceived creditworthiness or default of issuers of relevant debt securities or from trading counterparties failing to meet all or part of their obligations, such as reinsurers failing to meet obligations assumed under reinsurance arrangements or derivative counterparties or stock-borrowers failing to pay as required. Assets held to meet obligations to policyholders include debt securities. An increase in credit spreads on such securities, particularly if it is accompanied by a higher level of actual or expected issuer defaults, could have a material adverse impact on the Group's financial condition.	The Group regularly monitors its counterparty exposure and has specific limits relating to counterparty credit rating. Where possible, exposures are diversified through the use of a range of counterparty providers. All reassurance and derivative positions are appropriately collateralised or guaranteed.
Adverse changes in experience versus actuarial assumptions.	The Group has liabilities under annuities and other policies that are sensitive to future longevity and mortality rates. Changes in assumptions may lead to changes in the assessed level of liabilities to policyholders. The amount of additional capital required to meet those liabilities could have a material adverse impact on the Group's embedded value, results, financial condition and prospects.	The Group undertakes regular reviews of experience and annuitant survival checks to identify any variances in assumptions.
Competition and the ability to finance acquisitions may make it difficult for the Group to grow.	There are other closed fund consolidators as well as a number of other potential purchasers. While the prices of closed fund life companies and portfolios may have decreased due to recent market conditions, there can be no assurance that prices will not increase if markets continue to recover. Moreover, the Group may face difficulties in obtaining additional third-party financing for any acquisitions.	The Group is well positioned to be the natural consolidator for closed funds and although there are no immediate plans for further acquisitions the Group continually monitors market developments.

A more detailed analysis of the Group's inherent exposures to key financial and insurance risks, including the Group's specific objectives and policies for managing its market, credit, liquidity and insurance risks are set out in note 42 to the IFRS financial statements.

D) Remuneration report

The Remuneration Committee is responsible for making recommendations to the Board on the Group's remuneration and compensation plans, policies and practices and for determining, within agreed terms of reference, specific remuneration packages for the Group Chairman, Executive Directors, members of ExCo and other senior managers in the Group.

As the company is incorporated in the Cayman Islands and currently has a Standard Listing on the Official List, the Company is not required to provide information contained in this Remuneration report in accordance with the UK Companies Act 2006. However, in line with its intention to seek a Premium Listing and the enhanced level of disclosure that will entail, the Company has sought to comply with these provisions voluntarily.

Remuneration Committee

The Board Remuneration Committee was formed in February 2010 following the appointment of additional independent Non-Executive Directors to the Board. The Chairman of the Remuneration Committee is Ian Cormack. The other members of the Committee are David Barnes and Isabel Hudson. The Group Chairman, Group Chief Executive and Group Human Resources Director are invited to attend meetings but are not present when their own remuneration is discussed.

Prior to the establishment of the Remuneration Committee, and following the acquisition of the Pearl businesses on 2 September 2009, remuneration recommendations were presented to the Board of Phoenix Group Holdings. Advice was provided during 2009 by Hewitt New Bridge Street ("HNBS") and they continue to advise the Remuneration Committee. HNBS provided no other services to the Group during the year and their terms of engagement are available from the Company Secretary. The Company Secretary acted as secretary to the Remuneration Committee.

Remuneration policy

The success of the Group is dependent, amongst other things, upon the ability to attract, motivate and retain highly-skilled management and other specialist personnel. Competition for such individuals in the life insurance and asset management sectors remains significant and is anticipated to remain so for the foreseeable future.

Following a recent review of remuneration arrangements, the Remuneration Committee concluded that a remuneration policy consistent with UK listed comparators should be adopted whereby:

- base salaries are set at broadly mid-market levels; and
- a competitive set of annual and long-term incentives are used so that a significant proportion of total remuneration is performance-linked, being subject to challenging targets without encouraging excessive risk taking.

In light of the above policy, and following a detailed benchmarking exercise, Executive Directors' base salaries have been increased with effect from 1 January 2010, and maximum (and target) bonus potential has been reduced for 2010, so that these elements of the package, and the structure of packages more generally, better reflect the market.

The Remuneration Committee has also considered the implications for the Group of the recommendations of the FSA Code of Practice on Remuneration Policies, published in August 2009 and the Walker Review of Corporate Governance of UK Banking Industry, published in November 2009 and have incorporated relevant recommendations where appropriate.

Summary of remuneration practice

The Committee reviews base salaries for Executive Directors (and senior executives) annually, having regard to:

- the rates for similar roles in listed life assurance, asset management and general financial organisations (but avoiding the ratchet effect of following median or upper quartile levels);
- the performance of the individual concerned, together with any changes in responsibilities which may have occurred during the year; and
- pay quantum and structure throughout the Group.

An annual bonus scheme is operated for all employees including executives and senior managers, (other than for Ignis Asset Management). Payment of annual bonuses is dependent upon performance against embedded value, internal cost control and risk management targets, together with business-aligned challenging personal targets. Within Ignis Asset Management, separate annual bonus arrangements are in place, which are subject to review and approval by the Remuneration Committee.

Long-term incentives are provided through the Long-Term Incentive Plan ("LTIP") which is designed to ensure that Executive Directors and other senior executives focus effort on those performance measures of greatest relevance to the Group and are appropriately retained. Participants receive awards of conditional shares in the Group which normally vest three years after they are awarded, subject to the satisfaction of performance conditions and continued service. The Group operates a separate LTIP for senior executives within Ignis Asset Management which focuses on growth in the value of the asset management business.

The Group also introduced and operated the Bonus Share Plan ("BSP") during 2009 which was designed to reward Executive Directors and senior executives for their efforts and performance with respect to the capital reorganisation in the second half of the year. There is no intention to grant further BSP awards given that the LTIP will be the primary long-term incentive vehicle going forward.

Pension benefits are provided to all employees, including the Executive Directors, via defined contribution or defined benefit pension schemes, with the latter now closed to new entrants. Annual bonuses and long-term incentives are non-pensionable, save for a pensionable bonus element in the Pearl Group Staff Pension Scheme, for which only members of the Money Purchase (and hybrid) sections of the scheme are eligible.

Sharesave Scheme

The Group is keen to align employee and wider owner interests through share ownership. All UK-based staff, including Executive Directors, employed on 30 November 2009, became eligible under defined criteria for grants of options to acquire shares under the Phoenix Group Holdings 2010 Sharesave Scheme (the "Scheme"). The Scheme provides for the grant of options to subscribe for Group shares at the end of either three or five years, using the proceeds from a savings contract entered into at the time the option was granted. Options under the Scheme have been granted with a 15 percent discount to the market price at the time of the grant. As at 19 March 2010, 834 participants held options over 1,159,069 shares under the Scheme.

Non-Executive Directors

Determination of the remuneration of Non-Executive Directors remains a matter for the whole Board (with the Non-Executive Directors absenting themselves) in accordance with the Articles. The only exception to this is the setting of the expense claim policy which is delegated to the Remuneration Committee to consider.

Non-Executive Directors do not have service agreements with the Group, but are engaged under a formal letter of appointment setting out the Group's expectations of them, including the amount of time they are required to spend on Group business. Appointment is for a fixed term of three years, terminable with one months' notice on either side. Any subsequent terms are considered by the Group's Nomination Committee. Non-Executive Directors are not eligible to participate in incentive arrangements or receive pension provision.

Executive Directors

Service agreements

On 2 September 2009, Jonathan Moss, Group Chief Executive and Simon Smith, Group Finance Director were both appointed to the Board of Directors. There are no other Executive Directors. Jonathan Moss has a service agreement dated 5 February 2010 and Simon Smith has a service agreement dated 30 March 2005.

Base salary and benefits

At the beginning of 2009, the Board of the former Pearl Group Limited determined that base salaries should not be increased for Executive Directors.

With effect from 1 January 2010, the Remuneration Committee approved increases in the base annual salaries of the Group Chief Executive to £650,000 (from £400,000) and for the Group Finance Director to £400,000 (from £380,000).

These increases follow a review of remuneration arrangements which included a detailed assessment of base salary levels in the life assurance sector and listed environment more generally and have been accompanied by a reduction in the value of bonus potential to better align packages to market levels following the adoption of a market consistent remuneration policy.

The Executive Directors' remuneration includes a non-pensionable car allowance which is paid monthly. Non-pensionable benefits-in-kind also include private medical insurance, income protection and life assurance.

Annual bonus

For 2009, bonus potential for the Executive Directors under the Group annual bonus scheme was as follows:

	Target* (% of salary)	Maximum (% of salary)
Jonathan Moss	100	200
Simon Smith	85	170

* Assumes "on target" financial and personal performance

For the purposes of assessing the corporate element of performance, the following targets apply:

- 60 percent – targeted improvements in the Group Embedded Value over 2009.
- 20 percent – actual cost management performance against the annual Operating Plan budget, and
- 20 percent – achievement of risk management targets, as determined by the achievement of predetermined reductions in the 2009 ICA relative to 2008.

The business performance targets and relative weightings were recommended by ExCo to the Board and applied to all employees, including the Executive Directors and the remaining members of ExCo. A corporate "multiplier" of 1.02% percent was then calculated, reflecting actual Group performance in 2009 against each of the targets (with 1.0 reflecting an overall "on target" performance and 2.0 being the maximum multiplier which can be applied where the "stretch" target is exceeded in each of the three measures). Actual bonus amounts were finally determined by a combination of the "multiplier" and personal performance ratings.

In addition to the above, the Remuneration Committee of the former Pearl Group Limited awarded bonuses to the Group Chief Executive and the Group Finance Director following the successful achievement of a wide range of strategic and operational activities. Details of these payments, together with those determined by the combination of the "multiplier" and personal performance ratings referred to above, are set out in the emoluments table later in this report.

For 2010, bonus potential for the Executive Directors will be as follows:

	Target* (% of salary)	Maximum (% of salary)
Jonathan Moss	75	150
Simon Smith	75	150

* Assumes "on target" financial and personal performance

The same performance measures and relative weighting as between those measures will be applied in 2010 as were applied in 2009, with actual targets reflecting achievement of the 2010 Group plans.

Share awards

During 2009, 'B' ordinary shares were allocated to an employee benefit trust in relation to the LTIP and BSP and recommendations were made to the trustee in respect of the shares allocated. The Executive Directors are potential beneficiaries of the employee benefit trust and the terms of the recommendation requests the trustees to consider allocating the following number of 'B' ordinary shares to them or their family trusts:

	'B' ordinary shares subject of the recommendation under the LTIP	'B'ordinary shares subject of the recommendation under the BSP
Jonathan Moss	112,500	112,500

Simon Smith	100,000	100,000

1. Both the LTIP and BSP awards were granted on 21 September 2009
2. LTIP awards will automatically vest after 3 years and once the Premium Listing on the LSE has been attained
3. The BSP awards have no performance conditions attached and have a vesting period, as detailed within the Rules of the Scheme, of 2 years from grant
4. Both the LTIP and BSP awards are considered as conditional share awards

Neither of the Executive Directors or their respective family trusts has any entitlement to or interest in the shares unless or until the trustee exercises its discretion to allocate the shares to them.

In respect of LTIP awards to be granted in 2010, it is envisaged that the Executive Directors will each receive an award over shares worth 200 percent of salary with performance targets based predominantly on Group MCEV, being the performance metric considered by the Remuneration Committee to be the most appropriate measure of long-term Group performance with which to reward senior executives. The actual performance target(s) have yet to be finalised but will be appropriately challenging and disclosed in next year's Remuneration report.

On 22 January 2010, the Group Chief Executive and Group Finance Director were granted 1,611 and 2,761 options over shares under the Phoenix Group Holdings 2010 Sharesave Scheme. These options were granted at an exercise price of £5.63 and are exercisable from 1 March 2013 and 1 March 2015, respectively.

On 31 December 2009, the middle market price of Phoenix Group Holdings ordinary shares was £6.64 per share (€7.44 – Euronext), having varied from 17 November (when the Company obtained a Standard Listing on the Official List) to 31 December 2009, between a low of £6.60 and a high of £7.92.

The equivalent information for the year from 1 January to 31 December 2009, as traded on Euronext Amsterdam, was a low of €7.30 and a high of €10.03.

Pension entitlement

Jonathan Moss is a member of the Money Purchase Section (defined contribution) of the Pearl Group Staff Pension Scheme and receives a Group contribution of 11.7 percent of salary up to a maximum earnings limit (currently £123,600). For the period from 2 September 2009 until 31 December 2009, £4,820 was paid into his money purchase account.

Simon Smith is a member of the Pearl Final Salary Section (defined benefit) of the Pearl Group Staff Pension Scheme. His pension entitlement accrues at 1/60th for each year of service, with a maximum pension entitlement of 2/3rds pensionable salary at the age of 60. No contributions were paid or are payable by Simon Smith under the terms of the Scheme. The increase in his pension entitlement for the period from 2 September 2009 until 31 December 2009 was as follows:

Final salary pension as at 2 September 2009	Increase in final salary pension for the period	Final salary pension as at 31 December 2009	Transfer value as at 2 September 2009	Increase in transfer value for the period	Transfer value as at 31 December 2009
£22,488	£687	£23,175	£318,275	£10,242	£328,517

External appointments

Executive Directors are not permitted to accept any other non-Group engagement or office (other than at the request of the Group) without the prior approval of the Board. At present there are no external appointments held by any of the Executive Directors, other than when they are representing the Group.

Total Shareholder Return

In view of Phoenix Group Holdings acquiring the Pearl businesses during September, the Directors do not believe the provision of TSR information is meaningful this year. The Group intends to include a graph showing TSR against an appropriate broad equity index in the future.

Directors' interests

The interests of the Directors (including family interests) in Phoenix Group Holdings ordinary shares[1] both during the year ending 31 December 2009 and up to 30 March 2010, were as follows:

	As at 1 January 2009 or date of appointment if later	As at 31 December 2009 and 30 March 2010 or date of leaving if earlier
Ian Ashken[8] (appointed 2 September 2009)	–	–
René-Pierre Azria (appointed 2 September 2009)	–	16,391
David Barnes (appointed 2 September 2009)	–	–
Nicolas Berggruen[7] (resigned 2 September 2009)	7,404,600[2]	9,954,641[3]
Ian Cormack (appointed 2 September 2009)	–	–
Tom Cross Brown (appointed 24 September 2009)	–	–
Manjit Dale[4] (appointed 2 September 2009)	–	–
Jonathan Evans (appointed 2 September 2009, resigned 22 October 2009)	–	–
Martin Franklin[7] (resigned 2 September 2009)	7,404,600	9,954,641[3]
Dimitri Goulandris[7] (resigned 2 September 2009)	63,600	66,667
Jonathan Moss (appointed 2 September 2009)	33,989*	33,989*
Miguel Paes do Amaral[7] (resigned 2 September 2009)	63,600	66,667
Ron Sandler[5] (appointed 24 September 2009)	–	–
Simon Smith (appointed 2 September 2009)	32,200*	32,200*
Hugh Osmond (appointed 2 September 2009)	703,616*	717,166[6]*
Ashley Silverton (resigned 2 September 2009)	–	–

1 Disclosures presented above primarily represent Phoenix Group Holdings ordinary shares, except for holdings of 'B' ordinary shares which are marked*. Any warrant holdings are disclosed within the respective footnote.

2 Represents securities held indirectly by Nicolas Berggruen through Berggruen Acquisitions Holdings II Ltd. Nicolas Berggruen did not hold any securities of Phoenix Group Holdings directly

3 Consists of 7,954,641 ordinary shares and 2,000,000 Sponsors' Warrants that became exercisable upon consummation of the acquisition of the Pearl businesses on 2 September 2009.

4 TDR Capital Nominees Limited is a wholly-owned subsidiary of TDR Capital LLP, of which Manjit Dale is a founding partner. In addition, TDR Capital has contingent rights in respect of a further 10,871,095 shares.

5 As announced previously, Ron Sandler is entitled, under his letter of appointment, to an award of 300,000 Phoenix Group Holdings 'B' ordinary shares. In line with this agreement, Ron Sandler will receive 177,000 shares (i.e. the net of tax value, with the Group settling the relevant taxes) prior to the Premium Listing.

6 Hugh Osmond is a beneficial shareholder of Xercise Limited. Xercise Limited has contingent rights in respect of a further 9,180,660 shares.

7 On the consummation of the acquisition on 2 September 2009, 50% of all warrants held by warrant holders were mandatorily redeemed. As a result, 31,800 warrants each held by Miguel Pais do Amaral and Dimitri Goulandris were redeemed in exchange for 3,067 newly issued ordinary shares each. Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC (in which Nicolas Berggruen and Martin Franklin have each respectively been considered to have a beneficial interest) redeemed a total of 5,702,300 warrants each (2,000,000 sponsor warrants and 3,702,300 founder warrants), in exchange for 550,040 ordinary shares each. The exchange ratio equated to one ordinary share for each 10.36705 warrants redeemed. As at 2 September 2009, the share price of Phoenix Group Holdings was €9.28.

8 Ian Ashken does not hold any shares in Phoenix Group Holdings directly although he is a member of Marlin Equities IV,LLC. M E Franklin disclosed a significant interest in the Company through Marlin Equities IV, LLC.

Directors' emoluments[9]

The emoluments of the Directors were as follows:

	Fees/salary £	Benefits[10] £	Annual Bonus £	Bonus £	2009 Total £
Ron Sandler (appointed 24 September 2009)	121,154	–	–		121,154
Jonathan Moss (appointed 2 September 2009)	131,818	3,625	202,882[11]	433,333[12]	771,658
Simon Smith (appointed 2 September 2009)	125,227	4,933	162,473[11]	350,000[12]	642,633
Ian Ashken (appointed 2 September 2009)	33,333	–	–		33,333
René-Pierre Azria (appointed 2 September 2009)	33,333	–	–		33,333
David Barnes (appointed 2 September 2009)	36,667[16]	–	–		36,667
Nicolas Berggruen (resigned 2 September 2009)	–	–	–		–
Ian Cormack (appointed 2 September 2009)	62,710[16]	–	–		62,710
Tom Cross Brown (appointed 24 September 2009)	62,599[16]	–	–		62,599
Manjit Dale (appointed 2 September 2009)	5,385[13]	–	–		5,385
Jonathan Evans (appointed 2 September 2009, resigned 22 October 2009)	24,380[16]	–	–		24,380
Martin Franklin (resigned 2 September 2009)	–	–	–		–
Dimitri Goulandris (resigned 2 September 2009)	–	–	–		–
Hugh Osmond (appointed 2 September 2009)	5,385[14]	–	–		5,385
Miguel Paes do Amaral (resigned 2 September 2009)	–	–	–		–
Ashley Silverton (resigned 2 September 2009)	571,775[15]	–	–		571,775

* During 2008, with regard to Phoenix Group Holdings, none of the Directors received any remuneration.

9 Remuneration shown is only for the period that the Director was in office.

10 Benefits include car allowance, private medical insurance, income protection and life assurance, as applicable.

11 Relates to payments made in respect of the multiplier and personal performance ratings as part of the 2009 Annual bonus scheme.

12 Relates to additional payments awarded for the successful achievement of a wide range of strategic and operational activities, as referred to previously within the Remuneration report, contingent upon the directors remaining in service until the date the payments were made. These cash payments were made on 22 March 2010.

13 For the period from 2 September to 12 December 2009, TDR Capital were paid fees as disclosed under the "Related Party transaction" note.

14 For the period from 2 September to 12 December 2009, Hugh Osmond received under a Transitional Services Agreement, fees of £121,401

15 As set out in the Proxy Statement issued to shareholders in July 2009, Mr Silverton received £8,851 in fees and in addition, received £562,924 as a result of the consummation of the acquisition of the Pearl businesses on 2 September 2009.

16 Fees to these Non-Executive Directors include amounts due to them for service on the Boards of subsidiary companies.

E) IFRS financial statements

Consolidated income statement

for the year ended 31 December 2009

	Notes	2009 £m	Restated Period ended 31 Dec 2008 £m
Gross premiums written		545	-
Less: premiums ceded to reinsurers		(31)	-
Net premiums written		514	-
Fees	6	101	-
Net investment income	7	1,032	33
Total revenue, net of reinsurance payable		1,647	33
Other operating income	8	67	-
Net income		1,714	-
Policyholder claims		(2,043)	-
Less: reinsurance recoveries		105	-
Change in insurance contract liabilities		1,137	-
Change in reinsurers' share of insurance contract liabilities		142	-
Transfer to unallocated surplus	21	(175)	-
Net policyholder claims and benefits incurred		(834)	-
Change in investment contract liabilities		(429)	-
Acquisition costs	9	(8)	-
Change in present value of future profits	33	4	-
Amortisation of acquired in-force business	33	(50)	-
Amortisation of other intangible assets	33	(7)	-

	Note		
Administrative expenses	10	(255)	(2)
Net expense attributable to unit holders		43	-
Total operating expenses		(1,536)	(2)
Profit before finance costs and tax		178	31
Finance costs	12	(87)	-
Profit for the year before tax		91	31
Tax attributable to policyholders' returns	13	60	-
Profit before the tax attributable to owners		151	31
Tax credit	13	44	-
Less: tax attributable to policyholders' returns	13	(60)	-
Tax attributable to owners	13	(16)	-
Profit for the year attributable to owners		135	31
Attributable to:			
Owners of the parent		95	31
Non-controlling interests	19	40	-
		135	31
Earnings per ordinary share			
Basic earnings per ordinary share	15	102.9p	58.1p
Diluted earnings per ordinary share	15	89.8p	45.1p

The consolidated income statement for the year ended 31 December 2009 incorporates the results of the acquired Pearl businesses for the four month post-acquisition period only.

Statement of consolidated comprehensive income

for the year ended 31 December 2009

	Notes	2009 £m	Restated Period ended 31 Dec 2008 £m
Profit for the year		135	31
Other comprehensive income:			
Actuarial gains of defined benefit pension schemes		105	-
Exchange differences on translating foreign operations		(40)	133
		65	133
Tax charge	13	(31)	-
		34	133
Total comprehensive income for the year		169	164
Attributable to:			
Owners of the parent		129	164
Non-controlling interests		40	-
		169	164

The statement of consolidated comprehensive income for the year ended 31 December 2009 incorporates the results of the acquired Pearl businesses for the four month post-acquisition period only.

Pro forma reconciliation of Group operating profit to profit before the tax attributable to owners

for the year ended 31 December 2009

	Notes	2009 £m	Restated Period ended 31 Dec 2008 £m
Operating profit			
Phoenix Life		285	-
Ignis Asset Management		14	-
		299	-
Corporate costs		(17)	(2)
Total operating profit/(loss) before adjusting items	4.2	282	(2)
Investment return variances and economic assumption changes on long term business	5	145	-
Variance on owners' funds	5	(70)	33
Amortisation of acquired in-force business		(45)	-
Amortisation of other intangible assets		(7)	-
Non-recurring items	4.2	(105)	-
Profit before finance costs attributable to owners		200	31
Finance costs attributable to owners		(49)	-
Profit before the tax attributable to owners		151	31
Tax attributable to owners	13	(16)	-
Profit for the year attributable to owners		135	31

The analysis of pro forma profit attributable to owners for the year ended 31 December 2009 incorporates the results of the acquired Pearl businesses for the four month post-acquisition period only.

Statement of consolidated financial position

as at 31 December 2009

	Notes	2009	Restated 2008
		£m	£m
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	16	-	-
Share premium		859	401
Other reserves		257	6
Shares held by employee trust	17	(4)	-
Foreign currency translation reserve		93	133
Retained earnings		207	33
Total equity attributable to owners of the parent		1,412	573
Non-controlling interests	19	728	-
Total equity		2,140	573
Liabilities			
Pension scheme deficit	32	125	-
Insurance contract liabilities			
Liabilities under insurance contracts	20	50,291	-
Unallocated surplus	21	721	-
		51,012	-

	Note		
Financial liabilities			
Investment contracts		8,570	-
Borrowings	22	4,181	-
Deposits received from reinsurers	23	431	-
Derivatives	24	2,842	11
Net asset value attributable to unit holders		946	-
Obligations for repayment of collateral received	25	4,106	-
	26	21,076	11
Provisions	27	101	-
Deferred tax	28	776	-
Reinsurance payables		17	-
Payables related to direct insurance contracts	29	759	-
Current tax	28	103	-
Accruals and deferred income	30	177	9
Other payables	31	650	-
Total liabilities		74,796	20
Total equity and liabilities		76,936	593

Statement of consolidated financial position
as at 31 December 2009

	Notes	2009	Restated 2008
		£m	£m
ASSETS			
Intangible assets			
Goodwill		77	-
Acquired in-force business		2,163	-
Customer relationships		438	-
Present value of future profits		35	-
	33	2,713	-
Property, plant and equipment	34	34	-
Investment property	35	1,915	-
Financial assets			
Loans and receivables		1,081	-
Derivatives	24	3,540	-
Equities		13,151	-
Fixed and variable rate income securities		37,658	-
Collective investment schemes		6,094	-
	36	61,524	-
Deferred tax assets	28	81	-
Insurance assets			
Reinsurers' share of insurance contract liabilities	20	2,860	-
Reinsurance receivables		264	-

Insurance contract receivables		17	-
		3,141	-
Current tax	28	44	-
Prepayments and accrued income		622	-
Other receivables	38	781	-
Cash and cash equivalents	39	6,081	2
Amounts in trust	40	-	591
Total assets		76,936	593

Statement of consolidated cash flows

for the year ended 31 December 2009

	Notes	2009	Restated Period ended 31 Dec 2008
		£m	£m
Cash flows from operating activities			
Cash absorbed by operations	40	(357)	-
Taxation received		37	-
Net cash flows from operating activities		(320)	-
Cash flows from investing activities			
On acquisition of the Pearl businesses	40	6,146	-
Interest received		2	16
Net change in cash invested in trust account		591	(457)
Net cash flows from investing activities		6,739	(441)
Cash flows from financing activities			
Gross proceeds from issue of share capital		-	422
Repayment on redemption of shares		(41)	-
Proceeds from issue of warrants		-	31
Cost of issuing shares and warrants		-	(15)
Repurchase of shares from non-controlling interests		(3)	-
Interest paid on borrowings		(221)	-
Proceeds of new borrowings		42	-
Dividends paid to non-controlling interests		(8)	-
Repayment of borrowings		(110)	-

	Note		
Net cash flows from financing activities		(341)	438
Net increase/ (decrease) in cash and cash equivalents		6,078	(3)
Cash and cash equivalents at the beginning of the year		2	-
Effect of exchange rate changes on cash and cash equivalents		1	5
Cash and cash equivalents at the end of the year	39	6,081	2

The statement of consolidated cash flows for the year ended 31 December 2009 incorporates the cash flows of the acquired Pearl businesses for the four month post-acquisition period only.

Statement of consolidated changes in equity

for the year ended 31 December 2009

	Share capital (note 16) £m	Share premium £m	Other reserves £m	Shares held by employee trust (note 17) £m	Foreign currency translation reserve £m	Retained earnings £m	Total £m	Non-controlling interests (note 19) £m	Total £m
At 1 January 2009 – as restated	-	401	6	-	133	33	573	-	573
On acquisition of the Pearl businesses	-	-	-	-	-	-	-	699	699
Profit for the year	-	-	-	-	-	95	95	40	135
Other comprehensive income for the year	-	-	-	-	(40)	74	34	-	34
Total comprehensive income for the year	-	-	-	-	(40)	169	129	40	169
Dividends paid to non-controlling interests	-	-	-	-	-	-	-	(8)	(8)
Issue of share capital	-	440	-	-	-	-	440	-	440
Issue of share capital into employee trust	-	4	-	(4)	-	-	-	-	-
Redemption of shares	-	(41)	-	-	-	-	(41)	-	(41)

Contingent rights over shares: Shares to be issued	-	-	255	-	-	-	255	-	255
Credit to equity for equity-settled share-based payment	-	-	-	-	-	5	5	-	5
Conversion of warrants into ordinary shares	-	55	(4)	-	-	-	51	-	51
Repurchase of shares from non-controlling interests	-	-	-	-	-	-	-	(3)	(3)
At 31 December 2009	-	859	257	(4)	93	207	1,412	728	2,140

Statement of consolidated changes in equity - restated

for the period ended 31 December 2008

	Share capital (note 16)	Share premium	Other reserves	Shares held by employee trust (note 17)	Foreign currency translation reserve	Retained earnings		Non-controlling interests (note 19)	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 2 January 2008	-	-	-	-	-	-	-	-	-
Profit for the period	-	-	-	-	-	31	31	-	31
Other comprehensive income for the period	-	-	-	-	133	-	133	-	133

Total comprehensive income for the period	-	-	-	-	133	31	164	-	164
Issue of share capital	-	422	-	-	-	-	422	-	422
Capital contribution of Sponsors' warrants	-	-	6	-	-	-	6	-	6
Underwriting fee charged to equity	-	(20)	-	-	-	-	(20)	-	(20)
Expenses relating to issuing of shares charged to equity	-	(1)	-	-	-	-	(1)	-	(1)
Credit to equity for equity-settled share- based payment	-	-	-	-	-	2	2	-	2
At 31 December 2008	-	401	6	-	133	33	573	-	573

Notes to the consolidated financial statements

1. Accounting policies

(a) Basis of preparation

The consolidated financial statements for the year ended 31 December 2009 comprise the financial statements of Phoenix Group Holdings ("the Company") and its subsidiaries (together referred to as "the Group"). Following the completion of the acquisition of the Pearl businesses on 2 September 2009, Liberty Acquisition Holdings (International) Company changed its name to Pearl Group. Subsequently, on 15 March 2010, Pearl Group changed its name to Phoenix Group Holdings.

The consolidated financial statements have been prepared on a historical cost basis except for investment property, owner-occupied property, and those financial assets and financial liabilities that have been measured at fair value.

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union ("EU") and also in accordance with the statutory provision of Part 9, Book 2, of the Netherlands Civil Code.

The financial statements are presented in sterling (£) rounded to the nearest £ million except where otherwise stated.

The Group presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement more than twelve months after the period end is presented in the notes.

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expenses are not offset in the consolidated income statement unless required or permitted by an accounting standard or interpretation, as specifically disclosed in the accounting policies of the Group.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiary undertakings including collective investment schemes where the Group exercises overall control. Certain of the collective investment schemes have non-coterminous period ends and are consolidated on the basis of additional financial statements prepared to the period end. The non-controlling interest in the collective investment schemes is classified as a liability and shown in the statement of consolidated financial position as net asset value attributable to unit holders. Intragroup balances and income and expenses arising from intragroup transactions are eliminated in preparing the consolidated financial statements.

Subsidiary undertakings are consolidated from the date that effective control is obtained by the Group and are excluded from consolidation from the date they cease to be subsidiary undertakings.

The Group uses the purchase method to account for the acquisition of subsidiary undertakings. The cost of an acquisition is measured at the fair value of the consideration. Any excess of the cost of acquisition over the fair value of the net assets acquired is recognised as goodwill. Any excess of the fair value of the net assets acquired over the cost of acquisition is credited to the consolidated income statement. Directly attributable acquisition costs are included within the cost of the acquisition, with the exception of costs directly related to the issuing of debt or equity securities which are included within the initial carrying amount of debt or equity securities where these are not carried at fair value.

Non-controlling interests are stated at the initial amount attributed adjusted for the relevant share of subsequent changes in equity.

Prior period adjustments

Following a review of the agreements in relation to the Company's Initial Public Offering ("IPO") and Founders' warrants the comparative amounts for 2008 have been restated to classify the warrants as financial liabilities instead of equity instruments. As a result of this restatement retained earnings have increased by £17 million, the foreign currency translation reserve has decreased by £4 million, share premium has decreased by £24 million and derivative financial liabilities have increased by £11 million.

In 2008, 29.99% of the IPO shares were classified by the Company as a financial liability, 'Ordinary shares subject to possible redemption' as it was considered that Phoenix Group Holdings had an obligation to give the holders of the redeemable shares cash in exchange for their shares had they not wished to be involved in the consummation of an acquisition that Phoenix Group Holdings was proposing. It is considered that this obligation could have been avoided and therefore the 29.99% of the IPO shares have been reclassified as equity. This restatement has had the effect of increasing share premium by £132 million, increasing retained earnings by £3 million, increasing the foreign currency translation reserve by £41 million, decreasing ordinary shares subject to possible redemption by £172 million and decreasing deferred interest income on shares subject to possible redemption by £4 million.

In 2008, all share premium arising on the issue of share capital and all share issue costs taken to equity were accounted for within other reserves. The comparative amounts for 2008 have been restated to present these figures within a separate share premium account. The effect of this restatement is to increase share premium and decrease other reserves by £401 million.

Change in accounting policy

On 2 September 2009 the Company changed its functional currency from euros to sterling as from this date, and as a result of the acquisition of the Pearl businesses, the Company primarily generates and expends cash in sterling. All foreign currency transactions for the Company are now translated into the functional currency using the average rate. Details of the accounting policy with respect to foreign currency transactions are given in note 1(c).

The presentational currency of the Group has also been changed from euros to sterling as a result of the acquisition of the Pearl businesses which are predominately based in the UK and transact this business in sterling. The comparative amounts for 2008 have accordingly been restated. This change in accounting policy has resulted in the initial recognition of a foreign currency translation reserve in other comprehensive income for the period ended 31 December 2008 of £133 million and a subsequent reduction in the reserve in the year ended 31 December 2009 of £43 million. This change in accounting policy does not affect earnings and therefore there is no effect on the earnings per share calculation.

(b) Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Critical accounting estimates are those which involve the most complex or subjective judgements or assessments. The areas of the Group's business that typically require such estimates are insurance and investment contract liabilities, determination of the fair value of financial assets and liabilities, impairment tests for intangible assets, income taxes and pension benefit assets and liabilities.

Insurance and investment contract liabilities

Insurance and investment contract liability accounting is discussed in more detail in accounting policies (e) and (f) with further detail of the key assumptions made in determining insurance and investment contract liabilities included in note 42.

Fair value of financial assets and liabilities

The fair values of financial assets and liabilities are classified and accounted for as set out in accounting policies (r) and (g) respectively. Where possible, financial assets and liabilities are valued on the basis of listed market prices by reference to quoted market bid prices for assets and offer prices for liabilities, without any deduction for transaction costs. These are categorised as Level 1 financial instruments and do not involve estimates. If prices are not readily determinable, fair value is determined using valuation techniques including pricing models, discounted cash flow techniques or broker quotes. Financial instruments valued where valuation techniques are based on observable market data at the period end are categorised as Level 2 financial instruments. Financial instruments valued where valuation techniques are based on non observable inputs are categorised as Level 3 financial instruments. Level 2 and Level 3 financial instruments therefore involve the use of estimates.

Impairment of intangible assets

Intangible assets are subject to regular impairment reviews as detailed in accounting policy (n). Impairments are measured at the difference between the carrying value of a particular asset and its recoverable amount. Impairments are recognised in the consolidated income statement in the period in which they occur.

Income taxes

Deferred tax assets are recognised to the extent that they are regarded as recoverable, that is to the extent that, on the basis of all the available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which the losses can be relieved. The UK taxation regime applies separate rules to trading and capital profits and losses. The distinction between temporary differences that arise from items of either a capital or trading nature may affect the recognition of deferred tax assets. Any judgements made, and uncertainties considered, in arriving at deferred tax balances in the financial statements are discussed in note 28.

The accounting policy for income taxes (both current and deferred taxes) is discussed in more detail in accounting policy (l).

Pensions benefit assets and liabilities

The valuation of pension benefit assets and liabilities is determined using actuarial valuations, which involves making assumptions about discount rates, expected return rates on assets, future salary increases, mortality rates and future pension increases. As defined benefit pension plans are long term in nature, such assumptions are subject to significant uncertainty. Details of the key assumptions used are shown in note 32.

(c)Foreign currency transactions

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in sterling, which is the Group's presentation currency.

The results and financial position of all Group companies that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

assets and liabilities are translated at the closing rate at the period end;

income and expenses are translated at average exchange rates;

all resulting exchange differences are recognised through the statement of consolidated comprehensive income; and

cash flows are translated at average exchange rates.

Foreign currency transactions are translated into the functional currency of the transacting Group entity using average exchange rates. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement.

Translation differences on debt securities and other monetary financial assets measured at fair value through profit or loss are included in foreign exchange gains and losses. Translation differences on non-monetary items at fair value through profit or loss are reported as part of the fair value gain or loss.

(d) Classification of contracts

Contracts under which the Group accepts significant insurance risk are classified as insurance contracts.

Contracts under which the transfer of insurance risk to the Group from the policyholder is not significant are classified as investment contracts.

Some insurance and investment contracts contain a discretionary participation feature ("DPF"). This feature entitles the policyholder to additional discretionary benefits as a supplement to guaranteed benefits. Investment contracts with a DPF are recognised, measured and presented as insurance contracts.

(e) Insurance contracts and investment contracts with DPF

Under current IFRS requirements, insurance contracts and investment contracts with DPF are measured using accounting policies consistent with those adopted under UK GAAP. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsured policy.

Insurance liabilities

The insurance contract liability for non participating non linked business is calculated initially to comply with the requirements of the Prudential Sourcebook for Insurers issued by the Financial Services Authority ("FSA"), the UK Regulator. The liability for insurance contracts for business in the non profit fund is adjusted where necessary by removing excessively prudent margins required for statutory solvency purposes together with general contingency reserves and those reserves required only under the Prudential Sourcebook for Insurers.

Insurance contract liabilities for non participating business are calculated using either a net premium or gross premium method. Where a gross premium method is used, the liability includes allowance for prudent lapses. Negative policy values are allowed for individual policies:

where there are no guaranteed surrender values; or

in the periods where guaranteed surrender values do not apply even though guaranteed surrender values are applicable after a specified period of time.

The principal assumptions are given in note 42.

For participating business, the Group follows the provisions of the UK Accounting Standard Board's FRS 27 Life Assurance. In accordance with these requirements, the liabilities under insurance contracts and investment contracts with DPF are calculated on the FSA's realistic basis. The key aspects of this methodology are:

liabilities to policyholders arising from with profit life assurance business are stated at the amount of the realistic value of the liabilities, adjusted to exclude the owners' share of projected future bonuses;

acquisition costs are not deferred; and

reinsurance recoveries are measured on a basis that is consistent with the valuation of the liability to policyholders to which the reinsurance applies.

The principal assumptions are given in note 42.

Present value of future profits on non participating business in the with profit funds

For UK with profit life funds falling within the scope of the FSA realistic capital regime, and hence FRS 27, an amount may be recognised for the present value of future profits on non participating business written in a with profit fund where the determination of the realistic value of liabilities in that with profit fund takes account, directly or indirectly, of this value.

Where the value of future profits can be shown to be due to policyholders this amount is recognised as a reduction in the liability rather than as an intangible asset, and is then apportioned between the amounts that have been taken into account in the measurement of liabilities and other amounts which are shown as an adjustment to the unallocated surplus.

Where it is not possible to apportion the future profits on this non participating business to policyholders the present value of future profits ("PVFP") on this business is recognised as an intangible asset and changes in its value are recorded as a separate item in the consolidated income statement.

The value of the PVFP is determined in accordance with the FSA's realistic capital regime. The principal assumptions used to calculate the PVFP are the same as those used in calculating the insurance contract liabilities given in note 42.

Embedded derivatives

Embedded derivatives, including options to surrender insurance contracts, that meet the definition of insurance contracts or are closely related to the host insurance contract, are not separately measured. All other embedded derivatives are separated from the host contract and measured at fair value through profit or loss.

Liability adequacy

At each reporting date, liability adequacy tests are performed to assess whether the insurance contract and investment contract with DPF liabilities are adequate. Current best estimates of future cash flows are compared to the carrying value of the liabilities. Any deficiency is charged to the consolidated income statement.

The Group's accounting policies for insurance contracts meet the minimum specified requirements for liability adequacy testing under IFRS 4, as they allow for current estimates of all contractual cash flows and of related cash flows such as claims handling costs. Cash flows resulting from embedded options and guarantees are also allowed for, with any deficiency being recognised in the consolidated income statement.

Unallocated surplus

The unallocated surplus comprises the excess of the assets over the policyholder liabilities of the with profit business of the Group's life operations. For the Group's with profit funds, the amount included in the statement of consolidated financial position caption 'Unallocated surplus' represents amounts which have yet to be allocated to equity holders since the unallocated surplus attributable to policyholders has been included within liabilities under insurance contracts. The with profit funds are closed to new business and as permitted by IFRS 4, the whole of the unallocated surplus has been classified as a liability (either within insurance contract liabilities or unallocated surplus).

If the realistic value of liabilities to policyholders exceeds the value of the assets in the with profit fund, the unallocated surplus is valued at £nil.

(f) Investment contracts without DPF

Receipts and payments on investment contracts without DPF are accounted for using deposit accounting, under which the amounts collected and paid out are recognised in the statement of consolidated financial position as an adjustment to the liability to the policyholder.

The valuation of liabilities on unit linked contracts is based on the fair value of the related assets and liabilities. The financial liability is measured based on the carrying value of the assets and liabilities that are held to back the contract. The liability is the sum of the unit linked liabilities plus an additional amount to cover the present value of the excess of future policy costs over future charges.

Investment income and the movements in the fair value of investment contracts without DPF are included in the 'change in investment contract liabilities' in the consolidated income statement.

(g) Financial liabilities

On initial recognition, financial liabilities are recognised when due and measured at the fair value of the consideration received less directly attributable transaction costs (with the exception of liabilities at fair value through profit or loss for which all transaction costs are expensed).

Subsequent to initial recognition, financial liabilities (except for liabilities under investment contracts and other liabilities designated at fair value through profit or loss) are measured at amortised cost using the effective interest method.

Financial liabilities are designated upon initial recognition at fair value through profit or loss when doing so results in more meaningful information because either:

it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or

a group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the Group's key management personnel.

Warrants issued by the Company are recognised as a financial liability unless they can be exchanged for a fixed number of the Company's own shares, or are accounted for as an equity-settled share-based payments, in which case they are recognised as equity.

(h) Borrowings

The majority of interest bearing borrowings are recognised initially at fair value less any attributable transaction costs. The difference between initial cost and the redemption value is amortised through the consolidated income statement over the period of the borrowing using the effective interest method.

Certain borrowings are designated upon initial recognition at fair value through profit or loss and measured at fair value where doing so provides more meaningful information due to the reasons stated above in the financial liabilities accounting policy. Transaction costs relating to borrowings designated upon initial recognition at fair value through profit or loss are expensed as incurred.

(i) Deposits from reinsurers

It is the Group's practice to obtain collateral to cover certain reinsurance transactions, usually in the form of cash or marketable securities. Where cash collateral is available to the Group for investment purposes, the investments are recognised as 'financial assets' and the collateral repayable is recognised as 'deposits received from reinsurers'.

(j) Net asset value attributable to unit holders

The net asset value attributable to unit holders represents the non-controlling interest in collective investment schemes where the Group has a holding in excess of 50%. This interest is classified at fair value through profit or loss and measured at fair value, which is equal to the bid value of the number of units of the collective investment scheme not owned by the Group.

(k)Obligations for repayment of collateral received

It is the Group's practice to obtain collateral in stock lending transactions, usually in the form of cash or marketable securities. Where cash collateral is available to the Group for investment purposes, the investments are recognised as 'financial assets' and the collateral repayable is recognised as 'obligations for repayment of collateral received'. The 'obligations for repayment of collateral received' are measured at amortised cost, which in the case of cash is equivalent to cost.

(l) Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the consolidated income statement except to the extent that it relates to items recognised in the statement of consolidated comprehensive income or the statement of consolidated changes in equity, in which case it is recognised in these statements.

Current tax is the expected tax payable on the taxable income for the year, using tax rates and laws enacted or substantively enacted at the date of the statement of consolidated financial position together with adjustments to tax payable in respect of previous years.

Deferred tax is provided for on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not provided in respect of temporary differences arising from the initial recognition of goodwill and the initial recognition of assets or liabilities in a transaction that is not a business combination and that, at the time of the transaction, affects neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates and laws enacted or substantively enacted at the period end.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

The tax charge is analysed between tax that is payable in respect of policyholders' returns and tax that is payable on owners' returns. This allocation is calculated based on an assessment of the effective rate of tax that is applicable to owners for the year.

(m) Employee benefits

Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the consolidated income statement as incurred.

Defined benefit schemes

The net surplus or deficit (the economic surplus or deficit) in respect of the defined benefit pension schemes is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior years; that benefit is discounted to determine its present value and the fair value of any scheme assets is deducted. The discount rate is the yield at the period end on AA credit rated bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

The economic surplus or deficit is subsequently adjusted to eliminate on consolidation the carrying value of insurance policies issued by Group entities to the defined benefit pension schemes (the reported surplus or deficit). A corresponding adjustment is made to the carrying values of insurance contracts liabilities and investment contracts liabilities.

The movement in the reported surplus/deficit is analysed between the service cost (recognised within administrative expenses in the consolidated income statement), the net interest gain or loss on the liabilities less the expected return on assets, including any reimbursement assets (recognised within net investment income in the consolidated income statement), curtailment gains/losses and actuarial gains and losses (recognised in other comprehensive income). All actuarial gains and losses are recognised in full.

(n) Intangible assets

Goodwill

Business combinations are accounted for by applying the purchase method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill is measured on initial recognition at cost. Following initial recognition, goodwill is stated at cost less any accumulated impairment losses. It is tested for impairment annually or when there is evidence of possible impairment. Goodwill is not amortised. For impairment testing, goodwill is allocated to cash generating units (Phoenix Life and Ignis Asset Management). Goodwill is impaired when the recoverable amount is insufficient to support its carrying value.

Acquired in-force business

Insurance and investment contracts with and without DPF acquired in business combinations and portfolio transfers are measured at fair value at the time of acquisition. The difference between the fair value of the contractual rights acquired and obligations assumed and the liability measured in accordance with the Group's accounting polices for such contracts is recognised as acquired in-force business.

Acquired in-force business is amortised over the estimated life of the contracts on a basis which recognises the emergence of the economic benefits.

An impairment review is performed whenever there is an indication of impairment. When the recoverable amount is less than the carrying value, an impairment loss is recognised in the consolidated income statement. Acquired in-force business is also considered in the liability adequacy test for each reporting period.

Customer relationships and other intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets are not capitalised and expenditure is reflected in the consolidated income statement in the year in which the expenditure is incurred.

Intangible assets with finite lives are amortised over their useful economic life and assessed for impairment whenever there is an indication that the fair value of the intangible asset is less than its carrying value.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangibles are not amortised.

(o) Property, plant and equipment

Owner-occupied property is stated at fair value, being the estimated amount for which the property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction. Owner-occupied property is depreciated over its estimated useful life, which is taken as fifty years, except where the residual value is greater than its carrying value in which case, no depreciation is charged to profit or loss. Land is not depreciated. Gains and losses on owner-occupied property are recognised in the statement of consolidated comprehensive income.

Plant and equipment is stated at cost less accumulated depreciation. Depreciation is charged to the consolidated income statement on a straight-line basis over the estimated useful lives.

(p) Investment property

Investment property is stated at fair value. Fair value is based on market values, being the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction. Gains and losses arising from the change in fair value are recognised in the consolidated income statement.

(q) Investments in associates and joint ventures

Investments in associates and joint ventures that are held for investment purposes are accounted for under IAS 39 Financial Instruments: Recognition and Measurement as permitted by IAS 28 Interests in Associates and IAS 31 Interests in Joint Ventures. These are measured at fair value through profit or loss. There are no investments in associates and joint ventures which are of a strategic nature.

(r) Financial assets

Purchases and sales of financial assets are recognised on the trade date, which is the date that the Group commits to purchase or sell the asset.

Loans and receivables are non derivative financial assets with fixed or determinable payments that are not quoted in an active market. These investments are initially recognised at cost, being the fair value of the consideration paid for the acquisition of the investment. All transaction costs directly attributable to the acquisition are also included in the cost of the investment. Subsequent to initial recognition, these investments are carried at amortised cost, using the effective interest method.

Derivative financial instruments are classified as held for trading. They are recognised initially at fair value and subsequently are re-measured to fair value. Exchange-traded derivatives are valued at the published bid price, or, if these are not available, by using valuation techniques such as discounted cash flow models or option pricing models. The gain or loss on re-measurement to fair value is recognised in the consolidated income statement.

Equities, fixed and variable rate income securities and collective investment schemes are designated at fair value through profit or loss and accordingly are stated in the statement of consolidated financial position at fair value. They are designated at fair value through profit or loss because they are managed and evaluated on a fair value basis in accordance with the Group's stated risk management policies to maximise returns to equity holders.

Invested cash held in collective investment schemes that are consolidated is recognised as a financial asset rather than cash and cash equivalents.

Impairment of financial assets

The Group assesses at each period end whether a financial asset or group of financial assets held at amortised cost is impaired. The Group first assesses whether objective evidence of impairment exists for financial assets. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in the collective assessment of impairment.

Fair value estimation

The fair value of financial instruments traded in active markets such as publicly traded securities and derivatives are based on quoted market prices at the period end. The quoted market price used for financial assets is the current bid price on the trade date. The fair value of investments that are not traded in an active market is determined using valuation techniques such as broker quotes, pricing models or discounted cash flow techniques. Where pricing models are used, inputs are based on market related data at the period end. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market related rate for a similar instrument.

For units in unit trusts and shares in open-ended investment companies, fair value is by reference to published bid-values. The fair value of receivables and floating rate and overnight deposits with credit institutions is their carrying value. The fair value of fixed-interest bearing deposits is estimated using discounted cash flow techniques.

Stock lending

Financial assets that are lent under the Group's stock lending programme do not qualify for derecognition from the statement of consolidated financial position as the Group retains substantially all the risks and rewards of the transferred assets.

Collateral

The Group receives and pledges collateral in the form of cash or non-cash assets in respect of stock lending transactions, derivative contracts and reinsurance arrangements in order to reduce the credit risk of these transactions. The amount and type of collateral required where the Group receives collateral depends on an assessment of the credit risk of the counterparty.

Collateral received in the form of cash, where the Group has contractual rights to receive the cash flows generated, is recognised as an asset on the statement of consolidated financial position with a corresponding liability for its repayment. Non-cash collateral received is not recognised in the statement of consolidated financial position, unless the counterparty defaults on its obligations under the relevant agreement.

Cash and non-cash collateral pledged where the Group retains the contractual rights to receive the cash flows generated is not derecognised from the statement of consolidated financial position, unless the Group defaults on its obligations under the relevant agreement, and therefore continues to be recognised in the statement of consolidated financial position within the appropriate asset classification.

(s)Reinsurance

The Group cedes insurance risk in the normal course of business. Reinsurance assets represent balances due from reinsurance companies. Reinsurers' share of insurance contract liabilities are dependent on expected claims and benefits arising under the related reinsured policies.

Reinsurance assets are reviewed for impairment at each reporting date or more frequently when an indication of impairment arises during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the Group may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer. The impairment loss is recorded in the consolidated income statement.

Reinsurance premiums payable in respect of certain reinsured individual and group pensions annuity contracts are payable by quarterly instalments. Due to the period of time over which reinsurance premiums are payable under these arrangements, the reinsurance premiums and related creditor are discounted to present values using a pre-tax risk-free rate of return. The unwinding of the discount is included as a charge within the consolidated income statement.

Gains or losses on purchasing reinsurance are recognised in the consolidated income statement at the date of purchase and are not amortised. They are the difference between the premiums ceded to reinsurers and the related change in the reinsurers' share of insurance contract liabilities.

(t) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and short-term deposits with an original maturity term of three months or less at the date of placement. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are deducted from cash and cash equivalents for the purpose of the statement of consolidated cash flows.

(u) Provisions and contingent liabilities

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where the Group has a present legal or constructive obligation but it is not probable that there will be an outflow of resources to settle the obligation or the amount cannot be reliably estimated, this is disclosed as a contingent liability.

A provision is recognised for onerous contracts in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs reflect the least net cost of exiting the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

(v)Earnings per ordinary share

Basic earnings per share is calculated using the earnings attributable to ordinary equity holders of the parent, divided by the weighted average number of ordinary shares and 'B' ordinary shares in issue during the year.

For the diluted earnings per share, the weighted average number of ordinary shares and 'B' ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares, including warrants and potentially issuable ordinary shares.

(w) Dividends

Final dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Group's owners. Interim dividends are deducted from equity when they are paid.

Dividends for the year that are approved after the reporting period are dealt with as an event after the reporting period.

Declared dividends are those that are appropriately authorised and are no longer at the discretion of the entity.

(x)Income recognition

Gross premiums

In respect of insurance contracts and investment contracts with DPF, premiums are accounted for on a receivable basis and exclude any taxes or duties based on premiums. Funds at retirement under individual pension contracts converted to annuities with the Group are, for accounting purposes, included in both claims incurred and premiums within gross premiums written.

Reinsurance premiums

Outward reinsurance premiums are accounted for on a payable basis.

Fee and commission income

Fee and commission income relates to the following:

fund management based fees, which are recognised as the services are provided;

investment contract income – investment contract policyholders are charged for policy administration services, investment management services, surrenders and other contract fees. These fees are recognised as revenue over the period in which the related services are performed. If the fees are for services provided in future periods, then they are deferred and recognised over those periods. 'Front end' fees are charged on some non participating investment contracts. Where the non participating investment contract is measured at fair value, such fees which relate to the provision of investment management services are deferred and recognised as the services are provided; and

other fees, which are recognised as the services are provided.

Net investment income

Net investment income comprises interest, dividends, rents receivable, net expected return on pension assets, fair value gains and losses on financial assets and investment property and impairment losses on loans and receivables.

Interest income is recognised in the consolidated income statement as it accrues using the effective interest method. Dividend income is recognised in the consolidated income statement on the date the right to receive payments is established, which in the case of listed securities is the ex-dividend date.

Rental income from investment property is recognised in the consolidated income statement on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

Realised and unrealised gains and losses on financial assets designated at fair value through profit or loss are recognised in the consolidated income statement. Realised gains and losses are the difference between the net sale proceeds and the original cost. Unrealised gains and losses are the difference between the valuation at the period end and their valuation at the previous period end or purchase price, if acquired during the year.

Other operating income

Other operating income comprises the general business result and other non-investment income which is recognised on an accruals basis.

(y)Benefits, claims and expenses recognition

Gross benefits and claims

Claims on insurance contracts and investment contracts with DPF reflect the cost of all claims arising during the period, including policyholder bonuses allocated in anticipation of a bonus declaration. Claims payable on maturity are recognised when the claim becomes due for payment and on death are accounted for on notification. Surrenders are accounted for at the earlier of the payment date or when the policy ceases to be included within insurance contract liabilities. Where claims are payable and the contract remains in force, the claim instalment is accounted for when due for payment. Claims payable include the costs of settlement.

Reinsurance claims

Reinsurance claims are recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

Share-based payments

Equity-settled share-based payments to employees and others providing services are measured at the fair value of the equity instruments at the grant date. The fair value excludes the effect of non market-based vesting conditions. Details regarding the determination of the fair value of equity-settled share-based transactions are set out in note 18.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest. At each period end, the Group revises its estimate of the number of equity instruments expected to vest as a result of the effect of non market-based vesting conditions. The impact of the revision of the original estimates, if any, is recognised in the consolidated income statement such that the cumulative expense reflects the revised estimate with a corresponding adjustment to equity.

Where the terms and conditions of warrants are modified before they vest, the increase in the fair value of the warrants, measured immediately before and after the modification, is also charged to the consolidated income statement over the remaining vesting period.

Finance costs

Interest paid is recognised in the consolidated income statement as it accrues and is calculated by using the effective interest method. Accrued interest is included within the carrying value of the interest bearing financial liability.

(z)Share capital and shares held by employee trust

Ordinary share capital

The Group has issued ordinary shares and 'B' ordinary shares each of which is classified as equity. Incremental external costs that are directly attributable to the issue of these shares are recognised in equity, net of tax.

Shares held by employee trust

Where an employee trust acquires the Company's share capital or obtains rights to purchase its shares, the consideration paid (including any attributable transaction costs, net of tax) is shown as a deduction from owners' equity. Gains and losses on sales of shares held by employee trusts are charged or credited to the own shares account in equity. Any shares in the Company which are purchased by the Company itself would be cancelled automatically by operation of law and would not be held as own shares.

(aa) General business

The general insurance businesses have been closed to new business for a number of years and are in run off. The results are included in other operating income within the consolidated income statement. Provisions are made for the

estimated cost of claims, including claims incurred but not reported after taking into account handling costs, anticipated inflation and settlement trends. Any difference between the estimated provision and subsequent settlement is included in the consolidated income statement in later years.

(bb) Segmental reporting

The Group's results are analysed across two reportable segments: Phoenix Life and Ignis Asset Management. The revenues generated in each reported segment are shown in the segmental information in note 4.

There are no differences between the measurement of the assets and liabilities reflected in the primary statements and that reported for the segments. A reconciliation between the reported segment revenues and expenses and the Group's revenues and expenses is shown in note 4.

Assets, liabilities, revenues or expenses that are not directly attributable to a particular segment are allocated between segments where there is a reasonable basis for doing so.

(cc) Events after the reporting period

The financial statements are adjusted to reflect significant events that have a material effect on the financial results and that have occurred between the period end and the date when the financial statements are authorised for issue, provided they give evidence of conditions that existed at the period end. Events that are indicative of conditions that arise after the period end that do not result in an adjustment to the financial statements are disclosed.

Financial information

The consolidated financial statements for the year ended 31 December 2009, were authorised by the Board of Directors for issue on 30 March 2010. The financial statements have been prepared in accordance with IFRS adopted for use by the EU and also in accordance with the statutory provision of Part 9, Book 2, of the Netherlands Civil Code.

In preparing the consolidated financial statements the Group has adopted the following standards, amendments and interpretations:

IFRS 8 Operating Segments. This converges International and US reporting requirements relating to segmental information.

IAS 1 Presentation of Financial Statements (Revised). This revises and enhances the presentation of information in the financial statements.

IAS 27 Consolidated and Separate Financial Statements. This revises the accounting treatment of dividends paid out of the pre-acquisition reserves of subsidiaries.

Share-based Payment: Vesting conditions and cancellations (Amendments to IFRS 2). This results in an immediate acceleration of the expense that would otherwise have been recognised in future periods should an employee decide to stop contributing to the savings plan. The amendment has no impact on the results of the Group.

Improving disclosures about Financial Instruments (Amendments to IFRS 7). This requires enhanced disclosures about fair value measurements and liquidity risk.

Annual Improvements 2008. This makes a number of improvements to existing standards.

The International Accounting Standards Board ("IASB") has issued the following standards, amendments and interpretations which apply from the dates shown. The Group has decided, where permitted, not to adopt any of these standards, amendments or interpretations in advance of their implementation date. The impact of adopting them is not expected to have a material effect on the results of the Group.

IFRS 3 Business Combinations (Revised) (2010). This converges International and US reporting requirements relating to business combinations.

IFRS 9 Financial Instruments (2013). IFRS 9 is the first phase of the project to replace IAS 39 Financial Instruments: Recognition and Measurement and deals with the classification and measurement of financial assets, including some hybrid contracts.

IAS 24 Related Party Disclosures (2011). This amends the definition of a related party and clarifies its intended meaning.

IAS 27 Consolidated and Separate Financial Statements (Revised) (2010). This revises the accounting for non-controlling interests and the loss of control of subsidiaries.

Annual improvements 2009 (2010). This makes a number of minor improvements to existing standards and interpretations.

Embedded Derivatives (Amendments to IFRIC 9 and IAS 39) (2010). This clarifies the treatment of embedded derivatives.

IFRIC 17 Distributions of Non-Cash Assets to Owners (2010). IFRIC 17 provides guidance on how an entity should account for distributions of non-cash assets to its owners, other than in limited circumstances.

In addition, the following standards, amendments and interpretations have been issued but are not currently relevant to the Group:

IFRIC 18 Transfers of Assets from Customers (July 2009).

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments (2011).

Additional Exemptions for First-time Adopters (Amendments to IFRS 1) (2010).

Group Cash-settled Share-based Payment Transactions (Amendments to IFRS 2) (2010).

Classification of Rights Issues (Amendments to IAS 32) (2011).

Prepayments of a Minimum Funding Requirement (Amendments to IFRIC 14) (2011).

3. Acquisition of the Pearl businesses

With effect from 28 August 2009, the Company acquired 100% of the issued share capital of PGH (LCA) Limited (formerly Sun Capital Investments Limited), PGH (LCB) Limited (formerly Hera Investments One Limited), PGH (TC1) Limited (formerly SunCap Parma Topco Limited), PGH (TC2) Limited (formerly TDR Parma Topco Limited) and Opal Reassurance Limited, collectively the 'Pearl businesses', for a total consideration of £493 million. At the same time a third party's interest in a 49.4% holding in Ignis Investment Management Limited (formerly Axial Investment Management Limited) was purchased by Pearl Group Holdings (No. 2) Limited (formerly Pearl Group Limited) ("PGH2") for a consideration of £1. The Pearl businesses are involved in the management of various classes of insurance business and the provision of investment management services through their subsidiary companies.

On 2 September 2009, the date of legal completion of the acquisition, certain external debt of the Pearl businesses was restructured, specifically the £905 million Pearl facility, the £2,260 million Impala facility and the Royal London PIK notes and facility. Of the £825 million outstanding under the £905 million Pearl facility, £325 million was assigned to Phoenix Group Holdings in exchange for £75 million consideration, £75 million of the remaining £500 million was converted into two £37.5 million secured C loan notes and the terms of the remaining £425 million were amended. The terms of the £2,260 million Impala facility were also amended. Of the £350 million Royal London PIK notes and facility outstanding (comprising principal and capitalised interest), £250 million was assigned to Phoenix Group Holdings in exchange for the issue to Royal London of 1.5 million 'B' ordinary shares and 12.36 million warrants for 'B' ordinary shares. The terms of the remaining £100 million PIK notes and facility were then amended. The banks and other lenders involved in this restructuring are collectively known as "the Lenders". The restructuring formed an integral part of the acquisition transaction and the effect of the restructuring has been incorporated in determining the fair values of certain liabilities at the acquisition date.

The acquisition has been accounted for using the purchase method of accounting. There were no accounting policy adjustments made to the carrying values.

The table below summarises the assets and liabilities acquired and the fair value adjustments made at the date of acquisition:

	Notes	Carrying value	Fair value adjust-ments	Fair value
		£m	£m	£m
Assets				
Intangible assets	33	1,839	850	2,689
Property, plant and equipment	34	35	-	35
Investment property	35	1,807	-	1,807
Financial assets		62,269	32	62,301
Deferred tax assets	28	98	-	98
Insurance assets		2,983	-	2,983
Current tax		20	-	20
Deferred acquisition costs		15	(15)	-

	Note			
Prepayments and accrued income		562	-	562
Other receivables		821	21	842
Cash and cash equivalents		6,155	-	6,155
Total assets		76,604	888	77,492
Liabilities				
Pension scheme deficit	32	288	-	288
Liabilities under insurance contracts	20	51,413	-	51,413
Unallocated surplus	21	546	-	546
Borrowings		4,764	(529)	4,235
Other financial liabilities		16,450	-	16,450
Provisions	27	121	-	121
Deferred tax	28	474	319	793
Reinsurance payables		19	-	19
Payables related to direct insurance contracts		761	-	761
Current tax		54	-	54
Accruals and deferred income		296	(4)	292
Other payables		1,203	202	1,405
Total liabilities		76,389	(12)	76,377
Net assets		215	900	1,115
Less: Non-controlling interests				
UK Commercial Property Trust Limited	19			(181)
Perpetual Reset Capital Securities	19			(518)
Fair value of net assets acquired				416
Goodwill	33			77
Total consideration				493

Satisfied by:

Issue of 40.7 million fully paid up 'B' ordinary shares to vendors	(a)	332
Issue of 26.5 million contingent rights over shares to vendors	(b)	143
Issue of warrants to lenders	(c)	4
Issue of 1 million contingent rights over shares in settlement of underwriting fee	(d)	5
Acquisition expenses	(e)	9
		493

The goodwill arising on the acquisition of the Pearl businesses is attributed to the Ignis Asset Management business and the management services operations within Phoenix Life.

The Pearl businesses contributed £514 million to total revenue, net of reinsurance and £178 million profit before tax attributable to owners for the period between the date of acquisition and the period end. The Group's consolidated profit before tax attributable to the owners for the year ended 31 December 2009 of £91 million comprises the entity loss before tax of £87 million together with this contribution from the Pearl businesses of £178 million.

If the acquisition of the Pearl businesses had been completed on the first day of the financial year, Group total revenue, net of reinsurance for the year would have increased by £1,081 million from £541 million to £1,595 million. However, the impact on Group profit has not been disclosed as it is impracticable to calculate this given the complex nature of the acquisition of the Pearl businesses and the associated acquisition accounting.

(a) The share consideration to the vendors included the issue of 40.7 million fully paid up 'B' ordinary shares. The fair value of this consideration was ascertained using the market price of the Company's shares as quoted on Euronext. The market price on the date of acquisition was €9.26 (£8.16).

(b) In addition to these 'B' ordinary shares, 26.5 million contingent rights over shares were also given to certain of the vendors. These shares will be issued to the vendors depending upon the future performance of the Company's share price as follows:

- 8,833,333 shares will be issued when the share price is greater than or equal to €13 for 20 consecutive trading days;
- 8,833,333 will be issued when the share price is greater than or equal to €14 for 20 consecutive trading days; and finally
- 8,833,334 will be issued when the share price is greater than or equal to €15 for 20 consecutive trading days.

There is no quoted market price for these contingent rights over shares and therefore an appropriate valuation technique has been used to ascertain their fair value for accounting purposes. A Black–Scholes methodology has been used to value these contingent rights over shares as at the date of the acquisition. The key assumptions used to ascertain the fair value are as follows:

- Share price as at the date of acquisition of €9.28;
- Strike price of zero;
- Zero dividend schedule (with dividend adjustment);
- Zero stock borrowing cost assumption;
- Volatility of 30%; and
- Termination date of 2 September 2016.

The value of the contingent rights over shares has been calculated at €6.70 (£5.91) per share for the €13 threshold shares, €6.10 (£5.38) per share for the €14 threshold shares and €5.60 (£4.94) per share for the €15 threshold shares.

(c)As consideration for facilitating the acquisition, the Company issued 5 million warrants over its shares to the Lenders. The exercise of the warrants is dependent upon the performance of the business in that the warrants can be exercised at an exercise price of £15. There is no quoted market price for these warrants and therefore an appropriate valuation technique has been used to ascertain their fair value for accounting purposes. A Black–Scholes methodology has been used to value these warrants as at the date of the acquisition. The key assumptions used to ascertain the fair value are as follows:

- Share price as at the date of acquisition of €9.28;
- Volatility of 30%;
- The warrants are not adjusted for dividends;
- Upside participation limited to 60%; and
- Exercise period of 7 years.

The value of the warrants has been calculated at £0.75 per warrant. Details of these warrants are given in note 24.

(d) Prior to the acquisition, the Company entered into an underwriting agreement with certain of its existing owners to cover the value of any potential share redemption up to a maximum total of £75 million if required. 1 million 'B' ordinary shares are to be issued to the underwriters as a contingent fee for agreeing to perform this underwriting service. The issue of the shares is dependent upon the performance of the business in that the shares will be issued if the closing share price is greater than or equal to €15 for 20 consecutive trading days.

There is no quoted market price for these contingent rights over shares and therefore an appropriate valuation technique has been used to ascertain their fair value for accounting purposes. A Black–Scholes methodology has been used to value these contingent rights over shares as at the date of the acquisition. The key assumptions used to ascertain the fair value are as set out in (b) above. The value of these contingent rights over shares has been calculated at €5.60 (£4.94) per share.

(e) As part of the acquisition £9 million of professional fees were incurred. These have been capitalised and included within the total consideration. These costs were paid in the period.

4. Segmental analysis

The Group defines and presents operating segments based on the information which is provided to the Board.

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses relating to transactions with other components of the Group.

For management purposes, the Group is organised into business units based on their products and services and has two reportable segments as follows:

Phoenix Life – this segment manages a range of whole life, term assurance and pension products; and

Ignis Asset Management – this segment provides investment management services to the life companies within the Group and to third parties, covering both retail and institutional investors.

Segment performance is evaluated based on profit or loss which in certain respects is measured differently from profit or loss in the consolidated financial statements. Group financing (including finance costs) and owners' taxes are managed on a Group basis and are not allocated to individual operating segments.

Inter-segment transactions are set on an arm's length basis in a manner similar to transactions with third parties. Segment results include those transfers between business segments which are then eliminated on consolidation.

Predominantly all revenues from external customers is sourced in the UK.

No revenue transaction with a single customer amounts to greater than 10% of the Group's revenue.

Predominantly all non-current assets are located in the UK.

4.1 Segmental result

2009

	Phoenix Life	Ignis Asset Managemen t	Unallocate d corporate	Elimination s	Total
	£m	£m	£m	£m	£m
Net premiums written from:					
External customers	514	-	-	-	514
Other segment	-	-	-	-	-

	514	-	-		514
Fees from:					
External customers	71	30	-	-	101
Other segment	-	28	-	(28)	-
	71	58	-	(28)	101
Net investment income:					
Net investment income	1,095	-	(63)	-	1,032
Offset interest income on interest swaps against interest expenses	-	-	(16)	-	(16)
	1,095	-	(79)	-	1,016
Other operating income:					
Recurring	49	-	-	-	49
Non-recurring	18	-	-	-	18
	67	-	-	-	67
Net income	1,747	58	(79)	(28)	1,698
Net policyholder claims and benefits incurred:					
Recurring	(760)	-	-	-	(760)
Non-recurring	(74)	-	-	-	(74)
	(834)	-	-	-	(834)
Depreciation and amortisation:					
Depreciation of property, plant and equipment	(1)	(1)	-	-	(2)
Amortisation of acquired in-force business	(50)	-	-	-	(50)
Amortisation of other intangible assets	(6)	(1)	-	-	(7)
	(57)	(2)	-	-	(59)
Other operating expenses:					
Recurring	(562)	(43)	(17)	28	(594)
Non-recurring	(45)	(4)	-	-	(49)
	(607)	(47)	(17)	28	(643)
Total operating expense	(1,498)	(49)	(17)	28	(1,536)
Profit/(loss) before finance costs and tax	249	9	(96)	-	162

Finance costs	(22)	-	(65)	-	(87)
Offset interest income on interest swaps against interest expense	-	-	16	-	16
	(22)	-	(49)	-	(71)
Profit before tax	227	9	(145)	-	91
Tax attributable to policyholders' returns	60	-	-	-	60
Segmental result before the tax attributable to owners	287	9	(145)	-	151

4.2 Reconciliation of operating profit/(loss) before adjusting items to the segmental result

2009

	Phoenix Life	Ignis Asset Management	Unallocated corporate	Eliminations	Total
	£m	£m	£m	£m	£m
Operating profit/(loss) before adjusting items	285	14	(17)	-	282
Investment return variances and economic assumption changes on long term business	145	-	-	-	145
Variance on owners' funds	9	-	(79)	-	(70)
Amortisation of acquired in-force business	(45)	-	-	-	(45)
Amortisation of other intangible assets	(6)	(1)	-	-	(7)
Non-recurring items	(101)	(4)	-	-	(105)
Financing costs attributable to owners	-	-	(49)	-	(49)
Segment result before the tax attributable to owners	287	9	(145)	-	151

Non-recurring items include:

A charge of £78 million related to the court approved Guaranteed Annuity Option Compromise scheme for Phoenix & London Assurance Limited. This removed longevity risk from the business whilst providing immediate policyholder cash enhancements and resulted in a charge recognised in the consolidated income statement as a change in insurance contract liabilities and administrative expenses of £74 million and £4 million respectively.

Other non-recurring items of £27 million include costs associated with the Phoenix Life site rationalisation and associated staff reductions and the Group's transformation programme with its outsourcers.

4.3 Segmental total assets and total liabilities

2009

	Phoenix Life	Ignis Asset Managemen t	Unallocate d corporate	Total
	£m	£m	£m	£m
Total assets	76,633	303	-	76,936
Total liabilities	(71,652)	(120)	(3,024)	(74,796)

4.4 2008 segmental analysis

In 2008 the results and net assets relate to unallocated corporate items.

5. Investment return variances and economic assumption changes

The long term nature of much of the Group's operations means that, for internal performance management, the effects of short term economic volatility are treated as non operating items. The Group focuses instead on an operating profit measure that incorporates an expected return on investments supporting its long term business. This note explains the methodology behind this.

5.1 Life assurance business

Operating profit for life assurance business is based on expected investment returns on financial investments backing owners' and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities. Operating profit includes the effect of variance in experience for non-economic items, for example mortality, persistency and expenses, and the effect of changes in non-economic assumptions. Changes due to economic items, for example market value movements and interest rate changes, which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed separately outside operating profit.

The movement in liabilities included in operating profit reflects both the change in liabilities due to the expected return on investments and the impact of experience variances and assumption changes for non-economic items. The effect of differences between actual and expected economic experience on liabilities, and changes to economic assumptions used to value liabilities, are taken outside operating profit. For many types of long term business, including unit linked and with profit funds, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. For other long term business the profit impact of economic volatility depends on the degree of matching of assets and liabilities, and exposure to financial options and guarantees.

The investment variances and economic assumption changes excluded from the long term business operating profit reflects the benefit of the reduction in credit spreads on corporate bonds and favourable equity, property and yield movements and are as follows:

	2009	Period ended 31 Dec 2008
	£m	£m
Investment return variances and economic assumption changes on long term business	145	-

5.2 Owners' funds

For non long term business including owners' funds, the total investment income, including realised and unrealised gains, is analysed between a calculated longer term return and short-term fluctuations.

The variances excluded from operating profit in relation to owners' funds are as follows:

	2009	Period ended 31 Dec 2008
	£m	£m
Variances on owners' funds of:		
Subsidiary undertakings	9	-
The Company	(79)	33
	(70)	33

The variances on owners' funds of the Company comprises unrealised fair value losses arising from movements in the fair value of warrants in issue over the Company's shares together with foreign exchange losses experienced in the year.

5.3 Calculation of the long term investment return

The expected return on investments for both owner and policyholder funds is based on opening economic assumptions applied to the funds under management at the beginning of the reporting period. Expected investment return assumptions are derived actively, based on market yields on risk-free fixed interest assets at the start of each financial year. The same margins are applied on a consistent basis across the Group to gross risk-free yields, to obtain investment return assumptions for equities and properties.

The principal assumptions underlying the calculation of the longer term investment return are:

	2009	Period ended 31 Dec 2008
	%	%
Equities	6.3	-
Property	5.8	-
Gilts (15 year gilt)	3.7	-
Other fixed interest (15 year gilt plus 0.6%)	4.3	-

6. Fees

	2009	Period ended 31 Dec 2008
	£m	£m
Fund management based fees	30	-
Investment contract income	71	-
	101	-

7. Net investment income

	2009 £m	Restated Period ended 31 Dec 2008 £m
Investment income		
Interest income on loans and receivables	76	16
Interest income on financial assets designated at fair value through profit or loss on initial recognition	818	-
Dividend income	321	-
Rental income	52	-
Net expected return on pension assets	(9)	-
	1,258	16
Fair value gains/(losses)		
Financial assets at fair value through profit or loss		
Held for trading – derivatives	(385)	-
Designated upon initial recognition	-	17
Investment property	159	-
	(226)	17
Net investment income	1,032	33

8. Other operating income

	2009 £m	Period ended 31 Dec 2008 £m

General business result	2	-
Income under Royal London transitional services agreement	31	-
Insurance claim	11	-
Other income	23	-
	67	-

9. Acquisition costs

	2009	Period ended 31 Dec 2008
	£m	£m
Acquisition costs paid	8	-

10. Administrative expenses

	2009	Period ended 31 Dec 2008
	£m	£m
Employee costs	65	-
Outsourcer expenses	58	-
Investment management expenses and transaction costs	73	-
Non-recurring administrative expenses	27	-
Operating expenses in respect of investment properties	11	-
Depreciation of property, plant and equipment	2	-
Other	19	2
	255	2

Employee costs comprise:

	2009	Period ended 31 Dec 2008
	£m	£m
Wages and salaries	56	-
Social security contributions	5	-
Other pension costs	4	-
	65	-

	2009	2008
	Number	Number
Average number of persons employed		
Phoenix Life	875	-
Ignis Asset Management	534	-
	1,409	-

The average number of employees has been presented for the period following the acquisition of the Pearl businesses on 28 August 2009.

11. Auditors' remuneration

The remuneration of the auditors of the Company, including their associates, in respect of services supplied to entities included in the consolidated financial statements was £7.2 million (2008: £0.1 million). No services were provided to associated pension schemes.

	2009	Period ended 31 Dec 2008
	£m	£m
Audit of the consolidated financial statements	0.8	0.1
The auditing of accounts of associates of the Company pursuant to legislation	3.5	-

Other services supplied pursuant to such legislation:		
Audit related	0.7	-
Services as reporting accountants	0.2	-
Other services:		
Audit of MCEV supplementary information	0.6	-
Other	1.4	-
	7.2	0.1

12. Finance costs

	2009 £m	Period ended 31 Dec 2008 £m
Interest expense		
On borrowings at amortised cost	64	-
On borrowings at fair value through profit or loss	23	-
	87	-
Attributable to		
- policyholders	22	-
- owners	65	-
	87	-

13. Tax (credit)/charge

13.1 Current year tax (credit)/charge

	2009	Period ended 31 Dec 2008

	£m	£m
Current tax:		
UK Corporation tax	(15)	-
Overseas tax	5	-
	(10)	-
Adjustment in respect of prior years	(3)	-
	(13)	-
Deferred tax:		
Reversal/(origination) of temporary differences		
On non profit surpluses	(51)	-
On amortisation of acquired in-force business	(17)	-
On profit arising from the changes in assumptions used for determining insurance liabilities in accordance with PS 06/14	(5)	-
Capital allowances in excess of depreciation	1	-
Pension scheme movements	16	-
On provisions for future expenditure	(12)	-
Utilisation of tax losses	63	-
Tax losses arising in the current year carried forward	(26)	-
	(31)	-
Total tax credit	(44)	-
Attributable to:		
- policyholders	(60)	-
- owners	16	-
	(44)	-

The Group, as a proxy for policyholders in the UK, is required to pay taxes on investment income and gains each year. Accordingly, the tax benefit or expense attributable to UK life assurance policyholder earnings is included in income tax expense. The tax benefit attributable to policyholder earnings was £60 million (2008: £nil).

13.2 Tax charged to other comprehensive income

	2009	Period ended 31 Dec 2008
	£m	£m
Deferred tax on actuarial gains of defined benefit schemes	31	-

13.3 Reconciliation of tax credit

	2009	Period ended 31 Dec 2008
	£m	£m
Profit before tax	91	-
Policyholder tax credit	60	-
Profit before the tax attributable to owners	151	-
Tax at standard UK* rate of 28%	42	-
Net tax losses on corporate restructuring not matched in accounts	(63)	-
Disallowable expenses	10	-
Adjustment to tax charge in respect of prior years	(3)	-
Decrease in deferred tax on movement in non profit surplus	(51)	-
Policyholder tax calculation methodology	48	-
Tax relief on accrued interest not valued	11	-
Profits taxed at rates other than 28%	12	-
Other	10	-
Owners' tax charge	16	-

* The Group's two operating segments operate predominantly in the UK. The reconciliation of the tax credit has therefore been completed by reference to the standard rate of UK tax rather than by reference to the Jersey income tax rate of zero percent which is applicable to Phoenix Group Holdings.

Policyholder tax credit	(60)	-
Total tax credit for the year	(44)	-

14. Dividends on ordinary shares

On 30 March 2010 the Board declared a dividend in respect of 2009. Information on this is given in note 48. No dividends have been declared in respect of the previous period.

15. Earnings per share

The profit attributable to owners for the purposes of computing earnings per share has been calculated as set out below. This is after adjusting for profits attributable to non-controlling interests.

	2009 £m	Restated Period ended 31 Dec 2008 £m
Profit for the year	135	31
Share of result attributable to non-controlling interests	(40)	-
Profit attributable to owners	95	31

The basic earnings per share of 102.9p (2008: 58.1p) has been based on the profit of £95 million (2008 Restated: £31 million) and a weighted average number of ordinary shares outstanding during the year of 92 million (2008: 53 million), calculated as follows:

	2009 Number million	Restated 2008 Number million

Issued ordinary shares at beginning of the year	53	-
Effect of ordinary shares issued/redeemed	39	53
Weighted average number of ordinary shares	92	53

The diluted earnings per share of 89.8p (2008: 45.1p) has been based on the profit of £95 million (2008: £31 million) and a diluted weighted average number of ordinary shares outstanding during the year of 106 million (2008: 69 million) calculated as follows:

	2009 Number million	Restated 2008 Number million
Weighted average number of ordinary shares	92	53
Effect of warrants in issue	14	16
Weighted average number of ordinary shares (diluted)	106	69

The Founders', Sponsors' and IPO warrants issued in 2008 were dilutive up until 2 September 2009 and had the effect of increasing the weighted average number of ordinary shares by 14 million in calculating the diluted weighted averaged number of ordinary shares.

The following instruments could potentially dilute basic earnings per share in the future but have not been included in the diluted earnings per share figure because they are anti-dilutive for the periods presented:

5 million warrants issued to the Lenders on 2 September 2009.

12.36 million warrants issued to Royal London on 2 September 2009.

The Founders', Sponsors' and IPO warrants from 2 September 2009 on which date the exercise price of the outstanding warrants was increased from €7 to €11.

Details of the warrants are given in note 24.

The following contingently issuable shares have not been included in the diluted earnings per share figure none of the conditions would have been satisfied and therefore no shares would have been issued:

26.5 million contingent rights over shares issued to the vendors on 2 September 2009 as part of the consideration for the acquisition of the Pearl businesses. These are payable in three tranches conditional upon the share price reaching thresholds of €13, €14 and €15 for 20 consecutive dealing days.

1 million contingent rights over shares were granted in satisfaction of the contingent underwriting fee. These are payable on condition that the share price reaches €15.

8.5 million contingent rights over shares were granted on 2 September 2009 to the Lenders in part satisfaction of the financing fees incurred by the UK finance companies. These are payable in three tranches conditional upon the share price reaching thresholds of €13, €14 and €15 for 20 consecutive dealing days.

16. Share capital

	2009	2008
	£	£
Authorised:		
300 million (2008: 300 million) ordinary shares of €0.0001 each	22,050	22,050
110 million (2008: nil) 'B' ordinary shares of €0.0001 each	9,700	-
Nil (2008: 1 million) preferred shares of €0.0001 each	-	74
	31,750	22,124
Issued and fully paid:		
80.4 million (2008: 75 million) ordinary shares of €0.0001 each	6,067	5,583
49.8 million (2008: nil) 'B' ordinary shares of €0.0001 each	4,383	-
	10,450	5,583

The holders of the ordinary and 'B' ordinary shares have the same rights to returns and voting. The holders are entitled to one vote per share on matters to be voted on by owners and to receive such dividends, if any, as may be declared by the Board of Directors in its discretion out of legally available profits.

Ordinary shares and 'B' ordinary shares comprise 62% and 38% respectively of total issued shares.

Movements in share capital during the period:

	2009	2009	2008	2008
	Number	£	Number	£
Share in issue at 1 January 2009 (2 January 2008)	75,000,000	5,583	-	-

Ordinary shares issued to Founders at €0.00124 per unit	-	-	20,125,000	1,505
Redemption of Founders ordinary shares at par	-	-	(5,125,000)	(388)
IPO of ordinary shares	-	-	60,000,000	4,466
‘B’ ordinary shares issued on acquisition of the Pearl businesses	40,700,000	3,588	-	-
Ordinary shares issued in part settlement of debt restructuring fees	3,500,000	307	-	-
‘B’ ordinary shares issued in part settlement of debt restructuring fees	7,070,000	620	-	-
‘B’ ordinary shares issued on assignment of PIK notes and facility	1,500,000	131	-	-
‘B’ ordinary shares issued to the employee trust	500,000	44	-	-
Ordinary shares redeemed on acquisition of the Pearl businesses	(6,038,344)	(533)	-	-
Ordinary shares issued on conversion of warrants	7,969,076	710	-	-
Shares in issue at 31 December	130,200,732	10,450	75,000,000	5,583

On 2 September 2009, 3,500,000 ordinary shares and 7,070,000 ‘B’ ordinary shares were issued in part settlement of debt restructuring fees at a premium of £96 million. On the same date, 40,700,000 ‘B’ ordinary shares were issued to the vendors as consideration for the acquisition of the Pearl businesses. These were issued at a premium of £332 million. A further 1,500,000 ‘B’ ordinary shares were issued in exchange for assignment of PIK notes and facility, and were issued at a premium of £12 million. 500,000 ‘B’ ordinary shares were issued to the Pearl Group Limited Employee Benefit Trust (“PGL EBT”) at a premium of £4 million.

On 2 September 2009, 6,038,344 ordinary shares were redeemed at a premium of £41 million.

During the period, 63,298,332 warrants were converted into 7,969,076 ordinary shares. These shares were issued at a premium of £55 million.

17. Shares held by employee trust

	£m
At 2 January 2008 and 1 January 2009	-
Issued in year	4

This reserve represents the value of the shares transferred to the PGL EBT to satisfy awards granted to employees under the Bonus Share Plan ("BSP") and the Long Term Incentive Plan ("LTIP"). The number of shares held by the PGL EBT at 31 December 2009 was 500,000 (2008: nil).

18. Share-based payment

Equity-settled share-based payments

On 11 January 2008, the Company issued and sold to the Sponsors 8,000,000 Sponsors' warrants in a private placement immediately prior to the consummation of its IPO. The material terms and conditions of the warrants are as for the Founders' and IPO warrants and the details are disclosed in note 24. The fair value of the Sponsors' warrants was estimated by using a binominal valuation model on the date of issue based on certain assumptions.

The Sponsors' warrants were valued at €2.23 on the date of issue before taking account of the trading restriction. The Sponsors gave an undertaking that they would not transfer or sell any of the Sponsors' warrants, or any shares derived from the Sponsors' warrants, until one year after the Company consummated a business combination. Such a restriction reduced the fair value of the Sponsors' warrants below the market value of the public warrants which can be freely traded. The value was reduced to €1.56 on the date of issue after taking into consideration this restriction, using a 30% discount. As the Sponsors paid €1.00 for the warrants, the difference in value of €0.56 is required to be recognised as a charge which equates to £4 million. The fair value of £4 million has been charged over the two year vesting period. For the year ended 31 December 2009 £2 million has been recognised as a share-based payment charge (31 December 2008: £2 million).

The following information was relevant in the determination of the fair value of the Sponsors' warrants:

Share price: €10.00

Exercise price: €7.00

Expected life: an expected life equal to the maturity of the option of 5 years is used.

Risk free rate: 3.422%, being the yield on German Government Bonds on 13 February 2008.

Volatility: 26% which is the average volatility of shares in a sample of 10 companies with a similar market capitalisation.

Dividend yield: zero

On 2 September 2009, one half of the 8,000,000 outstanding Sponsors' warrants were converted into 385,838 ordinary shares and the exercise price of the remaining 4,000,000 warrants was increased to €11.00. As the terms of these remaining warrants were modified before vesting, this resulted in a change of fair value. An increase in the exercise price decreases the fair value and therefore, in accordance with IFRS 2, there was no change to the original accounting.

On 24 July 2009, the Company's owners approved the adoption of a suite of share-based incentive plans including the BSP and the LTIP. On 2 September 2009 500,000 'B' ordinary shares were issued to the trustees of the PGL EBT and on 21 September 2009 the Board of Phoenix Group Holdings made recommendations for awards to the Trustee of the PGL EBT in respect of 403,750 'B' ordinary shares under each of the BSP and the LTIP, and approved the issue of a further 307,500 'B' ordinary shares to the trustee of the PGL EBT to be held, together with the original 500,000 'B' ordinary shares, on an unallocated basis pending satisfaction of the performance and vesting conditions. A letter of wishes from Phoenix Group Holdings to the Trustee of the PGL EBT requested the apportionment of 403,750 shares to named individuals under each of the BSP and the LTIP, following satisfaction of performance and vesting conditions. The additional 307,500 shares have not yet been issued to the Trustee of the PGL EBT and the Company is now considering whether these shares should be issued to the Trustee of the PGL EBT, or whether other arrangements should be implemented to enable the Trustee to acquire these shares on market.

The rules for the BSP and the LTIP anticipate that awards to participants will be subject to 2 year and 3 year vesting periods respectively. The rules also note that there are no performance conditions associated with the BSP and following a meeting of the Board of Phoenix Group Holdings on 21 September 2009, the performance conditions attaching to the awards under the LTIP will be the achievement of a premium listing on the London Stock Exchange ("LSE").

As there either are no performance criteria (BSP), or the performance criteria are considered likely to be met (LTIP) the fair value of the awards has been determined assuming that all granted shares vest. The share price at 21 September 2009 has been used in determining the fair value of these awards, this date being the start of the vesting period. The resulting 2009 expense to be recognised in the consolidated income statement in relation to these schemes is £0.6 million (2008: £nil) based on a charge from 21 September 2009 and 2 and 3 year vesting periods for the BSP and LTIP respectively.

On 24 September 2009 it was agreed to grant to the Chairman 300,000 'B' ordinary shares as part of the remuneration package to secure his appointment. The grant date of this award was 24 September 2009 which is the date the Chairman's contract of employment was signed. All vesting conditions are considered to have been met on this date as by signing the contract the Chairman joined the Group and his appointment was thereby secured. The fair value of the award has been determined assuming that all shares vest and using a share price at 24 September 2009 of €9.35. The expense recognised in the income statement in relation to this award is £2.5 million (2008: £nil). After 31 December 2009, the terms of the Chairman's award were amended. Details of these changes can be found in the 'Directors' Interests' section of the Remuneration Report.

19. Non-controlling interests

	Perpetual Reset Capital Securities	UK Commercial Property Trust Limited	Total
	£m	£m	£m
At 2 January 2008 and 1 January 2009	-	-	-

On acquisition of the Pearl businesses	518	181	699
Profit for the year	9	31	40
Dividends paid	-	(8)	(8)
Effect of share transactions	-	(3)	(3)
At 31 December 2009	527	201	728

19.1 Perpetual Reset Capital Securities

Pearl Group Holdings (No. 1) Limited ("PGH1") has in issue £500 million of Perpetual Reset Capital Securities ("the Notes") which are admitted to the Official List of the UK Listing Authority and to trading on the LSE.

The Notes are unsecured obligations of PGH1 and are subordinate to the claims of senior creditors. Payments in respect of the Notes are conditional upon PGH1 being solvent at the time of payment and immediately following such payment.

The Notes have no fixed maturity date and interest payments may be deferred at the option of PGH1; accordingly the Notes meet the definition of equity for financial reporting purposes. The Notes also meet the conditions for Innovative Tier 1 capital treatment in the calculation of the Group Capital Resources under the rules of the FSA. As the Notes are not directly held by the Company, these are disclosed as a non-controlling interest in the consolidated financial statements.

The Notes may be redeemed at par at the option of PGH1 on the first reset date of 25 April 2016 or on any coupon payment date thereafter. Redemption is subject to the agreement of the FSA. In certain circumstances PGH1 has the right to substitute the Notes or to redeem the Notes before the first reset date.

Coupons are payable annually in arrears on 25 April, at the rate of 6.5864% per annum, until the first reset date. Thereafter coupons are payable semi-annually at 2.73% per annum over the then prevailing offered rate for six-month sterling deposits. The consent of certain Lenders is required to enable the payment of coupons due in 2010 and thereafter.

If PGH1 opts to defer a coupon payment, then PGH1 has the option to either leave the coupon outstanding or satisfy the deferred coupon payment by the issue of securities ("ACSM instruments") by either PGH1 or a special purpose subsidiary of PGH1 established for the purpose of issuing ACSM instruments and which are guaranteed by PGH1. The obligations of PGH1 in respect of such securities, or if applicable, guarantee will be subordinated to and rank or be expressed to rank junior to the Notes as to rights to payments of interest and participation in the assets of PGH1 in a winding up and shall comply with the then current requirements of the FSA in relation to Tier 1 Capital. ACSM instruments will in the first instance be offered to related parties (as defined in the Terms and Conditions of the Notes as amended by the Supplemental Trust Deed dated 30 July 2008) and to third parties if not purchased by related parties. In the event that neither such related parties nor third parties will purchase the required ACSM instruments then PGH2 is required to use its best endeavours to raise such funds as are deemed necessary to purchase the required amounts of ACSM instruments.

For so long as a deferred coupon payment has not been satisfied PGH1 may not declare, pay or distribute a dividend on any of its securities in issue ranking junior to the Notes including the ordinary shares of PGH1 or any parity securities or,

except in particular circumstances, redeem, purchase or otherwise acquire any of its securities in issue ranking junior to the Notes, including its ordinary shares or any parity securities.

On 25 March 2009, the Board of PGH1 gave notice to the holders of the Notes of its decision to defer the coupon payment on the Notes at the next payment date of 25 April 2009 and PGH1 indicated that it had no present intention to initiate the ACSM.

On 23 March 2010 PGH1 gave notice to the holders of the Notes of its decision to defer the coupon on the Notes which would otherwise have been due for payment on 25 April 2010. PGH1 announced that if certain amending proposals are agreed by the Noteholders this notice will be withdrawn and the 2010 coupon will be paid in full on the first business day after the payment date of 25 April 2010; in addition the deferred 2009 coupon will be paid by 31 December 2010. Further information on this is given in note 48.

19.2 UK Commercial Property Trust Limited

UK Commercial Property Trust Limited ("UKCPT") is a property investment subsidiary which is domiciled in Guernsey and listed on the LSE.

20. Liabilities under insurance contracts

	Gross liabilities	Re-insurers' share	Gross liabilities	Re-insurers' share
	2009	2009	2008	2008
	£m	£m	£m	£m
Life assurance business:				
Insurance contracts	38,965	2,860	-	-
Investment contracts with DPF	11,326	-	-	-
	50,291	2,860	-	-
Amounts due for settlement after 12 months	40,150	2,722	-	-

	Gross liabilities	Re-insurers' share
	£m	£m
At 2 January 2008 and 1 January 2009	-	-
On acquisition of the Pearl businesses	51,413	2,689

Premiums	545	31
Claims	(2,043)	(105)
Other changes in liabilities	361	216
Foreign exchange adjustments	15	29
At 31 December 2009	50,291	2,860

21. Unallocated surplus

	2009	2008
	£m	£m
At 2 January 2008 and 1 January 2009	-	-
On acquisition of the Pearl businesses	546	-
Transfer from income statement	175	-
At 31 December 2009	721	-

22. Borrowings

	2009	2008
	£m	£m
Carrying value		
Debenture loans		
Limited recourse bonds 2012 7.39% (note a)	48	-
Limited recourse bonds 2022 7.59% (note a)	86	-
Unsecured loan notes (note b)	18	-
£200 million 7.25% unsecured subordinated loans (note c)	119	-
£779 million loan (note d)	764	-
£15 million loan (note e)	15	-
£2,260 million syndicated loan (note f)	2,260	-
£80 million facility agreement (note g)	42	-
£100 million PIK notes and facility (note h)	102	-
£75 million secured loan note (note i)	70	-
£425 million loan facility (note i)	399	-
	3,923	-
Refinancing loan (note j)	258	-
	4,181	-

Amount due for settlement after 12 months	4,086	-

	2009	2008
	£m	£m
Fair value		
Debenture loans		
Limited recourse bonds 2012 7.39% (note a)	45	-
Limited recourse bonds 2022 7.59% (note a)	93	-
Unsecured loan notes (note b)	18	-
£200 million 7.25% unsecured subordinated loans (note c)	156	-
£779 million loan (note d)	751	-
£15 million loan (note e)	14	-
£2,260 million syndicated loan (note f)	2,260	-
£80 million facility agreement (note g)	42	-
£100 million PIK notes and facility (note h)	102	-
£75 million secured loan note (note i)	70	-
£425 million loan facility (note i)	399	-
	3,950	-
Refinancing loan (note j)	258	-
	4,208	-

Debenture loans

(a) In 1998, National Provident Institution raised £260 million of capital through the securitisation of embedded value on a block of existing unit linked and unitised with profit life and pension policies. Following the demutualisation of National Provident Institution, these were transferred to National Provident Life Limited ("NPLL"). The bonds are split between two classes, which rank pari passu. The £140 million 7.39% class A1 limited recourse bonds with an outstanding principal of £42 million have an average remaining life of 2 years maturing in 2012. The £120 million 7.59% limited recourse bonds with an outstanding principal of £120 million have an average remaining life of 9 years maturing in 2022. NPLL has provided collateral of £88 million to provide security to the holders of the NPLL recourse bonds in issue.

Phoenix Group Holdings acquired these bonds as part of the acquisition of the Pearl businesses and they were recognised at their fair value.

(b) Unsecured loan notes of £72 million were issued by Impala Holdings Limited ("Impala") at par on 14 May 2008 at an interest rate of LIBOR minus 1% per annum with a final maturity date of 2012. Phoenix Group Holdings acquired

these loan notes as part of the acquisition of the Pearl businesses and they were recognised at their fair value. As at 31 December 2009 £54 million of these loan notes had been repaid and £18 million were outstanding.

(c)Scottish Mutual Assurance Limited ("SMA") issued £200 million 7.25% undated, unsecured subordinated loan notes on 23 July 2001. The earliest repayment date of the notes is 25 March 2021 and thereafter on each fifth anniversary so long as the notes are outstanding. With effect from 1 January 2009, as a part of a Part VII transfer, these loan notes were transferred into the shareholder fund of Phoenix Life Limited ("PLL"). PLL has entered into interest rate swap agreements with Abbey National Treasury Services plc, the effect of which is to convert the fixed interest expense on the notes to a floating rate expense. In the event of the winding-up of PLL, the right of payment under the notes is subordinated to the rights of the higher-ranking creditors (principally policyholders). Phoenix Group Holdings acquired these loan notes as part of the acquisition of the Pearl businesses and they were recognised at their fair value.

(d) On 3 June 2008, Axial Fixed Income Opportunities S.a.r.l. issued A loans consisting of €459,886,325; £39,480,573 and US $288,125,702. On 13 June 2008, Axial Fixed Income Opportunities S.a.r.l. issued further A loans of £128,401,000 and on 11 July 2008, Axial Fixed Income Opportunities S.a.r.l. issued further A loans of US $29,780,400. These loans accrue interest at LIBOR plus 125 bps and mature in May 2016. Phoenix Group Holdings acquired these loans as part of the acquisition of the Pearl businesses and they were recognised at their fair value.

(e) On 3 June 2008, Axial Fixed Income Opportunities S.a.r.l. issued B loans consisting of €9,397,311; £3,015,429 and US $4,476,558. These loans accrue a fixed interest rate of 0.1% plus a variable profit related element and mature in May 2016. Phoenix Group Holdings acquired these loans as part of the acquisition of the Pearl businesses and they were recognised at their fair value.

(f) On 14 May 2008, PGH (LC1) Limited and PGH (LC2) Limited jointly obtained a £2,260 million loan facility from a syndicate of external banks (the "Impala Facility"). This facility was split into Tranche loans A, B and C of £1,275 million, £492.5 million and £492.5 million respectively. For financial reporting purposes, Phoenix Group Holdings was deemed to have acquired this facility as part of the acquisition of the Pearl businesses and it was recognised at its fair value. The terms of this facility were subsequently amended on 2 September 2009, to the following:

Tranche A loan of £1,275 million is repayable over the period from 30 April 2011 to 30 November 2014 and attracts interest at LIBOR plus a cash margin of 1.00% and a PIK margin of 1.00% for the first four years, and LIBOR plus a cash margin of 2.50% for the subsequent years;

Tranche B loan of £492.5 million is repayable on 30 November 2015 and attracts interest at LIBOR plus a cash margin of 1.25% and a PIK margin of 0.75% for the first four years, and LIBOR plus a cash margin of 3.25% for the subsequent years; and

Tranche C loan of £492.5 million is repayable on 30 November 2016 and attracts interest at LIBOR plus a cash margin of 1.75% and a PIK margin of 0.25% for the first four years, and LIBOR plus a cash margin of 3.75% for the subsequent years.

The borrowings under the £2,260 million facility are secured by:

First fixed and floating charges over all the assets and undertaking of PGH (LC1) Limited and PGH (LC2) Limited (including their respective 12.5% shareholding in Impala, all real estate, book debts, bank accounts, investments and other assets); and

A limited recourse share charge granted by PGH2 over its 75% shareholding in Impala.

(g) In 2008, UKCPT entered into an £80 million revolving loan facility agreement with Lloyds TSB. This loan accrues interest at LIBOR plus a variable margin of 0.50% to 0.70% per annum. The lender holds a floating charge over certain assets of UKCPT and its subsidiaries. The repayment date for this facility is 19 June 2015.

(h) On 14 May 2008, PGH (MC1) Limited issued PIK notes for the value of £154.5 million to Royal London and PGH (MC2) Limited obtained a £154.5 million PIK facility from Royal London. On 2 September 2009, £250 million in aggregate of the PIK notes and the facility outstanding (comprising principal and capitalised interest) was assigned to Phoenix Group Holdings as part of the acquisition of the Pearl businesses in exchange for the issue of 1.5 million shares and 12.36 million warrants. The acquired PIK notes and facility were recognised at their fair value. Interest accrues on the PIK notes and facility at LIBOR plus a margin of 2% unless an election is made by PGH (MC1) Limited or PGH (MC2) Limited to capitalise the interest, in which case the margin increases to 3.5%. In December 2009, interest of £2.3 million was capitalised on the PIK notes and facility. The final maturity date on the PIK notes and facility is 30 June 2019.

(i) On 15 November 2006, PGH (LCA) Limited and PGH (LCB) Limited jointly became a party to a £905 million loan facility from a syndicate of external banks. For financial reporting purposes, Phoenix Group Holdings was deemed to have acquired this facility as part of the acquisition of the Pearl businesses and it was recognised at its fair value. On 2 September 2009, this facility was restructured as follows:

£75 million of the existing facility was converted into two £37.5 million secured C loan notes repayable after 15 years and attracting interest at LIBOR plus a margin of 1.00%;

£325 million of the existing facility was assigned to Phoenix Group Holdings from the lending banks for consideration of £75 million, with a maturity date of 30 June 2016, attracting interest at LIBOR plus a margin of 1.25%; and

The terms of the remaining £425 million outstanding under the existing facility were amended and the facility is repayable over the period from 30 June 2011 to 30 June 2016, attracting interest at LIBOR plus a margin of 1.25%.

The borrowings under the £425 million facility are secured by first fixed and floating charges over all of the assets and undertakings of PGH (LCA) Limited and PGH (LCB) Limited (including their respective 50% shareholdings in Phoenix Life Holdings Limited ("PLHL"), all real estate, book debts, bank accounts, investments and other assets).

Refinancing loan

(j) The refinancing loan from Abbey National plc was acquired as part of the acquisition of the Pearl businesses. The loan was brought into the consolidated financial statements at fair value. It relates to the sale of Extra-Income Plan policies that Abbey National plc finances to the value of the associated property reversions. As part of the arrangement Abbey National plc receive an amount calculated by reference to the movement in the Halifax House Price Index and NPLL and NPI Limited ("NPI") have undertaken to indemnify Abbey National plc against profits or losses arising from mortality or surrender experience which differs from the basis used to calculate the reversion amount. Repayment will be on a policy-by-policy basis and is expected to occur over the next 10 to 20 years.

23. Deposits received from reinsurers

	2009	2008
	£m	£m

Carrying value:		
At 31 December	431	-
Amount due for settlement after 12 months	394	-

	2009	2008
	£m	£m
Fair value:		
At 31 December	431	-

In addition to receiving the cash collateral set out above, it is also the Group's practice to obtain collateral in the form of marketable securities. This collateral is held on behalf of the Group and is not recognised on the statement of consolidated financial position as either an asset or an associated liability as the Group is not permitted to sell or re-pledge the collateral in the absence of default. The total value of the collateral held under such arrangements in respect of reinsurance treaties was £1,846 million (2008: £nil).

24. Derivatives

The Group purchases derivative financial instruments in connection with the management of its insurance contract and investment contract liabilities based on the principles of reduction of risk and efficient portfolio management.

The fair values of derivative financial instruments are as follows:

	2009 Assets £m	2009 Liabilities £m	2008 Assets £m	Restated 2008 Liabilities £m
Warrants over shares in Phoenix Group Holdings	-	23	-	11
Forward currency	189	181	-	-
Credit default options	4	29	-	-
Interest rate swaps	1,683	1,430	-	-
Swaptions	285	-	-	-
Inflation swaps	20	2	-	-
Total return bond swaps	27	-	-	-

Equity options	191	-	-	-
Stock index futures	1,141	1,177	-	-
	3,540	2,842	-	11

The amount recoverable after one year is £2,143 million (2008: £nil). The amount payable after one year is £1,394 million (2008: £nil).

Certain cash collateral on derivatives is available to the Group for investment purposes and is therefore recognised as a financial asset and a liability, recorded as 'Obligations for repayment of collateral received' in the statement of consolidated financial position. At 31 December 2009, the amount of collateral recognised as a financial asset and 'Obligations for repayment of collateral received' amounted to £1,041 million (2008: £nil) and £1,099 million (2008: £nil) respectively.

Where collateral has been pledged by the Group and the right of set off is only enforceable on the occurrence of a particular future event then the pledged asset continues to be recognised by the Group. On the same basis the Group does not recognise collateral pledged by counterparties. Off balance sheet derivative collateral at 31 December 2009 which had been pledged to/by the Group amounted to £188 million (2008: £nil) and £455 million (2008: £nil) respectively.

Warrants over shares in Phoenix Group Holdings

In 2008 Phoenix Group Holdings issued 20.12 million Founders' warrants and 60 million IPO warrants. On 2 September 2009 12.36 million warrants were issued to Royal London and 5 million were issued to the Lenders. The table below shows a reconciliation of the outstanding number of these warrants.

	IPO warrants	Founders' warrants	Lenders warrants	Royal London warrants
	Number	Number	Number	Number
At 2 January 2008	-	-	-	-
Issuance to Founders (10 January 2008)	-	20,125,000	-	-
Redemption from Founders (5 February and 11 March 2008)	-	(5,125,000)	-	-
Initial Public Offering (13 February 2008)	60,000,000	-	-	-
At 31 December 2008	60,000,000	15,000,000	-	-

Forfeiture of Founders' warrants and shares (2 September 2009)	-	(63,600)	-	-
Conversion of 50% of outstanding warrants into ordinary shares (2 September 2009)	(30,000,000)	(7,468,200)	-	-
Issue of warrants to Royal London and Lenders (2 September 2009)	-	-	5,000,000	12,360,000
Conversion of IPO warrants into new ordinary shares (31 December 2009)	(21,830,132)	-	-	-
At 31 December 2009	8,169,868	7,468,200	5,000,000	12,360,000

IPO and Founders' warrants

The IPO and Founders' warrants originally entitled the holder to purchase one ordinary share at a price of €7.00 per share, subject to adjustment, at any time commencing on the consummation of a business combination. On 2 September 2009 the exercise price was increased to €11.

The exercise period commenced on the later of:

- consummation by the Company of a business combination; and
- first anniversary of the date the units are admitted to trading on Euronext.

The warrants will expire at the close of trading on Euronext on the first business day after 6 February 2013 or earlier upon redemption or liquidation. Once the warrants become exercisable, the Company may call the warrants for redemption:

in whole but not in part;

at a price of €0.01 per warrant;

upon not less than 30 days' prior written notice of redemption to each warrant holder; and

if, and only if, the reported last sale price of the share equals or exceeds €13.75 per share for any 20 trading days within a period of 30 consecutive trading days ending on the third business day prior to the notice of redemption to warrant holders. On 2 September 2009 the threshold of €13.75 was increased to €16.50.

If the foregoing conditions are satisfied and the Company issues notice of redemption of the warrants, each warrant holder shall be entitled to exercise their warrant prior to the scheduled redemption date. However, the price of the shares may fall below the redemption trigger price or the warrant exercise price after the redemption notice is issued.

If the Company calls the warrants for redemption as described above, it will have the option to require any holder that wishes to exercise its warrant (including the Founders' warrants) to do so on a cashless basis.

The Founders' and IPO warrants are listed and are valued using the warrant price quoted on Euronext for the Company. At 31 December 2009 the Founders' warrants were valued at £7 million (2008: £2 million) and the IPO warrants were valued at £8 million (2008: £9 million).

Lenders' warrants

On 2 September 2009, the Company issued 5 million warrants over its shares to the Lenders. These warrants entitle the holder to purchase one 'B' ordinary share at a price of £15 per share, subject to adjustment. Following the achievement of a premium listing of the ordinary shares on the LSE, the Lenders' warrants will be over ordinary shares rather than 'B' ordinary shares.

The exercise period commences on the date of the warrant agreement and terminates on the first to occur of:

15th anniversary of the date issued;

Date fixed for the redemption of the warrants; and

Liquidation of the Company.

The Company can issue a similar number of ordinary shares instead of 'B' ordinary shares. This is effective from the earlier of:

The date the ordinary shares are listed and traded on the LSE; and

1 July 2010.

All outstanding warrants may be redeemed at the option of the Company at any time after they become exercisable and prior to their expiration at a price of €0.01 per warrant provided that the last closing bid price of the ordinary shares is equal to or exceeds £19.50 on each of 20 consecutive trading days. The Company must give not less than 30 days notice of the redemption date. Each warrant may then be exercised by the warrant holder (in whole or any part) at its option.

The holders are entitled to exercise their warrants for cash, assignment of an amount of outstanding principal/accrued interest of any Global Debt (i.e. any debt owed to the registered holder by any Group company) or on a cashless basis where the Company redeems the warrants. Any warrant either not exercised or tendered back to the Company by the redemption date shall be cancelled on the books of the Company and have no further value except for the €0.01 redemption price.

These Lenders' warrants are not traded in an active market and have therefore been valued using a Black-Scholes valuation model. The key assumptions used to ascertain a value as at 31 December 2009 are as follows:

- Share price as at 31 December 2009 of €7.44;

- volatility of 30%;
- the warrants are not adjusted for dividends;
- the valuation incorporates the impact of the issuance of 4.0 million new ordinary shares in exchange for 21.8 million public warrants; and
- upside participation limited to 70%.

The value of the warrants at the year end was £2 million (2008: £nil).

Royal London warrants

On 2 September 2009, the Company issued 12.36 million warrants (2 million transferable and 10.36 million non-transferable) over its shares to Royal London as part consideration for acquiring the benefit of £250 million of the PIK notes and facility outstanding (comprising principal and capitalised interest). These warrants entitle the holder to purchase one 'B' ordinary share at a price of €11 per share, subject to adjustment. Following the achievement of a premium listing of the ordinary shares on the LSE, the Royal London warrants will be over ordinary shares rather than 'B' ordinary shares.

The exercise period commences on the date of the warrant agreement and terminates on the first to occur of:

5th anniversary of the date issued;

Date fixed for the redemption of the warrants; and

Liquidation of the Company.

The Company can issue a like number of ordinary shares instead of 'B' ordinary shares. This is effective from the earlier of:

The date the ordinary shares are listed and traded on the LSE; and

1 July 2010.

All outstanding warrants may be redeemed at the option of the Company at any time after they become exercisable and prior to their expiration at a price of €0.01 per warrant provided that the last closing bid price of the ordinary shares is equal to or exceeds €16.50 on each of 20 consecutive trading days. The Company must give not less than 30 days notice of the redemption date. Each warrant may then be exercised by the warrant holder (in whole or any part) at its option.

The holders are entitled to exercise their warrants for cash, assignment of an amount of outstanding principal plus accrued interest of any Global Debt (i.e. the PIK facility) or on a cashless basis where the Company redeems the warrants. Any warrant either not exercised or tendered back to the Company by the redemption date shall be cancelled on the books of the Company and have no further value except for the €0.01 redemption price.

The Royal London warrants are not traded in an active market and have therefore been valued using a Black-Scholes valuation model.

The key assumptions used to ascertain a value as at 31 December 2009 are as for the Lenders' warrants (see above). The value of the warrants at the year end was £6 million (2008: £nil).

25. Obligations for repayment of collateral received

	2009	2008
	£m	£m
Carrying value:		
At 31 December	4,106	-
Amount due for settlement after 12 months	1,054	-

	2009	2008
	£m	£m
Fair value:		
At 31 December	4,106	-

26. Financial liabilities

	2009	Restated 2008
	£m	£m
Carrying value:		
Financial liabilities at fair value through profit or loss:		
Designated upon initial recognition	9,774	-
Held for trading – derivatives	2,842	11
Financial liabilities measured at amortised cost	8,460	-
	21,076	11
Amount due for settlement after 12 months	6,928	-

	2009	Restated 2008

	£m	£m
Fair value:		
Financial liabilities at fair value through profit or loss:		
Designated upon initial recognition	9,774	-
Held for trading – derivatives	2,842	11
Financial liabilities measured at amortised cost	8,487	-
	21,103	11

27. Provisions

	Re-structuring	Leasehold properties	Staff related	Known incidents	Other	Total
	£m	£m	£m	£m	£m	£m
At 2 January 2008 and 1 January 2009	-	-	-	-	-	-
On acquisition of the Pearl businesses	13	38	22	18	30	121
Additions in the year	-	2	-	-	12	14
Utilised during the year	(5)	(2)	(3)	(4)	(10)	(24)
Released during the year	(1)	(1)	(3)	(6)	-	(11)
Effect of discounting and of changes in the discount rate	-	-	1	-	-	1
At 31 December 2009	7	37	17	8	32	101

The restructuring provision relates principally to the anticipated redundancy costs associated with the closure of the Group's Glasgow and Peterborough life operations, which is expected to occur in 2010 and 2011.

The leasehold properties provision has been made for amounts in respect of the excess of lease rentals and other payments on properties that are currently vacant or are expected to become vacant, over the amounts to be recovered from subletting these properties. The discount rate used ranged between 5.00% and 6.07% and it is expected that the provision will be utilised over the next 8 years.

Staff related provisions primarily relate to redundancy costs of staff that have been transferred under outsourcing contracts. This provision will be utilised over the next 2 years.

The known incidents provision was created for historical data quality, administration systems problems and process deficiencies on the policy administration, financial reconciliations and operational finance aspects of business outsourced.

Included in other provisions is £9 million in respect of investment contracts representing the excess of future costs over future charges on the Group's unit linked business, assessed at a product level. The discount rate used in calculating the provision is 4% and the provision is expected to run off over the remaining life of the business, estimated at 30 years. The remainder of the balance includes litigation and onerous contract provisions.

28. Tax assets and liabilities

	2009	2008
	£m	£m
Current tax receivables	44	-
Net deferred tax assets	81	-
Total tax assets	125	-
Current tax payables	103	-
Net deferred tax liabilities	776	-
Total tax liabilities	879	-

Deferred tax assets comprise

	2009	2008
	£m	£m
Trading losses	28	-
Expenses and deferred acquisition costs carried forward	142	-
Provisions and other temporary differences	30	-
Pension scheme deficit	34	-
Accelerated capital allowances	24	-
Unpaid interest	45	-
Gross deferred tax assets	303	-
Less: offset against deferred tax liabilities	(222)	-
Net deferred tax assets	81	-

Deferred tax liabilities comprise

	2009	2008
	£m	£m
Acquired in-force business	736	-
Unrealised gains on investments	7	-
Surplus within the non profit funds	96	-
Provisions and other temporary differences	19	-
Adjustment for insurance policies held with related parties in respect of the PGL Pension Scheme	17	-
Intangible assets	123	-
Gross deferred tax liabilities	998	-
Less: offset against deferred tax assets	(222)	-
Net deferred tax liabilities	776	-

Movements in deferred tax assets/(liabilities) comprise

	2009	2008
	£m	£m
At 1 January 2009 (2 January 2008)	-	-
On acquisition of the Pearl businesses	(695)	-
Amounts credited to the income statement	31	-
Amounts charged to the statement of other comprehensive income	(31)	-
At 31 December	(695)	-

Deferred tax has been provided on the surpluses within the non profit funds on the assumption that all such surpluses will eventually be distributed to owners.

Deferred income tax assets are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable.

	2009	2008
	£m	£m
Deferred tax assets have not been recognised in respect of:		
Tax losses carried forward	141	-
Excess expenses and deferred acquisition costs carried forward	50	-

Provisions and other temporary differences	3	-
Deferred tax assets not recognised on capital losses	210	-

These can only be offset against future capital gains and have no expiry date.

29. Payables related to direct insurance contracts

	2009 £m	2008 £m
Payables related to direct insurance contracts	759	-
Amount due for settlement after 12 months	66	-

General insurance

Due to the historic diversity of issued general insurance policies and taking into account the legal and regulatory environment for hazardous risks, it is possible that additional claims could emerge from long tail unexpired risks albeit it is not possible to predict the quantum, location or timing of such occurrences.

The estimation of the provisions for the ultimate cost of claims for asbestos and environmental pollution is subject to a range of uncertainties that is generally greater than those encountered for other classes of insurance business and as a consequence of this uncertainty the eventual costs of settlement of outstanding claims and unexpired risks can vary substantially from the estimates.

Pearl Assurance plc

Within Pearl Assurance plc ("Pearl") the provision for the future claims payments has primarily been assessed in accordance with actuarial methods projecting the number and amount of claims separately. Where there is a notable exposure to long term asbestos, pollution and health hazard liabilities, external independent actuaries provide best estimate benchmarks. An appropriate prudential margin is applied to certain lines of business as it is recognised that the estimation of certain future claims payments is an inherently uncertain exercise and future experience could be more adverse.

In calculating the provisions in respect of long term UK Industrial disease business the future investment income on the assets held to cover the related provisions has been taken into account by discounting future cash flows. The average period before the undiscounted liability will be settled has been estimated at 14 years for 2009 and the provision has been discounted at 2.5% per annum.

The overall effect is to reduce the gross and net claims outstanding financial liability for those classes of business referred to above at 31 December 2009 by £9 million from £35 million to £26 million. The total amount of the investment return which corresponds to the unwinding of the discount is £0.6 million.

PA (GI) Limited

Within PA (GI) Limited the provision for outstanding general insurance claims comprises the estimated ultimate cost of settling claims notified but not settled by the period end. It includes related expenses and a deduction for the expected value of salvage and other recoveries. The provision is determined using the best information available of claims

settlement patterns, forecast inflation and settlement of claims. The general insurance liabilities of PA (GI) Limited are wholly reinsured externally to RSA.

30. Accruals and deferred income

	2009	2008
	£m	£m
Accruals	177	9
Amount due for settlement after 12 months	4	-

31. Other payables

	2009	2008
	£m	£m
Investment broker balances	420	-
Other payables	230	-
	650	-
Amount due for settlement after 12 months	8	-

32. Pension schemes

The Group operates two main staff Pension Schemes, the Pearl Group Staff Pension Scheme and the PGL Pension Scheme.

The carrying value of the defined benefit pension schemes is set out below.

	2009	2008
	£m	£m
Pearl Group Staff Pension Scheme deficit	(121)	-
PGL Pension Scheme – economic surplus	62	-
Adjustment for insurance policies held with related parties and eliminated on consolidation	(66)	-
PGL Pension Scheme – reported deficit	(4)	-

Total deficit	(125)	-

Information on each of these schemes is set out below. This principally relates to the period from 28 August 2009 to 31 December 2009.

32.1 Pearl Group Staff Pension Scheme

The Pearl Group Staff Pension Scheme ("the Pearl Scheme") comprises a final salary section, a money purchase section and a hybrid section (a mix of final salary and money purchase). The final salary and hybrid sections of the Pearl Scheme are closed to new members.

Defined contribution scheme

The Group participates in the defined contribution section of the Pearl Scheme. Contributions in the period 28 August to 31 December 2009 amounted to approximately £1 million.

Defined benefit scheme

The Pearl Scheme is funded by payment of contributions to a separately administered trust fund and is subject to regular valuations by an independent qualified actuary. A Group company, PGH2 is the principal employer of the Pearl Scheme.

Given the deficit in the Pearl Scheme, the principal employer and the Trustees of the Pearl Scheme entered into an agreement effective 2 September 2009, the principal terms of which provided for the following:

A cash payment into the scheme of £50 million in October 2009 followed by cash payments of £25 million per annum for a period of 10 years, commencing on 30 September 2010, subject to certain capital resource and other requirements being maintained.

The Trustees being granted a first charge over shares in Pearl, NPLL, London Life Limited, Pearl Group Services Limited and PGS 2 Limited to secure an amount not exceeding 60% of the deficit arising on the triennial scheme valuation (as calculated in accordance with the terms of the agreement), subject to an initial amount and a maximum of £600 million, such security ceasing on a scheme buy out, the principal employer discharging its liabilities under the agreement or upon a valuation of the scheme demonstrating there is no funding deficit if earlier. Enforcement of the security may take place on the occurrence of various events, the key ones being (i) a failure by the principal employer to pay agreed cash contributions to the scheme, (ii) an insolvency or other similar financial difficulties of the principal employer, (iii) except in certain defined circumstances, payments of interest or principal to the principal employer's lenders or of dividends to the principal employer's owners being made at a time when the principal employer has failed to maintain an embedded value of at least 1.3 times the amount secured, (iv) the principal employer failing to maintain an embedded value of at least 1.05 times the amount secured or (v) the principal employer granting certain types of

security over its assets. NP Life Holdings Limited has also granted a limited recourse share charge over the shares it holds in NPLL in favour of the Trustee in respect of the principal employer's obligation under this agreement. This security is granted on substantially the same terms as the security granted by the principal employer. The principal employer has also agreed to provide a share charge over NPI if NPI is not transferred within the Group by 14 April 2010.

In addition, the principal employer meets the administration expenses of the Pearl Scheme.

The valuation has been based on an assessment of the liabilities of the Pearl Scheme as at 31 December 2009, undertaken by independent qualified actuaries. The present values of the defined benefit obligation and the related current service costs have been measured using the projected unit credit method.

The principal financial assumptions of the Pearl Scheme are set out below.

	2009	2008
Rate of general long term increase in salaries	4.5%	-
Rate of increase in pensions	3.5%	-
Discount rate	5.7%	-
Inflation	3.5%	-
Expected rate of return on scheme assets	5.1%	-

The discount rate and inflation rate assumptions used for the calculation of the liabilities have been determined by considering the shape of the appropriate yield curves and the duration of the Pearl Scheme liabilities. This method determines an equivalent single rate for both the discount and inflation rates, which is derived from the profile of projected benefit payments.

The expected rate of return on scheme assets is derived after considering historical returns and assuming that asset classes with higher volatility generate higher returns (consistent with widely accepted capital market principles). The overall expected return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation.

It has been assumed that post retirement mortality is in line with standard tables PMA92C2009 for males and PFA92C2009 for females, based on year of use and including Medium Cohort projections for future mortality improvements. Under these assumptions, the average life expectancy from retirement for a member currently aged 40 retiring at age 60 is 26.8 years and 29.8 years for male and female members respectively.

The amounts recognised in the income statement are as follows:

	2009	2008
	£m	£m

Current service cost	-	-
Interest cost	(32)	-
Expected return on scheme assets	27	-
	(5)	-

The net actuarial gains and losses recognised in other comprehensive income comprise the following:

	2009	2008
	£m	£m
Actual return less expected return on scheme assets	36	-
Experience gains arising on scheme liabilities	58	-
Loss due to changes in assumptions underlying scheme liabilities	(65)	-
	29	-

The cumulative net actuarial gains recognised in other comprehensive income since 28 August 2009 amounted to £29 million.

The amounts recognised in the statement of financial position are as follows:

	2009	2008
	£m	£m
Fair value of scheme assets	1,684	-
Present value of defined benefit obligation	(1,805)	-
Deficit	(121)	-

The actual return on the scheme assets comprises the following:

	2009	2008
	£m	£m
Expected return on scheme assets	27	-
Actuarial gains on scheme assets	36	-
	63	-

The change in the present value of the defined benefit obligation is as follows:

	2009	2008
	£m	£m
At 1 January 2009 (2 January 2008)	-	-
On acquisition of the Pearl businesses	1,791	-
Current service cost	-	-
Interest cost	32	-
Actuarial losses	7	-
Benefits paid	(25)	-
At 31 December	1,805	

The defined benefit obligation arises from plans that are wholly or partly funded.

The change in the fair value of the scheme assets is as follows:

	2009	2008
	£m	£m
At 1 January 2009 (2 January 2008)	-	-
On acquisition of the Pearl businesses	1,583	-
Expected return on scheme assets	27	-
Actuarial gains on scheme assets	36	-
Contributions by the employer	63	-
Benefits paid	(25)	-
At 31 December	1,684	-

The distribution of the scheme assets at the end of the year was as follows:

	2009	2008
	£m	£m
Equities	318	-
Bonds	1,215	-
Properties	63	-
Cash	72	-
Other	16	-

1,684	-

Contributions totalling £25 million are expected to be paid into the scheme in 2010 in accordance with the agreement with the Trustees of the Pearl Scheme.

Table of historical information from 2009

	2009
	£m
Fair value of scheme assets	1,684
Defined benefit obligation	(1,805)
Deficit	(121)
Experience gains on scheme assets	36
Experience gains on scheme liabilities	58

32.2 PGL Pension Scheme

Defined contribution scheme

The Group participates in the defined contribution section of the PGL Pension Scheme ("the PGL Scheme"). Contributions in the period from 28 August 2009 to 31 December 2009 amounted to £1 million.

Defined benefit scheme

The defined benefit section of the PGL Scheme is a final salary arrangement which is generally closed to new entrants and, in respect of former members of the Phoenix Life Group pension scheme (which merged with the PGL Scheme in 2006) to future service accruals.

The valuation has been based on an assessment of the liabilities of the PGL Scheme as at 31 December 2009, undertaken by independent qualified actuaries. The present values of the defined benefit obligation and the related current service costs have been measured using the projected unit credit method.

The principal financial assumptions of the PGL Scheme are set out below.

	2009	2008
Rate of general long term increase in salaries	4.6%	-
Rate of increase in pensions	3.5%	-
Discount rate	5.7%	-
Inflation	3.6%	-
Expected rate of return on scheme assets	5.4%	-

The discount rate and inflation assumptions used for the calculation of the liabilities have been determined by considering the shape of the appropriate yield curves and the duration of the PGL Scheme liabilities. This method determines an equivalent single rate for both the discount and inflation rates, which is derived from the profile of projected benefit payments.

The expected rate of return on scheme assets is derived after considering historical returns and assuming that asset classes with higher volatility generate higher returns (consistent with widely accepted capital market principles). The overall expected return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation.

It has been assumed that post retirement mortality is in line with standard tables PNA00 with a scaling factor of 105% being applied, allowing for future improvements in line with the long cohort improvement factors, subject to a minimum improvement from 2007 onwards of 1.25% p.a. and 0.75% p.a. for males and females respectively. Under these assumptions, the average life expectancy from retirement for a member currently aged 40 retiring at age 57 is 33.9 years and 35.0 years for male and female members respectively. The average life expectancy from retirement for a member currently aged 50 retiring at age 57 is 32.5 years and 34.2 years for male and female members respectively.

The economic value of the PGL Scheme assets as at 31 December 2009 amounted to £1,192 million and the economic value of the surplus amounted to £62 million. For financial reporting purposes the carrying value of the insurance policies effected by the PGL Scheme with the Group amounting to £66 million have been eliminated on consolidation, resulting in reported assets of the PGL Scheme as at 31 December 2009 of £1,126 million and a reported deficit of £4 million.

The amounts recognised in the income statement are as follows:

	2009 £m	2008 £m
Current service cost	(2)	-
Interest cost	(21)	-
Expected return on scheme assets	17	-
	(6)	-

The net actuarial gains and losses recognised in other comprehensive income comprise the following:

	2009	2008
	£m	£m
Actual return less expected return on scheme assets	23	-
Experience gain arising on scheme liabilities	18	-
Gain due to changes in assumptions underlying scheme liabilities	35	-
Actuarial gain	76	-

The cumulative net actuarial gains recognised in other comprehensive income since 28 August 2009 amounted to £76 million.

	2009	2008
	£m	£m
Fair value of scheme assets	1,126	-
Present value of defined benefit obligation	(1,130)	-
Deficit	(4)	-

The actual return on the scheme assets comprises the following:

	2009	2008
	£m	£m
Expected return on scheme assets	17	-
Actuarial gains on scheme assets	23	-
	40	-

The change in the present value of the defined benefit obligation is as follows:

	2009	2008
	£m	£m
At 1 January 2009 (2 January 2008)	-	-
On acquisition of the Pearl businesses	1,176	-

Current service cost	2	-
Interest cost	21	-
Actuarial gains	(53)	-
Benefits paid	(16)	-
At 31 December	1,130	-

The defined benefit obligation arises from plans that are wholly or partly funded.

The change in the fair value of the scheme assets is as follows:

	2009	2008
	£m	£m
At 1 January 2009 (2 January 2008)	-	-
On acquisition of the Pearl businesses	1,096	-
Expected return on scheme assets	17	-
Actuarial gain on scheme assets	23	-
Contributions by the employer	6	-
Benefits paid	(16)	-
At 31 December	1,126	-

The distribution of the scheme assets at the end of the year was as follows:

	2009	2008
	£m	£m
Bonds	995	-
Properties	110	-
Cash and other	21	-
	1,126	-

Contributions totalling £15 million are expected to be paid into the scheme in 2010.

Table of historical information from 2009

	2009

	£m
Fair value of scheme assets	1,126
Defined benefit obligation	(1,130)
Deficit	(4)
Experience gains on scheme assets	23
Experience gains on scheme liabilities	18

33. Intangible assets

	Goodwill	Acquired in-force business	Customer relation-ships	Present value of future profits	Total
	£m	£m	£m	£m	£m
Cost or valuation					
At 2 January 2008 and 1 January 2009	-	-	-	-	-
On acquisition of the Pearl businesses	77	2,213	445	31	2,766
Revaluation	-	-	-	4	4
At 31 December 2009	77	2,213	445	35	2,770
Amortisation					
At 2 January 2008 and 1 January 2009	-	-	-	-	-
Amortisation charge for the year	-	50	7	-	57
At 31 December 2009	-	50	7	-	57
Carrying amount					
At 31 December 2009	77	2,163	438	35	2,713
Amount recoverable after 12 months	77	1,992	420	35	2,524

Goodwill

Goodwill of £77 million was created upon the acquisition of the Pearl businesses and is not amortised. The carrying value of goodwill has been tested for impairment at the period end. No impairment has resulted as the value in use of this intangible continues to exceed its carrying value. Value in use has been determined as the present value of certain future cash flows associated with the Ignis Asset Management business and the management services business of the Phoenix Life segment. The cash flows used in this calculation are consistent with those adopted by management in the Group's operating plan and for the period 2014 and beyond, reflect the anticipated run-off of the Phoenix Life insurance business. Future cash flows have been valued using a discount rate of 10.0%.

The carrying amount of goodwill allocated to the Phoenix Life segment is £39 million and to the Ignis Asset Management segment is £38 million.

Acquired in-force business

Acquired in-force business of £2,213 million was recognised upon the acquisition of the Pearl businesses and represents the difference between the fair value of the contractual rights acquired and obligations assumed under insurance and investment contracts with and without DPF and the liability measured in accordance with the Groups accounting policies for such contracts.

The acquired in-force business is allocated to the Phoenix Life segment.

Customer relationships

The customer relationships intangible includes an intangible representing vesting pension premiums which captures the new business arising from policies in-force at the acquisition date, specifically top-ups made to existing policies and annuities vested from matured pension policies. The total value of this customer relationship intangible at acquisition was £297 million and has been allocated to the Phoenix Life segment. This intangible is being amortised over a 20 year period.

The second part of the customer relationships intangible relates to the investment management contracts ("IMCs") held within Ignis Asset Management. These are further split into IMCs held with open ended funds and institutional mandates. The open ended IMCs had a value at acquisition of £130 million and an indefinite useful economic life ("UEL"). The reason for the indefinite UEL is that funds are open ended and indefinite in nature. An impairment review has been completed for these intangibles at the period end with an indefinite life and no impairment has arisen. Under this impairment review, value in use has been determined as the present value of future cash flows associated with the open-ended IMCs. The cash flows used in this calculation are consistent with those adopted by management in the Group's operating plan with a declining growth rate assumed for the extended forecast period beyond the period of this plan and a terminal value applied at the year where growth stabilises to 2% per annum. Future cash flows have been valued using a discount rate of 11.4%. The institutional mandate IMCs had a value at acquisition of £18 million and a UEL of between 5 and 7 years. These investment management contract customer relationships intangibles have been allocated to the Ignis Asset Management segment.

The amortisation in relation to these customer relationship intangibles is presented separately on the consolidated income statement.

PVFP on non participating business in the with profit fund

The value of the PVFP is determined in accordance with the FSA's realistic capital regime and is allocated in full to the Phoenix Life segment. The principal assumptions used to calculate the PVFP are the same as those used in calculating the insurance contract liabilities given in note 42.5.1.

During the year £4 million of PVFP was credited directly to the consolidated income statement.

34. Property, plant and equipment

	£m
Cost or valuation	
At 2 January 2008 and 1 January 2009	-
On acquisition of the Pearl businesses	35
Additions	1
At 31 December 2009	36
Depreciation	
At 2 January 2008 and 1 January 2009	-
Charge for the year	(2)
At 31 December 2009	(2)
Carrying amount	
At 31 December 2009	34

The useful lives of plant and equipment have been taken as follows: motor vehicles 3-4 years, computer equipment 3-4 years, furniture and office equipment 5-10 years.

The valuation of land and buildings is carried out at least every three years as at 31 December by external surveyors in accordance with the Royal Institution of Chartered Surveyors' requirements under an open market valuation basis. The latest valuation was undertaken on 31 December 2009.

35. Investment property

£m

	£m
At 2 January 2008 and 1 January 2009	-
On acquisition of the Pearl businesses	1,807
Additions	189
Improvements	5
Disposals	(245)
Gains on adjustments to fair value	159
At 31 December 2009	1,915

Investment property is stated at fair value and is independently valued in accordance with the Royal Institute of Chartered Surveyors' guidelines on the basis of the open market value of such properties.

Investment properties include £252 million property reversions arising from sales of the NPI Extra Income Plan. The reversionary interest is valued as the NPI and NPLL proportion of the current market value, projected for the lifetime of the policyholder at the assumed future increase in house prices, then discounted back by the valuation rate of interest.

Direct operating expenses (included within administrative expenses) in respect of investment properties that generated rental income during the year amounted to £8 million. The direct operating expenses arising from investment property that did not generate rental income during the year amounted to £3 million.

36. Financial assets and financial instrument fair value hierarchy

	2009 £m	2008 £m
Loans and receivables at amortised cost	1,081	-
Financial assets at fair value through profit or loss		
Held for trading – derivatives	3,540	-
Designated upon initial recognition		
Equities	13,151	-
Fixed and variable rate income securities	37,658	-
Collective investment schemes	6,094	-
	61,524	-
Amount recoverable after 12 months	39,822	-

The fair value of loans and receivables at amortised cost amounted to £1,074 million (2008: £nil).

Determination of fair value and fair value hierarchy of financial instruments

Level 1 financial instruments. The fair value of financial instruments traded in active markets (such as publicly traded securities and derivatives) is based on quoted market prices at the period end. The quoted market price used for financial assets is the current bid price on the trade date. If the bid price is unavailable a 'last traded' approach is adopted. For units in unit trusts and shares in open ended investment companies, fair value is by reference to published bid values.

Level 2 financial instruments. The fair values of investments that are not traded in an active market are determined using valuation techniques with observable market inputs. The fair value of shares and other variable yield securities and of derivative financial instruments, are estimated using pricing models, discounted cash flow techniques or broker quotes. Where pricing models are used, inputs are based on market related data at the period end. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market related rate for a similar instrument.

Level 3 financial instruments. The Group's financial assets determined by valuation techniques using non observable inputs are based on a combination of independent third party evidence and internally developed models. Third party evidence in the form of net asset valuation statements, are used in the valuation of the majority of indirect property, private equity and hedge funds. Broker quotes are received for certain bonds where the market is considered to be inactive. Internally developed models have been used in the valuation of a small number of investment vehicles which due to their nature and complexity have no external market. Inputs into the internally developed models are based on market observable data where available.

Fair value hierarchy of financial instruments measured at fair value

At 31 December 2009	Level 1	Level 2	Level 3	Total fair value
	£m	£m	£m	£m
Financial assets at fair value				
Derivatives	1,312	2,228	-	3,540
Financial assets designated at fair value through profit or loss upon initial recognition				
Equities	11,012	645	1,494	13,151
Fixed and variable rate income securities	33,672	3,167	819	37,658
Collective investment schemes	5,859	-	235	6,094
	50,543	3,812	2,548	56,903

Total financial assets at fair value	51,855	6,040	2,548	60,443

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial liabilities at fair value				
Derivatives	1,297	1,545	-	2,842
Financial liabilities designated at fair value through profit or loss upon initial recognition				
Investment contract liabilities	-	8,570	-	8,570
Borrowings	-	258	-	258
Net asset value attributable to unit holders	792	-	154	946
	792	8,828	154	9,774
Total financial liabilities at fair value	2,089	10,373	154	12,616

Level 3 financial instrument sensitivities

Included in Level 3 investments are two property investment structures with a value of £106m and £110m respectively.

The first of these investments has been independently valued using a multi scenario discounted cash flow model. Under the optimistic scenario, the fair value of the investment would increase by £18m and in the worst case scenario the fair value would decrease by £8m.

The second investment has been valued by taking the fair value of the property within the structure, which has been independently valued, less the fair value of the debt within the structure. The valuation is sensitive to movements in yields on the underlying property portfolio. An increase in yields of 25bps would reduce the value of the investment by £19m and a reduction in yields of 25bps would increase the value by £21m.

Level 3 investments in indirect property, private equity and hedge funds are valued using net asset statements provided by independent third parties and therefore no sensitivity analysis has been prepared.

Debt securities categorised as Level 3 investments are valued using broker quotes. Although such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternative assumptions would not change the fair value significantly.

Significant transfers of financial instruments between level 1 and level 2

At 31 December 2009	From level 1 to level 2	From level 2 to level 1
	£m	£m
Financial assets at fair value		
Derivatives	-	-
Financial assets designated at fair value through profit or loss upon initial recognition		
Equities	-	-
Fixed and variable rate income securities	226	334
Collective investment schemes	-	-
	226	334
Financial liabilities at fair value		
Derivatives	9	-
Financial liabilities designated at fair value through profit or loss upon initial recognition		
Investment contract liabilities	-	-
Borrowings	-	-
Net asset value attributable to unit holders	-	-
	9	-

2009 saw an improvement in the liquidity of the fixed and variable rate securities market which has resulted in a number of securities moving from level 2 into level 1. There were however, a number of securities that moved from level 1 to 2 as a result of a downgrading in their credit rating. These securities were mainly in the financial sector with issuers such as banks and insurance companies.

Movement in level 3 financial instruments measured at fair value

	At 1 Jan 2009	Arising on acquisition of the Pearl businesses	Total gains/ (losses) in income statement	Purchases and sales	Transfers from level 1 and level 2	At 31 Dec 2009	Unrealised gains/ (losses) on assets held at end of year
	£m	£m	£m	£m	£m	£m	£m
Financial assets designated at fair value through profit or loss upon initial recognition							
Equities	-	1,513	2	(25)	4	1,494	29
Fixed and variable rate income securities	-	839	(18)	80	(82)	819	(18)
Collective investment schemes	-	259	40	(64)	-	235	37
	-	2,611	24	(9)	(78)	2,548	48

	At 1 Jan 2009	Arising on acquisition of the Pearl businesses	Total gains in income statement	Purchases and sales	Transfers from level 1 and level 2	At 31 Dec 2009	Unrealised gains on liabilities held at end of year
	£m	£m	£m	£m	£m	£m	£m
Financial liabilities designated at fair value through profit or loss upon initial recognition							
Net asset value attributable to unit holders	-	170	8	(24)	-	154	29

Gains and losses on Level 3 financial instruments are included in net investment income in the consolidated income statement. There were no gains or losses recognised in other comprehensive income.

37. Stock lending

The Group lends listed financial assets held in its investment portfolio to other institutions. The Group conducts its stock lending programme only with well-established, reputable institutions in accordance with established market conventions.

The financial assets do not qualify for derecognition as the Group retains all the risks and rewards of the transferred assets except for the voting rights. The carrying value of listed financial assets lent at 31 December 2009 that have not been derecognised amounted to £8,612 million (2008: £nil).

It is the Group's practice to obtain collateral in stock lending transactions, usually in the form of cash or marketable securities. Certain cash collateral is available to the Group for investment purposes and is therefore recognised as a financial asset and a financial liability. The amount recognised as a financial asset and a financial liability at 31 December 2009 is £2,780 million (2008: £nil) and £3,007 million (2008: £nil) respectively. Other collateral is held on behalf of the Group and is not recognised in the statement of consolidated financial position as the Group is not permitted to sell or re-pledge the collateral in the absence of default.

The reinvested assets are primarily AAA listed securities and cash and the Group also has other readily realisable financial assets which are available to settle the collateral liabilities if required.

38. Other receivables

	2009	2008
	£m	£m
Unsettled trades	550	-
Other debtors	231	-
	781	-
Amount recoverable after 12 months	-	-

39. Cash and cash equivalents

	2009	2008
	£m	£m
Bank and cash balances	2,223	2
Short term deposits (including demand and time deposits)	3,858	-
	6,081	2

All deposits are subject to fixed interest rates. The carrying amounts approximate to fair value at the period end. Cash and cash equivalents in long term business operations and collective investment schemes of £5,551 million (2008: £nil) are primarily held for the benefit of policyholders and so are generally not available for use by the owners.

40. Cash flows

40.1 Cash flows from operating activities

	2009	Restated Period ended 31 Dec 2008
	£m	£m
Profit for the year before tax	91	31
Non-cash movements in profit for the year before tax		
Fair (gains)/losses on:		
Investment property	(159)	-
Financial assets	354	-
Unrealised (losses)/gains on:		
Financial liabilities	-	(17)
Borrowings	32	-
Depreciation of property, plant and equipment	2	-
Amortisation of intangible assets	57	-
Change in present value of future profit	(4)	-
Change in unallocated surplus	175	-
Change in deposits received from reinsurers	(25)	-
Interest income on trust account	(2)	(16)
Share-based payment charge	5	2
Interest expense on borrowings	87	-
Net expected return on pension assets	9	-
Foreign currency exchange gains	(1)	-
Decrease in investment assets	487	-
Increase in reinsurance assets	(160)	-
Decrease in insurance contract and investment contract liabilities	(951)	-

Net increase in working capital	(354)	-
Cash absorbed by operations	(357)	-

40.2 Cash flows on acquisition of the Pearl businesses

	2009	Period ended 31 Dec 2008
	£m	£m
Consideration settled in cash	-	-
Acquisition expenses	9	-
	9	
Cash and cash equivalents of the Pearl businesses	(6,155)	-
	(6,146)	-

40.3 Trust account

The trust account was held at Goldman Sachs, International, London branch and consisted of the net proceeds of the IPO, the proceeds of the sale of the Founders' units sold to the Founders prior to the consummation of the IPO, the proceeds of the sale of the Sponsors' warrants and £9 million of the underwriting fee that the underwriters had agreed to defer until the consummation of a business combination. Release of this amount was not at the discretion of the Company. The amounts held in the trust account were only to be released to the Company upon the consummation of a business combination, as set forth in the offering circular dated 25 January 2008 and the supplement thereto dated 5 February 2008. The trust account was under supervision of the trustee under the Trust Agreement. Following the acquisition of the Pearl businesses, £45 million was returned from the Trust Account to subscribers for IPO shares who did not vote in favour of the business combination comprising £41 million share premium and £4 million accrued interest. The remainder of the Trust Account was transferred to the Company.

41. Capital statement

Capital Management Framework

The Group's Capital Management Framework is designed to achieve the following objectives:

Provide appropriate security for policyholders and meet all regulatory capital requirements whilst not retaining unnecessary excess capital;

Ensure sufficient liquidity to meet obligations to policyholders and other creditors; and

Meet the dividend expectations of owners as set by the Group's dividend policy.

The framework comprises a suite of capital management policies that govern the allocation of capital throughout the Group to achieve the framework objectives under a range of stress conditions. The policy suite is defined with reference to policyholder security, creditor obligations, owner dividend policy and regulatory capital requirements.

The capital policy of each Group holding company is set by the Board of Phoenix Group Holdings and monitored each month at both the executive and Board level. The policies ensure sufficient liquidity to meet creditor and dividend obligations through the combination of cash buffers and cash flows from the Group's operating companies. Volatility in the latter is monitored at the executive and Board level through stress and scenario testing. Where cash flow volatility is judged to be in excess of the Board's risk appetite, de-risking activities are undertaken.

The capital policy of each life company is set by each life company Board and monitored on a daily basis. These policies ensure there is sufficient capital within each life company to meet regulatory capital requirements under a range of stress conditions. The capital policy of each life company varies according to the risk profile and financial strength of the company.

Regulatory capital requirements

Each UK life company must retain sufficient capital at all times to meet the regulatory capital requirements mandated by the FSA. In addition to EU-directive-based "Pillar 1" and group capital requirements, the FSA has also stipulated a "Pillar 2" of risk-based capital requirements that have been implemented in the UK. A life company's actual capital requirement is based on whichever of the Pillar 1 or Pillar 2 requirement turns out to be more onerous for the company. Each life company generally holds an amount of capital that is greater than the minimum required amount to allow for adverse events in the future that may use capital and might otherwise cause the company to fail the minimum level of regulatory capital test.

Pillar 1

With the exception of with profit businesses, the regulatory capital requirement under Pillar 1 is the total amount held in respect of investment, expense and insurance risks (the "long term insurance capital requirement" ("LTICR")) and any additional amounts required to cover the more onerous of two specified stress tests (the "resilience capital requirement" ("RCR")). The regulatory capital requirement is then deducted from the available capital resources to give the excess capital on a regulatory basis.

A further test is required under Pillar 1 in respect of with profit funds which may result in an additional capital requirement referred to as the "with profit insurance capital component" ("WPICC").

Pillar 2

The Pillar 2 capital requirements are based on a self-assessment methodology, the so called Individual Capital Assessment ("ICA"). This methodology determines the capital requirement to ensure that the life company's realistic

liabilities can be met in one year's time with a 99.5% confidence level, or in other words to be able to withstand a one in 200 year event. The FSA reviews each life company's ICA and may impose additional capital requirements if necessary in the form of Individual Capital Guidance ("ICG").

Insurance Groups' Directive ("IGD")

FSA regulated insurance groups (including their holding companies) are also required to provide an assessment of capital adequacy on a group-wide basis to enable the FSA to assess both the level of insurance and financial risk within the group and the capital resources available to cover that risk. The assessment is known as the IGD and is the Group's primary capital and solvency measure.

The Group's IGD assessment is made at the highest EEA level insurance Group holding company, which is PLHL. PLHL is a subsidiary of the Company.

Regulatory capital position statement

The purpose of the capital position statement is to set out the capital resources of the Phoenix Life segment of the Group and to provide an analysis of the disposition and constraints over the availability of capital to meet risks and regulatory requirements. The capital position statement also provides a reconciliation of owners' funds to regulatory capital and an analysis of the regulatory capital between the Group's with profit funds, non participating business, life business owners' funds and its other activities.

The Group acquired its life assurance business upon the purchase of the Pearl businesses, information on which is given in note 3. The Group's material with profit funds at 31 December 2009 are shown separately in the capital position statement and the less material with profit funds are aggregated and shown as "Other". The with profit funds shown separately are the Phoenix with profit fund ("PLL PWP"), the Britannic with profit fund ("PLL BWP") , the SMA with profit fund ("SMA WPF"), the Scottish Provident with profit fund ("SPL WPF") and the Pearl with profit fund ("Pearl WPF"). The with profit funds of London Life Limited and Phoenix & London Assurance Limited ("PALAL") are aggregated within the "Other" column.

The contributions made by Phoenix Pensions Limited ("PPL") and NPLL to the Group's capital resources are included in the column headed "Phoenix Life owners' funds", since they are owned by the Group's life business owners' funds. An allocation of capital and loans from the Phoenix Life owners' funds to the Group's non participating business is made in respect of PPL and to the Pearl WPF in respect of NPLL representing capital resources to cover the capital resources requirement of the PPL and NPLL long term funds respectively. The non participating business and other activities are shown in aggregate in the capital position statement. Virtually all activities of the Group relate to UK business.

The Group has a number of internal loan arrangements in place, which allow the Group to provide capital support to other areas of the business. In addition to these internal loan arrangements, the Group has in place a number of internal reinsurance contracts which are structured to manage the capital position between certain life funds.

The available capital resources in each part of the business are generally subject to restrictions as to their availability to meet requirements that may arise elsewhere in the Group. The principal restrictions are:

With profits funds – any available surplus held in each fund can only be used to meet the requirements of the fund itself or be distributed to policyholders and owners. In 90:10 with profit funds, policyholders are entitled to at least 90% of the distributed profits while owners receive the balance. In 100:0 with profit funds, policyholders are entitled to 100% of the distributed profits. Any distribution to the owners would be subject to a tax charge which, for some funds, would be deducted from the amount received by owners.

Non participating funds – any available surplus held in these funds is attributable to owners. Capital within the non participating funds may be made available to meet capital requirements elsewhere in the Group subject to meeting regulatory and legal requirements, and after consideration of the internal capital requirements of the relevant fund and company. Any transfer of surplus may give rise to a tax charge subject to availability of tax relief elsewhere in the Group.

Pearl Pacific fund – the owner attributed assets, known as the Pacific fund, are held within the surplus of the 0:100 fund of Pearl and are attributable to owners. The assets can only be released when, in the opinion of the Actuarial Function Holder and the Board, to do so would not adversely affect either the reasonable expectations of with profit policyholders or the security of non profit policyholders.

The capital statement and movement analysis that follows presents information about the capital resources for the Group's UK life businesses.

2009

	With profit (see below)	Non partici-pating	Phoenix Life owners' funds	Total Phoenix Life business	Other activities and consoli-dation adjust-ments (note 4)	Group total
	£m	£m	£m	£m	£m	£m
Owners' funds held outside long term fund	-	-	2,475	2,475	(1,955)	520
Owners' funds held in long term fund	-	902	(10)	892	-	892
Total owners' funds at 31 December 2009	-	902	2,465	3,367	(1,955)	1,412
Adjustments onto a regulatory basis:						
Unallocated surplus	710	-	11	721		
Adjustments to assets (note 1)	(64)	(298)	(810)	(1,172)		

Adjustments to liabilities (note 2)	3,237	(87)	40	3,190
Valuation difference between IFRS basis and regulatory basis	-	91	(8)	83
Other qualifying capital:				
Subordinated debt (note 3)	83	-	637	720
Contingent loans	382	(228)	(88)	66
Allocation of group capital	122	206	(328)	-
Total available capital resources at 31 December 2009	4,470	586	1,919	6,975

With profits

2009

	Pearl WPF	PLL PWP	PLL BWP	SMA WPF	SPL WPF	Other	Total
	£m	£m	£m	£m	£m	£m	£m
Owners' funds held outside long term fund	-	-	-	-	-	-	-
Owners' funds held in long term fund	-	-	-	-	-	-	-
Total owners' funds at 31 December 2009	-	-	-	-	-	-	-

Adjustments onto a regulatory basis:

Note 1: Regulatory adjustments to assets reflect adjustments to derecognise inadmissible assets such as intangibles and deferred tax assets as well as those adjustments that are necessary where asset and counterparty exposures exceed the prescribed regulatory limits.

Note 2: Regulatory adjustments to liabilities reflect the different valuation basis for insurance liabilities on a regulatory basis.

Note 3: Of the £720 million subordinated debt attributed to the Phoenix Life segment of the Group £520 million is internal to the Group, comprising £250 million provided to Pearl and £270 million provided to PALAL. The remaining £200 million is external subordinated debt issued by PLL.

Note 4: "Other activities and consolidation adjustments" represent the contribution to consolidated owners' funds arising outside of the Phoenix Life business. This includes the owners' funds of Ignis Asset Management and the holding companies of the Group but primarily consists of the consolidation adjustments to eliminate the cost of the Group's investment in the Phoenix Life business.

Unallocated surplus	209	128	254	29	55	35	710
Adjustments to assets	(34)	(3)	(11)	-	1	(17)	(64)
Adjustments to liabilities	604	802	560	265	587	419	3,237
Other qualifying capital:							
Subordinated debt	83	-	-	-	-	-	83
Contingent loans	-	-	-	-	-	382	382
Allocation of group capital	122	-	-	-	-	-	122
Total available capital resources at 31 December 2009	984	927	803	294	643	819	4,470

An analysis of the movement in available capital resources for the period 1 January 2009 to 31 December 2009 is shown below:

	With profits								
	Pearl WPF	PLL PWP	PLL BWP	SMA WPF	SPL WPF	Other	Non partici-pating	Phoenix Life owners' funds	Total Phoenix Life business
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Total available capital resources at 1 January 2009	-	-	-	-	-	-	-	-	-
On acquisition of the Pearl businesses	850	738	634	357	619	427	659	1,902	6,186
Regular surplus	111	27	17	48	(2)	20	101	-	322
Investment return	60	224	230	82	203	248	(17)	100	1,130
Cost of bonus	(27)	(47)	(33)	(16)	(26)	(13)	-	15	(147)
Changes in methodology and assumptions:									
Longevity	1	26	1	18	15	32	(4)	-	89
Expenses	-	(6)	-	(9)	14	(18)	13	-	(6)
Other	1	(13)	(2)	-	-	(7)	21	-	-
Management actions:									
Investment strategy	-	-	-	-	-	276	-	-	276
Proceeds from issue of subordinated debt	-	-	-	-	-	-	-	250	250
Dividends paid by Phoenix Life	-	-	-	-	-	-	-	(406)	(406)

New business and other factors:

Intragroup capital movement	-	-	-	-	-	(6)	(241)	216	(31)
Valuation rate of interest	-	(72)	(7)	(126)	(160)	(142)	(2)	-	(509)
Adjustment for internal loans in excess of counterparty limits	-	-	-	-	-	-	-	(37)	(37)
Other	(12)	50	(37)	(60)	(20)	2	56	(121)	(142)
Total available capital resources at 31 December 2009	984	927	803	294	643	819	586	1,919	6,975

Changes in methodology and assumptions

Changes to capital resources arising from changes in methodology and assumptions occur in the normal course of the assumption setting process and reflect changes in available data inputs.

Management actions

The management actions that have had the most significant impact on available capital resources of the Phoenix Life segment of the Group during the period to 31 December 2009 generally comprise financing activities, both to strengthen the Phoenix Life segment in the form of subordinated debt, and to pay dividends to finance corporate activities. In respect of investment strategy, the improvement in capital resources has arisen from an initiative to restructure the with profit fund of PALAL to improve the outlook for policyholders of that fund.

42. Risk management

The Group is exposed to a number of risks in its business including those arising from underlying assets and liabilities. The Group's overall approach to risk management is described in the Performance section of the annual report and accounts.

42.1 Risk and capital management objectives

The risk management objectives and policies of the Group are based on the requirement to protect the Group's regulatory capital position, thereby safeguarding policyholders' guaranteed benefits whilst also ensuring the Group can meet various cash flow requirements. Subject to this, the Group seeks to use available capital to achieve increased investment returns, balancing risk and reward, to generate additional value for policyholders and shareholders.

In pursuing these objectives, the Group deploys financial assets and incurs financial liabilities. Financial assets principally comprise investments in equity securities, fixed and variable rate income securities, collective investment schemes, property, derivatives, reinsurance, trade and other receivables, and banking deposits. Financial liabilities comprise investment contracts, borrowings for financing purposes, derivative liabilities and other payables.

42.2 Asset liability management ("ALM") framework

The use of financial instruments naturally exposes the Group to the risks associated with them, chiefly, market risk, credit risk and liquidity risk.

Responsibility for agreeing the financial risk profile rests with the Board of each life company, as advised by investment managers, internal committees and the actuarial function. In setting the risk profile, the Board of each life company will receive advice from the appointed investment managers and the relevant actuary as to the potential implications of that risk profile with regard to the probability of both realistic insolvency and of failing to meet the regulatory minimum capital requirement. The actuary will also advise the extent to which the investment risk taken is consistent with the Group's commitment to treat customers fairly.

Derivatives are used in a number of the Group's funds, within policy guidelines agreed by the Board of each life company and overseen by Investment Committees of the Boards of each life company supported by management oversight committees. Derivatives are primarily used for efficient portfolio management or for risk hedging purposes.

More detail on the Group's exposure to financial risk is provided in note 42.3 below.

The Group is also exposed to insurance risk arising from its Phoenix Life segment. Life assurance risk in the Group arises through its exposure to mortality, longevity and to variances between assumed and actual experience in factors such as persistency levels and management and administrative expenses. More details on the Group's exposure to insurance risk is provided in note 42.5 below.

The Group's overall exposure to investment risk is monitored by appropriate committees, which agree policies for managing each type of risk on an ongoing basis, essentially within the ALM framework that has been developed to achieve investment returns in excess of amounts due in respect of insurance contracts. The effectiveness of the Group's ALM relies on close matching of assets and liabilities arising from insurance and investment contracts, taking into account the types of benefits payable to policyholders under each type of contract. Separate portfolios of assets are maintained for with profit business, which includes all of the Group's participating business, non linked non participating business and unit linked business.

42.3 Financial risk analysis

Transactions in financial instruments may result in the Group assuming financial risks. This includes credit risk, market risk and liquidity risk. Each of these are described below, together with a summary of how the Group manages them.

42.3.1 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. These obligations can relate to both on and off balance sheet assets and liabilities.

There are two principal sources of credit risk for the Group:

Credit risk which results from direct investment activities, including investments in fixed interest securities, equities, derivatives, collective investment vehicles, hedge funds and the placing of cash deposits; and

Credit risk which results indirectly from activities undertaken in the normal course of business. Such activities include premium payments, outsourcing contracts, reinsurance, exposure from material suppliers and the lending of securities.

The amount disclosed in the statement of consolidated financial position in respect of all financial assets, together with rights secured under off-balance sheet collateral arrangements, and excluding those that back unit linked liabilities, represents the Group's maximum exposure to credit risk.

Credit risk is managed by the monitoring of aggregate Group exposures to individual counterparties and by appropriate credit risk diversification. The Group manages the level of credit risk it accepts through divisional credit risk tolerances. In certain cases, protection against exposure to particular credit risk types may be

achieved through use of derivatives. The credit risk borne by the shareholder on with profit policies is usually minimal unless the insurance fund is relying on shareholder support.

Quality of credit assets

An indication of the Group's exposure to credit risk is the quality of the investments and counterparties with which it transacts. The following table provides information regarding the aggregate credit exposure with external credit ratings:

2009

	AAA	AA	A	BBB	BB	B and below	Non rated	Unit linked	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Loans and receivables	-	-	-	-	-	1,027	46	8	1,081
Derivatives	-	73	3,368	-	-	-	50	49	3,540
Fixed and variable rate income securities	23,690	3,873	5,343	2,474	514	400	843	521	37,658
Reinsurers' share of insurance contract liabilities	13	595	2,124	20	-	-	98	10	2,860
Cash and cash equivalents	2,141	2,442	1,003	6	-	-	92	397	6,081

2008

	AAA	AA	A	BBB	BB	B and below	Non rated	Unit linked	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and cash equivalents	2	-	-	-	-	-	-	-	2
Amounts in trust	-	-	591	-	-	-	-	-	591

Credit ratings have not been disclosed in the above tables for equities. Whilst the Group is exposed to the impact of credit default on its equity holdings, this risk is not considered significant due to the spread of holdings. Non-equity based derivatives are included in the credit risk table above.

Credit ratings have also not been disclosed in the above tables for holdings in collective investment schemes. The risk of loss to the Group due to credit default on its holdings in collective investment schemes is considered low due to the tradeable nature of these investments.

It is also the Group's policy to maintain accurate and consistent internal risk ratings across its asset portfolio. This enables management to focus on the applicable risks and to compare credit exposures across all lines of business, geographical regions and products. The rating system is supported by a variety of financial analytics combined with market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories of assets and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly.

A further indicator of the quality of the Group's financial assets is the extent to which they are neither past due nor impaired. The following table gives information regarding the ageing of financial assets that are past due but not impaired and the carrying value of financial assets that have been impaired.

2009

	Neither past due nor impaired	Less than 30 days	30-90 days	Greater than 90 days	Impaired	Unit linked	Carrying value
	£m	£m	£m	£m	£m	£m	£m
Loans and receivables	1,073	-	-	-	-	8	1,081
Derivatives	3,491	-	-	-	-	49	3,540
Fixed and variable rate income securities	37,137	-	-	-	-	521	37,658
Reinsurers' share of insurance contract liabilities	2,850	-	-	-	-	10	2,860
Reinsurance receivables	264	-	-	-	-	-	264
Prepayments and accrued income	518	84	-	1	-	19	622
Other receivables	765	6	1	6	3	-	781
Cash and cash equivalents	5,684	-	-	-	-	397	6,081

2008

	Neither past due nor impaired	Less than 30 days	30-90 days	Greater than 90 days	Impaired	Unit linked	Carrying value
	£m	£m	£m	£m	£m	£m	£m
Cash and cash equivalents	2	-	-	-	-	-	2
Amounts in trust	591	-	-	-	-	-	591

Assets backing unit linked business have not been analysed in these tables as the credit risk on such financial assets is borne by the policyholders. However, these assets have been included as a separate column in these tables to reconcile the information to the primary financial statements. Shareholder credit exposure on unit linked assets is limited to the level of asset manager fee which is dependent on the underlying assets. In certain circumstances the shareholder funds may be used to re-establish unit linked assets in line with regulatory and policyholder expectations.

Concentration of credit risk

Concentration of credit risk might exist where the Group has significant exposure to an individual counterparty or a group of counterparties with similar economic characteristics that would cause their ability to meet

contractual obligations to be similarly affected by changes in economic and other conditions. The Group has most of its counterparty risk within its life business and this is monitored by the counterparty limits contained within the investment guidelines and investment management agreements, overlaid by regulatory requirements.

The Group is also exposed to concentration risk with outsourced service providers. This is due to the nature of the outsourced services market. The Group operates a policy to manage outsourcer service counterparty exposures and the impact from default is reviewed regularly by executive committees and measured though the ICA stress and scenario testing.

Collateral

The credit risk of the Group is mitigated, in certain circumstances, by entering into collateral agreements. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and the valuation parameters. Collateral is mainly obtained for securities lending, certain reinsurance arrangements and to provide security against the maturity proceeds of derivative financial instruments. Management monitors the market value of the collateral received, requests additional collateral when needed and performs an impairment valuation when impairment indicators exist and the asset is not fully secured.

42.3.2 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises interest risk, currency risk and other price risk.

The Group is mainly exposed to market risk as a result of:

the mismatch between liability profiles and the related asset investment portfolios;

the investment of surplus assets including shareholder reserves yet to be distributed, surplus assets within the with profit funds and assets held to meet regulatory capital and solvency requirements; and

the income flow of management charges from the invested assets of the business.

The Group manages the levels of market risk that it accepts through an approach to investment management that determines:

the constituents of market risk for the Group;

the basis used to fair value financial assets and liabilities;

the asset allocation and portfolio limit structure;

diversification from benchmarks by type of instrument and geographical area;

the net exposure limits by each counterparty or group of counterparties, geographical and industry segments;

control over hedging activities;

reporting of market risk exposures and activities; and

monitoring of compliance with market risk policy and review of market risk policy for pertinence to the changing environment.

All operations comply with regulatory requirements relating to the taking of market risk.

Interest risk

Interest risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates due to the effect such movements have on the value of interest-bearing assets and on the value of future guarantees provided under certain contracts of insurance.

Interest risk is managed by matching assets and liabilities where practicable and by entering into swap arrangements where appropriate. This is particularly the case for the non participating funds. For participating business, some element of investment mismatching is permitted where it is consistent with the principles of treating customers fairly. The with profit funds of the Group provide capital to allow such mismatching to be effected. In practice, the life companies of the Group maintain an appropriate mix of fixed and variable rate instruments according to the underlying insurance or investment contracts and will review this at regular intervals to ensure that overall exposure is kept within the risk profile agreed for each particular fund. This also requires the maturity profile of these assets to be managed in line with the liabilities to policyholders.

The sensitivity analysis for interest risk indicates how changes in the fair value or future cash flows of a financial instrument arising from changes in market interest rates at the reporting date result in a change in profit after tax and in equity. It takes into account the effect of such changes in market interest rates on all assets and liabilities that contribute to the Group's reported profit after tax and in equity.

With profits business and non profit business within the with profit funds are exposed to interest risk as guaranteed liabilities are valued relative to market interest rates and investments include fixed interest stocks and derivatives. For with profit business the profit or loss arising from mismatches between such assets and liabilities is largely offset by increased or reduced discretionary policyholder benefits. The contribution of these funds to the Group result is determined primarily by either the shareholders' share of the declared annual bonus or by the shareholders' interest in any change in value in the capital advanced to the Group's with profit funds.

In the non participating funds, policy liabilities are duration matched with primarily fixed interest securities, with the result that sensitivity to changes in interest rates is very low.

An increase of 1% in interest rates, with all other variables held constant, would result in decreases in the profit after tax in respect of a full financial year and in equity of £61 million (2008: £nil). A decrease of 1% in interest rates, with all other variables held constant, would result in an additional profit after tax in respect of a full financial year and an increase in equity of £89 million (2008: £nil).

Price risk

The Group's price risk exposure relates to financial assets and liabilities whose values will fluctuate as a result of changes in market prices other than from interest rate and currency fluctuations. This is due to factors specific to individual instruments, their issuers or factors affecting all instruments traded in the market. Accordingly, the Group limits its exposure to any one counterparty in its investment portfolios and to any one foreign market.

The portfolio of marketable equity securities and property investments which is carried in the statement of consolidated financial position at fair value has exposure to price risk. The Group's objective in holding these

assets is to earn higher long term returns by investing in a diverse portfolio of high quality equities and properties. Portfolio characteristics are analysed regularly and price risks are actively managed in line with investment mandates. The Group's holdings are diversified across industries, and concentrations in any one company or industry are limited.

Equity and property price risk is primarily borne in respect of assets held in with profit or unit linked funds. For unit linked funds this risk is borne by policyholders and asset movements directly impact unit prices and hence policy values. For with profit funds policyholders' future bonuses will be impacted by the investment returns achieved and hence the price risk. In addition some equity investments are held in respect of equity holders' funds. The Group as a whole is exposed to price risk fluctuations impacting the income flow of management charges from the invested assets of all funds.

Equity and property price risk is managed through the agreement and monitoring of financial risk profiles that are appropriate for each of the Group's life funds in respect of maintaining adequate regulatory capital and treating customers fairly. This is largely achieved through asset class diversification.

The impact of non-government fixed interest securities and, inter alia, the change in market credit spreads during the year are fully reflected in the values shown in these financial statements. Similarly, the value of derivatives that the Group holds takes into account fully the changes in swap spreads.

The sensitivity analysis for equity and property price risk illustrates how a change in the fair value of equities and properties affects the Group result. It takes into account the effect of such changes in equity and property prices on all assets and liabilities that contribute to the Group's reported profit after tax and in equity.

A 10% decrease in equity/property prices, with all other variables held constant, would result in a decrease in the profit after tax in respect of a full financial year and in equity of £17 million (2008: £nil).

A 10% increase in equity/property prices, with all other variables held constant, would result in an increase in the profit after tax in respect of a full financial year and in equity of £13 million (2008: £nil).

There is also an exposure to spread changes affecting the prices of corporate bonds and derivatives. This exposure applies to with profit funds, unit linked funds, non profit funds (where risks and rewards fall wholly to shareholders) and in shareholders' funds.

A 100 basis point widening of credit spreads, with all other variables held constant, would result in a decrease in the profit after tax in respect of a full financial year and in equity of £196 million (2008: £nil).

A 100 basis point narrowing of credit spreads, with all other variables held constant, would result in an increase in the profit after tax in respect of a full financial year and in equity of £216 million (2008: £nil).

Currency risk

The Group's principal transactions are carried out in sterling and therefore its exchange risk is limited principally to foreign operations.

The Group's foreign operations (taken to be those denominated in non-sterling) generally invest in assets in the same currency denomination as their liabilities, so foreign currency mismatch risk between assets and liabilities is largely mitigated. Consequently, the foreign currency risk from the foreign operations mainly arises when the assets and liabilities denominated in a foreign currency are translated into sterling.

The Group's financial assets are primarily denominated in the same currencies as its insurance and investment liabilities. Thus the main foreign exchange risk arises from recognised assets and liabilities

denominated in currencies other than those in which insurance and investment liabilities are expected to be settled and, indirectly, from the earnings of UK companies arising abroad.

Certain Phoenix Life with profit funds have an exposure to overseas assets which is not driven by liability considerations. The purpose of this exposure is to reduce overall risk whilst maximising returns by diversification. This exposure is limited and managed through investment mandates which are subject to the oversight of the Investment Committees of the Boards of each life company. Fluctuations in exchange rates from holdings in overseas assets are hedged against currency risks.

Sensitivity of profit after tax and in equity to fluctuations in currency exchange rates is not considered significant at 31 December 2009, since unhedged exposure to foreign currency was relatively low.

42.3.3 Liquidity risk

Liquidity risk is defined as the failure of the Group to maintain adequate levels of financial resources to enable it to meet its obligations as they fall due. The Group has exposure to liquidity risk as a result of servicing its external debt and equity investors, and from the operating requirements of its subsidiaries. The Group's subsidiaries have exposure to liquidity risk as a result of normal business activities, specifically the risk arising from an inability to meet short term cash flow requirements.

The Board of Phoenix Group Holdings has defined a number of governance objectives and principles and the liquidity risk frameworks of each subsidiary are designed to ensure that:

liquidity risk is managed in a manner consistent with the subsidiary companies Boards' strategic objectives, risk appetite and Principles and Practices of Financial Management ("PPFM");

cash flows are appropriately managed and the reputation of the Group is safeguarded; and

appropriate information on liquidity risk is available to those making decisions.

The Group's policy is to maintain sufficient liquid assets of suitable credit quality at all times and, where appropriate, to have access to borrowings so as to be able to meet all foreseeable current liabilities as they fall due in a cost-effective manner. Forecasts are prepared regularly to predict required liquidity levels over both the short and medium term allowing management to respond appropriately to changes in circumstances.

Some of the Group's commercial property investments are held through a unit trust managed by Ignis Asset Management. This unit trust has the power to restrict and/or suspend withdrawals, which would, in turn, affect liquidity. To date, the unit trust has continued to process both investments and realisations in a normal manner and has not imposed any restrictions or delays.

The following table provides a maturity analysis showing the remaining contractual maturities of the Group's undiscounted financial liabilities and associated interest. Liabilities under insurance contract contractual maturities are included based on the estimated timing of the amounts recognised in the statement of consolidated financial position in accordance with the requirements of IFRS 4:

2009

	1 year or less or on deman d	1-5 years	Greater than 5 years	No fixed term	Total
	£m	£m	£m	£m	£m
Liabilities under insurance contracts	10,141	14,539	23,748	1,863	50,291
Investment contracts	8,570	-	-	-	8,570
Borrowings	95	2,447	1,950	258	4,750
Deposits received from reinsurers	38	138	522	-	698
Derivatives	1,448	363	1,511	-	3,322
Net asset value attributable to unit holders	946	-	-	-	946
Obligations for repayment of collateral received	3,054	158	412	484	4,108
Reinsurance payables	17	-	-	-	17
Payables related to direct insurance contracts	693	66	-	-	759
Accruals and deferred income	174	3	-	-	177
Other payables	325	8	-	317	650

2008

	1 year or less or on deman d	1-5 years	Greater than 5 years	No fixed term	Total
	£m	£m	£m	£m	£m
Accruals and deferred income	9	-	-	-	9

Investment contract policyholders have the option to terminate or transfer their contracts at any time and to receive the surrender or transfer value of their policies. Although these liabilities are payable on demand, and are therefore included in the contractual maturity analysis as due within one year, the Group does not expect all these amounts to be paid out within one year of the reporting date.

A significant proportion of the Group's financial assets are held in gilts, cash, supranationals and highly rated securities which the Group considers sufficient to meet the liabilities as they fall due.

42.4 Unit linked contracts

For unit linked contracts the Group matches all the liabilities with assets in the portfolio on which the unit prices are based. There is therefore no interest, price, currency or credit risk for the Group on these contracts.

In extreme circumstances, the Group could be exposed to liquidity risk in its unit linked funds. This could occur where a high volume of surrenders coincides with a tightening of liquidity in a unit linked fund to the point where assets of that fund have to be sold to meet those withdrawals. Where the fund affected consists of property, it can take several months to complete a sale and this would impede the proper operation of the fund. In these situations, the Group considers its risk to be low since there are steps that can be taken first within the funds themselves both to ensure the fair treatment of all investors in those funds and to protect the Group's own risk exposure.

42.5 Insurance risk

Insurance risk refers to the risk that the frequency or severity of insured events may be worse than expected and includes expense risk. The Phoenix Life segment contracts include the following sources of insurance risk:

Mortality – Higher than expected number of death claims on assurance products and occurrence of one or more large claims;

Longevity - Faster than expected improvements in life expectancy on immediate and deferred annuity products;

Morbidity – Higher than expected number of serious illness claims or more sickness claims which last longer on income protection policies;

Expenses – Policies cost more to administer than expected;

Lapses – The numbers of policies terminating early is different to that expected in a way which increases expected claims costs or expenses or reduces future profits; and

Options – Unanticipated changes in policyholder option exercise rates giving rise to increased claims costs.

Objectives and policies for mitigating insurance risk

The Group uses several methods to assess and monitor insurance risk exposures both for individual types of risks insured and overall risks. These methods include internal risk measurement models, experience analyses, external data comparisons, sensitivity analyses, scenario analyses and stress testing.

The profitability of the run-off of the closed long term insurance businesses within the Group depends to a significant extent on the values of claims paid in the future relative to the assets accumulated to the date of claim. Typically, over the lifetime of a contract, premiums and investment returns exceed claim costs in the early years and it is necessary to set aside these amounts to meet future obligations. The amount of such future obligations is assessed on actuarial principles by reference to assumptions about the development of financial and insurance risks.

It is therefore necessary for the Boards of each life company to make decisions, based on actuarial advice, which ensure an appropriate accumulation of assets relative to liabilities. These decisions include investment policy, bonus policy and, where discretion exists, the level of payments on early termination.

Sensitivities

Insurance liabilities are sensitive to changes in risk variables, such as prevailing market interest rates, currency rates and equity prices, since these variations alter the value of the financial assets held to meet obligations arising from insurance contracts and changes in investment conditions also have an impact on the value of insurance liabilities themselves. Additionally, insurance liabilities are sensitive to the assumptions which have been applied in their calculation, such as mortality and lapse rates. Sometimes allowance must also be made for the effect on future assumptions of management or policyholder actions in certain economic scenarios. This could lead to changes in assumed asset mix or future bonus rates. The most significant non-economic sensitivities arise from mortality, longevity and lapse risk.

A decrease of 5% in assurance mortality, with all other variables held constant, would result in an increase in the profit after tax in respect of a full year and an increase in equity of £27 million (2008: £nil).

An increase of 5% in assurance mortality, with all other variables held constant, would result in a decrease in the profit after tax in respect of a full year and a decrease in equity of £27 million (2008: £nil).

A decrease of 5% in annuitant longevity, with all other variables held constant, would result in an increase in the profit after tax in respect of a full year and an increase in equity of £91 million (2008: £nil).

An increase of 5% in annuitant longevity, with all other variables held constant, would result in a decrease in the profit after tax in respect of a full year and a decrease in equity of £83 million (2008: £nil).

A decrease of 25% in lapse rates, with all other variables held constant, would result in a decrease in the profit after tax in respect of a full year and a decrease in equity of £50 million (2008: £nil).

An increase of 25% in lapse rates, with all other variables held constant, would result in an increase in the profit after tax in respect of a full year and an increase in equity of £41 million (2008: £nil).

42.5.1 Assumptions

Valuation of participating insurance and investment contracts

For participating business, which is with profit business (insurance and investment contracts), the insurance contract liability is calculated in accordance with the FSA's realistic capital regime, adjusted to exclude the shareholders' share of future bonuses and the associated tax liability as required by FRS 27 "Life Assurance". This is a market consistent valuation, which involves placing a value on liabilities similar to the market value of assets with similar cash flow patterns.

Valuation of non participating insurance contracts

The non participating insurance contract liabilities are determined using either a net premium or gross premium valuation method.

Process used to determine assumptions

For participating business in realistic basis companies the assumptions about future demographic trends are intended to be "best estimates". They are determined after considering the companies' recent experience and/or relevant industry data. Economic assumptions are market consistent.

For other business, demographic assumptions are derived by adding a prudent margin to best estimate assumptions. Economic assumptions are prudent estimates of the returns expected to be achieved on the assets backing the liabilities.

During the year a number of changes were made to assumptions to reflect changes in expected experience or to harmonise the approach across the enlarged Group. The impact of material changes during the year were as follows:

	Increase/ (decrease) in insurance liabilities 2009 £m	Increase/ (decrease) in insurance liabilities 2008 £m
Change in longevity assumptions	(73)	-
Change in persistency assumptions	94	-

Valuation interest rate

For realistic basis companies the liabilities are determined stochastically using an appropriate number of risk neutral scenarios produced by an economic scenario generator calibrated to market conditions and gilt yields as at the valuation date.

For funds not subject to realistic reporting, the method used to determine valuation interest rates generally follows the regulations set out in the Prudential Sourcebook for Insurers.

Assets are firstly hypothecated to classes of business being valued. The valuation interest rates for each block of business are based on the expected returns of the hypothecated assets. The yield is then adjusted to make allowance for credit risk, liquidity risk, reinvestment risk and investment management expenses.

Valuation interest rates (after tax for life policies) are typically in the following ranges:

	2009 %	2008 %
Life policies	2.14% - 3.82%	-
Pension policies	2.76% - 4.84%	-

Expense inflation

Expenses are assumed to increase at the rate of increase in the Retail Price Index ("RPI") plus fixed margins in accordance with the various management service agreements ("MSAs") the Group has in place with outsourced service providers. For with profit business the rate of RPI inflation is determined within each stochastic scenario. For other business it is based on the Bank of England inflation spot curve. For MSAs with contractual increases set by reference to national average earnings inflation, this is approximated as RPI inflation plus 1%. In instances in which inflation risk is not mitigated, a further margin for adverse deviations may then be added to the rate of expense inflation.

Mortality and longevity rates

Mortality rates are based on published tables, adjusted appropriately to take account of changes in the underlying population mortality since the table was published, company experience and forecast changes in future mortality. Where appropriate, a margin is added to assurance mortality rates to allow for adverse future deviations. Annuitant mortality rates are adjusted to make allowance for future improvements in pensioner longevity.

Lapse and surrender rates (persistency)

The assumed rates for surrender and voluntary premium discontinuance depend on the length of time a policy has been in force and the relevant company. Surrender or voluntary premium discontinuances are only assumed for realistic basis companies. Withdrawal rates used in the valuation of with profit policies are based on observed experience and adjusted when it is considered that future policyholder behaviour will be influenced by different considerations than in the past. In particular, it is assumed that withdrawal rates for unitised with profit contracts will be higher on policy anniversaries on which Market Value Adjustments do not apply.

Discretionary participating bonus rate

For realistic basis companies, the regular bonus rates assumed in each scenario are determined in accordance with each company's PPFM. Final bonuses are assumed at a level such that maturity payments will equal asset shares subject to smoothing rules set out in the PPFM.

Policyholder options and guarantees

Some of the Group's products give potentially valuable guarantees, or give options to change policy benefits which can be exercised at the policyholders' discretion. These products are described below.

Most with profit contracts give a guaranteed minimum payment on a specified date or range of dates or on death if before that date or dates. For pensions' contracts, the specified date is the policyholder's chosen retirement date or a range of dates around that date. For endowment contracts, it is the maturity date of the contract. For with profit bonds it is often a specified anniversary of commencement, in some cases with further dates thereafter. Annual bonuses when added to with profit contracts usually increase the guaranteed amount.

There are guaranteed surrender values on a small number of older contracts.

Some pensions' contracts include guaranteed annuity options (see deferred annuities in section 42.5.2 for details). The total amount provided in the with profit and non profit funds in respect of the future costs of guaranteed annuity options are £1,469 million (2008: £nil) and £52 million (2008: £nil) respectively.

In common with other life companies in the UK which have written pension transfer and opt-out business, the Group has set up provisions for the review and possible redress relating to personal pension policies. These provisions, which have been calculated from data derived from detailed file reviews of specific cases and using a certainty equivalent approach, which give a result very similar to a market consistent valuation, are included in liabilities arising under insurance contracts. The total amount provided in the with profit funds and non profit funds in respect of the review and possible redress relating to pension policies, including associated costs, are £325 million (2008: £nil) and £46 million (2008: £nil) respectively.

With profits deferred annuities participate in profits only up to the date of retirement. At retirement, a guaranteed cash option allows the policyholder to commute the annuity benefit into cash on guaranteed terms.

42.5.2 Managing product risk

The following sections give an assessment of the risks associated with the Group's main life assurance products and the ways in which the Group manages those risks.

	2009 Gross		2009 Reinsurance	
	Insurance contracts	Investment contracts with DPF	Insurance contracts	Investment contracts with DPF
	£m	£m	£m	£m
With profits funds:				
Pensions:				
Deferred annuities – with guarantees	8,821	73	392	-
Deferred annuities – without guarantees	1,550	112	-	-
Immediate annuities	3,679	-	671	-
Unitised with profits	1,279	9,051	90	-
Total pensions	15,329	9,236	1,153	-
Life:				
Immediate annuities	74	-	7	-
Unitised with profits	1,398	601	40	-

Life with profits	7,725	-	12	-
Total life	9,197	601	59	-
Other	2,290	6	92	-
Non profit funds:				
Deferred annuities – with guarantees	117	-	59	-
Deferred annuities – without guarantees	1,012	5	474	-
Immediate annuities	8,073	-	704	-
Protection	610	-	290	-
Unit linked	1,888	1,423	13	-
Other	449	55	16	-
	38,965	11,326	2,860	-

With Profit Fund (Unitised and Traditional)

The Group operates a number of with profit funds in the UK in which the with profit policyholders benefit from a discretionary annual bonus (guaranteed once added in most cases) and a discretionary final bonus. Non profit business is also written in some of the with profit funds and some of the funds may include immediate annuities and deferred annuities with Guaranteed Annuity Rates ("GAR").

The investment strategy of each fund differs, but is broadly to invest in a mixture of fixed interest investments and equities and/or property in such proportions as is appropriate to the investment risk exposure of the fund and its capital resources.

The Group has significant discretion regarding investment policy, bonus policy and early termination values. The process for exercising discretion in the management of the with profit funds is set out in the PPFM for each with profit fund and is overseen by with profit committees. Advice is also taken from the with profit actuary of each company which has a with profit fund. Compliance with the PPFM is reviewed annually and reported to the FSA and policyholders.

The bonuses are designed to distribute to policyholders a fair share of the return on the assets in the with profit funds together with other elements of the experience of the fund. The shareholders of the Group are entitled to receive one-ninth of the cost of bonuses declared for some funds and £nil for others.

Unitised and traditional with profit policies are exposed to equivalent risks, the main difference being that unitised with profit policies purchase notional units in a with profit fund whereas traditional with profit policies do not. Benefit payments for unitised policies are then dependent on unit prices at the time of a claim, although charges may be applied. A unitised with profit fund price is typically guaranteed not to fall and increases in line with any discretionary bonus payments over the course of one year.

Deferred annuities

Deferred annuity policies are written to provide either a cash benefit at retirement, which the policyholder can use to buy an annuity on the terms then applicable, or an annuity payable from retirement. The policies contain an element of guarantee expressed in the form that the contract is written in i.e. to provide cash or an annuity. Deferred annuity policies written to provide a cash benefit may also contain an option to convert the cash benefit to an annuity benefit on guaranteed terms; these are known as GAR policies. Deferred annuity policies written to provide an annuity benefit may also contain an option to convert the annuity benefit into cash benefits on guaranteed terms; these are known as Guaranteed Cash Option ("GCO") policies.

During the last decade, interest rates and inflation have fallen and life expectancy has increased more rapidly than originally anticipated. Deferred annuity policies which are written to provide annuity benefits are managed in a similar manner to immediate annuities and are exposed to the same risks.

The guaranteed terms on GAR policies are more favourable than the annuity rates currently available in the market available for cash benefits. The guaranteed terms on GCO policies are currently not valuable.

The option provisions on GAR policies are particularly sensitive to downward movements in interest rates, increasing life expectancy and the proportion of customers exercising their option. Adverse movements in these factors could lead to a requirement to increase reserves which could adversely impact profit and potentially require additional capital. In order to address the interest rate risk (but not the risk of increasing life expectancy or changing customer behaviour with regard to exercise of the option), insurance subsidiaries within the Group have purchased derivatives that provide protection against an increase in liabilities and have thus reduced the sensitivity of profit to movements in interest rates.

The Group seeks to manage this risk in accordance with both the terms of the issued policies and the interests of customers, and has obtained external advice supporting the manner in which it operates the long term funds in this respect.

Immediate annuities

This type of annuity is purchased with a single premium at the outset, and is paid to the policyholder for the remainder of their lifetime. Payments may also continue for the benefit of a surviving spouse or partner after the annuitant's death. Annuities may be level, or escalate at a fixed rate, or may escalate in line with a price index and may be payable for a minimum period irrespective of whether the policyholder remains alive.

The main risks associated with this product are longevity and investment risks. Longevity risk arises where the annuities are paid for the lifetime of the policyholder, and is managed through the initial pricing of the annuity and through reinsurance (appropriately collateralised) or transfer of existing liabilities. Annuities may also be a partial 'natural hedge' against losses incurred in protection business in the event of increased mortality (and vice versa) although the extent to which this occurs will depend on the similarity of the demographic profile of each book of business.

The pricing assumption for mortality risk is based on both historic internal information and externally generated information on mortality experience, including allowances for future mortality improvements. Pricing will also include a contingency margin for adverse deviations in assumptions.

Investment risk depends on the extent to which the annuity payments under the contracts have been matched by suitable assets which is managed under the ALM framework. Asset/liability modelling is used to monitor this position on a regular basis.

Protection

These contracts are typically secured by the payment of a regular premium payable for a period of years providing benefits payable on certain events occurring within the period. The benefits may be a single lump sum or a series of payments and may be payable on death, serious illness or sickness.

The main risk associated with this product is the claims experience and this risk is managed through the initial pricing of the policy (based on actuarial principles), the use of reinsurance and a clear process for administering claims.

43. Operating leases

Operating lease rentals charged within administrative expenses amounted to £15 million (2008: £nil).

The Group has commitments under non-cancellable operating leases as set out below:

	2009	2008
	£m	£m
Not later than one year	11	-
Later than one year and no later than five years	42	-
Later than five years	54	-

The principal operating lease commitments primarily concern office space located at Bothwell Street, Glasgow; St Vincent Street, Glasgow; Juxon House, London and Harcourt Street, London.

44. Commitments

	2009	2008
	£m	£m
To subscribe to private equity funds and other unlisted assets	520	-
To purchase, construct or develop investment property	108	-
For repairs, maintenance or enhancements of investment property	3	-

45. Related party transactions

The Group has related party transactions with its pension schemes, its Directors and entities where its Directors are deemed to have significant influence.

Transactions with pension schemes

During the year the Group entered into the following transactions with its pension schemes:

	Transactions	Balances outstanding
	2009	2009
	£m	£m
Pearl Scheme		
Investment management fees	1.4	1.4
Payment of administrative expenses	(1.0)	(0.3)
	0.4	1.1
PGL Scheme		
Investment management fees	0.7	0.5

The Pearl Scheme has invested in collective investment schemes that are controlled by the Group. At 31 December 2009 the Pearl Scheme held 1,118,197 units in the Axial Systematic Strategies Fund and 115,477,491 units in the Ignis Liquidity Fund. The value of these investments at 31 December 2009 was £154 million (2008: £nil) and £115 million (2008: £nil) respectively.

Other transactions and transactions with Directors and former Directors

Major Group decisions are made by the Board. Total remunerations received by current Directors in the year ended 31 December 2009 totalled £2.4 million (2008: £nil). Further details are given in the Remuneration Report.

On 4 January 2008, the one ordinary share issued at formation was transferred to Berggruen Acquisition Holdings Limited (an affiliate of Berggruen Acquisition Holdings II Ltd) and one additional ordinary share was issued to Marlin Equities IV, LLC. These two shares were subsequently repurchased by the Company on 11 January 2008.

Nicholas Berggruen is the President of Berggruen Acquisition Holdings II Ltd and Martin Franklin is the majority owner and managing member of Marlin Equities IV, LLC. The interests of these former Directors in the ordinary shares of the Company represent the interests of Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC respectively. On 9 January 2008, each of Berggruen Acquisition Holdings II Ltd, Marlin Equities IV, LLC, and the Company's three initial independent Directors, Dimitri Goulandris, Guy Naggar and Miguel Pais do Amaral (collectively, the "Founders") issued a non-interest bearing note in favour of the Company for the purchase price of the Founders' ordinary shares ("Founders shares") and warrants ("Founders' warrants") in the aggregate amount of €25,000. These notes were repaid by the Founders on 28 January 2008. On 10 January 2008, 20,125,000 units (each unit consisting of one Founders' share and one Founders' warrant and together referred to herein as a "Founders' unit") were issued as follows:

	Units	Subscription price
		€
Berggruen Acquisition Holdings II Ltd	9,934,505	12,341
Marlin Equities IV, LLC	9,934,505	12,341
Dimitri Goulandris	85,330	106
Guy Naggar	85,330	106
Miguel Pais do Amaral	85,330	106
Total	20,125,000	25,000

On 11 January 2008, each of Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC agreed to invest €4.0 million (€8.0 million in the aggregate) in the Company in the form of Sponsors' warrants to purchase 4,000,000 shares (8,000,000 in the aggregate) at a price of €1.00 per warrant. Each of Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC purchased such Sponsors' warrants from the Company immediately prior to the consummation of the IPO on 13 February 2008.

On 11 January 2008, each of Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC agreed to invest €25.0 million and Guy Naggar agreed to invest €10.0 million (€60.0 million in the aggregate) in the Company in the form of co-investment units at a price of €10.00 per unit immediately prior to the consummation of a business combination. In connection with the business combination the co-investment rights were cancelled.

On or about 5 February 2008, in connection with the pricing of the IPO, the Company repurchased an aggregate of 2,875,000 of the Founders' units as follows:

	Units	Subscription price
		€
Berggruen Acquisition Holdings II Ltd	1,419,215	1,760
Marlin Equities IV, LLC	1,419,215	1,760
Dimitri Goulandris	12,190	15

Guy Naggar	12,190	15
Miguel Pais do Amaral	12,190	15
Total	2,875,000	3,565

On 11 March 2008, as a result of the expiration without exercise of the underwriters over allotment option in connection with the IPO, Founders' units were automatically redeemed as follows:

	Units
Berggruen Acquisition Holdings II Ltd	1,110,690
Marlin Equities IV, LLC	1,110,690
Dimitri Goulandris	9,540
Guy Naggar	9,540
Miguel Pais do Amaral	9,540
Total	2,250,000

On 29 October 2008, Guy Naggar resigned from the Board of Directors and agreed to forfeit his Founders' shares and Founders' warrants, which forfeiture was effected by the Company's repurchase of his Founders' shares at par value (and the concurrent cancellation of his Founders' warrants) upon the approval by the Company's owners and the Company's consummation of a business combination. On 29 October 2008, the Company's Board of Directors appointed Ashley Silverton to fill the vacancy on the Board of Directors. The Company paid Ashley Silverton €10,000 as compensation for his agreeing to fill this vacancy and agreed to pay Ashley Silverton a fee in the amount of €636,000 upon the consummation of a business combination. In connection with his appointment to the Board of Directors, Ashley Silverton resigned his position as vice president of the Company. The fee of €636,000 was paid to Ashley Silverton on 2 September 2009.

Prior to the IPO, the Company agreed to pay Berggruen Holdings Ltd, an affiliate of Nicholas Berggruen, a total of €10,000 per month commencing on the date of the IPO for certain operating services and support until the earlier of the Company's consummation of a business combination or its liquidation. This arrangement with Berggruen Holdings Ltd was agreed to by Berggruen Holdings Ltd for the Company's benefit and was not intended to provide Berggruen Holdings Ltd compensation in lieu of a management fee. The Company believes that such fees are at least as favourable as it could have obtained from an unaffiliated third party. Prior to the IPO, Berggruen Holdings Ltd provided the Company with certain operating services and support at no charge. This fee ceased on the acquisition of the Pearl businesses and €80,000 was charged in 2009. No amounts were outstanding at 31 December 2009.

Other than part of the €10,000 per month for operating services and support payable to Berggruen Holdings Ltd and a €1,000 per month fee payable to Ashley Silverton for his services as an officer of the Company, the €10,000 payment to Mr Silverton for his agreeing to fill the vacancy on the Board of Directors following Guy Naggar's resignation, the €636,000 fee payable to Ashley Silverton upon the consummation of a business combination and reimbursable out-of-pocket expenses payable to the Company's officers and Directors, no compensation or fees of any kind, including finders and consulting fees, have been or will be paid to the Company's officers or its Directors who owned the Company's shares prior to the IPO, or to any of their

respective affiliates for services rendered to the Company prior to or in connection with a business combination.

On 27 June 2009, the Company entered into a contingent subscription agreement with Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC where by the Company agreed to grant to them or their nominees the right to receive 1,000,000 'B' ordinary shares in exchange for Berggruen Acquisition Holdings II Ltd and Marlin Equities IV, LLC agreeing to subscribe for new shares to a maximum value of £75 million, should the available cash in the Company fall below £450 million on the acquisition of the Pearl businesses. These will be issued if the share price of the company exceeds €15.00 for 20 consecutive trading days.

On 2 September 2009, in connection with the acquisition of the Pearl businesses, the Company repurchased the Founders' shares from Guy Naggar and concurrently cancelled the related Founders' warrants.

On the same date, 50% of the remaining Founders' warrants were converted into ordinary shares as follows:

	Units	Number of ordinary shares
Berggruen Acquisition Holdings II Ltd	3,702,300	357,122
Marlin Equities IV, LLC	3,702,300	357,122
Dimitri Goulandris	31,800	3,067
Miguel Pais do Amaral	31,800	3,067
Total	7,468,200	720,378

Also on 2 September 2009, 50% of the sponsors warrants were converted into ordinary shares as follows:

	Units	Number of ordinary shares
Berggruen Acquisition Holdings II Ltd	2,000,000	192,919
Marlin Equities IV, LLC	2,000,000	192,919
Total	4,000,000	385,838

During the year the Group has been charged a transitional services fee of £0.4 million from TDR Capital LLP a company in which Manjit Dale is deemed to have significant influence. This amount was outstanding at 31 December 2009.

As a result of the acquisition of the Pearl businesses, TDR Capital Nominees Limited (as nominee for TDR Capital I and other related entities) received 13,014,055 'B' ordinary shares and 10,871,095 contingent rights

over shares in Phoenix Group Holdings in exchange for shares they held in the acquired group of companies. TDR Capital Nominees Limited is a subsidiary of TDR Capital LLP.

The Group is party to an uncollateralised total return swap with TDR Capital Nominees Limited in relation to the performance of certain investments of Axial Income Opportunities S.a.r.l. As at 31 December 2009 a fair value of £27.1 million (2008: £nil) has been attributed to these swaps and interest of £1.4 million (2008: £nil) has been charged by TDR Capital Nominees Limited. At 31 December 2009, interest of £0.3 million was outstanding (2008: £nil).

As a result of the acquisition of the Pearl businesses the Jambright Limited group of companies, a group in which Manjit Dale is deemed to have significant influence, received 4,506,268 'B' ordinary shares in Phoenix Group Holdings in exchange for shares it held in the acquired group of companies.

During the year the Group has also been charged a transitional services fee of £0.1million and investment management fees of £0.4 million from Sun Capital Partners Limited, a company in which Hugh Osmond is deemed to have significant influence. The transitional services fee was outstanding at 31 December 2009.

During the year an associate of the Group, Sant Topco Holdings I S.a.r.l has been charged a financial consulting fee of €0.1million by Sun Capital Partners Limited.

As a result of the acquisition of the Pearl businesses O-Re Holdings (Netherlands) BV, a company in which Manjit Dale and Hugh Osmond are deemed to have significant influence, received 2,481,064 'B' ordinary shares and 2,198,970 contingent rights over shares in Phoenix Group Holdings in exchange for shares they held in the acquired group of companies.

As a result of the acquisition of the Pearl businesses the Xercise Limited group of companies, a group in which Hugh Osmond is deemed to have significant influence, received 14,108,205 'B' ordinary shares and 9,180,660 contingent rights over shares in Phoenix Group Holdings in exchange for shares it held in the acquired group of companies.

As a result of the acquisition of the Pearl businesses, some of the Directors received shares and contingent rights over shares in Phoenix Group Holdings in exchange for shares they held in the acquired group of companies. Details of the shareholdings of Directors are provided in the Remuneration Report.

46. Contingent liabilities

In the normal course of business the Group is exposed to certain legal issues, which involve litigation and arbitration, and as at the period end, the Group has a contingent liability in this regard.

Following a previous acquisition by the Pearl businesses, the shares in PLL and certain loans were transferred from the non profit fund to the shareholder fund of PA (GI) Limited at their admissible regulatory value. HM Revenue & Customs ("HMRC") has challenged the tax treatment of these transfers in the year ended 31 December 2004 and litigation may follow in 2010. The Directors do not consider it probable that any additional tax liability will arise. However, were HMRC's challenge to be successful, the Group expects that the liability (before interest and penalties) should not exceed £45 million.

London Life Limited has provided information to the FSA on its categorisation of £54 million of working capital to owner funds in 2006. The Directors are confident in this treatment, which is supported by legal and

actuarial advice, but note that the FSA have not concluded their review into the matter and therefore a contingent liability of £54 million exists if London Life Limited were required to transfer this working capital back to policyholder funds.

47. Group entities

The principal subsidiary undertakings of the Group are as follows:

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned unless otherwise indicated)
Insurance companies		
BA (GI) Limited (general insurance company)	UK	Ordinary shares of £0.05
London Life Limited	UK	Ordinary shares of £1
National Provident Life Limited	UK	Ordinary shares of £1
NPI Limited	UK	Ordinary shares of £1
Pearl Assurance plc	UK	'A' ordinary shares of £0.05
PA (GI) Limited (general insurance company)	UK	Ordinary shares of £0.01 Deferred shares of £0.25
Phoenix Life Limited	UK	Ordinary shares of £1
Phoenix & London Assurance Limited	UK	Ordinary shares of £1
Phoenix Pensions Limited	UK	Ordinary shares of £1
Scottish Mutual International Limited	ROI	Ordinary shares of €1.25
Non-insurance companies		
Axial Fixed Income Opportunities S.a.r.l. (investment vehicle)	Luxembourg	Ordinary shares of €100
Ignis Asset Management Limited (investment management company)	UK	Ordinary shares of £1
Ignis Investment Management Limited (investment management company)	UK	Ordinary shares of £1
Ignis Fund Managers Limited (unit trust management)	UK	Ordinary shares of £1
Ignis Investment Services Limited (investment management company)	UK	Ordinary shares of £1
Impala Holdings Limited (holding company)	UK	'A' ordinary shares of £1, 'B' ordinary shares of £1 and 'D' ordinary shares of £1
Mutual Securitisation plc (finance company)	ROI	Quasi subsidiary
NP Life Holdings Limited (holding company)	UK	'A' ordinary shares of £1 and 'B' ordinary shares of £1

Opal Reassurance Limited	Bermuda	‘A’ ordinary shares of £1 and ‘B’ ordinary shares of £1
PGH (LCA) Limited (finance company)	UK	Ordinary shares of £1
PGH (LCB) Limited (finance company)	UK	Ordinary shares of £1
PGH (LC1) Limited (finance company)	UK	Ordinary shares of £1
PGH (LC2) Limited (finance company)	UK	Ordinary shares of £1
PGH (MC1) Limited (finance company)	UK	Ordinary shares of £1
PGH (MC2) Limited (finance company)	UK	Ordinary shares of £1
PGH (TC1) Limited (holding company)	UK	Ordinary shares of £1
PGH (TC2) Limited (holding company)	UK	Ordinary shares of £1
Pearl Group Holdings (No. 1) Limited (finance company)	UK	Ordinary shares of £1
Pearl Group Holdings (No. 2) Limited (holding company)	UK	Ordinary shares of £1
Pearl Life Holdings Limited (holding company)	UK	Ordinary shares of £1
Pearl Group Services Limited (service company)	UK	Ordinary shares of £1
PGS 2 Limited (finance company)	UK	Ordinary shares of £1
Pearl Group Management Services Limited (service company)	UK	Ordinary shares of £1
Phoenix Life Holdings Limited (holding company)	UK	Ordinary shares of £1
UK Commercial Property Trust Limited (property fund)	Guernsey	72% of ordinary shares of £0.25

The information disclosed above is only in respect of those undertakings which principally affect the figures shown in the Group’s accounts. There are a number of other subsidiaries and associated undertakings whose business does not materially affect the Group’s profits or the amount of its assets and particulars of these have been omitted in view of their excessive length.

There is a restriction on the ability of some Group companies to distribute funds to Phoenix Group Holdings as a result of restrictions imposed by the Impala facility and the £425 million loan facility agreements.

48. Events after the reporting period

On 5 January 2010 PGH1 announced a proposed restructuring of the Notes. The proposed restructuring was not approved by Noteholders and consequently those proposals were not implemented.

On 23 March 2010 PGH1 gave notice to the holders of the Notes of its decision to defer the coupon payment on the Notes which would otherwise have been due at the next payment date of 25 April 2010. PGH1 announced that this notice will be withdrawn and the 2010 coupon will be paid in full on 25 April 2010 if certain amending proposals are approved by, amongst others, the Noteholders. These proposals include a reduction of 15% in the face value of the Notes and the payment in full of the deferred 2009 coupon by 31 December 2010. Both proposed coupon payments are to be based on the current nominal value of the Notes, being £500 million.

On 15 March 2010 the Company changed its name from Pearl Group to Phoenix Group Holdings.

On 30 March 2010 the Board declared a dividend of €0.17 per share for the year ended 31 December 2009. The cost of this dividend has not been recognised as a liability in the financial statements for 2009 and will be charged to the statement of changes in equity in 2010.

R Sandler

J Moss

S Smith

A Lyons

I Ashken

R-P Azria

D Barnes

C Clarke

I Cormack

T Cross Brown

M Dale

I Hudson

H Osmond

D Woods

St Helier, 30 March 2010

F) MCEV supplementary information

Summarised consolidated income statement – pro forma Group MCEV basis

For the year ended 31 December 2009

	2009 £m
Life MCEV operating earnings	380
Management services operating profit	14
Ignis Asset Management operating profit	34
Corporate operating loss	(54)
Group MCEV operating earnings before tax	**374**
Economic variances on covered business	701
Economic variances on non-covered business	(245)
Non-recurring items	(78)
Gain on debt refinancing	491
Finance costs attributable to owners	(390)
Group MCEV earnings before tax	**853**
Tax on operating earnings	(105)
Tax on non-operating earnings	(197)
Total tax	**(302)**
Group MCEV earnings	**551**

Pro forma MCEV earnings per ordinary share

For the year ended 31 December 2009

	2009
Group MCEV operating earnings after tax	

Basic[3]	291.5p
Diluted[4]	254.4p

Group MCEV earnings after tax

Basic[3]	597.2p
Diluted[4]	521.1p

The earnings on covered business are calculated on a post-tax basis and are grossed up at the effective rate of shareholder tax for presentation in the income statement. The tax rate used is the UK corporate tax rate of 28%.

[3] Based on 92,269,310 shares
[4] Based on 105,732,020 shares, allowing for warrants in issue

Statement of consolidated comprehensive income – pro forma Group MCEV basis

For the year ended 31 December 2009

	2009 £m
Group MCEV earnings for the year after tax	**551**
Other comprehensive income	
Actuarial losses on defined benefit pension schemes	(14)
Exchange differences on translating foreign operations	(44)
	(58)
Total comprehensive income for the year	**493**

Reconciliation of movement in pro forma Group MCEV equity

For the year ended 31 December 2009

	2009 £m
Pro forma Group MCEV equity at 1 January 2009	**1,044**
Total comprehensive income for the year	493
Issue of share capital	275
Conversion of warrants into ordinary shares	51
Redemption of shares	(41)
Credit to equity for equity-settled share-based payments	5
Group MCEV equity at 31 December 2009	**1,827**

Analysis of movement in pro forma Group MCEV equity

Life MCEV operating earnings

Life MCEV operating earnings (after tax)		**2009**
Expected existing business contribution		95
New business value		22
Non-economic experience variance and assumption changes		
- Experience variances	62	
- Other operating variances	21	
- Assumption changes	73	
Total non-economic experience variances and assumption changes		156
Life MCEV operating earnings after tax[1]		**273**

1 Life MCEV operating earnings is derived on an after tax basis. For presentational purposes Life MCEV operating earnings before tax has been calculated by grossing up the after tax Life MCEV operating earnings using a tax rate of 28 percent. Life MCEV operating earnings before tax of £380 million is therefore calculated as £273 million (as above) grossed up for tax at 28 percent

Expected existing business contribution

The expected contribution of the existing business for the year ended 31 December 2009 was £95 million after tax. This represents the expected return on the opening MCEV using a one year gilt forward rate plus the Group's short-term expectations of excess investment returns on equities, properties and bonds. This rate is expected to increase in line with the forward gilt yield curve.

New business value

New business profits generated during the year amounted to £22 million after tax and represent the value of vesting pension policies not reflected in the opening MCEV. These arise from pension policies which have no attaching annuity guarantees.

The new business margin is 5% after tax and represents the ratio of the net of tax new business value to the amount received as new single premiums.

Non-economic experience variances and assumption changes

The life companies' non-economic experience variances and assumption changes for the year ended 31 December 2009 contributed £156 million to pro forma MCEV operating earnings after tax.

Favourable experience and other operating variances of £83 million primarily related to several management actions including the resolution of certain legacy issues, partially offset by the strengthening of regulatory capital requirements and capital policy in some life companies following the acquisition of the Pearl businesses by Phoenix Group Holdings. Favourable assumption changes of £73 million mainly related to harmonisation of longevity assumptions across the Group and the results of an annuitant survival investigation.

Ignis Asset Management operating profit

Ignis Asset Management's performance was favourable throughout the year generating a pro forma IFRS operating profit before tax of £34 million.

Corporate operating loss

The Corporate operating loss of £54 million before tax for the year ended 31 December 2009 includes:

- corporate office costs and project spend of £14 million; and
- net expected charge on the Pearl Group Staff Pension Scheme of £22 million and a £17 million contribution to the PGL pension scheme. The £17 million contribution is an expense under the Group's MCEV methodology as a deduction to the Group MCEV is made for pension schemes in deficit, but no credit is taken for pension scheme surpluses.

Economic variances on covered business

Positive economic variances in 2009 of £504 million after tax reflect the benefit of the reduction in credit spreads on corporate bonds and favourable equity and yield movements, partially offset by an increase of £36 million in the market value of listed debt issued by Phoenix Life Limited (ex Scottish Mutual Assurance).

Economic variances on non-covered business

The economic variances on non covered business of £245 million before tax primarily relate to the increase in the market value of listed debt issued by the Group's subsidiary Pearl Group Holdings (No. 1) Limited and Phoenix Group Holdings warrants, which reduced MCEV earnings by £169 million and £51 million respectively. In addition, the economic variances include a £29 million foreign exchange loss incurred by Phoenix Group Holdings primarily related to its euro cash holdings prior to its capital injection into the Pearl businesses. Having reduced its euro cash holdings, Phoenix Group Holdings' exposure to foreign exchange fluctuations has reduced.

Non-recurring items

Non-recurring items reduced the embedded value by £78 million before tax and primarily include:

- £27 million of costs associated with the Phoenix Life site rationalisation and associated staff reductions and the Group's transformation programme with its outsourcers
- £44 million of acquisition related expenditure incurred by Phoenix Group Holdings subsidiaries
- A charge of £78 million after tax as a consequence of the restructuring of the Pearl businesses external debt which reduced the expected tax attributes available to the Group to relieve the tax on the emerging surpluses from the operating businesses
- A charge of £12 million after tax related to the court approved Guaranteed Annuity Option Compromise Scheme for Phoenix and London Assurance. This removed longevity risk from the business whilst providing policyholder benefit enhancements
- Offset by a profit of £102 million after tax as a result of reassessing the impairment of a loan made to the PALAL long term fund. The improved recoverability of the loan reflects the outcome of risk management activity within PALAL and the improved financial position of the fund

Gain on debt refinancing

As part of their acquisition by Phoenix Group Holdings, the Pearl businesses successfully refinanced their external borrowings resulting in an overall reduction of £575 million in exchange for cash and an issue of warrants totalling £84 million.

Finance costs attributable to owners

	2009
Debt finance costs[1]	176
Debt issue	202
Other finance costs	12
Finance costs attributable to owners	**390**

1 Finance costs on the Impala and Pearl facility agreements (and associated swap interest) and the Royal London PIK notes

Debt financing costs include interest of £142 million on the holding company debt for the 8 month period prior to the refinancing (as discussed above) and interest on the refinanced debt on amended terms thereafter of £34 million for the final 4 month period.

As part of Phoenix Group Holdings' acquisition of the Pearl businesses, fees of £202 million were paid to the banks as consideration to facilitate the transaction. The consideration was in the form of equity issued to the lenders by Phoenix Group Holdings and therefore resulted in a corresponding increase in capital. Under IFRS these debt issue costs are taken into account in determining the cost of acquisition of the Pearl businesses.

Capital and other movements

Other comprehensive income of £58 million includes £14 million of actuarial losses on defined benefit pension schemes, and £44 million exchange rate losses which will reduce going forward as Phoenix Group Holdings changed its functional currency from euros to sterling during the year.

Capital movements comprised additional shares issued of £275 million at the time of the acquisition of the Pearl businesses, £51 million of shares issued on conversion of the warrants, £5 million of share-based payments offset by £41 million of shares redeemed at the time of the acquisition of the Pearl businesses.

The £275 million of share capital issued includes £202 million in connection with the associated debt restructuring and an additional cash equity injection of £73 million at the time of the acquisition of the Pearl businesses by Phoenix Group Holdings.

Pro forma Group MCEV Analysis of Earnings

For the year ended 31 December 2009

		Non-covered business			
	Covered business MCEV	Management services IFRS	Asset Management IFRS	Corporate[1] IFRS	Group MCEV
	£m	£m	£m	£m	£m
Pro forma Group MCEV at 1 January 2009	4,081	122	34	(3,193)	**1,044**
Operating MCEV earnings (post-taxation)	273	10	24	(38)	269
Non – operating MCEV earnings (post-taxation)	511	(25)	(4)	(200)	282
Total MCEV earnings	**784**	**(15)**	**20**	**(238)**	**551**
Foreign exchange	-	-	-	(44)	(44)
Other movements	-	-	-	(14)	(14)
Capital and dividend flows - internal	(134)	(51)	(15)	200	-
Capital and dividend flows - external	-	-	-	290	290
Closing value at 31 December 2009	**4,731**	**56**	**39**	**(2,999)**	**1,827**

1 Comprises the Group holding companies that do not form part of the Phoenix Life and Ignis Asset Management divisions

Reconciliation of Group IFRS equity to MCEV net worth

For the year ended 31 December 2009

	2009
	Group
	£m
Group net assets attributable to owners of the parent as reported under IFRS at 31 December 2009	**1,412**

Goodwill and other intangibles in accordance with IFRS (after tax)	(413)
Value of in-force business in accordance with IFRS (after tax)	(1,419)
Adjustments to IFRS reserving	(98)
Tax adjustments	(99)
Revalue listed debt to market value	235
Eliminate value of contingent loan asset[5]	(194)
Fair value adjustments[6]	(40)
Eliminate pension scheme surplus[7] (after tax)	(45)
Other adjustments	(9)
MCEV net worth attributable to owners of the parent at 31 December 2009	**(670)**

[5] Removal of value attributed to contingent loans issued by holding companies to long term funds as their expected repayments are captured within the MCEV VIF calculations

[6] Investments carried at amortised cost under IFRS are revalued at market value

[7] The pension scheme surplus removed is the economic surplus of the PGL scheme, as described in note 32 to the IFRS consolidated financial statements, after tax.

Notes to the pro forma MCEV financial statements

1. Basis of preparation

Overview

The supplementary information covering the year to 31 December 2009 has been prepared on a Market Consistent Embedded Value ("MCEV") basis except for the items described further below.

Whilst the IFRS consolidated financial statements consolidate the results of the Pearl businesses for the period from acquisition on 28 August 2009 to 31 December 2009, the pro forma MCEV results include a full year's contribution for the acquired Pearl businesses. The pro forma MCEV results are therefore based on the results of the Group plus the Pearl businesses for the period prior to their acquisition by Phoenix Group Holdings.

The supplementary MCEV information reflects the financial position of the Group at 31 December 2009. The asset management and management service businesses are included in the Group MCEV at the value of IFRS net assets and do not include the future earnings from their existing business. This is because, in the opinion of the Directors, applying the CFO Forum MCEV principles and guidance to these businesses would not provide a fair reflection of the Group's financial position, as explained in note 10.

The MCEV methodology adopted by the Group is in accordance with the MCEV principles and guidance published by the CFO Forum in October 2009, except that:

- Risk-free rates have been defined as the annually compounded UK government nominal spot curve plus ten basis points rather than as a swap rate curve;
- No allowance for the cost of residual non-hedgeable risk (CNHR) has been made because, in the opinion of the Directors, the Group operates a robust outsourcer model in terms of operational risk, does not write new business, is focussed entirely on the back book, and has succeeded in closing out significant legacy risks. The theoretical value of CNHR is disclosed separately in note 1 (b);
- As indicated above the value of the asset management and management service companies are calculated on an IFRS basis.

The Group MCEV allows for methodology changes from previously published embedded values. The methodology changes have been implemented to better align the Group's MCEV methodology with the CFO Forum principles. Details of the methodology changes and a reconciliation to the Group MCEV at December 2008, as published in the proxy statement of 3 July 2009, are provided in note 10.

Covered business

The MCEV calculations cover all long term insurance business written by the Group, but exclude Ignis Asset Management, the management service companies and business carried on at the Corporate entity level.

Opal Re is included within covered business and is valued on a basis consistent with the annuity business within the life companies.

MCEV methodology

The embedded value of covered business is based on a market-consistent methodology. Under this methodology, assets and liabilities are valued in line with market prices and consistently with each other. Details of the key components of the MCEV are discussed below.

The components of MCEV are:

- Assets available for distribution to shareholders, or free surplus; plus
- Assets supporting the solvency requirements of the business, or required capital; plus
- The value of in-force covered business.

a) Free surplus and required capital

Free surplus and required capital together comprise the net worth of the life insurance business.

For the Group's life companies, net worth is defined as the market value of shareholder funds plus the shareholders' interest in surplus assets held in long-term business funds less the market value of any outstanding debt of the life companies.

Loans from the life companies to holding companies have been consolidated out such that they do not appear as an asset in the life company nor as a liability in the holding company. This presentation has no impact on the overall MCEV but does affect the allocation of net assets between covered and non-covered business.

MCEV allocates net worth between required capital, whose future distribution to shareholders is restricted by regulatory requirements, and free surplus.

For the Group, required capital is defined as the greater of:

- the amount of capital required to meet the FSA capital adequacy requirements, consisting of the greater of Pillar 1 and Pillar 2 capital requirements where:
    - under Pillar 1, the life companies are required to maintain excess capital in excess of policy liabilities calculated using a basis specified by the FSA; and
    - under Pillar 2, the life companies are required to carry out and submit their own assessment of capital requirements by assessing the major risks they are running and the capital they need to ensure that they remain able to meet their liabilities to policyholders in all but the most extreme circumstances;
- the capital required under the Group's capital management policy.

On this basis the required capital measure is 125% of the solvency capital at which the regulator is empowered to take action.

Net worth in excess of required capital is free surplus.

The European Solvency II Directive will introduce a new capital regime for insurers during 2012. These disclosures do not take account of the impact of the change in regime as this is still under development.

b) Value of in-force business ("VIF")

The value of in-force covered business consists of the following components:

- Present value of future profits;
- Time value of financial options and guarantees; and
- Frictional costs of required capital.

The market consistent value of in-force business represents the present value of profits attributable to shareholders arising from the in-force business, less an allowance for the time value of financial options and guarantees embedded within life insurance contracts and frictional costs of required capital.

The approach adopted to calculate VIF combines deterministic and stochastic techniques (each of which is discussed in more detail below):

- Deterministic techniques have been used to value cash flows whose values vary in a linear fashion with market movements. These cash flows are valued using discount rates that reflect the risk inherent in each cash flow. In practice, it is not necessary to discount each cash flow at a different discount rate, as the same result is achieved by projecting and discounting all cash flows at risk-free rates. This is known as the "certainty equivalent approach."; and
- Stochastic techniques have been used to value cash flows that have an asymmetric effect on cash flows to shareholders. Here, the calculation involves the use of stochastic models developed for the purposes of realistic balance sheet reporting.

Present value of future profits ("PVFP")

The present value of future profits represents the present value of profits attributable to shareholders arising from the in-force business. The PVFP is calculated by projecting and discounting using risk-free rates, with an allowance for liquidity premiums where appropriate.

The projection is based on actively reviewed best estimate non-economic assumptions. Best estimate assumptions make appropriate allowance for expected future experience where there is sufficient evidence to justify; for example in allowing for future mortality improvements on annuity business.

Time value of financial options and guarantees ("TVFOGs")

The Group's embedded value includes an explicit allowance for the time value of financial options and guarantees embedded within insurance contracts, including investment performance guarantees on participating business and guaranteed vesting annuity rates. The cost of these options and guarantees to

shareholders is calculated using market-consistent stochastic models calibrated to the market prices of financial instruments as at the period end.

The TVFOGs allow for the impact of management actions, consistent with those permitted by the Principles and Practices of Financial Management. The modelling of management actions vary for each of the funds but typically include management of bonus rates and policy enhancements, charges to asset share to cover increases to the cost of guarantees and alterations to investment strategy.

Frictional cost of capital ("COC")

Cost of capital is defined as the difference between the market value of shareholder-owned assets backing required capital and the present value of future releases of those assets allowing for future investment returns on that capital, investment expenses and taxes.

Cost of residual non-hedgeable risks ("CNHR")

The CNHR should allow for risks that can have an asymmetric impact on shareholder value to the extent these risks have not already been reflected in the PVFP or TVFOGs. The majority of such risks within the Group are operational and tax risks.

No allowance for the cost of non-hedgeable risk has been made, as in the opinion of the Directors, the cost of residual non-hedgeable risk calculated in accordance with CFO Forum principles and guidance does not anticipate further risk management actions and therefore does not provide a fair reflection of the Group's ongoing risk.

However, the cost of residual non-hedgeable risk calculated in accordance with the CFO Forum principles and guidance, and therefore without anticipating further risk management actions, has been disclosed below.

For with profits business the cost of residual non-hedgeable risk would increase the TVFOGs by £93 million.

For other business the cost would be £141 million. This equates to an equivalent average cost of capital charge of 1.6%. The level of capital assumed in this calculation is determined based on a 99.5% confidence level over a one year time horizon, consistent with the ICA methodology. Allowance is made for diversification benefits between non-hedgeable risks, but not between hedgeable and non-hedgeable risks.

c) Valuation of debt

Listed debt issued by the Group is valued at the market value quoted at the reporting date which is consistent with MCEV principles.

The National Provident Life Securitised Bonds are backed by surpluses that are expected to emerge on blocks of its unit linked and unitised with profits business. This securitisation has been valued on a cash-flow basis, allowing for payments expected to be due based on the projected level of securitised surpluses

emerging. The full VIF of the securitised unit linked and unitised with profits business is expected to be payable to bondholders; therefore, no additional value accrues to the embedded value.

Unlisted bank debt owed by the holding companies is included at face value.

d) Taxation

Full allowance has been made for the value of tax that would become payable on the transfer of surplus assets out of non profit funds. This allowance reflects the projected pace of releases of surplus from non profit funds that is not required to support with profits funds.

Allowance has also been made for the tax relief arising from interest payments made on the debt of the holding companies. The value of the tax relief is determined by offsetting the tax payable on profits emerging from covered business against the tax relief afforded by interest payments on the debt. Interest payments are projected assuming that current levels of debt are reduced and then refinanced to maintain a long term level of debt that the Directors consider to be supported by the projected embedded value of the Group's businesses.

e) New business

The MCEV places a value on the profits expected to be earned on annuities arising from policies vesting with guaranteed annuity terms. These policies are excluded from the definition of new business on the basis that the annuity being provided is an obligation under an existing policy and the life companies are already reserving for the cost of these guarantees.

New business includes all other annuities written by the life insurance companies.

f) Participating business

Allowance is made for future bonus rates on a basis consistent with the projection assumptions and established company practice.

The time value of options and guarantees used in the calculation of MCEV also allows for expected management action and policyholder response to the varying external economic conditions simulated by the economic scenario generators. Policyholder response has been modelled based on historical experience. Management actions have been set in accordance with each life companies' Principles and Practices of Financial Management.

g) Pension schemes

The MCEV allows for pension scheme deficits as calculated on an IFRS basis, but no benefit is taken for pension scheme surpluses.

2. Components of the MCEV of covered business

	2009 MCEV £m	2008 MCEV £m
Net worth	2,234	1,816
PVFP	2,864	2,680
TVFOG	(97)	(206)
COC	(270)	(209)
	4,731	**4,081**

The net worth of covered business of £2,234 million at December 2009 consisted of £1,826 million of required capital and £408 million of free surplus.

3. Analysis of covered business MCEV earnings (after tax)

			2009
	Net worth	VIF	Total Life MCEV
		£m	£m
Life pro forma MCEV at 1 January 2009	1,816	2,265	4,081
New business value	18	4	22
Expected existing business contribution (reference rate)	32	27	59
Expected existing business contribution (in excess of reference rate)	10	26	36
Transfer from VIF and required capital to free surplus	181	(181)	-
Experience variances	51	11	62
Assumption changes	165	(92)	73
Other operating variances	(14)	35	21
Operating Life MCEV earnings	**443**	**(170)**	**273**
Economic variances	66	438	504
Other non-operating variances	12	(5)	7
Total Life MCEV earnings	**521**	**263**	**784**
Capital and dividend flows	(103)	(31)	(134)
Life MCEV at 31 December 2009	**2,234**	**2,497**	**4,731**

4. New business

The value generated by new business written during the period is calculated as the present value of the projected stream of after tax distributable profits from that business. This contribution has been valued using economic and non-economic assumptions at the point of sale. The value of new business is shown after the effect of frictional costs of holding required capital on the same basis as for the in-force covered business

			2009
	Premium	MCEV	MCEV/Premium
	£m	£m	%
New business	401	22	5%

5. Maturity profile of business

This note sets out how the PVFP is expected to emerge into net worth over future years. Surpluses are projected on a certainty equivalent basis with allowance for liquidity premiums as appropriate and are discounted at risk-free rates.

	Years					2009
	1-5	6-10	11-15	16-20	20+	Total
	£m	£m	£m	£m	£m	£m
Present value of future profits (PVFP)	975	767	508	305	309	2,864

6. Economic assumptions

Reference Rates

(a) Risk-free rates

Risk-free rates are based on the annually compounded UK government bond nominal spot curve plus ten basis points, extrapolated as necessary to meet the term of the liabilities. Recognising that this is a departure from MCEV principles, a sensitivity based on swap yields is disclosed.

The risk-free rates assumed for a sample of terms were as follows:

	Year ended 31 December 2009		Year ended 31 December 2008	
Term	**Gilt Yield +10 bps**	**Swap Yield**	**Gilt Yield +10 bps**	**Swap Yield**
1 year	0.97%	1.02%	1.22%	n/a
5 years	3.13%	3.49%	2.87%	n/a
10 years	4.35%	4.27%	3.58%	n/a
15 years	4.80%	4.55%	4.13%	n/a
20 years	4.86%	4.55%	4.34%	n/a

The swaps rates above are only applicable to sensitivity (12) as disclosed in note 9.

(b) Liquidity Premiums

In October 2009, the CFO Forum published an amendment to MCEV principles to reflect the inclusion of a liquidity premium. The changes affirm that the reference rate may include a liquidity premium over and above the risk-free yield curve for liabilities which are not liquid, given that the matching assets are able to be held to maturity.

The liabilities to which a liquidity premium is applied include immediate annuities, pensions policies with benefits defined as an annuity or with in-the-money guaranteed annuity options. The liquidity premium is determined by reference to the yield on the bond portfolios held after allowing for credit risk by deducting margins for best estimate defaults and unexpected default risk premiums. At 31 December 2009 the

calculated liquidity premium represented an additional yield above risk-free rates of 30 basis points (31 December 2008: 70 basis points).

Inflation

For purposes of the MCEV calculation, the rate of increase in the UK Retail Price Index ("RPI") as at 31 December 2009 was taken from the implied inflation curve at a term appropriate to the liabilities. The rate of increase in UK National Average Earnings inflation is assumed to be RPI + 100 basis points as at 31 December 2009.

Stochastic economic assumptions

The time value of options and guarantees is calculated using an economic scenario generator. The model is calibrated to market conditions as at 31 December 2009. The scenario generator and calibration are consistent with that used for realistic balance sheet reporting.

A Libor Market Model is used to generate risk-free rates over a complete yield curve, calibrated to the UK nominal spot curve plus ten basis points, consistent with the deterministic projections. Interest rate volatility is calibrated to swaption implied volatilities, as per the sample below.

End 2009	Swap term (years)					
Option term (years)	5	10	15	20	25	30
5	17.0%	13.1%	14.3%	15.1%	15.9%	15.4%
10	15.7%	13.8%	14.8%	15.4%	15.6%	14.7%
20	15.9%	14.1%	14.6%	14.4%	14.0%	13.0%
30	15.7%	13.6%	13.5%	13.0%	12.3%	11.5%

End 2008	Swap term (years)					
Option term (years)	5	10	15	20	25	30
5	16.6%	15.4%	15.5%	15.9%	16.1%	-
10	12.5%	13.9%	14.5%	14.5%	14.1%	-
20	18.4%	18.6%	17.4%	15.9%	14.3%	-
30	17.6%	17.1%	15.5%	14.1%	12.8%	-

Real interest rates have been modelled using the two-factor Vasicek model, calibrated to index-linked gilts.
Equity volatility is calibrated to replicate the prices on a range of FTSE equity options, and extrapolated beyond terms available in the market. The equity volatility model used allows volatility to vary with both term and the level of the equity index.

Term (years)		5	10	15	20	25	30
Equity implied volatility (ATM)	End 2009	25.3%	26.6%	27.3%	27.5%	27.6%	27.7%
	End 2008	34.4%	34.6%	33.4%	33.1%	32.8%	32.5%

Best estimate levels of volatility are assumed for directly held property. The model implied volatility for 2009 is 15%.
The modelling of corporate bonds allows for credit transitions and defaults, calibrated to historic data, with an additional allowance for the credit risk premium, derived from current markets.

Operating earnings

MCEV operating earnings assume investment returns based on the one year risk-free rate at the beginning of the reporting period, plus expected returns in excess of the risk-free rate (an asset risk premium). The table below sets outs the asset risk premiums used:

	2009
Equities	2.5%
Property	2.0%
Gilts	0.0%

The return assumed on corporate bond portfolios is the redemption yield for the portfolio less an allowance for credit risk.

Expenses

Each life company's projected per policy expenses are based on existing management services agreements with the Group's service companies, adjusted to allow for additional costs incurred directly by the life companies, including, for example, regulatory fees and one-time expenses.

The life companies' projected investment expenses are based on the fees agreed with Ignis Asset Management, (or external fund managers, where appropriate), allowing for current and projected future asset mixes.

Valuation of debt and non-controlling interests

The Group's consolidated balance sheet as at 31 December 2009 includes Perpetual Reset Capital Securities with a face value of £500 million and subordinated debt with a face value of £200 million in relation to Phoenix Life Limited (ex Scottish Mutual Assurance). These listed securities have been included within the MCEV at their market value quoted at the reporting date.

The table below summarises the value of these debt obligations as at 31 December 2009.

Listed debt and non-controlling interests	2009		2008	
	Face value (including accrued interest)	Market value	Face value (including accrued interest)	Market value
Perpetual Reset Capital Securities	540	264	517	95
Phoenix Life Limited (ex Scottish Mutual Assurance) subordinated debt	211	156	211	120

Unlisted debt has been included at face value.

	2009	2008
Unlisted debt	Face value	Face value
Pearl and Impala facilities	2,760	3,085
Royal London PIK note	102	332

9. Sensitivity to assumptions

The table below summarises the key sensitivities of the MCEV of covered business at 31 December 2009:

		2009 MCEV £m
(1)	Base	4,731
(2)	1% decrease in risk-free rates	135
(3)	1% increase in risk-free rates	(167)
(4)	10% decrease in equity / property market values	(156)

(5)	100 bps increase in credit spreads[8]	(365)
(6)	25% Increase in equity / property implied volatilities	(19)
(7)	25% Increase in swaption implied volatilities	(57)
(8)	10% decrease in lapse rates and paid-up rates	(19)
(9)	5% decrease in annuitant mortality	(183)
(10)	5% decrease in non-annuitant mortality	20
(11)	Required capital equal to the minimum regulatory capital	81
(12)	Swap curve as reference rate, retaining appropriate liquidity premiums	(160)

No expense sensitivity has been shown as maintenance costs incurred by the covered business are largely fixed under the terms of agreements with the management services companies.

[8] 25 bps is assumed to relate to default risk

10. Reconciliation of pro forma Group MCEV to previously published EV

The MCEV allows for methodology changes from previously published embedded values. The methodology changes have been implemented to better align the Group's methodology with the CFO Forum principles. Details of these adjustments and methodology changes and a reconciliation to the EV at December 2008, as published in the proxy statement of 3 July 2009, are provided below.

	Note	Group
		£m
Unaudited historical pro forma net EV as disclosed in the Proxy Statement as at 31December 2008		**1,265**
Phoenix Group Holdings IFRS Net Assets at 31 December 2008		573
MCEV of Opal Re at 31 December 2008	(a)	12
Pro forma Group MCEV before methodology changes		**1,850**
Methodology changes:		
PVFP of non-covered business	(b)	(630)
Reduced liquidity premiums	(c)	(251)
Vesting annuities	(d)	65
Other changes		10
Pro forma Group MCEV at 31December 2008		**1,044**

(a) As Opal Re is now part of the Group it is included within covered business from 31 December 2008 and is valued on a basis consistent with the annuity business within the life companies.

(b) Asset management and management service companies have been excluded from the definition of covered business. Under CFO Forum principles and guidance productivity gains should not be recognised until achieved. This treatment is inconsistent with the cost profile of a closed fund where continual cost reductions are expected to maintain unit costs as the business runs off. In the opinion of the Directors, if the MCEV principles and guidance were to be applied to the asset management and the management service companies, it would not provide a fair reflection of the Group's financial position. These companies are therefore reported alongside the Group's other non-life Group companies at their IFRS net asset value.

(c) The allowance for default risk has been increased to include an explicit margin for unexpected default risk premium. This reduces the value of liquidity premiums within the MCEV. This change is to align the Group's methodology with the risk-neutral principles that form the basis of the CFO Forum's MCEV methodology.

(d) The MCEV places a value on the profits expected to be earned on annuities arising from policies vesting with guaranteed annuity terms. These policies are excluded from the definition of new business on the basis that the annuity being provided is an obligation under an existing policy and the life companies are already reserving for the cost of these guarantees.