PEARL GROUP HOLDINGS (NO. 1) LIMITED

Company Registration Number: 3524909

REPORT AND ACCOUNTS
For the year ended 31 December 2009

CONTENTS

Registered Office:

Juxon House,
100 St. Paul's Churchyard,
London,
EC4M 8BU

BOARD OF DIRECTORS

J S Moss
J S B Smith

Company Secretary

Pearl Group Secretariat Services Limited

DIRECTORS' REPORT

The directors have pleasure in presenting the Report and Accounts of Pearl Group Holdings (No. 1) Limited ("the Company") company registration number 3524909 for the year ended 31 December 2009.

Principal activity and future developments

The principal activity of the Company is that of an investment company. This will continue to be the principal activity for the foreseeable future.

Business review

Performance during 2009

The Company generated a profit after taxation for the year of £134m (2008: £1,542m).

Position as at 31 December 2009

The net assets of the Company at 31 December 2009 were £3,449m (2008: £3,322m). The increase in the year reflects shareholders' recognised gains of £127m.

Principal risks and uncertainties

The main risks facing the Company are:

- interest rate risk, since the movement in interest rates will impact the value of interest payable by the Company;
- liquidity risk, arising from insufficient liquid assets to meet payment obligations; and
- credit risk, arising from the default of the counterparty to a particular financial asset.

The Company's exposure to all these risks is monitored by the Board which agrees policies for managing each of these risks on an ongoing basis. The Company uses interest rate hedges, where appropriate to mitigate the impact of interest rate risk to the Company.

Key Performance Indicators ("KPIs")

Given the straightforward nature of the business, the Company's directors are of the opinion that analysis using KPIs is not necessary for an understanding of the development, performance or position of the business.

Material developments

On 25 March 2009, the Board of Pearl Group Holdings (No. 1) Limited gave notice to the holders of the £500m 6.5864% Fixed/Floating Rate Perpetual Reset Capital Securities ("the Notes") of its decision to defer the coupon payment on the Notes which would otherwise have been due for payment on 25 April 2009.

On 2 September 2009, the ultimate shareholders of Pearl Group Limited (subsequently renamed Pearl Group Holdings (No.2) Limited), which at the time was the Company's ultimate parent undertaking, exchanged their interests in the group for the issue of shares in Liberty Acquisition Holdings (International) Company. Following this, Liberty Acquisition Holdings (International) Company became the Company's ultimate parent undertaking and subsequently changed its name to Pearl Group. On 15 March 2010 Pearl Group changed its name to Phoenix Group Holdings.

Also on 2 September, the FSA lifted the Own Initiative Variation in Permission which it had, in 2008, imposed on those regulated entities which were subsidiaries of the Pearl Group Holdings (No.2) Limited group.

Dividends

The directors have declared and paid dividends on ordinary shares of £nil during the year ended 31 December 2009 (2008: £1,150m).

DIRECTORS' REPORT (continued)

Going concern

Having reviewed the position in light of the Financial Reporting Council Guidance from October 2009, the Directors are satisfied that the Company has adequate resources to meet its liabilities as they fall due for the foreseeable future. The Directors believe it is therefore appropriate to prepare the financial statements on a going concern basis.

Post balance sheet event

On 5 January 2010 the Company 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 the Company 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. The Company announced that this notice would be withdrawn and the 2010 coupon would be paid in full on 25 April 2010 if certain amending proposals were agreed by the Noteholders. These proposals included a reduction of 15% in the face value of the Notes, amendment of the Alternative Coupon Satisfaction Mechanism, the imposition of a restriction on the payment of coupons by Phoenix Group Holdings if future coupons are deferred, and the satisfaction in full of the deferred 2009 coupon by 31 December 2010. Both proposed coupon payments are to be based on the original nominal value of the Notes, being £500 million. These amending proposals were agreed by the Noteholders on 22 April 2010 and the 2010 coupon was paid on 26 April 2010. On 22 April 2010 PGH1 also entered into a balancing instrument under which notes with a principal amount of £75,000,000 (equal to the amount of the reduction in principal amount of the Notes) were issued to its ultimate parent company Phoenix Group Holdings. The terms of such notes are substantially the same as the terms of the Notes but they are subordinated to the Notes.

Corporate governance statement

The Board has overall responsibility for the Company's systems of internal controls and for reviewing their effectiveness.

The Company's planning and financial reporting procedures include detailed operational budgets for the year ahead and a five year rolling plan. Performance is monitored and relevant action taken throughout the year through the monthly reporting of key performance indicators (primarily cash flows), updated forecasts for the year together with information on the key risk areas.

The use of the Phoenix Group Holdings standard accounting manual by the Company ensures that transactions and balances are recognised and measured in accordance with prescribed accounting policies and that information is appropriately reviewed and reconciled as part of the reporting process.

Additional information for shareholders

The following provides the additional information required for shareholders as a result of the implementation of the Takeovers Directive into UK Law.

At 31 December 2009, the Company's issued share capital comprised:

	No ('000)	£m	% of total share capital
Ordinary shares of £0.05 each	687,810	34	100

On a show of hands at a general meeting of the Company every holder of ordinary shares present in person and entitled to vote shall have one vote and on a poll, every member present in person or by proxy and entitled to vote shall have one vote for every ordinary share held. All of the Company's issued share capital is owned by Impala Holdings Limited.

Directors

The names of the directors as at the date of this report are set out on page 3. Additional information in relation to changes in directors is as follows:

S D Huckle	Resigned 3 September 2009
H M Maxwell	Resigned 3 September 2009

DIRECTORS' REPORT (continued)

Disclosure of indemnity

Pearl Group Holdings (No. 2) Limited has agreed to provide an Indemnity to certain persons associated with that company and its subsidiaries. These persons include nominated directors and secretaries of Pearl Group Holdings (No. 2) Limited, directors and secretaries of subsidiary companies together with alternate directors and approved persons, being persons in relation to whom the Financial Services Authority has given its approval under section 59 of the Financial Services and Markets Act 2000 ("FSMA") for the performance of a controlled function. This indemnity will cover all losses, costs and expenses incurred by an indemnified person in the exercise, execution and discharge of his duties, or connected to the same, to the fullest extent permitted, consistent with the Companies Act 2006 and the FSA Rules. In addition, with effect and on from 1 March 2010, Impala Holdings Limited has also agreed to provide an Indemnity to certain persons associated with the Company. These persons include the Company's directors, secretary and approved persons. This indemnity will cover all losses, costs and expenses incurred by an indemnified person in the exercise, execution and discharge of his duties, or connected to the same, to the fullest extent permitted, consistent with the Companies Act 2006 and the FSA Rules. Both indemnities state that they do not apply to any loss suffered or incurred by an indemnified person to the extent that he is indemnified by any third party (including under any Directors & Officers liability insurance). Directors, alternate directors and company secretaries of the Company may still benefit from the provisions of an earlier Deed of Indemnity entered into by the Company.

Disclosure of information to auditors

So far as each of the directors is aware, there is no relevant audit information (as defined in the Companies Act 2006) of which the Company's auditors are unaware, and each of the directors has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information (as defined) and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 (2) of the Companies Act 2006.

Reappointment of auditors

In accordance with section 487 of the Companies Act 2006, the Company's auditors, Ernst & Young LLP, will be deemed to have been reappointed at the end of the period of 28 days following circulation of copies of these accounts as no notice has been received from members pursuant to section 488 of the Companies Act 2006 prior to the end of the accounting reference period to which these accounts relate.

By order of the directors

Jonathan Moss
16 June 2010

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Directors Report and the accounts in accordance with applicable law and regulations.

Company law requires the directors to prepare accounts for each financial year. Under that law the directors have elected to prepare the accounts in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the accounts comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PEARL GROUP HOLDINGS (NO. 1) LIMITED

We have audited the Company accounts ("the accounts") of Pearl Group Holdings (No. 1) Limited for the year ended 31 December 2009 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet and the related notes 1 to 21. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 7, the directors are responsible for the preparation of the accounts and for being satisfied that they give a true and fair view. Our responsibility is to audit the accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the accounts

An audit involves obtaining evidence about the amounts and disclosures in the accounts sufficient to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the accounts.

Opinion

In our opinion the accounts:

- give a true and fair view of the state of the company's affairs as at 31 December 2009 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the accounts are prepared is consistent with the accounts.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the accounts are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

George M Reid

George M Reid (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
23 June 2010

PROFIT AND LOSS ACCOUNT
For the year ended 31 December 2009

	Notes	2009 £m	2008 £m
Investment income	1	237	673
Administrative expenses		(5)	(71)
Investment expenses and charges	2	(45)	(109)
Profit on ordinary activities before exceptional items and taxation		187	493
Non-operating exceptional items	6	-	1,043
Profit on ordinary activities before taxation		187	1,536
Tax (charge)/credit on profit on ordinary activities	7	(53)	6
Profit on ordinary activities after taxation		134	1,542

All activities relate to continuing operations.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
For the year ended 31 December 2009

	Notes	2009 £m	2008 £m
Profit for the financial year		134	1,542
Actuarial losses on pension scheme	13	(10)	(4)
Tax credit in respect of actuarial losses on pension scheme		3	1
Shareholders' recognised gains arising in the year		127	1,539

BALANCE SHEET
At 31 December 2009

	Notes	2009 £m	2008 £m
Fixed assets			
Investments in group undertakings	9	3,348	3,186
Current assets			
Debtors	10	144	129
Investments	11	134	71
Cash at bank and in hand		2	-
		280	200
Creditors: amounts falling due within one year	12	(191)	(83)
Net current assets		89	117
Net assets excluding pension asset		3,437	3,303
Pension asset	13	12	19
Net assets		3,449	3,322
Capital and reserves			
Ordinary share capital	14	34	34
Share premium account	15	1,541	1,541
Perpetual reset capital securities	15/17	497	497
Profit and loss account	15	1,377	1,250
Shareholders' funds attributable to equity interests	15	3,449	3,322

The accounts were approved by the directors on 16 June 2010 and were signed on their behalf by:

Jonathan Moss
Director

ACCOUNTING POLICIES

Basis of presentation

The accounts have been prepared in accordance with applicable accounting standards and under the historical cost convention rules except for derivative financial instruments which have been measured at fair value.

Investment income, realised and unrealised gains and losses on investments

Interest income is recognised as the interest accrues using the effective yield method.

Dividends are included as investment income on receipt of payment.

Realised gains and losses on investments are calculated as the difference between the net sales proceeds and original cost. Unrealised gains and losses on investments represent the difference between the valuation of investments at the balance sheet date and their original cost, or if they have been previously revalued, the valuation at the last balance sheet date. The movement in unrealised gains and losses recognised in the period also includes the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

Perpetual Reset Capital Securities

The Perpetual Reset Capital Securities meet the definition of equity for accounting purposes. Accordingly, they are shown at the proceeds of issue and the coupons on the securities are recognised on the date of payment and are charged directly to equity holders' funds.

Dividends

Dividends on equity shares are recognised when they become a legal liability. For dividends declared by equity holders this is the date of declaration and for dividends declared by the directors this is on the date of payment.

Fixed asset investments

Fixed asset investments consist of loans to parent and group undertakings and are valued at amortised cost.

Taxation

The UK taxation in the profit and loss account is based on profits/(losses) and income in the year as determined in accordance with the relevant tax legislation, together with adjustments to provisions of prior years.

The Company recognises deferred tax assets and liabilities on a discounted basis to reflect the time value of money. A discount rate has been selected that reflects the yield on government bonds which have a maturity date similar to the likely average period for assets upon which deferred tax liabilities and assets arise. Deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date with the exception of deferred tax assets which are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax on changes in the fair value of investments is recognised in the profit and loss account.

Derivative financial instruments

The Company uses derivative financial instruments, where appropriate, to hedge against interest rate risk. Derivative financial instruments are classified as held for trading and carried at fair value as assets or liabilities. Fair values are based on quoted market prices or valuation techniques as appropriate. Changes in fair values are recognised in the profit and loss account. Derivative financial instruments include swaps which derive their value mainly from underlying interest rates.

ACCOUNTING POLICIES (CONTINUED)

Fair value estimation

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 balance sheet date. The quoted market price used for financial assets is the current bid price. The fair value of investments that are not traded in an active market is determined using valuation techniques. Various valuation techniques are used including the use of comparable recent arm's length transactions, discounted cashflow analysis, option pricing models and other valuation techniques commonly used by market participants.

Collateral

The Company receives collateral in the form of cash in respective of derivative contracts in order to reduce the risk of these transactions. Collateral received in the form of cash, where the Company has contractual rights to receive the cash flows generated, is recognised as an asset in the balance sheet with a corresponding liability for its repayment.

Cash flow statement

The Company has taken advantage of the exemption given by FRS1 (revised 1996) to subsidiary undertakings where 90% or more of the voting rights are controlled within the group, by not preparing a cash flow statement. Details of the ultimate holding company are given in note 19 to the accounts.

Pension scheme benefits

The Company provides certain employees with retirement benefits through both defined benefit and defined contribution plans. The assets of these plans are generally held separately from the Company's general assets in trustee-administered funds and are valued at fair value. Defined benefit obligations and the cost of providing benefits are determined annually by qualified actuaries using the projected unit credit method. The obligation is measured as the present value of the estimated future cash outflows using a discount rate based on corporate bonds of appropriate duration and quality. The resulting recoverable surplus/deficit of defined benefit assets less liabilities is recognised in the balance sheet. The Company's expense related to these plans is accrued over the employees' service periods based upon the actuarially determined cost for the period. Actuarial gains and losses are recognised in full in the period in which they occur in the statement of total recognised gains and losses. Contributions to the defined contribution scheme are charged to the profit and loss account as they become payable in accordance with the rules of the scheme.

The net surplus and the movement in the surplus are currently allocated in the ratio 26:74 (2008: 37:63) between the Company and a fellow subsidiary undertaking of Impala Holdings Limited, Pearl Group Management Services Limited, the joint sponsoring employers of the pension scheme. The net surplus comprises the surplus in the defined benefit scheme after deducting the amount that cannot be recovered (the irrecoverable surplus) through reduced contributions in the future or from refunds from the scheme that have been agreed by the trustees.

The pension asset shown in the balance sheet comprises the surplus net of the associated deferred tax liability.

Other defined benefit post-employment benefits, such as medical care and life insurance, are also provided for certain employees. The cost of such benefits is accrued over the service period of the employee based upon the actuarially determined cost for the period using a methodology similar to that for defined benefit pension plans.

Segmental analysis

The Company operates a single class of business which is undertaken solely in the United Kingdom.

NOTES TO THE ACCOUNTS

1. Investment income

	2009 £m	2008 £m
Dividends from subsidiary undertakings	-	507
Interest receivable on loans to group companies	192	77
Other interest receivable	1	17
Swap interest receivable	36	1
Unrealised gain on investments	8	71
	237	673

2. Investment expenses and charges

	2009 £m	2008 £m
Interest payable on loans from group companies	-	28
Other interest payable	-	6
Swap interest payable	36	1
Unrealised losses on investments	8	72
Net expected charge on pension assets (see note 13)	1	2
	45	109

3. Auditors' remuneration

The remuneration receivable by the Company's auditors for auditing the accounts amounted to £69,000 (2008: £69,000). Auditor's remuneration for the current year was borne by Impala Holdings Limited.

4. Employee information

The Company has no employees. Services are provided by Pearl Group Management Services Limited and Pearl Group Services Limited.

5. Directors' emoluments

	2009 £'000	2008 £'000
Emoluments (excluding pension contributions and awards under share option schemes and other long-term incentive schemes)	2,441	4,160
Contributions to money purchase schemes	52	176
Awards (other than shares and share options) receivable during the year under long term incentive schemes	-	6,783
Compensation to former directors for loss of office	-	1,235
Number of directors who:		
- are members of a defined benefit pension scheme	1	1
- are members of a money purchase pension scheme	3	6
- exercised share options	-	3

NOTES TO THE ACCOUNTS (CONTINUED)

5. Directors' emoluments (continued)

	2009 £'000	2008 £'000
Highest paid director's remuneration:		
Aggregate amount of emoluments and cash awards under long-term incentive schemes (excluding pension contributions, share options gains and share awards arising from long-term incentive schemes)	1,024	2,335
Contributions to money purchase pension schemes	14	12

The emoluments disclosed in the notes to these accounts are in respect of the directors with qualifying services for the Phoenix Life Holdings Limited group of companies for the period from 1 January 2009 to 1 September 2009 and the Phoenix Group Holdings group of companies for the period from 2 September 2009 to 31 December 2009 and for those directors comprise their total emoluments in respect of services to these groups. These total emoluments have also been included in each of the other companies of the above groups for which the director has qualifying services.

6. Non-operating exceptional items

On 31 December 2008 the Company disposed of the entire issued share capital of its investments in subsidiary undertakings to Impala Holdings Limited for a total consideration of £2,606m. The consideration comprised the assumption by Impala Holdings Limited of £764m of loans and associated accrued interest payable by the Company to other group undertakings with the balance of £1,842m left outstanding as an interest bearing intra-group loan (see note 9). A profit on disposal of £1,043m was recognised.

7. Taxation

	2009 £m	2008 £m
The charge/(credit) for taxation in the profit and loss account comprises:		
UK Corporation tax:		
Current tax charge/(credit) for the year	41	(6)
Adjustments in respect of prior periods	12	1
Total current tax charge/(credit)	53	(5)
Deferred taxation:		
Origination and reversal of timing differences	-	(1)
Total tax charge/(credit)	53	(6)

NOTES TO THE ACCOUNTS (CONTINUED)

7. Taxation (continued)

UK corporation tax for the current year in the profit and loss account is more than the standard rate of 28% (2008: less than 28.5%) due to the items set out in the reconciliation below:

	2009 £m	2008 £m
Profit on ordinary activities before taxation	187	1,536
Tax at 28% (2008: 28.5%)	52	438
Factors affecting charge:		
Non-deductible expenses	-	8
Subsidiary undertakings dividends not taxable	-	(145)
Non-operating exceptional items	-	(297)
Adjustment for share scheme	-	(1)
Corporation tax adjustments in respect of prior periods	12	1
Movement in unprovided deferred tax	(11)	-
Other	-	(9)
Current tax charge/(credit) for the year	53	(5)

8. Dividends

	2009 £m	2008 £m
Interim ordinary paid dividends: nil (2008: 167p) per £0.05 share	-	1,150

9. Investments in group undertakings

Loans to parent and group undertakings	2009 £m	2008 £m
At 1 January	3,186	897
Issue of loans	188	2,690
Repayment of loans	(26)	(401)
At 31 December	3,348	3,186

NOTES TO THE ACCOUNTS (CONTINUED)

9. Investments in group undertakings (continued)

a) On 1 August 2008 the Company provided a loan to Impala Holdings Limited of £736m. The loan accrues interest at six month LIBOR plus 2.94% which is capitalised half yearly on 7 April and 7 October. Interest of £53m (2008: £12m) was capitalised during the year. The loan has a maturity date of December 2016.

b) On 4 December 2008 the Company provided a loan to Pearl Life Holdings Limited of £55m. The loan accrues interest at six month LIBOR plus 2.94% which is capitalised half yearly on 7 April and 7 October. Interest of £3m (2008: £nil) was capitalised during the year. The loan has a maturity date of December 2016 or can be repaid as agreed between the borrower and the Company.

c) On 26 September 2008 the Company provided a loan to Pearl Life Holdings Limited of £45m. The loan accrues interest at 12 month LIBOR plus 2.00% which is capitalised annually on 31 December. Interest of £3m (2008: £nil) was capitalised during the year. The loan has a maturity date of December 2016 or can be repaid as agreed between the borrower and the Company.

d) On 31 December 2008 the Company disposed of the entire issued share capital of its investments in subsidiary undertakings to Impala Holdings Limited. £1,842m was left outstanding as an interest bearing intra-group loan. The loan accrues interest at 6 month LIBOR plus 3.42% which is capitalised half yearly on 30 June and 31 December. During the year, Impala Holdings Limited made repayments totalling £26m and interest of £103m (2008: £nil) was capitalised. The loan is repayable upon demand but has a maturity date of December 2016.

e) At 31 December 2009, the balance of the £2,943m loan facility issued to Pearl Life Holdings Limited on 31 August 2006 remains at £7m (2008: £7m). The loan is repayable on demand.

f) In September 2007, the Company granted a revolving credit facility of £110m to Pearl Group Management Services Limited. During the year £26m has been drawn down (2008: £30m) and as at 31 December 2009 the total drawn down balance is £56m. Interest is calculated at six month LIBOR plus 2.00%. Repayment of the loan is subject to a number of detailed provisions.

g) In November 2005, the Company granted a loan of £459m to Pearl Life Holdings Limited. Interest is calculated at 7% per annum and is payable annually on 31 December. The loan is repayable on demand.

10. Debtors

	2009 £m	2008 £m
Amounts owed by group undertakings	136	125
Deferred tax debtor	1	1
Other debtors	7	3
	144	129

Included in amounts owed by group undertakings are loans of £88m (2008: £98m). During 2008, the Company entered into an agreement with Impala Holdings Limited and Pearl Life Holdings Limited whereby from 1 May 2008, any of those parties could lend to or borrow from each other as agreed. As at 31 December 2009, under this agreement, the Company has lent £29m (2008: £32m) to Pearl Life Holdings Limited and £59m (2008: £66m) to Impala Holdings Limited. Interest on these loans accrues at six month LIBOR plus 2.94% which is capitalised half yearly on 7 April and 7 October.

All debtors, with the exception of deferred tax, are expected to be recovered within 12 months.

NOTES TO THE ACCOUNTS (CONTINUED)

11. Investments

	2009 £m	2008 £m
Derivative assets	63	71
Other investments	71	-
	134	71

Derivative assets comprise the fair value of the £1,130m variable to fixed interest rate swaps entered into during 2008.

The derivative assets are categorised as level 2 financial instruments as their fair value is determined using a valuation technique based on observable market data at the year end.

The other investments are categorised as level 1 financial instruments as their fair value is based on quoted market prices at the year end.

12. Creditors: amounts falling due within one year

	2009 £m	2008 £m
Derivative liabilities	64	72
Amounts owed to group undertakings	46	2
Other creditors	3	2
Tax payable	8	7
Collateral creditors	70	-
	191	83

Derivative liabilities comprise the fair value of the £1,130m fixed to variable interest rate swaps entered into during 2008.

The derivative liabilities are level 2 financial instruments as their fair value is determined using a valuation technique based on observable market data at the year end.

13. Staff pension scheme

(a) Defined contribution scheme

The Company participates in the defined contribution section of the PGL Pension Scheme (formerly the Resolution Group Pension Scheme) ('the Scheme'). The Company did not make any contributions to this section in the year ended 31 December 2009 or 2008.

(b) Defined benefit scheme

The Company and a fellow subsidiary undertaking of Impala Holdings Limited, Pearl Group Management Services Limited, are joint sponsoring employers of the Scheme. The defined benefit section of the 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 Scheme in 2006) to future service accrual.

The valuation has been based on an assessment of the liabilities of the 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 Company's share in the net surplus before tax of the pension Scheme amounts to £16m (2008: £26m).

NOTES TO THE ACCOUNTS (CONTINUED)

13. Staff pension scheme (continued)

The principal financial assumptions of the Scheme are set out below.

	2009	2008
Rate of general long term increase in salaries	4.6%	3.9%
Rate of increase in pensions	3.5%	2.8%
Discount rate	5.7%	6.3%
Inflation	3.6%	2.9%
Expected rate of return on Scheme assets	5.4%	4.6%

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 Scheme liabilities. This method results in an equivalent single rate for both the discount and inflation rates, which is derived from the profile of projected benefit payments.

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 amounts recognised in the profit and loss account are as follows:

	2009 £m	2008 £m
Current service cost	(2)	(3)
Interest cost	(21)	(22)
Expected return on Scheme assets	20	20
	(3)	(5)

The amounts recognised in the statement of total recognised gains and losses are as follows:

	2009 £m	2008 £m
Actuarial losses	(10)	(4)

The net actuarial losses recognised during the year comprise the following:

	2009 £m	2008 £m
Actual return less expected return on Scheme assets	(9)	8
Experience gains/(losses) arising on Scheme liabilities	5	(2)
Changes in assumptions underlying Scheme liabilities	(80)	64
	(84)	70
Decrease/(increase) in irrecoverable surplus	74	(74)
	(10)	(4)

The cumulative net actuarial losses recognised in the statement of recognised income and expense since 1 January 2004 amounts to £19m (2008: £9m).

NOTES TO THE ACCOUNTS (CONTINUED)

13. Staff pension scheme (continued)

The amounts recognised in the balance sheet are as follows:

	2009 £m	2008 £m
Fair value of Scheme assets	307	423
Present value of defined benefit obligation	(291)	(323)
Surplus	16	100
Less: Irrecoverable surplus	-	(74)
Net surplus	16	26
Deferred tax	(4)	(7)
	12	19

The irrecoverable surplus is the amount that cannot be recovered through reduced contributions in the future or from refunds from the Scheme that have been agreed by the trustees.

The actual return on the Scheme assets comprises the following:

	2009 £m	2008 £m
Expected return on Scheme assets	20	20
Actuarial (losses)/gains on Scheme assets	(9)	8
	11	28

The Company employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The assumed long-term rate of return on each asset class is set out within this note. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the benchmark asset allocation for the Scheme.

The change in the present value of the defined benefit obligation is as follows:

	2009 £m	2008 £m
At 1 January	323	389
Effect of changes in allocations between sponsoring employers	(112)	(13)
Current service cost	2	3
Interest cost	21	22
Actuarial gains/(losses)	75	(62)
Benefits paid	(18)	(16)
At 31 December	291	323

The defined benefit obligation arises from plans that are wholly funded.

The change in the fair value of the Scheme assets is as follows:

	2009 £m	2008 £m
At 1 January	423	419
Effect of changes in allocations between sponsoring employers	(112)	(13)
Expected return on Scheme assets	20	20
Actuarial (losses)/gains on Scheme assets	(9)	8
Contributions by the employer	3	5
Benefits paid	(18)	(16)
At 31 December	307	423

NOTES TO THE ACCOUNTS (CONTINUED)

13. Staff pension scheme (continued)

The distribution of the Scheme assets at the end of the year was as follows:

	2009 £m	2008 £m
Bonds	272	370
Properties	29	46
Cash	6	7
	307	423

Contributions totalling £3m are expected to be paid into the Scheme in 2010.

Table of historical information:	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Fair value of Scheme assets	307	423	419	387	390
Defined benefit obligation	(291)	(323)	(389)	(357)	(356)
	16	100	30	30	34
Less: Irrecoverable surplus	-	(74)	-	-	-
Net surplus	16	26	30	30	34
Experience (losses)/gains on Scheme assets	(9)	8	(4)	(6)	32
Experience gains/(losses) on Scheme liabilities	5	(2)	(3)	2	(1)

14. Share capital

	2009 £m	2008 £m
Issued and fully paid		
Equity shares:		
687,809,559 (2008: 687,809,559) ordinary shares of £0.05 each	34	34

The Company's Articles of Association contain a restriction on the number of shares that may be allotted.

NOTES TO THE ACCOUNTS (CONTINUED)

15. Reserves and reconciliation of movements in shareholders' funds

	Share capital £m	Share premium £m	Perpetual reset capital securities £m	Other reserves – share options £m	Profit & loss account £m	Total shareholders' funds £m
Shareholders' funds at 1 January 2008	34	1,537	497	5	901	2,974
Profit for the financial year 2008	-	-	-	-	1,542	1,542
Actuarial losses on pension Scheme	-	-	-	-	(4)	(4)
Tax on items taken directly to equity	-	-	-	-	1	1
Dividends (note 8)	-	-	-	-	(1,150)	(1,150)
Coupon paid on perpetual reset capital securities	-	-	-	-	(33)	(33)
Re-purchase of share options	-	-	-	(5)	(7)	(12)
Issue of ordinary share capital – share option schemes	-	4	-	-	-	4
Shareholders' funds at 31 December 2008	34	1,541	497	-	1,250	3,322
Profit for the financial year 2009	-	-	-	-	134	134
Actuarial losses on pension Scheme	-	-	-	-	(10)	(10)
Tax on items taken directly to equity	-	-	-	-	3	3
Shareholders' funds at 31 December 2009	34	1,541	497	-	1,377	3,449

The profit and loss account of the Company at 31 December 2009 includes £1,055m which is non-distributable (2008: £1,062m).

16. Share options

There were no share-based payment arrangements during the year. The acquisition of the Company by Impala Holdings Limited on 1 May 2008 triggered vestings across the share schemes operated by the Company at the time. The Company has not launched any new share-based payment arrangements since this date and therefore all information provided below has no impact on the results or position of the Company in 2009.

For share options granted before 7 November 2002, the recognition and measurement principles of FRS 20 *Share-based Payment* have not been applied, as permitted by the transitional provisions in FRS 20.

The weighted average share price of the Company's shares in the period 1 January 2008 to the date of acquisition of the Company by Impala Holdings Limited amounted to 698.0p.

The total payments for 2008 arising from share-based payment transactions were £24m, of which £5m related to equity-settled share-based payments and £19m to cash-settled share-based payments.

In addition, the Company compensated SAYE option holders in cash for the loss of benefit in respect of lapsed share options and bore the cost of income tax and national insurance that would otherwise have fallen on option holders from the early vesting of the share option schemes. The cost of this to the Company in 2008 was £4m before tax relief.

The share option equity reserve at 31 December 2009 was £nil (2008: £nil).

NOTES TO THE ACCOUNTS (CONTINUED)

17. Perpetual Reset Capital Securities

	2009 £m	2008 £m
At 1 January and 31 December	497	497

The Company had in issue £500m 6.5864% Fixed/Floating Rate Perpetual Reset Capital Securities ("the Notes") which are admitted to the Official List of the UK Listing Authority and to trading on the London Stock Exchange. The proceeds of the issue amounted to £497m.

The Notes are unsecured obligations of the Company and are subordinate to the claims of senior creditors. Payments in respect of the Notes are conditional upon the Company 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 the Company; 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 Financial Services Authority.

The Notes may be redeemed at par at the option of the Company on the first reset date of 25 April 2016 or on any coupon payment date thereafter. Redemption is subject to the agreement of the Financial Services Authority. In certain circumstances the Company 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 finance providers of the Phoenix Group was required to enable the payment of Coupons due in 2010.

If the Company opts to defer a coupon payment, then it has the option to either leave the coupon outstanding or satisfy the deferred coupon payment by the issue of securities ('ACSM instruments') by either the Company or a special purpose subsidiary of the Company established for the purpose of issuing ACSM instruments and which are guaranteed by the Company. The obligations of the Company 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 the Company in a winding up and shall comply with the then current requirements of the Financial Services Authority 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 Pearl Group Holdings (No. 2) Limited is required to use its best endeavours to raise such funds as are deemed necessary to purchase the required amounts of ACSM instruments. Post the restructuring set out in note 21 the operation of the ACSM has subsequently been amended.

For so long as a deferred coupon payment has not been satisfied the Company and, post the restructuring set out in note 21, its ultimate parent Phoenix Group Holdings may not declare, pay or distribute a dividend or make a payment on any of its securities in issue ranking junior to the Notes, including the ordinary shares of the Company (and Phoenix Group Holdings) 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 Company gave notice to the holders of the Notes of its decision to defer the coupon payment at the next payment date of 25 April 2009. Post the restructuring set out in note 21 it was agreed that the deferred 2009 coupon would be settled in full by 31 December 2010 through the operation of the amended ACSM.

NOTES TO THE ACCOUNTS (CONTINUED)

18. Related party transactions

The Company has taken advantage of the exemption given by FRS 8 to subsidiary undertakings, 100% or more of whose voting rights are controlled within the Phoenix Group, by not disclosing information on related party transactions with entities that are part of this group, or investees of this group qualifying as related parties.

All major decisions are made by the Board therefore there are no transactions with key management personnel to disclose other than in the directors' emoluments note.

19. Parent undertaking

The Company's immediate parent undertaking is Impala Holdings Limited.

Prior to 2 September 2009 the Company's ultimate parent undertaking was Pearl Group Holdings (No.2) Limited. Subsequent to this date, the ultimate parent undertaking became Phoenix Group Holdings whose registered office is c/o Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104 Cayman Islands and is the parent undertaking of the smallest and largest group to consolidate these accounts. A copy of the accounts of Phoenix Group Holdings can be obtained from the Company Secretary, 1st Floor, 32 Commercial Street, St Helier, Jersey, JE2 3RU.

20. Pension scheme guarantee

The Company has guaranteed the performance by another group undertaking, Pearl Life Holdings Limited, of a guarantee given by Pearl Life Holdings Limited to the trustees of the PGL Pension Scheme (formerly known as the Resolution Group Pension Scheme) ('the Scheme') in respect of the obligations and liabilities of the participating employers to make payments to the Scheme. The principal obligations that are subject to the guarantee are cash contributions totalling £37.5m, which are payable in instalments over the period to June 2012.

21. Post balance sheet event

On 5 January 2010 the Company 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 the Company 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. The Company announced that this notice would be withdrawn and the 2010 coupon would be paid in full on 25 April 2010 if certain amending proposals were agreed by the Noteholders. These proposals included a reduction of 15% in the face value of the Notes, amendment of the Alternative Coupon Satisfaction Mechanism, the imposition of a restriction on the payment of coupons by Phoenix Group Holdings if future coupons are deferred, and the satisfaction in full of the deferred 2009 coupon by 31 December 2010. These amending proposals were agreed by the Noteholders on 22 April 2010 and the 2010 coupon was paid on 26 April 2010. Both proposed coupon payments are to be based on the original nominal value of the Notes, being £500 million.

On 22 April 2010 PGH1 also entered into a balancing instrument under which notes with a principal amount of £75,000,000 (equal to the amount of the reduction in principal amount of the Notes) were issued to its ultimate parent company Phoenix Group Holdings. The terms of such notes are substantially the same as the terms of the Notes but they are subordinated to the Notes.