23 March 2012

PHOENIX GROUP REPORTS STRONG 2011 FINANCIAL RESULTS, WITH OPERATING CASHFLOWS OF £810 MILLION

Phoenix Group, the UK's largest specialist closed life fund consolidator, today announces full year results for the year ending 31 December 2011.

Financial Highlights

- Operating companies' cash generation at £810 million (2010: £734m), above the mid-point of the £750 - £850 million target range
- Resilient Market Consistent Embedded Value ('MCEV') of £2,118 million (2010: £2,104m)
- £165 million of incremental MCEV delivered, ahead of £100 million average annual target
- Strong Group IFRS operating profit of £387 million (2010: £373m)
- Group assets under management of £72.1 billion (2010: £69.6bn)
- Gearing reduced to 46%, ahead of 50% target (2010: 52%)
- 21p final dividend per share recommended, total 42p for 2011 (2010: 42p)

Operational Highlights

- Life company structure further streamlined, enabling the Group to benefit from increased efficiencies
- Over 2 million live policies now transferred onto new BaNCS administration system
- Investment and distribution teams strengthened at Ignis, leading to above benchmark investment performance and an increase in net new third party assets to £1.7 billion

Financial Targets

- £500-600 million target for 2012 operating companies' cash generation
- Operating companies' cash generation target for 2011-2016 of £3.2 billion
- Incremental MCEV target of £100 million p.a. on average between 2011-2014
- Gearing target of 43% or below by the end of 2012

Commenting on the results, Group CEO, Clive Bannister said:

"Phoenix has continued to make considerable progress in 2011, despite the volatile market conditions. We have achieved or exceeded all of our 2011 financial targets including cash generation, gearing and MCEV enhancement, demonstrating the resilience of the Phoenix business model.

"We have a clear strategy to harvest value for our shareholders through the release of the stable long term cashflows inherent within the business. The generation of £810 million of cash, above the mid-point of our target range, and our improved group capital position reinforces our confidence in our ability to progress discussions with our lenders, as we look to align the maturity of our debt to the profile of our long term cashflows."

Presentation

There will be a presentation for analysts and investors today at 9.30 am (GMT) at:

Deutsche Bank, Winchester House, 1 Great Winchester Street, London, EC2N 2DB.

A link to a live webcast of the presentation, with the facility to raise questions, and a copy of the presentation will be available at www.thephoenixgroup.com

A replay of the presentation will also be available through the website.

Participants may also dial in as follows:

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Notes

1. Phoenix Group is the UK's largest specialist consolidator of closed life funds with approximately six million customers and over £72 billion of assets under management.
2. Gearing is calculated as net shareholder debt as a percentage of the sum of Group MCEV, net shareholder debt and the present value of future profits of Ignis. Net shareholder debt is shareholder debt (including hybrid debt) less Holding Company cash and cash equivalents.
3. Operating companies' cash generation is a measure of cash and cash equivalents, remitted by the Group's operating subsidiaries to the Holding Companies and is available to cover dividends, bank interest and other items.
4. The recommended final dividend of 21p per share is expected to be paid on 8 May 2012, subject to compliance with the processes set out in the Group's main credit facilities and shareholder approval at Phoenix Group Holdings' AGM. The ordinary shares will be quoted ex-dividend on the London Stock Exchange as of 4 April 2012. The record date for eligibility for payment will be 10 April 2012. The Company will be also offering a scrip dividend alternative, details of which will be made available to shareholders shortly.

5. 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 2011. The Ernst & Young Accountants LLP audit opinion on the Phoenix Group Holdings accounts is unqualified. The Annual Report & Accounts of Phoenix Group Holdings will be published on 28 March 2012 in advance of the Annual General Meeting on 3 May 2012.

6. This announcement in relation to Phoenix Group Holdings and its subsidiaries (the 'Group') contains, and we may make other statements (verbal or otherwise) containing, forward-looking statements about the Group's current plans, goals and expectations relating to future financial conditions, performance, results, strategy and/or objectives.

   Statements containing the words: 'believes', 'intends', 'expects', 'plans', 'seeks', 'targets', 'continues' and 'anticipates' or other words of similar meaning are forward-looking. Forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group's control. For example, certain insurance risk disclosures are dependent on the Group's choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that we have estimated.

   Other factors which could cause actual results to differ materially from those estimated by forward-looking statements include but are not limited to: domestic and global economic and business conditions; asset prices; market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally; the policies and actions of governmental and/or regulatory authorities, including, for example, new government initiatives related to the financial crisis and the effect of the European Union's "Solvency II" requirements on the Group's capital maintenance requirements; the impact of inflation and deflation; market competition; changes in assumptions in pricing and reserving for insurance business (particularly with regard to mortality and morbidity trends, gender pricing and lapse rates); the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; risks associated with arrangements with third parties, including joint ventures; inability of reinsurers to meet obligations or unavailability of reinsurance coverage; 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.

   As a result, the Group's actual future financial condition, performance and results may differ materially from the plans, goals and expectations set out in the forward-looking statements within this announcement. The Group undertakes no obligation to update any of the forward-looking statements contained within this announcement or any other forward-looking statements it may make. Nothing in this announcement should be construed as a profit forecast.

PHOENIX GROUP HOLDINGS
ANNUAL REPORT AND ACCOUNTS 2011

Introduction

Business overview
Phoenix Group is the UK's largest specialist closed life and pension fund consolidator with approximately 6 million policyholders and in excess of £72 billion of assets under management.

As a closed life fund consolidator Phoenix Life focuses on the efficient run-off of existing policies, maximising economies of scale and generating capital efficiencies through operational improvements. Ignis Asset Management focuses on delivering strong investment performance and high quality service to its clients.

The Group's strength derives from the combination and leverage of both the Phoenix Life and Ignis Asset Management businesses.

Our business model
Our business manages closed life funds in an efficient and secure manner, protecting and enhancing policyholders' interests whilst maximising value for the Group's shareholders.

Phoenix Life
Aims to deliver innovative financial management and operational excellence

Ignis Asset Management
Targets superior investment performance, client service and operational efficiency

Phoenix Group
Delivery of strategic initiatives

Contents

2011 Key performance indicators

£810m
Operating companies' cash generation

42p
Dividend per share

£2,118m
Group MCEV

£72.1bn
Group assets under management

£387m
Group IFRS operating profit

£46m
Asset management IFRS operating profit

£1.3bn
IGD surplus (estimated)

46%
Gearing ratio

£3.1bn
IGD Excess Capital (estimated)

CHAIRMAN’S STATEMENT

Phoenix Group has enjoyed another year of successful delivery against our targets. We achieved our target range for cash flow generation, delivered substantial additional value through management actions and continued to delever the Group’s capital structure.

These achievements were realised in the face of considerable market uncertainty and volatility during the second half of 2011, demonstrating the resilience of the Group and its ability to manage prudently risk and capital.

I am pleased to report to shareholders that this performance has led the Board to recommend a final dividend of 21p per share, bringing the total dividend for the financial year to 42p per share. Shareholders may again elect to receive their dividends as scrip.

Since the Premium Listing in 2010, which was a major step forward for Phoenix, there has been no diminution in the level of activity undertaken by the Group. We have continued to develop our operating platform for the management of our closed life funds in order to deliver greater efficiency, flexibility and resilience in the face of significant changes in economic and regulatory environments. The development of ‘The Phoenix Way’ provides us with a consistent methodology for the structuring, integration and management of closed life funds. In addition, Ignis has made significant progress towards becoming a high performing asset management business, providing above benchmark investment performance for our policyholders and developing an attractive proposition for third party clients.

The Group remains focused on our responsibilities to our 6 million customers, and our custodianship of policyholder assets. The progress of the Group, in conjunction with our outsourced partners, to improve customer service and outcomes has continued and will remain a top priority.

2011 was the first complete year for Phoenix as a Premium Listed company and a FTSE participant. Details of the Board’s activities are contained in the Corporate Governance Report. I am pleased to report that an independent Board Evaluation undertaken towards the end of 2011 concluded that the Phoenix Board is functioning well and that the quality of the directors and the level of boardroom debate have improved substantially in the last two years.

In December 2011, we announced that Jonathan Yates, Group Finance Director, would be leaving the Group to pursue another opportunity. On behalf of the Board, I should like to express our thanks to Jonathan for his contribution to the Group and we wish him well for the future. We will announce his replacement once the Board has concluded the selection process.

Turning to my own future within the Group, I have indicated my intention to retire from the Board during the course of 2012, once a suitable successor has been identified. Whilst the journey is by no means complete, Phoenix is now well positioned for the next stage of its development and I have decided that it is the right time to pass on the baton. Having made this decision, I feel it appropriate to give my Board colleagues ample notice of my intention to retire so that the process for the appointment of my successor can start immediately and with no time pressure to complete that task.

During the course of 2011, we announced that we had been approached by a number of parties regarding a possible transaction with the Group. These approaches were unsolicited and did not lead to any formal offers being made. They did not distract us from continuing to work towards our vision of being the saver-friendly, ‘industry solution’ for the safe, innovative and profitable management of closed life funds and a leading asset management business.

I remain confident that given our strategy, the capabilities of our people and our performance to date, we can deliver this vision and in so doing, create significant value for our shareholders.

The scale and predictability of the Group’s cash flows underpin our ability to harvest value for our shareholders. This cash flow has allowed us to make further progress in delevering the Group’s capital structure during 2011 and, in due course, we expect that we will put in place new banking arrangements to provide the Group with the long-term capital structure that meets our strategic objectives and allows the fulfilment of the Group’s vision.

In a challenging year for financial markets, Phoenix Group has demonstrated its resilience and is well positioned for the future. On behalf of the Board, I should like to thank all of our employees for their contribution to the Group’s success in 2011.

Ron Sandler
Chairman

22 March 2012

GROUP CHIEF EXECUTIVE OFFICER’S REPORT

Phoenix has continued to make considerable progress in 2011, despite volatile market conditions, and has a clear strategy to deliver shareholder value.

Introduction

At the end of my first year as Group Chief Executive Officer, I am able to look back at 12 months of substantial achievement. The effective combination of the closed life fund business of Phoenix Life and the asset management capability of Ignis has proven itself able to create value in challenging market environments. We have continued to develop Phoenix's business model and through 'The Phoenix Way' we have created a template that can be used to integrate additional closed life funds in the future.

Despite the volatile investment markets, Phoenix Life and Ignis have provided strong customer service and investment returns and we continue to work with our outsourced partners to improve our proposition for policyholders.

Reterming our debt is our top priority in terms of corporate activity, as we look to align our debt profile to our longer term cash flows. The more tranquil market conditions since year end, and the improvements in our cash position and in our IGD headroom during 2011, reinforce our confidence in our ability to progress these reterming discussions.

Group highlights

In 2011, Phoenix Group achieved or exceeded its three financial operating targets, as set out last year. In particular, we generated cash flows of £810 million from our operating companies, compared with a target range of between £750 million and £850 million. This demonstrates the organic cash generative nature of our business model, even in difficult macroeconomic conditions, and has also allowed us to reduce our gearing ratio at the end of 2011 to 46%, well ahead of our previous target of less than 50%. We are targeting a further reduction to 43% or below by the end of 2012.

Our year end MCEV was broadly unchanged at £2,118 million, despite the impact of investment market volatility in the second half of the year. MCEV included an incremental £165 million delivered through management actions, significantly in excess of our average annual target of £100 million.

Our estimated IGD surplus was £1.3 billion at 31 December 2011, up from £1.0 billion a year earlier, with headroom over our IGD capital policy of £0.4 billion. During 2011 we undertook several management actions to strengthen our IGD position through the simplification of the Group's structure. The headroom over our IGD capital policy allows us greater flexibility in the repayment of our bank debt and we have identified additional actions that will improve this surplus further in 2012.

Phoenix Life highlights

Phoenix Life, led by its Chief Executive Officer Mike Merrick, contributed IFRS operating profit of £395 million, slightly above the £388 million achieved in 2010.

The Group has a well established Solvency II programme and has continued to progress towards meeting the Solvency II requirements. The FSA has recently announced a change to the implementation date of Solvency II to 1 January 2014 (a year later than previously envisaged) and the Group is on track to meet this timetable.

Underpinning the development of the Solvency II internal model is the Group's Actuarial Systems Transformation ('AST') project which will deliver a single actuarial modelling platform across the business, transforming modelling capability and efficiency.

Our existing long-term relationships with our outsourced partners are a key aspect of Phoenix's business model, helping us to ensure our customers are treated fairly whilst managing our cost base efficiently. Together with Diligenta, our largest outsourced partner, we have continued to transform our administrative systems, including completing the transfer of a total of over 2 million live policies onto the BaNCS policy administration platform. This transfer from outdated legacy systems to a modern, 'future proofed' administration platform has provided our policyholders with online access to their investments, improving both service levels and transparency. This work will continue during 2012, with the planned transfer of a further 1 million live policies onto BaNCS.

Ignis highlights

Ignis Asset Management, led by its Chief Executive Officer, Chris Samuel, was able to increase assets under management, administration and oversight by 3% to £70.7 billion. In addition, Ignis has shown stable financial performance in difficult markets, with an IFRS operating profit of £46 million in 2011.

Ignis has made excellent progress in strengthening its investment management capabilities and this has already yielded results in the investment performance achieved for the Group's life companies. During 2011, 11 out of 15 of the Group's main life funds achieved investment performance above their benchmark targets and, as a result, Ignis has generated significant performance fees during the year. This clearly demonstrates how we have aligned policyholder interests with those of our shareholders in the management of their investments.

Ignis is also in the process of putting in place an appropriate back office structure to support its future plans by partnering with HSBC Securities Services to deliver investment administration and other related activities. As with Phoenix Life, the use of outsourced partners allows Ignis to focus on the key areas of investment and distribution, whilst providing a more predictable and lower cost operating model for the Group.

As the Group's life company assets run-off over time, it is important that Ignis develops its capabilities and brand as a manager of third party assets. In 2011 Ignis attracted net inflows of £1.7 billion and given its improved investment performance across many asset classes, is well placed to build on the progress it has made in 2011 in developing a strong third party proposition and expanding into the institutional market.

People

Phoenix Group's business model relies on having the necessary specialist expertise in closed life fund and asset management. This involves being able to recruit and retain people who have outstanding skills in areas such as capital, cost, risk and investment management. That we have such a team of individuals is a testament to the Group's capability in recruitment, training and development, and employee engagement. This capability has now been externally recognised, with Phoenix being awarded the 2011 Strategic Communications Management (Melcrum) Award for Employee Engagement.

At the time of going to print I am also delighted to report that Phoenix Group is one of 'Britain's Top Employers 2012'. This certification is awarded to companies that have been independently recognised as being amongst the best companies to work for in the UK.

These are well-deserved awards, which are also reflected in our higher than ever employee engagement results.

Customers

'Treating Customers Fairly' is central to how we run our business. We have streamlined our life companies through a programme of fund mergers which, together with a rebranding of our life funds, aims to simplify our policyholder communications and provide customers with enhanced fund security. A new website for a number of our life funds will be launched this year to enhance the online customer experience.

In co-operation with our outsourced partners, we have transformed many of our systems to improve customer service and operational efficiency. We have been working diligently to ensure that any customer complaints are dealt with in an efficient and timely manner and we have already seen a real improvement in customer satisfaction in this area.

We are always seeking initiatives that may be of benefit to our policyholders. During 2011 we launched a scheme to enable some holders of paid-up life insurance policies to cash these in without penalty and benefit from the proceeds immediately. This initiative was a great success, with over 85% of customers involved in the scheme taking up this offer. Other similar initiatives are being considered for the remainder of 2012. A team of experts has been brought together within the life companies to review and enhance our investment strategy and governance. We also continue, where possible, to try to improve returns for our policyholders through the distribution of the estate within the life funds. As a result, certain maturity payouts are being enhanced in some of our funds by up to 12%.

Economic and industry overview

As in 2010, financial markets in 2011 were volatile and global economic growth was subdued. Given the ongoing pressures in the Eurozone and, in particular, the high sovereign debt of many of its members, I expect this uncertainty to continue during 2012. Although Phoenix is not immune to further negative developments in the region, we have carefully managed our exposure to Peripheral Eurozone countries, reducing shareholder debt securities held in Peripheral Eurozone sovereign debt to £9 million. We are well positioned to react to further changes to ensure policyholder and shareholder investments are secure.

2012 Outlook and prospects

Developing 'The Phoenix Way'

The Phoenix Way characterises an approach and infrastructure for the efficient and effective structuring, integration and management of closed life funds and the investments they hold. By applying a consistent framework across the Group, The Phoenix Way reduces risk, complexity and cost; improves investment performance; enhances customer service through effectively working with our outsourced partners; increases MCEV and releases capital to shareholders.

During 2011 we have continued to progress our AST project and have also set out a clear template to ensure that the Group's 14 with-profit funds are managed in a consistent way. This work will continue in 2012.

Financial targets

Despite the challenging market conditions experienced in 2011 we have reiterated our operating company cash generation target of £3.2 billion for the six year period between 2011 to 2016. Of this, we are aiming to deliver operating company cash generation of between £500 million and £600 million in 2012 which will be weighted towards the second half of the year. In addition, we maintain our previously set annual average target of £100 million of MCEV enhancements through management actions over the period 2011 to 2014.

The combination of cash flow generation and enhancement to MCEV will allow us to delever the Group's capital structure. Having already achieved the target to reduce our level of gearing to below 50%, we have now set ourselves a further target to reduce this to 43% or below by the end of 2012.

Conclusion
I look forward to 2012 with confidence and believe that we can continue to demonstrate the great strengths of Phoenix Life and Ignis, building and delivering value for all our stakeholders. I would like to thank my colleagues for their hard work during a challenging period. Although it is difficult to predict how the economic climate will develop, the quality of the teams in Phoenix Group, the discipline with which the Group manages risk and capital and the proven resilience of its business model will stand us in good stead during the coming year.

Clive Bannister
Group Chief Executive Officer

22 March 2012

2011 HIGHLIGHTS

Financial
Generated £810 million operating companies' cash generation – above the mid-point of the target range

Delivered £165 million of MCEV enhancement through management actions

Reduced gearing to 46% through organic cash generation

Achieved net third party sales by Ignis of £1.7 billion

Customer
Increased policyholder payouts through inherited estate distribution

Improved customer service, including providing online access for policyholders

Operational
Further simplified life company structure through consolidation of life companies and recapture of internal reassurance, enhancing the IGD capital position of the Group

Completed the transfer of 2 million live policies onto the BaNCS administration platform

De-risked Group pension scheme liabilities through liability management exercises

Restructured Ignis joint ventures to give the businesses a greater degree of independence in the future

Initiated the outsourcing of Ignis' back office functions in partnership with HSBC

BUSINESS AND STRATEGY
Our business brings together complementary skills to deliver improved performance for our life company and asset management customers. With a simple mission and a clear strategy we are well positioned to capitalise on opportunities to deliver value as they arise in the future.

In this section

OUR BUSINESS
Phoenix Group combines the financial and operational expertise of Phoenix Life with the investment management capabilities of Ignis to create value for policyholders and shareholders.

Phoenix Life
Aims to deliver innovative financial management and operational excellence

6m
Policyholders

£778m
Cash generation

What we do

Life assurance
Through Phoenix Life we manage life assurance funds which no longer actively sell new life assurance policies and which run-off gradually over time. These so-called 'closed life funds' within the Group consist of millions of policyholders and a total of approximately £63 billion of financial assets.

Phoenix Life manages these funds using its specific skills and expertise in the areas of capital, financial, risk and cost management.

How we create value
Unlike open life businesses, we are not required to allocate significant capital to support the writing and distribution of new insurance products. This means that the capital requirements of our operating life companies decline as policies mature, releasing excess capital as free surplus in the form of cash.

In addition to this released capital we create value from our in-force book of closed life funds, generating profits from participation in investment returns, policyholder charges and management fees earned on assets (to the extent they exceed expenses). These additional profits from the in-force policies can also be released by the Group's life companies as free surplus in the form of cash.

External outsourced partners are used for policy administration thereby minimising fixed costs.

Ignis Asset Management
Targets superior investment performance, client service and operational efficiency

£70.7bn
Assets under management, administration and oversight

£46m
IFRS operating profit

Asset management
Through Ignis, the Group both manages the funds that back the investments of our policyholders and develops investment propositions for third party clients in the institutional, retail and international markets.

Ignis aims to maximise risk-adjusted returns on the assets it manages for the benefit of policyholders, third party clients and shareholders.

How we create value
Ignis generates revenues from managing the investments of the Group's life companies as well as third party clients.

Ignis is incentivised to maximise investment performance for the Group's policyholders through performance fee arrangements. In addition, Ignis is seeking to grow the assets it manages for third party investors in both the retail and institutional markets.

Ignis has announced a restructuring of its operations to support its future strategy, including the use of its own outsourced partner to provide investment administration and related back office services.

Phoenix Group
Value generated by Phoenix Life and Ignis is distributed to the Holding Companies in the form of cash. The Holding Companies use this cash to fund group expenses, pension contributions, debt interest and repayments and shareholder dividends.

The Group functions provide support for, and coordination and delivery of, the Group's strategic objectives and manages our relationships with our external stakeholders, including shareholders, our lenders, our Group pension schemes and the Financial Services Authority ('FSA').

OPERATING STRUCTURE
Our structure is aligned to the market sectors in which we operate.

The Group has two core segments: life assurance – Phoenix Life; and asset management – Ignis. In addition, our Group functions provide support and coordination for the delivery of the Group's strategic initiatives.

Group functions
At Group level, Phoenix operates centralised functions that provide Group-wide and corporate-level services and manage corporate activity. The Group-level operations include Group Finance, Treasury, Group Tax, Group Actuarial, Group Risk, Legal

Services, HR, Corporate Communications, Strategy and Corporate Development, Investor Relations, Company Secretariat and Internal Audit.

Phoenix Life

Phoenix Life is responsible for the management of the Group's life funds. Phoenix Life's experienced and focused management team is led by its Chief Executive Officer, Mike Merrick. Based in Wythall, near Birmingham, it has a track record of successfully integrating life assurance businesses and is developing a leading-edge model and infrastructure into which future acquired funds can be integrated.

Manage capital

Phoenix Life continually manages the capital requirements of the Group's life companies, ensuring that policyholder security is protected whilst maximising the release of capital as cash to the Group's Holding Companies. We combine sophisticated asset liability matching techniques with a prudent approach to risk management to ensure the Group's life companies are capital efficient.

The Group has continued its programme of activity to further integrate its life companies in order to optimise capital allocation and economies of scale. During 2011, the internal reassurance arrangement between Phoenix Life Limited ('PLL') and Phoenix Pensions Limited ('PPL') was also recaptured by PLL, resulting in PPL no longer holding any life assurance business.

As a result, the Group had 6 operating life companies at the end of 2011, consisting of 14 with-profit funds and 7 non-profit funds. Further transfers of business will be progressed during 2012. Simplifying the number of life companies within the Group through such business transfers both reduces complexity and releases capital.

Drive value

Driving value consists of more than just targeting enhanced investment returns. The Group also aims to ensure that unrewarded exposure to market volatility is minimised or the risks from sudden market movements are managed through hedging. In addition, regular re-balancing of asset and liability positions is required to ensure that only those assets which deliver the appropriate level of return for the risk assumed are held within life funds and to take into account any guarantees which attach to the liabilities.

Improve customer outcomes

Improving customer outcomes is a key focus for Phoenix Life. During 2011, the Group concentrated on some specific areas including increasing estate distribution for with-profit policyholders and improving the speed of claims payouts. As in 2010, ensuring fast and efficient claims payouts for our customers continued to be a priority and in addition to using the ABI-sponsored Origo service for open market option payments relating to pension-to-annuity transfers, we also used it for pension-to-pension transfers during the year. This initiative reduced transfer times from around 30 days to under 12 days on average.

Although the life companies are closed and generally do not 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. The Group has a strong and steady stream of internal annuity vestings at a very low cost, so we can offer policyholders competitive annuity rates whilst generating additional value for shareholders.

Management services

The Group's management services companies are charged with the efficient provision of financial and risk management services, sourcing strategies and delivering all administrative services required by the Group's life companies. By using management services companies, the life companies benefit from price certainty and a transfer of some operational risks to the management services companies.

As the number of policies held by the Group gradually declines over time, the fixed cost base of our operations as a proportion of policies will increase. Our management services team manages this risk by putting in place long-term arrangements for third party policy administration. By paying a fixed price per policy to our outsourced partners we minimise the fixed cost element of our operations.

These outsourced partners have scale and common processes, often across multiple clients, which provide several benefits for the Group, including converting fixed costs to variable costs, reducing investment requirements, improving the technology used within our administrative capability, and reducing our operational risk.

Specialist roles such as finance, actuarial and risk are retained in-house, ensuring Phoenix Life retains full control over the core capabilities necessary to manage and integrate closed life funds.

The Phoenix Way: Methodology

The Phoenix Way characterises an approach and infrastructure for the efficient and effective structuring, integration and management of closed life funds and the investments held within them.

The Phoenix Way aims to provide a consistent approach to managing each Group life company which, given their different histories, have previously all adopted different methodologies.

The Phoenix Way covers areas such as operational management, outsourcing, investment management, restructuring and risk management. Examples include establishing a standardised with-profit ‘model fund’, consolidating outsourcing arrangements and developing standard systems for actuarial modelling as part of our AST project.

The Phoenix Way also provides a template which can then be applied in a consistent manner to newly acquired closed life funds within the Group.

Ignis Asset Management

Ignis Asset Management is the Group’s asset management business and is led by its Chief Executive Officer, Chris Samuel.

It provides investment management services to the Group’s life companies as well as to third party clients, including both retail and institutional investors in the UK and overseas. Now one of the largest 15 UK asset management firms, Ignis is responsible for £70.7 billion of assets, including £62.1 billion of assets for the Group’s life companies.

With offices in London and Glasgow, and over 540 employees, Ignis has investment capabilities across multiple asset classes organised into six investment business units.

Ignis’ vision is to develop into a leading asset management business committed to performance excellence and innovation, where talented people want to work and, most importantly, where clients want to invest their money.

The business strategy to develop this vision has four goals:

- Meeting or exceeding the investment performance expectations of Ignis’ clients
- Working with clients to provide creative solutions to changing product needs
- Maintaining a well controlled and efficient operating platform
- As a result, developing further as a high quality, profitable company.

This strategy is underpinned by:

- **Innovative people** focused on Ignis’ clients and provided with the freedom to perform
- **A partnership culture** that ensures clear accountability and supports both the work within Ignis and with Ignis’ clients and counterparties
- **Processes and technology** to identify risks and opportunities
- **Stability** that comes from a strong governance and control culture and being part of the Phoenix Group.

Deploying The Phoenix Way: Actuarial Systems Transformation (‘AST’)

An important part of The Phoenix Way involves addressing legacy issues to maximise cost efficiency and improve functionality.

The Group has grown through the acquisition of a number of closed life fund businesses, resulting in a disparate collection of actuarial valuation models on a variety of platforms. To address this, Phoenix Life has entered into a long-term relationship with Milliman to consolidate these valuation models onto the MG ALFA platform.

The Group will derive benefits from a number of areas:

- Reduced operational risk (and associated capital) of actuarial modelling
- Improved quality and frequency of capital monitoring
- Improved cost efficiency by simplification/standardisation of actuarial processes
- Creation of an acquisition-ready platform

The AST programme is progressing to plan and will be an essential part of managing the Group’s life businesses under the Solvency II regime, as well as providing a platform for the integration of newly acquired closed life funds within the Group.

Ignis investment business units

Ignis Fixed Income

- Liquidity
- Rates
- Credit

Ignis Equities

- UK
- Europe

- Far East
- US
- Global
- Emerging markets

Ignis Real Estate

- Unit trust
- Investment trust
- Segregated mandates

Ignis Advisors

- Fund of Hedge Funds
- Fund of Private Equity
- Fund of Real Estate
- Retail multi-manager

Ignis Solutions

- Liability driven investments
- Asset liability matching and risk management

Ignis Partners

Investment boutiques:

- Argonaut
- Cartesian
- Castle Hill
- Hexam

Sales, marketing and client service

Insurance (life company)

UK Institutional

UK Retail

International

Operations, support and controls

Ignis has recently developed a number of pooled funds across a range of asset classes. The creation of these pooled funds has allowed Ignis to simplify its relationship with the Group's life companies by replacing a large number of individually segregated mandates. In addition, Ignis is incentivised to maximise investment performance for policyholders through a performance fee structure.

At the same time, Ignis has further strengthened its investment, distribution and operations teams in order to develop its proposition to third party clients. Ignis develops new products that it believes would be of interest to the third party market, for example it launched an Absolute Return Government Bond Fund during 2011. Ignis has also sought to leverage its knowledge of the requirements of the Group's life companies by creating solutions which target the provision of Liability Driven Investment ('LDI') products to the institutional market. An example of the success that Fixed Income and Solutions have already had in this area was in winning a £430 million LDI mandate from one of the Group's pension schemes during 2011, competing against other third party providers.

As part of its strategy to develop the Ignis brand as a third party asset manager in its own right, Ignis has renegotiated its joint venture agreement with Argonaut, which will provide the business with a greater level of independence. As with its existing partnerships with Castle Hill and Hexam, Ignis will retain a minority interest in Argonaut.

Ignis has broad distribution capabilities and is well placed to take its strong investment capabilities to market in the coming year, with a particular focus on building its position within the institutional market.

Deploying The Phoenix Way: Outsourcing arrangements

One element of The Phoenix Way involves consolidating our internal and external arrangements to further transform the model and improve outcomes for our policyholders and customers. In line with this, Ignis is planning to enter into a partnership with HSBC Securities Services to deliver its investment administration and other related back office administration services. As part of this, Phoenix Life will also consolidate certain existing ancillary investment related outsourced services with HSBC.

The benefits of this new partnership to the Group will be derived from a number of areas:

- It allows Ignis to focus on its strategic priorities of investment and distribution
- HSBC will provide a standard back office framework enabling Ignis to focus future systems development on the front office
- It reduces and simplifies the network
- of external suppliers for both Ignis and Phoenix Life
- It provides a single source of data for Phoenix Life, assisting with reconciliation and consolidation work
- It facilitates the introduction of innovative new products by enabling Ignis to leverage HSBC's existing capabilities to provide increased speed to market

OUR STRATEGY

Phoenix Group's strategic journey continues to build on our recent achievements. Our mission is simple: to improve returns for Phoenix policyholders and Ignis customers and deliver value for shareholders.

Areas of strategic focus

Manage capital

Risk management is a key component of the Group's strategic agenda. The effective management of our risks and the efficient allocation of capital against them is critical in allowing us to achieve our strategic and operational objectives. This includes ensuring there are robust capital policies within the life companies.

We are well positioned to adapt to new requirements arising from Solvency II regulatory changes. Simplifying our capital structure brings greater flexibility and is a fundamental enabler of the strategic growth ambitions of the Group.

Drive value

At Phoenix we drive value in many ways. There are a number of management actions undertaken by the Group such as fund mergers and de-risking which can accelerate cash or increase our MCEV.

Management of costs is also an important aspect of our value creation. Part of The Phoenix Way involves improving the efficiency of operational management through the standardisation and streamlining of key processes across the Group which will in turn reduce costs, improve performance and maximise value.

Improve customer outcomes

We have three key areas of focus in relation to our customers:

Value – we aim to manage customer outcomes to their maximum benefit

Service – customers want to be treated fairly, with empathy and respect in a timely fashion

Security – customers expect their investment to be secure in a well managed company.

Engage people

Building its reputation as an employer of choice, the Group specifically targets, recruits and develops top quality people.

The Group invests in its people whose talent, enthusiasm and support makes its strategy and objectives achievable.

Developing the platform for growth

During 2011, the Group has made further progress in building a stable and simplified business. Results to date, both financial and non-financial, have continued to demonstrate the delivery of our strategy.

DELIVERING ON OUR STRATEGY

Phoenix Life

Our objectives for 2011
Optimisation of life company capital through further transfers of business

Achieve all Solvency II programme critical milestones

Develop with-profit 'Model Fund' investment strategy

Improve speed of payments across all claims and enhance complaint handling processes

Our achievements in 2011
Recaptured the internal reassurance between PPL and PLL

Acceptance by the FSA of Phoenix's initial Solvency II Self Assessment template

Established a standardised with-profit 'Model Fund'

Transferred over 2 million live policies from legacy systems to improve service and contain future costs

Met 12 day industry target for Origo Open Market Option transfers

Delivered £165 million of MCEV enhancement through management actions

Increased distributable estate by over £126 million in 2011

Our priorities for 2012
Progress further funds mergers

Achieve £100 million of MCEV enhancing management actions each year on average from 2011 to 2014

Commence 'Use Test' period running Solvency II comformant processes in advance of the Internal Model Application

Ignis Asset Management

Our objectives for 2011
Grow third party sales and revenue in Ignis through a number of areas including:

– Sustained investment performance and service for all our clients

– Taking Fixed Income and Solutions to market

– Accelerating third party Real Estate growth

– Developing Advisors business

– Harvesting revenues from joint ventures

– Transforming operations.

Increase Ignis brand recognition

Our achievements in 2011
Achieved net third party sales of £1.7 billion

Restructured Argonaut joint venture to provide the business with a greater degree of independence

Initiated an outsourcing of Ignis' investment administration and back office services, in partnership with HSBC

Strengthened Ignis investment and distribution teams

Our priorities for 2012
Continue to deliver strong investment performance

Develop proposition for third party clients, including for the institutional marketplace

Complete outsourcing of investment administration and related back office services

Phoenix Group

Our objectives for 2011
Maintain strong cash flow delivery

Examine opportunities to refinance and/or restructure existing Group debt arrangements

Further strengthen risk capabilities

Continue to develop our business readiness to acquire and integrate new closed life funds in the future

Further reduction in tax risks and resolution of legacy tax issues

Maintain high employee engagement

Achieve employee retention above sector benchmark for each business unit

Maintain our market presence to ensure visibility of potential opportunities

Build reputation in public policy arena

Our achievements in 2011
Achieved cash flow generation of £810 million

Reduced gearing to 46%, below our 50% target

Resolved a number of legacy tax issues allowing the release of £47 million of provisions on an IFRS basis

Increased employee engagement with an overall Group engagement score of 74%

Won the 2011 Strategic Communications Management (Melcrum) Award for Employee Engagement

Launched liability management initiatives for the Group pension schemes

Our priorities for 2012
Achieve cash flow target of £500 million – £600 million

Reduce gearing to 43% or below

Improve capital structure

BUSINESS REVIEW

The Group has delivered a strong operating performance across all areas of its business. Increased cash generation by the operating subsidiaries and embedded value growth from value enhancing management actions allowed the Group to meet its targets for 2011 despite ongoing market volatility.

In this section

KEY PERFORMANCE INDICATORS

The KPIs comprise:

£810m
Operating companies' cash generation

2010: £734m

42p
Dividend per share

2010: 42p

£2,118m
Group MCEV

2010: £2,104m

£72.1bn
Group assets under management

2010: £69.6bn

£387m
Group IFRS operating profit

2010: £373m

£46m
Asset management IFRS operating profit

2010: £46m

£1.3bn
IGD surplus (estimated)

2010: £1.0bn

46%
Gearing ratio

2010: 52%

£3.1bn
IGD Excess Capital (estimated)

2010: £2.8bn

The Group's financial KPIs are analysed overleaf.

£810m

Operating companies' cash generation

2010: £734m

2009*	£716m
2010	£734m
2011	£810m

* Pro forma. For ease of comparison 2009 pro forma information includes a full year's results for the Pearl businesses even though Phoenix Group Holdings only acquired the Pearl businesses in the third quarter of 2009.

Maintaining strong cash flow delivery underpins debt servicing and repayment as well as shareholder dividends:

Analysis
Continued strong cash generation of £810 million by the Group's operating companies enabled the Group to achieve its 2011 target for cash generation of £750 million to £850 million despite challenging market conditions.

Management actions in themselves generated cash flows of £359 million, mainly related to restructuring and de-risking activities.

Definition and calculation
Operating companies' cash generation is a measure of cash and cash equivalents remitted by the Group's operating companies to the Holding Companies and is available to cover dividends, debt servicing and repayment, pension scheme contributions and operating expenses.

Quantified target
The cumulative cash flow target for 2011 to 2016 is £3.2 billion.

£500 million to £600 million of these cash flows are expected to be generated in 2012 and will be weighted towards the second half of the year.

£2,118m
Group MCEV

2010: £2,104m

2009	£1,827m
2010	£2,104m
2011	£2,118m

The Board considers that MCEV provides the most relevant and consistent means of assessing the Group's ability to increase value:

Analysis
MCEV increased by £14 million in the period reflecting the resilience of the Group. Value enhancing management actions delivered an incremental uplift to MCEV of £165 million against a target of £100 million.

Definition and calculation
Note 1 of the MCEV supplementary information sets out the basis of calculation of Group MCEV.

Quantified target
The Group's target is an average contribution to embedded value from management actions of £100 million per annum between 2011 and 2014.

£387m
Group IFRS operating profit

2010: £373m

2009*	£457m
2010	£373m
2011	£387m

* Pro forma.

The Board considers that Group IFRS operating profit is a more representative measure of performance than Group IFRS profit before tax as it provides long-term performance information unaffected by short-term economic volatility and gives an insight into the Group's ability to generate cash flows to support dividends[1]:

1 Phoenix Group Holdings is subject to Cayman Islands Companies Law. Under Cayman Islands 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.

Analysis
Group IFRS operating profit of £387 million (2010: £373 million) reflects a strong performance from both the Group's operating segments.

Definition and calculation
Note 5 of the IFRS financial statements sets out the basis of calculation of Group IFRS operating profit.

£1.3bn
IGD surplus (estimated)

2010: £1.0bn

2009	£1.2bn
2010	£1.0bn
2011	£1.3bn

Insurance Groups' Directive ('IGD') surplus is the regulatory assessment of capital adequacy on a Group-wide basis:

Analysis
The estimated IGD surplus has increased to £1.3 billion with IGD capital generation of £0.6 billion offsetting the payment of dividends, debt interest and debt repayments of £0.3 billion. The surplus of £1.3 billion represents headroom of £0.4 billion (2010: £0.1 billion) over the Group's IGD capital policy.

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 Phoenix Life Holdings Limited ('PLHL'). IGD surplus is defined as group capital resources less the group capital resource requirement.

IGD capital policy: The Group maintains group capital resources at the PLHL level at an amount in excess of 105% of the with-profit insurance capital component ('WPICC'), being an additional capital requirement of with-profit funds, plus 145% of the group capital resource requirement less the WPICC.

£3.1bn

IGD Excess Capital (estimated)

2010: £2.8bn

2009	£3.1bn
2010	£2.8bn
2011	£3.1bn

IGD Excess Capital represents the total capital available to the Group (both policyholder and shareholder) in excess of capital requirements. It is a measure of the capital strength of the Group and the capital available to protect policyholders and shareholders from adverse events.

Analysis
The increase in the IGD Excess Capital from 2010 is consistent with the increase in the IGD surplus. The IGD Excess Capital coverage percentage was 182% at 31 December 2011 (2010: 170%).

Definition and calculation
IGD Excess Capital includes policyholder and certain shareholder capital currently excluded under FSA rules from the calculation of IGD surplus at the PLHL level and is explained on page 35.

42p

Dividend per share

2010: 42p

2009*	15p
2010	42p
2011	42p

* Dividend paid in respect of the 4 month period post acquisition of Pearl businesses (€0.17 converted using the 15 April 2010 exchange rate).

Analysis
The Board has recommended a final dividend of 21 pence per share bringing the total dividend for the year to 42 pence. The final dividend is due to be paid on 8 May 2012, subject to compliance with the processes set out in the Group's main credit facilities and shareholder approval at the Company's AGM. A scrip dividend option will be available to shareholders.

£72.1bn

Group assets under management

2010: £69.6bn

2009	£68.3bn
2010	£69.6bn
2011	£72.1bn

Assets under management are a key driver of operating profit:

Analysis
Total Group assets under management increased by £2.5 billion to £72.1 billion[1].

The increase was driven by net third party sales of £1.7 billion and positive fair value movements on the Group's fixed interest portfolio which offset the run-off of the closed life business.

Definition and calculation
Group assets under management represent life company assets (excluding collateral on stock-lending arrangements), Holding Company cash, and third party assets managed by Ignis.

1 Includes cash equivalents of £nil (2010: £39 million). Cash equivalents are defined by management as investments that can readily be converted into cash.

£46m
Asset management IFRS operating profit

2010: £46m

2009* £34m

2010 £46m

2011 £46m

* Pro forma.

Analysis
Ignis' IFRS operating profit of £46 million remained stable (2010: £46 million) despite increased costs of new business development.

Definition and calculation

Ignis' IFRS operating profit excludes non-recurring income and expenses.

46%
Gearing ratio

2010: 52%

2009 58%

2010 52%

2011 46%

The gearing ratio is the Group's measure of its level of debt compared to its equity on an MCEV basis:

Analysis
The Group has met its target of reducing gearing to below 50% through strong cash generation and an increase in MCEV.

Definition and calculation
Gearing is calculated as net shareholder debt[2] divided by the sum of Group MCEV, net shareholder debt and the present value of future profits of Ignis.

Target
The Group's target is to reduce the gearing ratio to 43% or below during the course of 2012.

2 Net shareholder debt is defined as shareholder debt (including hybrid debt) less Holding Company cash as set out on page 37.

CASH GENERATION

£810m
Operating companies' 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-off, policyholder charges and fees earned on assets under management. The Group's closed life funds provide predictable fund maturity and liability profiles, creating stable long-term cash flows for distribution to shareholders and for repayment of outstanding debt. Although investment returns are less predictable, some of the investment risk is borne by policyholders.

Holding Companies' cash flows
The statement of cash flows prepared in accordance with IFRS combines cash flows relating to policyholders and cash flows relating to shareholders, 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 the availability and transferability of capital. For this reason, the following analysis of cash flows focuses on the Holding Companies' cash flows, which reflect cash flows relating only to shareholders and which are, therefore, more representative of the cash that could potentially be distributed as dividends, or used for the repayment of debt. This cash flow analysis reflects the cash paid by the operating companies to the Holding Companies, as well as the uses of those cash receipts.

In 2011, the Group has delivered cash flows from its operating subsidiaries of £810 million, including cash flows of £359 million from management actions. The latter increased cash flows primarily through the restructuring of a portfolio of corporate bonds and investment and operational de-risking activities.

	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Cash and cash equivalents at 1 January	**486**	202
Operating companies' cash generation:		
Cash receipts from Phoenix Life[1]	**778**	708
Cash receipts from Ignis Asset Management	**32**	26
Total receipts of cash by Holding Companies[2]	**810**	734
Uses of cash:		
Operating expenses	**52**	45
Pension scheme contributions	**35**	38
Debt interest	**122**	123
Total recurring outflows	**209**	206
Non-recurring outflows	**24**	79
Uses of cash before debt repayments and shareholder dividend	**233**	285
Debt repayments	**171**	122
Shareholder dividend	**55**	43
Total uses of cash	**459**	450
Cash and cash equivalents at 31 December[3]	**837**	486

2 Includes amounts received by the Holding Companies in respect of tax losses surrendered to the operating companies.

3 Closing balance at 31 December 2011 includes required prudential cash buffer of £150 million (2010: £150 million).

Operating companies' cash generation

Cash remitted by Phoenix Life increased by £70 million to £778 million (2010: £708 million) reflecting the benefit of management actions. This strong cash generation coupled with increased cash flows from Ignis Asset Management of £32 million (2010: £26 million) enabled the Group to achieve its target for cash generation in 2011 of £750 million to £850 million despite challenging market conditions.

Phoenix Life free surplus

The generation of free surplus, net of movements in required capital, underpins the cash remittances from Phoenix Life. The table below analyses the movement in free surplus of Phoenix Life which represents the life companies' free surplus plus the IFRS net assets of the service companies:

	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Opening free surplus	**750**	464
IFRS operating profit	**395**	388
IFRS investment variances and non-recurring items	**(336)**	(73)
IFRS tax	**(20)**	76
Movements in capital requirements and policy	**84**	405
Valuation differences and other[1]	**(2)**	198
Cash distributed to Holding Companies	**(778)**	(708)
Closing free surplus[2]	**93**	750

1 Includes differences between IFRS valuation of assets and liabilities and valuation for capital purposes.

2 Position at 16 March 2012 increased to an estimated £250 million.

The Phoenix Life IFRS operating profit is discussed in the Group IFRS operating profit section and reflects recurring margins and return on surplus assets, within the £275 million to £325 million expected annual range, plus the effects of non-economic experience variances and assumption changes.

Movements in capital requirements and policy in 2011 include the inherent release of capital from the run-off of the life funds as well as management actions, offset by an increase in capital requirements in annuity and other non-profit funds due to falling interest rates in the second half of the year.

Valuation differences and other in 2010 included a £125 million benefit from the restructuring of a portfolio of corporate bonds.

Recurring cash outflows

Operating expenses of £52 million (2010: £45 million) increased primarily due to the payment of expenses related to previous years. The remaining recurring cash outflows were in line with 2010.

Non-recurring cash outflows

Non-recurring cash outflows of £24 million were significantly lower than in 2010 (2010: £79 million) reflecting reduced investment in the Group's transformation programmes with its outsourced partners which are nearing completion and the non-recurrence of certain costs related to the Group's Premium Listing in 2010.

Debt repayments and shareholder dividend

Debt repayments of £171 million in the period comprise a £21 million voluntary debt prepayment and scheduled repayments totalling £150 million[1] in respect of the Group's two main credit facilities.

The shareholder dividend of £55 million comprises the payment of the 2010 final and 2011 interim cash dividend.

Target cash flows

The Group is targeting operating companies' cash generation of £3.2 billion for the period from 1 January 2011 to 31 December 2016:

Sources of cash flows	1 January 2011 to 31 December 2016 £bn
Future cash flows:	
Emergence of surplus	**1.1**
Release of capital	**1.1**
Recurring cash receipts generated by life companies	**2.2**
Other[2]	**0.2**
Total future cash flows target	**2.4**
Achieved cash flows	**0.8**
Operating companies' cash generation target	**3.2**

1 This includes £1 million paid to Pearl Assurance Limited, a subsidiary undertaking. Pearl Assurance Limited is a lender under the Pearl facility.

2 Includes cash flows from Ignis and the management services companies.

£500 million to £600 million of these targeted cash flows are expected to be generated in 2012.

The resilience of the cash generation target is demonstrated by the following stress testing:

Stress testing	1 January 2011 to 31 December 2016 £bn
Base case 6-year projections	**3.2**
20% fall in equity markets	**3.1**
15% fall in property values	**3.1**
75bps increase in yields	**3.2**
Credit spreads widening[3]	**2.9**
Combined stress[4]	**2.6**

3 10 year term: AAA – 52bps, AA – 72bps, A – 104bps, BBB – 152bps.

4 20% fall in equity markets, 10% fall in property, 80bps increase in yields and credit spreads widening (10 year term: AAA – 70bps, AA – 97bps, A – 140bps, BBB – 205bps).

One-off shocks would be expected to lead to a deferral of cash emergence rather than a permanent diminution.

GROUP MCEV

£2,118m

Group MCEV

Group MCEV operating earnings[1]

The increase in MCEV despite difficult market conditions reflects the resilience of the life division and the realisation of significant value from management actions.

MCEV operating earnings after tax were lower at £394 million (2010: £543 million) primarily due to a decrease in the long-term risk-free rate and the non-recurrence of significant positive experience variances in 2010.

MCEV operating earnings	**Year ended 31 December 2011 £m**	Year ended 31 December 2010 £m
Life MCEV operating earnings[2]	**556**	758
Management services operating profit	**17**	20
Ignis Asset Management operating profit	**46**	46
Group costs	**(84)**	(70)
Group MCEV operating earnings before tax	**535**	754
Tax on operating earnings	**(141)**	(211)
Group MCEV operating earnings after tax	**394**	543

1 The Phoenix Group Market Consistent Embedded Value methodology (referred to herein and in the supplementary information as MCEV) is set out in note 1 in the MCEV supplementary information.

The asset management and management services businesses are included in the Group MCEV at the value of IFRS net assets. The Group MCEV does not include the future earnings from their businesses.

2 Life MCEV operating earnings are derived on an after tax basis. For presentational purposes Life MCEV operating earnings before tax have been calculated by grossing up the after tax Life MCEV operating earnings. Life MCEV operating earnings before tax of £556 million (2010: £758 million) are therefore calculated as £409 million operating earnings (2010: £546 million) grossed up for tax at 26.5% (2010: 28%).

Life MCEV operating earnings after tax

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

Life MCEV operating earnings after tax	**Year ended 31 December 2011 £m**	Year ended 31 December 2010 £m
Expected existing business contribution	**254**	306
New business value	**13**	19
Non-economic experience variances and assumption changes:		
Experience variances	**181**	264
Assumption changes	**(18)**	(38)
Other operating variances	**(21)**	(5)
Total non-economic experience variances and assumption changes	**142**	221
Life MCEV operating earnings after tax	**409**	546

Expected existing business contribution

The Group uses long-term investment returns in calculating the expected existing business contribution. The expected contribution in 2011 of £254 million after tax is £52 million lower than in 2010, primarily due to a decrease in the long-term risk-free rate and a lower opening MCEV for life business. The long-term risk-free rate is based on the opening position at 1 January.

New business value

New business profits generated from vesting annuities during 2011 were £13 million after tax (2010: £19 million).

The new business margin is 5% after tax (2010: 5%) and represents the ratio of the net of tax new business value to the amounts received as new single premiums.

Non-economic experience variances and assumption changes

Non-economic experience variances and assumption changes increased MCEV by £142 million after tax in 2011, the main driver being positive experience variances.

Positive experience variances of £181 million mainly related to the benefits of improved asset allocations of £95 million, data cleansing projects of £30 million and the resolution of legacy tax issues of £20 million. Experience variances in 2010 included a £139 million benefit from the restructuring of a portfolio of corporate bonds and £78 million of tax optimisation benefits.

Negative assumption changes were primarily driven by a reduction in assumed surrender rates in funds with valuable policyholder guarantees.

Management services and Ignis Asset Management operating profit

Commentary on the management services companies and Ignis Asset Management operating profit is provided in the Group IFRS operating profit section.

Group costs

Group costs were £84 million before tax in the period, of which costs relating to Group functions amounted to £39 million (2010: £40 million). The balance of the charge in both periods relates primarily to pension scheme costs, partly offset by miscellaneous income. The pension scheme costs are different to IFRS as the MCEV does not recognise pension schemes in surplus.

Reconciliation of Group MCEV operating earnings to Group MCEV earnings

Group MCEV operating earnings are reconciled to Group MCEV earnings, as follows:

	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Group MCEV operating earnings after tax	**394**	543
Economic variances on life business	**(426)**	101
Economic variances on non-life business	**38**	(38)
Other non-operating variances on life business	**(12)**	(54)
Non-recurring items on non-life business	**(9)**	(75)
Finance costs attributable to owners	**(123)**	(168)
Tax on non-operating earnings	**169**	(54)
Group MCEV earnings after tax	**31**	255

Economic variances on life business

Negative economic variances reflect the difference between actual short-term rates and the long-term investment return assumption, widening of credit spreads and the fall in equity and property markets; partly offset by the positive impact of a falling yield curve.

Economic variances on non-life business

MCEV was positively impacted by a decrease in the market value of the Tier 1 Bonds which increased MCEV earnings by £48 million before tax (2010: reduced MCEV earnings by £40 million before tax). This gain was partly offset by losses on interest rate swaps held in the Holding Companies.

Other non-operating variances on life business

Other non-operating variances on life business of negative £12 million before tax primarily relate to regulatory change and systems transformation costs.

Non-recurring items on non-life business

Overall, non-recurring items on non-life business reduced embedded value by £9 million before tax. Non-recurring items include restructuring costs of £51 million (2010: £68 million) and regulatory change and systems transformation costs of £12 million (2010: £7 million). These costs are offset by a gain of £19 million arising from closing the Pearl Group Staff Pension Scheme to future accrual and implementing a pension increase exchange programme and a £35 million recovery of historic costs under the management services agreements with the life division.

Finance costs attributable to owners

	Year ended	Year ended

	31 December 2011 £m	31 December 2010 £m
Debt finance costs[1]	**96**	102
Tier 1 coupon[2]	**27**	66
Finance costs attributable to owners	**123**	168

1 Finance costs in respect of the Impala and Pearl facility agreements (and associated swap interest) and the Royal London Payment in Kind ('PIK') notes and facility.

2 The 2010 amount includes the 2010 coupon and 2009 deferred coupon on the Tier 1 Bonds. The 2009 deferred Tier 1 Bond coupon of £33 million was paid in November 2010.

Group MCEV

Group MCEV increased by £14 million over the year to £2,118 million at 31 December 2011 as shown below:

Movement in Group MCEV	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Group MCEV at 1 January	**2,104**	1,827
Group MCEV earnings after tax	**31**	255
Other comprehensive income:		
Actuarial gains on defined benefit pension scheme (net of tax)	**32**	27
Capital and dividend flows	**(49)**	(5)
Group MCEV at 31 December	**2,118**	2,104

The actuarial gains on defined benefit scheme relate to the Pearl Group Staff Pension Scheme and were capped at the point at which the Scheme returned to surplus on an accounting basis. Capital and dividend flows in 2011 mainly comprise external dividend cash payments of £55 million.

GROUP IFRS OPERATING PROFIT

£387m

IFRS operating profit

Group IFRS operating profit

The Group has generated an IFRS operating profit of £387 million (2010: £373 million), demonstrating the strength of its business model.

Group operating profit	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Phoenix Life	**395**	388
Ignis Asset Management	**46**	46
Group costs	**(54)**	(61)
Operating profit before tax[1]	**387**	373

1 Operating profit is presented before adjusting items.

Phoenix Life

Operating profit for Phoenix Life is based on expected investment returns on financial investments backing shareholder and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities (being the release of prudential margins and the interest cost of unwinding the discount on the liabilities). The principal assumptions underlying the calculation of the longer term investment return are set out in note 5 to the IFRS consolidated financial statements.

Operating profit includes the effect of variances in experience for non-economic items, such as mortality and expenses, and the effect of changes in non-economic assumptions. Changes due to economic items which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are accounted for outside of operating profit. Phoenix Life operating profit is net of policyholder finance charges and policyholder tax.

Phoenix Life operating profit	**Year ended 31 December 2011 £m**	Year ended 31 December 2010 £m
With-profit	**69**	55
With-profit where internal capital support provided	**66**	(7)
Non-profit and unit-linked	**206**	278
Longer term return on owners' funds	**37**	42
Management services	**17**	20
Phoenix Life operating profit before tax	**395**	388

The owners' one-ninth share of the policyholder with-profit bonus of £69 million increased by £14 million on the 2010 result primarily due to higher terminal bonuses following an increase in maturities, and improved bonus rates.

The with-profit funds where internal capital support has been provided experienced an operating profit of £66 million (2010: £7 million operating loss). The 2011 result included the benefits of modeling improvements of £21 million (2010: negative £20 million) and data cleansing benefits of £18 million following the transfer of policies onto the BaNCS policy administration platform. This was partly offset by a reduction in assumed surrender rates in funds with valuable policyholder guarantees of £5 million (2010: £37 million). The 2010 operating profit included £17 million of margins on funds where internal capital support is no longer required.

The operating profit on non-profit and unit-linked funds was £206 million (2010: £278 million). This includes margin emergence of £162 million (2010: £168 million), return on surplus assets of £10 million (2010: £18 million) and new business from vesting annuities of £27 million (2010: £22 million). The benefits of data cleansing projects of £33 million in 2011 were offset by negative longevity and mortality assumption changes of £29 million. The 2010 result benefited from positive longevity and morbidity assumption changes of £41 million.

The longer term return on owners' funds for 2011 of £37 million reflects the asset mix of owners' funds: primarily cash based assets and fixed interest securities. The investment policy for managing these assets remains prudent.

The operating profit for management services of £17 million (2010: £20 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 operating profit of the asset management business was stable as the costs of new business development were partly offset by an increase in fees earned on managing stock lending collateral.

Ignis Asset Management operating profit	**Year ended 31 December 2011 £m**	Year ended 31 December 2010 £m
Third party[1]	**29**	29
Life fund revenue[2]	**114**	113
Other income	**3**	2
Total revenues	**146**	144
Staff costs	**(64)**	(59)
Other operating expenses	**(36)**	(39)
Total expenses	**(100)**	(98)
Ignis Asset Management operating profit before tax	**46**	46

1 Includes performance fees of £1 million (2010: £nil).

2 Includes performance fees of £33 million (2010: £35 million).

The increase in expenses reflects investment in additional asset management capability together with the infrastructure to support growth in third party business. This includes new premises in London, building up support functions and investing in system architecture.

Group costs

Group costs were £54 million in the period of which costs relating to Group functions amounted to £39 million before tax (2010: £40 million). The balance of the charge in both periods relates primarily to pension scheme costs, partly offset by miscellaneous income.

IFRS result after tax

The IFRS operating result is reconciled to the IFRS result after tax, as follows:

	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Operating profit before adjusting items	**387**	373
Investment return variances and economic assumption changes on long-term business	**(338)**	18
Variance on owners' funds	**9**	19
Amortisation of acquired in-force business and other intangibles	**(139)**	(150)
Non-recurring items	**14**	(139)
(Loss)/profit before finance costs attributable to owners	**(67)**	121
Finance costs attributable to owners	**(110)**	(115)
(Loss)/profit before the tax attributable to owners	**(177)**	6
Tax credit attributable to owners	**79**	74
(Loss)/profit for the period attributable to owners	**(98)**	80

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

Overall, the Phoenix Life business had unfavourable investment return variances and economic assumption changes of £338 million in 2011. This reflects the widening of credit spreads and the falling yield curve as the increase in liabilities calculated on a prudent basis was not fully offset by a corresponding increase in assets.

Variance on owners' funds

The favourable variance on owners' funds of £9 million for 2011, mainly relates to fair value gains on swaps and gilts held in the shareholder funds.

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 £121 million (2010: £132 million). Amortisation of other intangible assets totalled £18 million in the period (2010: £18 million).

Non-recurring items

Non-recurring items include restructuring costs of £37 million (2010: £103 million) and regulatory change and systems transformation costs of £21 million (2010: £36 million). These costs are offset by a gain of £37 million arising from closing the Group's pension schemes to future accrual and implementing a pension increase exchange programme and a £35 million recovery of historic costs under the management services agreements with the life division.

Finance costs attributable to owners

	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m
Debt finance costs[1]	**96**	102
Other finance costs	**14**	13
Finance costs attributable to owners	**110**	115

1 Finance costs in respect of the Impala and Pearl facility agreements (and associated swap interest) and the Royal London PIK notes and facility.

Tax credit attributable to owners

The Company is exempt from tax in the Cayman Islands on any profits, income, gains or appreciations for a period of 30 years from 11 May 2010 (the previous exemption was for 20 years from 15 January 2008).

With effect from the acquisition of the Pearl businesses in the third quarter of 2009, the Company has been managed and controlled from Jersey, where its permanent office premises are located. As a Jersey resident holding company the Company is 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 subsidiaries, excluding Opal Re, have their centre of operations.

The Group tax credit for the period attributable to owners is £79 million, based on a loss (after policyholder tax) of £177 million. The difference between the actual credit of £79 million and the expected credit (based on the UK corporation tax rate of 26.5%) of £47 million primarily reflects the benefit of a decrease of £41 million in deferred tax liabilities as a result of the ongoing reduction in UK corporation tax rates and a £47 million benefit from the resolution of legacy tax issues, partly offset by the £49 million impact of losses and deductions not fully valued by the Group, or for which relief at the full rate of tax is not available.

GROUP ASSETS UNDER MANAGEMENT

Group assets under management represent all assets actively managed or administered by or on behalf of the Group including life companies' funds managed by third parties. It includes Holding Company cash and cash equivalents but excludes stock lending collateral.

Group assets under management	Life and Holding Companies £bn	Third party £bn	Total Group assets under management £bn	Stock lending collateral £bn	Total including stock lending collateral £bn
As at 1 January 2011	**62.1**	**7.5**	**69.6**	**9.2**	**78.8**
Inflows	–	2.6	2.6	1.6	4.2
Outflows	(4.4)	(0.9)	(5.3)	–	(5.3)
Market movements	5.8	–	5.8	–	5.8
Other[1]	–	(0.6)	(0.6)	–	(0.6)
As at 31 December 2011	**63.5**	**8.6**	**72.1**	**10.8**	**82.9**

1 Includes the transfer of £1.0 billion of assets in respect of the Hexam partnership following its restructuring in 2010. £0.9 billion of third party assets under management in respect of the Argonaut Capital Partnership are due to transfer from Ignis administration in the first half of 2012.

Life and Holding Companies' assets increased by £1.4 billion to £63.5 billion in the year as positive market movements of £5.8 billion, driven by gilt holdings, offset the run-off of the closed life business of £4.4 billion.

Third party (including Group pension schemes) net inflows were £1.7 billion in the year (2010: £1.3 billion) mainly reflecting strong sales of real estate and liquidity funds and a £0.4 billion new rates Liability Driven Investing ('LDI') mandate from the PGL Pension Scheme.

Of the assets in the table above, Ignis manages, provides oversight and advisory services on or administers the following:

Ignis assets under management	Life and Holding Companies £bn	Third party £bn	Total Ignis assets under management £bn	Stock lending collateral £bn	Total including stock lending collateral £bn
Direct asset management	54.7	8.6	63.3	10.8	74.1
Oversight and advice	7.2	–	7.2	–	7.2
Administration	0.2	–	0.2	–	0.2
As at 31 December 2011	**62.1**	**8.6**	**70.7**	**10.8**	**81.5**

CAPITAL MANAGEMENT

£1.3bn

IGD surplus (estimated)

£3.1bn

IGD Excess Capital (estimated)

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
- Optimise the overall gearing ratio to ensure an efficient capital base
- Meet the dividend expectations of shareholders as set by the Group's dividend policy, within the restrictions in the Group's two main credit agreements.

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

The capital policy of the Holding Companies ensures sufficient liquidity to meet creditor obligations. This is monitored at both Executive Committee and Board level.

Targets are established in relation to regulatory capital requirements and debt ratios and are used in managing capital in accordance with the Group's risk appetite and the interests of its stakeholders.

The capital policy of each life company is set and monitored by each life company board. 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 maintain sufficient capital at all times to meet the regulatory capital requirements mandated by the FSA[1]. These measures are aggregated under the European Union Insurance Groups' Directive ('IGD') as implemented by the FSA, to calculate regulatory capital adequacy at a Group level.

The Group's IGD assessment is made at the level of the highest EEA insurance group holding company, which is PLHL. The estimated IGD surplus at 31 December 2011 is £1.3 billion (2010: £1.0 billion). The components of the estimated IGD calculation are shown below:

	31 December 2011 £bn	31 December 2010 £bn
Group capital resources ('GCR')	**5.6**	5.3
Group capital resource requirement ('GCRR')	**(4.3)**	(4.3)
IGD surplus (estimated)	**1.3**	1.0

1 Further details on the regulatory capital requirements of the individual life companies are included within note 42 of the IFRS financial statements.

The key drivers of the change in solvency position in the year are:

- Capital generation items[1] of £0.6 billion including capital benefits from the transfer of the Phoenix & London Assurance Limited business into Phoenix Life Limited (effective from 1 January 2011) and the recapture of an internal reinsurance arrangement
- Partly offset by the payment of dividends, debt interest and debt repayments of £0.3 billion.

The Group's capital policy, which is agreed with the FSA, is to maintain GCR at the PLHL level of:

- 105% of the with-profit insurance component ('WPICC'), being an additional capital requirement of with-profit funds; plus
- 145% of the GCRR less the WPICC.

The Group's headroom at 31 December 2011 was £0.4 billion (2010: £0.1 billion).

IGD Excess Capital

IGD Excess Capital represents a more realistic measure of the capital strength of the Group as it includes policyholder and certain shareholder capital which is currently excluded under FSA rules from the PLHL Group's IGD surplus calculation. This capital provides the Group with financial flexibility and is available to protect policyholders and shareholders from adverse events.

The excluded capital relates to:

- The surplus estate of the with-profit funds which is treated as a policyholder liability for IGD purposes due to the closed fund nature of the business
- Restricted surplus which mainly relates to surplus excluded from the IGD calculation due to the corporate structure of the PLHL Group.

At 31 December 2011 the IGD Excess Capital was £3.1 billion (2010: £2.8 billion) and is reconciled to the IGD surplus as shown below:

	31 December 2011 £bn	31 December 2010 £bn
IGD Excess Capital	**3.1**	2.8
Restricted surplus	**(0.3)**	(0.4)
Excess policyholder capital	**(1.5)**	(1.4)

IGD surplus (estimated)	**1.3**	1.0

1 Capital generation includes increases in GCR as well as reductions in the GCRR.

Sensitivity and scenario 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 our target in a range of stress conditions. The results of that stress testing are provided below:

	Estimated IGD surplus	IGD Excess Capital
Base: 31 December 2011	1.3	3.1
Following a 20% fall in equity markets	1.3	3.0
Following a 15% fall in property values	1.2	3.0
Following a 75bps parallel increase in yields	1.2	2.9
Following a 75bps parallel decrease in yields	1.2	3.1
Following credit spread widening[1]	1.2	2.9
Combined stress[2]	1.1	2.5

1 10 year term: AAA – 52bps, AA – 72bps, A – 104bps, BBB – 152bps.

2 20% fall in equity markets, 10% fall in property, 80bps increase in yields and credit spreads widening (10 year term: AAA – 70bps, AA – 97bps, A – 140bps, BBB – 205bps).

The relative insensitivity of the Group's IGD surplus reflects the impact of hedges put in place as part of the long-term strategy to protect the Group from extreme market movements. The IGD Excess Capital is more sensitive to market movements than the IGD surplus because it includes excess policyholder capital in the non-supported with-profit funds which hold more equities, property and non-duration matched credit than other funds. This policyholder capital is excluded from in the IGD surplus.

Solvency II
The Group has a well established Solvency II programme and has continued to progress development towards meeting the Solvency II requirements. 2012 is a key year in the development of Solvency II. The Omnibus II Directive and the Level 2 Implementing Measures are expected to be approved by the European Parliament and adopted by the European Council during 2012. Also, the European Insurance and Occupational Pensions Authority ('EIOPA') will consult on Level 2 technical standards and Level 3 guidelines and recommendations and will submit final proposals to the European Commission during the year. The Group remains actively engaged in supporting the development of Solvency II through industry consultation and participation in FSA and ABI industry fora. As part of the negotiations surrounding the Omnibus II Directive the time frame for implementation of Solvency II is being discussed. The FSA's implementation assumptions are that 1 January 2013 will be the date at which the responsibilities of supervisors and EIOPA will commence, but Solvency II requirements will not commence for firms until 1 January 2014.

The Group remains on track to deliver an approved partial Group internal model and was accepted into the pre-application phase of the FSA internal model approval process following the submission of the pre-application qualifying criteria template in 2010. In respect of the resources the FSA will devote to the pre-application process, it has stated that it will concentrate its resources on a smaller population of firms representing a significant market share and which it regards as having the highest potential impact on its objectives. The Group is included in this category and remains in continuous and constructive dialogue with the FSA in this regard. The Model Governance Committee, established in 2011, will continue to play a central role in the oversight of the design, implementation and operation of the partial internal model being built for Solvency II. Furthermore, the Group's application for internal model approval will be supported by a continued programme of education for its Boards, Committees and senior management who will review and challenge the outputs from the internal model over the coming year.

The Group's Actuarial Systems Transformation project ('AST') will deliver a single actuarial modelling platform across the business, transforming modelling capability and efficiency and underpinning development of the Solvency II internal model and Own Risk and Solvency Assessment.

Capital resources
The primary sources of capital used by the Group are equity and borrowings.

Leverage
In managing capital the Group seeks to optimise the level of debt on its balance sheet. The Group's closed book business model allows it to operate with higher leverage than life companies that are still writing new business, as it does not need to fund upfront capital requirements and new business acquisition expenses.

The Group has net shareholder debt of £2,140 million (2010: £2,733 million). The gearing ratio[1] is 46% (2010: 52%) based on Ignis present value of future profits ('PVFP') of £0.4 billion (2010: £0.4 billion) and an MCEV of £2,118 million (2010: £2,104 million).

Shareholder debt (including hybrid debt) at 31 December 2011:

	31 December 2011 £m	31 December 2010 £m
Bank debt at face value		
– Pearl facility	**400**	425
– Pearl loan notes	**78**	76
– Impala facility	**1,993**	2,138
– Royal London PIK notes and facility	**111**	106
Tier 1 Bonds at market value	**256**	304
PLL subordinated debt at market value	**139**	170
Shareholder debt (including hybrid debt)[2]	**2,977**	3,219
Holding Company cash and cash equivalents	**(837)**	(486)
Net shareholder debt	**2,140**	2,733

1 Net shareholder debt as a percentage of the sum of Group MCEV, net shareholder debt and PVFP of Ignis.

2 The unsecured loan notes of £7 million (2010: £12 million) are excluded from this shareholder debt analysis as their repayment will be funded in 2012 from an escrow account which is not included in the Holding Company cash and cash equivalents.

Further detail on shareholder debt is included in note 22 to the IFRS financial statements.

The Group has two main credit agreements (the Pearl and Impala facilities), which have separate security arrangements. Although these facilities carry favourable interest rates and are tax efficient, they are scheduled to mature in the period 2014 to 2016.

The Group's target is to reduce the gearing ratio to 43% or below during the course of 2012.

Liquidity management

Details of the Group's objectives and policies for the management of liquidity risk are included within the Risk management section and note 43 of the IFRS financial statements.

RISK MANAGEMENT

Risk management lies at the heart of what we do and is a source of value creation, making it a key component of the Group's strategic agenda. The Board seeks to ensure that the Group identifies and manages all risks accordingly, either to create additional value for its stakeholders or to mitigate any potentially adverse effects. A summary of the principal risks and uncertainties facing the Group is provided on page 42.

The Group's Risk Management Framework

The Group operates a Risk Management Framework ('RMF') which seeks to establish a coherent and interactive set of arrangements and processes to support the effective management of risk throughout the Group. The components of the framework are shown below. The outputs of the RMF provide assurance that risks are being appropriately identified and managed and that an independent assessment of management's approach to risk management is being performed.

During the year, the Group has continued to strengthen the components of the RMF to ensure that they are aligned with the requirements of Solvency II and external best practice.

Risk strategy

The Group's risk strategy provides an overarching view of how risk management is incorporated consistently across all levels of the business, from decision-making to strategy implementation. It also sets out how overall risk management within the Group is proportionate to the nature, scale and complexity of the risks faced by the business.

Risk appetite

The Group's risk appetite framework consists of a set of statements and targets that articulate the level of risk the Group is willing to accept, in pursuit of shareholder value and achievement of the Group's strategic objectives. The statements encapsulate policyholder security, earnings volatility, liquidity and the internal control environment as follows:

- **Capital –** The Group and each life company will hold sufficient capital to meet regulatory requirements in a number of asset and liability stress scenarios

- **Cash flow –** The Group will seek to ensure that it has sufficient cash flow to meet its financial obligations and will continue to do this in a volatile business environment
- **Embedded value –** The Group will take action to protect embedded value
- **Regulation –** The Group and each life company will, at all times, operate a strong control environment to ensure compliance with all internal policies and applicable laws and regulations, in a commercially effective manner.

The risk appetite framework supports the Group in operating within the boundaries of these statements by seeking to limit the volatility of key parameters, defined with respect to the above statements, under a range of adverse scenarios agreed with the Board. Risk appetite limits are chosen which specify the maximum acceptable likelihood for breaching the agreed limits and assessment against the appetite targets is undertaken through scenario testing. Breaches of appetite are corrected through management actions where appropriate.

Risk universe

A key element of effective risk management is to ensure that the business has a complete and robust understanding of the risks it faces. Within the Group, these are set out, categorised and defined in the risk universe.

These risks are monitored and reported across the organisation to ensure that they are adequately managed.

External communication and stakeholder management

The Group has a number of internal and external stakeholders, each of whom has an active interest in the Group's performance, including how it is managing its risks. Significant effort is made to ensure that our stakeholders have appropriate, timely and accurate information to support them in forming views of the Group.

Governance, organisation and policies

Overall responsibility for approving, establishing and maintaining the RMF rests with the Board. The Board recognises the critical importance of having an efficient and effective RMF and appropriate oversight of its operation. There is a clear organisational structure in place with documented, delegated authorities and responsibilities from the Group Board to the Board of Phoenix Life Holdings Limited ('PLHL') and the Executive Committee.

The RMF is underpinned by the operation of a three lines of defence model with clearly defined roles and responsibilities for statutory boards and their committees, management oversight committees, Group Risk and Group Internal Audit.

First line: management of risk is delegated from the Board to the Group Chief Executive Officer, Executive Committee members and through to business managers. A series of business unit management oversight committees operate within the Group. They are responsible for ensuring the risks associated with the business's activities are identified, assessed, controlled, monitored and reported.

Second line: risk oversight is provided by the Group Risk function and business unit risk and compliance functions and the Board Risk Committee, which is responsible for the oversight of risk across the Group. The Board Risk Committee comprises five Non-Executive Directors, three of whom are independent. It is supported by the Chief Risk Officer and met six times during the year.

Third line: independent verification of the adequacy and effectiveness of the internal controls and risk management is provided by the Board Audit Committee, which is supported by the Group Internal Audit function.

Risk organisation

The Chief Risk Officer manages the Group Risk function and has responsibility for the implementation and oversight of the Group's RMF. The Group Risk function has responsibility for financial and operational risk, risk governance, FSA relationship management and regulatory risk. Risk review functions across the Group manage the RMF in line with the Group's established standards. The risk functions ensure that business unit risk committees are provided with meaningful risk reports and that there is appropriate information to assess and aggregate risks.

Risk policies

The Group policy framework comprises a set of policies that support the delivery of the Group's strategy by establishing operating principles and expectations for managing the key risks to our business. The policy set contains the minimum control standards that each business unit must adhere to and report compliance against through the operation of local processes/procedures. The policies define:

- The individual risks the policy is intended to manage
- The degree of risk the Group is willing to accept (which is set out in the policy risk appetite statements)
- The minimum controls required in order to manage the risk to an acceptable level
- The frequency of the control's operation.

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

Business performance and capital management

Business unit plans are assessed to ensure that they do not breach any of the Board's risk appetite statements over the planning horizon. Business performance is routinely monitored at a business unit executive level with consolidated reporting against the annual operating plan approved by the Board and reviewed by the Executive Committee.

The impact of any proposed changes to the Group's operating plan and ongoing compliance with the Group's risk appetite statements are reviewed on a quarterly basis by the Board Risk Committee.

The Group's business units operate capital management processes that meet the Group's Capital Management Policy. Under these processes, capital is allocated across risks where capital is held as a mitigant and, in turn, to individual risk owners who hold risk capital budgets. The amount of risk capital required is reviewed regularly to ensure the risk remains within budget. Any increases in capital allocation required are referred to the relevant business unit for approval to assess whether the increased capital allocation requested is within appetite for that particular risk type or whether further risk mitigation is required.

Risk and capital assessment

The Group operates 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 and establishes a basis, not only for the approach to risk assessment, management and reporting 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 their financial impact.

A Group level risk assessment process determines the most significant risks to the Group and the options available for their management.

Management information

Overall monitoring and reporting against the risk universe is undertaken through business unit management committees through to the relevant business unit executive committee and reported to the Executive Committee, PLHL Board and Group Board via regular risk reporting.

The Board Risk Committee receives a consolidated risk report on a quarterly basis, detailing the risks facing the Group and the overall position against risk appetite limits. The Board Risk Committee is also provided with regular reports on the activities of the Group Risk function.

People and reward

Effective risk management is central to the Group's culture and its values. Processes are operated that seek to measure both individual and collective performance and discourage incentive mechanisms which could lead to undue risk taking. Training and development programmes are in place to support employees in their understanding of the operation of the RMF and during 2011, Group Risk delivered training and awareness sessions across the Group.

Technology and infrastructure

The Group employs systems to support the assessment and reporting of the risks it faces as a business and to enable management to document its key risks and controls and evidence the assessment of them at a frequency appropriate to the operation of the control. The Group is continuing to assess the need for additional systems to further support the embedding of the RMF.

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 its business units. The emerging cash flows of the Group may be impacted during periods of extreme	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

	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.	implement de-risking strategies to mitigate against unwanted outcomes. The Group also maintains cash buffers in its Holding Companies to reduce reliance on emerging cash flows.
The Group could be adversely affected by the level of its indebtedness and its financing structure.	The total principal amount outstanding under the Groups main credit facilities as at 31 December 2011 was £2,471 million. These main credit facilities require that a significant portion of the principal amount outstanding is repaid in the years 2014 to 2016. The Group may need to refinance the outstanding principal amounts on terms which are not as favourable as the existing terms or it may be unable to refinance those obligations at all.	The Group undertakes regular meetings and reviews with the lending banks to ensure open dialogue is maintained and that all relevant parties are aware ofthe current position.
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 its lending syndicates. In the event that transfers from the Group's insurance and investment management subsidiaries are limited by any law, regulatory action or change in established approach, 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.	The Group puts considerable effort into managing relationships with its regulators so that it is 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.	Assets held to meet obligations to policyholders include debt securities. Phoenix Life 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. 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 reinsurance and derivative positions are appropriately collateralised and 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.

CORPORATE RESPONSIBILITY

"Corporate Responsibility at Phoenix Group is about doing the right thing and acting responsibly in everything we do. We wish to be seen as a company that prospective employees wish to join, investors wish to support, customers choose to remain with and at the same time create opportunities to forge links within our local community."

Clive Bannister
Group Chief Executive Officer

In this section

CORPORATE RESPONSIBILITY

At Phoenix Group we are committed to managing our business in a responsible manner, taking seriously the impact we have on our employees, our stakeholders, the communities in which we operate and the wider environment. We believe that operating responsibly creates value for our business through building the trust and confidence of our stakeholders.

Corporate Responsibility ('CR') is firmly embedded in our corporate culture and built into our governance framework through a Group CR Policy which is sponsored by the Group Chief Executive Officer.

During 2011 we have taken time to reflect on what has already been achieved, how this links with our aspirations and how we can best further develop our programme into the future, being mindful of the current economic climate.

We have been members of Business in the Community ('BITC') for the past year, which has given us excellent support and has provided a useful insight into what has worked best for other companies – helping us to further shape our programme.

Following the refresh of our Group website at www.thephoenixgroup.com we now have a comprehensive section for CR, which explains more about our programme and provides more detail on our CR activities.

At Phoenix Group we categorise and report on CR in four areas.

Environment

Our environmental impact is lower than that of many other industries, however, we recognise that we have a duty to ensure this impact, however small, is minimised. Our employees also have a shared desire to protect and preserve the wider environment. As part of our staff CR awareness programme we provided staff with information to help them consider their impact on the environment, both at home and in the workplace.

Some environmentally friendly initiatives undertaken by the Group this year are noted below:

- We introduced a paper cup recycling facility (previously 900 cups per day were sent to landfill). This facility joins our other recycling collections – paper, plastic, cardboard, ink cartridges and mobile phones
- Employees collected in excess of five sacks of Christmas cards which were passed on to a recycling scheme that pledged to plant 1 tree for every 1,000 cards donated
- Two new flexible benefit options were introduced: the opportunity to purchase a bicycle tax-free for use in commuting to and from work and membership of the Woodland Trust
- Following site moves all unusable stationery items were donated to local schools and nurseries and surplus fixtures and fittings were recycled
- Our new office site for Ignis in London has an excellent BREEAM rating, with its own environmental policy. As tenants we are obliged to comply with this policy.

Looking ahead, some of our plans for 2012 are noted below:

- By the end of 2012, all of our paper will be Programme for the Endorsement of Forest Certification ('PEFC') and Forest Stewardship Council ('FSC') sourced from sustainable, managed forests
- IT systems in Phoenix Life and Group will be updated, including video and teleconferencing facilities thus reducing the need for business travel. Our existing equipment will be re-used, recycled or disposed of via a registered 'Waste Electrical and Electronic Equipment' scheme.

Alan Jones, Group HR Director comments on our CR staff awareness programme: *"We aim to create a fulfilling working environment in which every individual can excel and contribute to our ongoing CR programme. By providing a platform for encouraging community and environmental awareness, we are providing staff with the necessary skills to make a difference, both at work and at home."*

Community

Despite the current economic climate, Phoenix Group continues to support a number of charity and community initiatives. Our commitment to the community leads to greater employee engagement and is welcomed by our customers, suppliers and potential employees.

The Group's approach to charitable donations is three-fold: an annual programme of staff fundraising events held at our offices; matched donations for employees participating in charitable activity and donations to selected causes.

A staff volunteering programme was also established during the year and good links were forged with schools and community groups operating in the vicinity of our largest office in Wythall.

Further details on our community activities are provided within the Corporate Responsibility section of our Group website.

Charitable giving

During 2011 just under £100,000 was donated by Phoenix Group to selected charities. Our focus has been on selecting and supporting charities which benefit the local communities in which we live and work and those nominated by our staff.

In addition to the above donations made by the Group, over £20,000 was raised for charities selected by employees through fundraising activities organised on our premises.

Volunteering

During the year the Group formalised its volunteering programme and gave staff at its Wythall site the opportunity to participate in two one-day events. The first, was undertaken as part of the national BITC 'Give and Gain Day', whilst the second, was arranged directly through links with a local secondary school. Both events were beneficial in helping forge stronger links with the local community and building employee engagement.

Community links

The Group developed links with a variety of community groups operating close to its Wythall site including local schools, the City of Birmingham Choir and the Wythall Community Association.

2011 was the 15th successive year that Ignis Asset Management was the main sponsor of the annual Women's 10k Road Race in Glasgow. The race regularly attracts over 12,000 runners and organisers Glasgow Life estimated that more than £1 million was raised for numerous charitable causes.

Workplace

Phoenix Group employed 1,394 staff at the end of December 2011 across three divisions – Group, Phoenix Life and Ignis Asset Management, mainly based at sites in London, Wythall and Glasgow.

Employee engagement

Employee engagement helps drive business performance and so increases value for our policyholders and shareholders. Phoenix Group and Phoenix Life were short-listed for the Marketing Society's Employee Engagement Award, and won the 2011 Strategic Communications Management (Melcrum) Award for Excellence in Employee Engagement, highlighting our success in this area. At time of going to print we are also delighted to report that Phoenix Group is one of 'Britain's Top Employers 2012'. This certification is awarded only to organisations that meet the highest standards in Human Resources policy benchmarking. The companies awarded with this certification have all been independently recognised as being amongst the best companies to work for in the UK.

All divisions participated in the same employee survey this year achieving an overall employee engagement index ('EEI') of 74% with a response rate of 93%.

Phoenix Life and Group returned an EEI of 78%, an increase of 1% on 2010, and for all questions, were at or above Financial Services Benchmark (or Private Sector Benchmark where a Financial Services comparison is not available). This was the second year that Ignis participated and its EEI increased from 60% to 68%.

Employee benefits

Our ability to attract and retain the best and most talented people represents a key focus area for the Group. We continue to offer our staff access to a range of policies and benefits including:

- Personal development plans
- Transparent remuneration benchmarking and reward programmes
- Flexible benefits scheme
- Share-save scheme
- Opportunity to participate in regular and transparent employee surveys
- Succession planning

- Fully trained people managers
- Clear anti-discrimination and anti-bullying policies
- Access to flexible working arrangements.

Diversity
We value diversity in the workplace and have a strict equal opportunities policy. At least 11% of our workforce this year is of 'non-white British' origin, and our gender split is 60% male, 40% female. Three out of nine members of the Group Executive Committee are female and we have one female non-executive on the Phoenix Group Holdings Board. Our Chairman commented during the year on 'Women on Boards', noting that we have set targets of two female directors on the Phoenix Group Holdings Board by 2013 and a further female director by 2015.

Employee metrics
The Human Resources function continues to monitor employee metrics related to turnover, sickness and training. Employee metrics help us to compare ourselves to industry benchmarks and previous years. Staff turnover is down compared to last year and we are pleased to report we are now below the industry average of 8.7% for employees leaving voluntarily. We also recorded one of the lowest levels of absence through sickness in our sector.

	2011	2010	2009
Staff turnover (employees choosing to leave voluntarily)	**7.5%**	9.9%	3.8%
Annual new starter turnover (number of employees leaving voluntarily within 12 months of starting)	**10.0%**	13.0%	7.3%
Percentage of days lost through sickness	**1.4%**	1.3%	1.6%
Percentage of employees sponsored on a professional qualification	**22.6%**	17.4%	21.1%

Staff training
In 2011 we started to track two new measures around external staff training and spend. In addition to the externally run training days, our Learning and Development team managed a range of in-house training sessions, ranging from induction programmes, through to coaching and leadership skills. During the year staff within our Phoenix Life and Group divisions received training on our Risk Management Framework, which amounted to 850 training days. This helps demonstrate our commitment to continuing education within the workplace and providing our staff with the necessary skills they need in a market which is becoming increasingly regulated and highly competitive. Recent benchmarking indicates that we invest approximately twice the sector average in learning and development.

	2011
Total number of external staff training days	**1,961**
Total spend on external staff training	**£1,137,123**

External stakeholders

Risk management/governance
Due to the highly regulated nature of our business and the importance of security to our policyholders, we take risk seriously and have a dedicated risk management team to measure and monitor all risks across our business. We also have a strong corporate governance framework in place. Information about the Group's management of risk and the Group's corporate governance framework can be viewed on pages 38 to 43 and 52 to 71 respectively.

Responsible investment
Phoenix Group supports the principles of good stewardship as set out on our Ignis website www.ignisasset.com. We take our responsibilities seriously and consider the environmental, social and governance procedures of companies in which we invest.

Investors
Two external presentations were given during the year by our Investor Relations department, to allow our investors to understand better our Phoenix Life and Ignis Asset Management divisions.

Procurement/suppliers
During 2011 we strengthened our Procurement policy, commenced implementation of our Strategic Supplier Management Framework and reviewed our standard terms and conditions – all of which are in line with our CR programme. In 2012 we intend to optimise collaborative working across our Group with our suppliers and outsourced partners to achieve a higher level of integrated, sustainable and responsible supplier relationships.

Media
During 2011, we have kept the local press up-to-date with our CR initiatives which has helped to share information within our local community and has consequently led to an increased local awareness of the Group.

Customers
The Group recognises the responsibility we have to our customers, as both custodian of their financial assets, supplier of their pension and investment needs and life cover.

Customer satisfaction
We expanded our research programme to further understand what our customers think about us and the service we offer. From our programme of focus groups, detailed telephone interviews and face-to-face meetings, we believe our customers are happy with the service they receive from us.

By continually listening to our customers, we can focus on any areas of improvement to ensure that we provide a responsible, fair and helpful service.

Improving outcomes
As part of our overall strategy to improve outcomes for our customers, we wrote to a group of policyholders who held paid-up life insurance policies, to give them the opportunity to cash in without penalty and benefit from any proceeds immediately, or to keep the policy in force for their estate to benefit from the life insurance pay-out on their death. Over 85% of those contacted who were eligible for the offer, accepted and chose to cash in their benefits.

Mike Merrick, Chief Executive Officer, Phoenix Life comments on the initiative: *"We recognised that many customers will have taken out these policies to cover funeral expenses but with the impact of inflation, the real value of these policies was eroding. We wanted to offer these customers a choice – to either keep the policy in force or take the benefits to save or spend as they choose."*

We have worked on improving the way we communicate with our customers and this will continue to be a focus during 2012. There are customers who may have forgotten they have a policy with us and we will be looking at different ways to find these customers and reduce the incidence of 'missing' customers in the future.

Dealing with complaints
We take complaints very seriously and we recognise that with approximately six million customers and several million transactions being handled each year, that there will be occasions when our customers feel the need to express their dissatisfaction. It is important that customers can contact us easily when they wish to complain and that they can be confident of someone resolving the complaint promptly.

Further information on our complaints data can be viewed on our website.

Third party services
In line with our 'Treating Customers Fairly' proposition, we have carefully selected third party providers to offer our customers an increased range of products and services which we do not offer ourselves and which meet their needs. For example, we are currently piloting an arrangement with a specialist annuity provider to make it easier for our customers to get access to enhanced annuities.

Conclusion
In summary, 2011 has been a busy year for our CR programme as we have been formalising and communicating our approach. We are delighted with the progress that has been made and in particular the support our employees have given. In 2012, we will give higher profile to the communication of different aspects of our programme to our employees and we will set measurable environmental targets. We are absolutely committed to remaining a responsible organisation and employer.

For more information on Phoenix Group's Corporate Responsibility programme, please contact corporateresponsibility@thephoenixgroup.com.

GOVERNANCE

Strong and effective governance is crucial to our aim of delivering value to shareholders and policyholders.

The Board is committed to high standards of corporate governance. This section includes details of our application of the provisions of the UK Corporate Governance Code and profiles of our Board of Directors.

In this section

BOARD OF DIRECTORS

Ron Sandler

Chairman
Ron Sandler was appointed Chairman of the Company on 24 September 2009. He is Chairman of Ironshore Inc, is an adviser to Palamon Capital Partners and was Executive Chairman of Northern Rock plc whilst the bank was in public ownership. Mr Sandler has an MA from Queens' College, Cambridge and an MBA from Stanford University. He was previously Chief Executive of Lloyd's of London and played a key role in the Lloyd's reconstruction and renewal programme. Subsequently, he was Chief Operating Officer of NatWest Group. In 2002, at the request of the Chancellor of the Exchequer, he led an independent review of the UK long-term savings industry. He is a recent past president of the Chartered Institute of Bankers. Mr Sandler is Chairman of the Board Nomination Committee.

Clive Bannister

Group Chief Executive Officer
Clive Bannister joined the Group in February 2011 as Group Chief Executive Officer. Prior to this, he was Group Managing Director of Insurance and Asset Management at HSBC. Clive joined HSBC in 1994 and held various leadership roles in Planning and Strategy in the Investment Bank (USA) and was Group General Manager and CEO HSBC Group Private Banking. He started his career at First National Bank of Boston and prior to working at HSBC was a partner in Booz Allen Hamilton in the Financial Services Practice providing strategic support to financial institutions including leading insurance companies, banks and investment banks. Throughout his career he has lived and worked internationally. Mr Bannister was appointed to the Board of Directors of the Company on 28 March 2011.

Alastair Lyons

Senior Independent Director
Alastair Lyons was appointed to the Board of Directors of the Company as Senior Independent Director on 29 March 2010. He is also Chairman of Admiral Group plc, the FTSE 100 direct motor insurer, Chairman of Serco Group plc, the FTSE 100 international services company, Deputy Chairman of Bovis Homes Group plc and Chairman of the Towergate Insurance Group. In his executive career he was Chief Executive Officer of the National Provident Institution, Executive Director of Abbey National responsible for the insurance division and Chief Executive Officer of the National & Provincial Building Society. He is a Fellow of the Institute of Chartered Accountants and has been a Non-Executive Director of both the Department for Work and Pensions and the Department for Transport. Mr Lyons is Chairman of the Board Audit Committee.

Ian Ashken

Non-Executive Director
Ian Ashken is Vice Chairman and Chief Financial Officer of Jarden Corporation, a NYSE listed Fortune 500 U.S. conglomerate. Mr Ashken has had extensive public company experience over the last 20 years, including as Chief Financial Officer of Benson Eyecare Corporation, Lumen Technologies and Bollé Inc. Mr Ashken is a Principal and Executive Officer of a number of private investment entities. He was appointed to the Board of Directors of the Company on 2 September 2009.

René-Pierre Azria

Non-Executive Director
René-Pierre Azria is Chief Executive Officer of Tegris Advisors LLC, a U.S. private advisory firm specialised in strategic financial analysis and mergers and acquisitions. Prior to founding Tegris, Mr Azria was a worldwide partner with Rothschild & Co. Prior to joining Rothschild in 1996, Mr Azria served as Managing Director of Blackstone Indosuez and President of Financiére Indosuez Inc. in New York. Mr Azria serves as a Director and Audit Committee member of Jarden Corporation, a NYSE listed Fortune 500 U.S. conglomerate and as a Director of two privately held book publishers in France and the U.S. Mr Azria was appointed to the Board of Directors of the Company on 2 September 2009. He is a member of the Board Investment and Board Risk Committees.

David Barnes

Non-Executive Director
David Barnes joined the RBS Group (then Williams & Glyn's Bank) in 1973 and remained there in various roles until his early retirement in February 2009. His roles included Relationship Banker in the then newly established Corporate Division, Managing Director of the Financial Institutions Relationship Management team and member and subsequently Chairman of RBS's Credit Committee. From 2005 he was responsible for all lending to financial institutions and for capital management for RBS's Financial Institutions Group. Mr Barnes was appointed to the Board of Directors of the Company on 2 September 2009. He is a member of the Board Audit and Board Remuneration Committees.

Charles Clarke

Non-Executive Director
Charles Clarke is a Jersey-resident Chartered Accountant who spent some 30 years with KPMG. Having qualified in London, he was a financial sector audit partner in London, Kuala Lumpur and Jersey. He was also senior partner of the KPMG Channel Island firm for seven years and, during his final year, Chairman of the grouping of KPMG member firms in offshore jurisdictions. Since retiring from KPMG at the end of 2005, he has acted as an independent Non-Executive Director ('NED') and established an offshore governance consultancy and NED recruitment service. His current NED appointments include SG Hambros Bank. Mr Clarke was appointed to the Board of Directors of the Company on 18 February 2010. He is a member of the Board Audit and Board Investment Committees.

Ian Cormack

Non-Executive Director
Ian Cormack is Non-Executive Chairman of Maven Income & Growth VCT 4 plc and is a Non-Executive Director of Bloomsbury Publishing Plc, Aspen Insurance Holdings, the Qatar Financial Centre and the Qatar Insurance Service. Mr Cormack was Chief Executive Officer of AIG, Inc. in Europe from 2000 to 2002 and was Chairman of Citibank International plc and co-head of the Global Financial Institutions Client Group at Citigroup. Mr Cormack served on the Board of Directors of the former Pearl Group Limited from May 2005 to September 2009. He was appointed to the Board of Directors of the Company on 2 September 2009. Mr Cormack is Chairman of the Board Remuneration Committee and a member of the Board Nomination Committee.

Tom Cross Brown

Non-Executive Director
Tom Cross Brown was Global Chief Executive of ABN AMRO Asset Management (which managed some €160 billion of assets, with offices in 30 countries around the world) from 2000 to 2003, as well as Chairman of ABN AMRO Asset Management in the UK from 1997 to 2003. Prior to this, he spent 21 years with Lazard Brothers in London, latterly as Chief Executive Officer of Lazard Brothers Asset Management. Mr Cross Brown is Non-Executive Chairman of Just Retirement (Holdings) Limited and is a Non-Executive Director of Artemis Alpha Trust plc, as well as of other private companies and charities. Mr Cross Brown served on the Board of Directors of the former Pearl Group Limited from May 2005 until September 2009. He was appointed to the Board of Directors of the Company on 24 September 2009. He is Chairman of the Board Investment Committee and a member of the Board Nomination and Board Risk Committees.

Manjit Dale

Non-Executive Director
Manjit Dale is a founding partner of TDR Capital, a private equity firm established in 2002. TDR Capital manages over €2.6 billion of assets on behalf of a variety of institutional pension funds, university endowments and wealthy private individuals. Prior to founding TDR Capital, Mr Dale was Managing Partner at Deutsche Bank Capital Partners Europe. He has served on the Boards of Pizza Express and Center Parcs and currently also serves on the Board of Algeco Scotsman. Mr Dale has over 20 years' experience in private equity, finance and consulting gained with Bankers Trust, 3i plc, NM Rothschild and Andersen Consulting. Mr Dale graduated from Cambridge University with an Honours Degree in Economics. He served on the Board of Directors of the former Pearl Group Limited from December 2004 to September 2009. Mr Dale was appointed to the Board of Directors of the Company on 2 September 2009 and is a member of the Board Investment Committee.

Isabel Hudson

Non-Executive Director
Isabel Hudson is a former Executive Director of Prudential Assurance Company Limited. She was also Chief Financial Officer at Eureko BV. Ms Hudson is Executive Chair of the National House Building Council and a Non-Executive Director of QBE Insurance, MGM Advantage and The Pensions Regulator and a member of the With-Profit Committee of Standard Life. Ms Hudson is Chairman of the business development Board of Scope, a UK charity, and has 30 years experience in the insurance

industry in the UK and mainland Europe. She was appointed to the Board of Directors of the Company on 18 February 2010. She is a member of the Board Risk and Board Remuneration Committees.

Hugh Osmond

Non-Executive Director

Hugh Osmond founded Punch Group and served as its Executive Chairman between 1997 and 2001, during which time he built Punch Group into one of the UK's largest pub companies. He previously co-led the acquisition and market listing of Pizza Express in 1993 and helped build it into the UK's largest sit-down restaurant chain. Mr Osmond served on the Board of Directors of the former Pearl Group Limited from December 2004 until September 2009. He was appointed to the Board of Directors of the Company on 2 September 2009 and is a member of the Board Investment and Board Risk Committees.

David Woods

Non-Executive Director

David Woods is a Fellow of the Institute of Actuaries and a Non-Executive Director of Standard Life UK Smaller Companies Trust plc, Murray Income Trust plc and The Moller Centre for Continuing Education. He is also Chairman of the pension fund trustee companies responsible for the governance of all the UK pension schemes in the Steria Group and is a trustee of the Scottish Provident Pension Fund. Between 1988 and 2002, he was Group Managing Director of the Scottish Provident Group and was Non-Executive Chairman of Royal Liver Assurance from 2003 to 2011. He was appointed to the Board of Directors of the Company on 18 February 2010 and is Chairman of the Board Risk Committee.

OUR MANAGEMENT TEAM

Executive management of the Group is led by the Group Chief Executive Officer, Clive Bannister, who is supported by the Executive Management Committee ('ExCo'). ExCo oversees matters relating to the implementation of the Group's strategy.

Clive Bannister

Group Chief Executive Officer

- Lead and direct the Group's businesses in delivery of the Group strategy and business plan
- Safeguard returns for policyholders and grow shareholder value
- Embed a risk-conscious Group culture which recognises policyholder obligations in terms of service and security
- Manage the Group's key external stakeholders.

Paul Miles

Acting Group Finance Director

- Contribute to the development and delivery of the Group's financial business plan in line with strategy
- Ensure the Group's finances and capital are managed and controlled
- Ensure the Group has effective processes in place to enable all reporting obligations to be met
- Support the Group Chief Executive Officer in managing the Group's key external stakeholders
- Maximise shareholder value though clear, rigorous assessment of business opportunities.

Mike Merrick

Chief Executive Officer, Phoenix Life

- Lead development and delivery of the Phoenix Life business strategy, including the continued integration of life businesses
- Ensure optimisation of outcomes for customers in terms of both value and security
- Ensure Phoenix Life deploys capital efficiently and effectively, with due regard to regulatory requirements.

Chris Samuel

Chief Executive Officer, Ignis Asset Management

- Lead development of Ignis' business strategy and plans
- Deliver, over the longer term, Ignis' vision of becoming a leading asset management business committed to performance excellence and innovation

- Ensure Ignis achieves its key goals of meeting or exceeding investment performance expectations, providing clients with creative solutions to changing product needs and maintaining a well controlled and efficient operating platform
- Ensure Ignis' chosen foundations of innovative people, a partnership culture, suitable processes and technology and stability are in place to support these plans.

Fiona Clutterbuck

Head of Strategy, Corporate Development and Communications
- Support the Group Chief Executive Officer in the formulation of the strategy and the business planning for the Group
- Lead implementation of the Group's strategy as regards any potential acquisitions or disposals
- Lead external Group Communications in liaison with the Group Finance Director and Head of Investor Relations.

Alan Jones

Group Human Resources Director
- Deliver high quality Human Resources services to the Group
- Lead the implementation of the Group's employee strategy in order to recruit, retain, motivate and develop high quality employees
- Provide guidance and support on all HR matters to the Group Chief Executive Officer, ExCo and Group Board.

Jane MacLeod

General Counsel
- Lead provision of legal advice to the Group Board, other Group Company Boards, ExCo and senior management
- Oversee and co-ordinate maintenance of and adherence to appropriate corporate governance procedures across the Group
- Design and implement a framework to manage legal risk within the Group including compliance by Group companies and staff with relevant legal obligations.

Jean Park

Chief Risk Officer
- Lead the Group's risk management function, embracing changes in best practice and regulation including Solvency II
- Oversee and manage the Group's relationship with the FSA
- Support the Board Risk Committee in the oversight of the Group's risk framework, in line with risk strategy and appetite.

David Richardson

Group Chief Actuary
- Ensure capital is managed efficiently across the Group
- Manage the Group's solvency position
- Lead development of the Group's investment strategy
- Identify and deliver opportunities to enhance shareholder value across the Group.

DIRECTORS' REPORT

Introduction

Principal activities and business review
The Company is incorporated in the Cayman Islands and has a Premium Listing on the London Stock Exchange. The Company is not required to comply with the requirements of the UK Companies Act 2006. However, the Directors support these enhanced standards for disclosure and have sought to comply voluntarily with these requirements.

The UK Companies Act 2006 requires a company to set out in this report a fair review of the business of the Group during the financial year ended 31 December 2011, including an analysis of the position of the Group at the financial year end and a description of the principal risks and uncertainties facing the Group (known as a 'Business review').

The information that fulfils the Business review requirements can be found in the 'Business and strategy' and 'Business review' sections on pages 8 to 17 and 18 to 43 respectively and is incorporated by reference into this Directors' report.

Shareholders

Dividends
Dividends for the year are as follows:

Ordinary shares
Paid interim dividend of 21p per share (last year 21p per share)
Recommended final dividend of 21p per share (last year 21p per share)
Total ordinary dividend of 42p per share (last year 42p per share)

Share capital
The issued share capital of the Company was increased by 3,017,205 ordinary shares during the year. 12,112 shares were allotted under the Group's employee share plans and 3,005,093 were allotted under the Group's scrip dividend scheme for the final 2010 and interim 2011 dividends. At 31 December 2011, the issued ordinary share capital totalled 174,472,815.

Full details of the authorised, issued and fully paid share capital as at 31 December 2011 and movements in share capital during the period are presented in note 16 to the IFRS financial statements.

The rights and obligations attaching to the Company's ordinary shares are set out in the Company's Articles of Association ('the Articles') which are available on the Company's website at www.thephoenixgroup.com/about-us/corporate-governance/articles-of-association.aspx.

Where the Employee Benefit Trust ('EBT') holds shares for unvested awards the voting rights for these shares are exercisable by the trustees of the EBT at their discretion, taking into account the recommendations of the Group. For shares that have vested into respective sub funds underneath the EBT, the voting rights are exercisable by the trustees of the respective sub funds at their discretion, taking into account the recommendations of the relevant participant of the respective sub funds.

Restrictions on transfer of shares
The lock-up restrictions relating to 31,251,401 ordinary shares ended in July 2011. The orderly market arrangements which were entered into by certain shareholders and the Company on 22 June 2010 still apply. These arrangements prevent a disposal of any ordinary shares (that these shareholders held on 5 July 2010) for a period of 24 months from 5 July 2010 if the disposal would negatively affect the orderly market in ordinary shares. The Prospectus issued by the Company on 4 June 2010 provides further details of this and is available on the Company's website at www.thephoenixgroup.com/investor-relations/archive/archive-key-documents.aspx.

Under the Articles, the Directors may in certain circumstances refuse to register transfers of shares. In particular, the Board of Directors may refuse to register the transfer of shares to a person who is a Non-Qualified Person (as defined in the Articles of Association).

Certain restrictions on the transfer of shares may be imposed from time to time by applicable laws and regulations (for example, insider trading laws), and pursuant to the Listing Rules of the Financial Services Authority ('FSA') and the Group's own share dealing rules whereby Directors and certain employees of the Group require the approval of the Company to deal in the Company's ordinary shares.

Substantial shareholdings
Information provided to the Company pursuant to the FSA's Disclosure and Transparency Rules ('DTR') is published on a Regulatory Information Service and on the Company's website. As at 22 March 2012, the Company had been notified of the following significant holdings of voting rights in its shares.

Name	No. of ordinary shares held	Percentage of shares in issue
TDR Capital Nominees Limited	**28,003,087**	**16.05%**
Xercise2 Limited	**22,610,453**	**12.96%**
Hugh Edward Mark Osmond[1]	**9,161,266**	**5.25%**
Lloyds Banking Group plc	**7,051,934**	**4.04%**
Nicholas Berggruen Charitable Trust	**6,924,239**	**3.97%**
Royal London Asset Management Limited	**6,862,908**	**3.93%**
William Alan McIntosh	**6,844,529**	**3.92%**
Alpha-Gamma Shares Limited	**6,585,499**	**3.77%**

Martin E Franklin	**5,885,048**	**3.37%**
Jeff Greene	**5,752,498**	**3.30%**

1 Hugh Osmond's share disclosure differs from that shown in the Directors' interest table within the Remuneration report due to differing reporting requirements as a shareholder and a director under DTR3 and DTR5 respectively. Further information and details can be found within the announcements made on 8 October 2010 and 12 October 2011 and available on the 'Investor Relations' section of the Company's website at www.thephoenixgroup.com.

Certain of the above shareholders also hold warrants (details of which are provided in note 24 to the IFRS financial statements) and contingent rights over shares (details of which are provided in note 15 to the IFRS financial statements).

Annual General Meeting ('AGM')
The AGM of the Company will be held at 32, Commercial Street, St Helier, Jersey JE2 3RU on Thursday, 3 May 2012 at 1pm.

A separate notice convening this meeting will be distributed to shareholders in due course and will include an explanation of the items of business to be considered at the meeting.

Board

Board of Directors
The membership of the Board and biographical details of the Directors are given on pages 54 to 57 and are incorporated by reference into this report. Details of Directors and their connected persons' beneficial and non-beneficial interests in the shares of the Company are shown in the Remuneration report on pages 72 to 82.

During 2011 and up to the date of this report, the following changes to the Board took place:

- Jonathan Moss resigned from the Board on 7 February 2011. He was replaced as Group Chief Executive Officer by Clive Bannister who was appointed to the Board on 28 March 2011
- Jonathan Yates resigned from the Board on 21 December 2011.

Details of related party transactions which took place during the year with Directors of the Company and entities where Directors are deemed to have significant influence, are provided in the Remuneration report and in note 46 to the IFRS financial statements.

The rules about the appointment and replacement of Directors are contained in the Company's Articles of Association. These state that a Director may be appointed by an ordinary resolution of the shareholders or by a resolution of the Directors. If appointed by a resolution of the Directors, the Director concerned holds office only until the conclusion of the next AGM following the appointment.

Following the evaluation of the Board of Directors conducted in 2011 and in accordance with the UK Corporate Governance Code, the Board of Directors will be unanimously recommending that all of the Directors should be put forward for re-election at the forthcoming AGM to be held on 3 May 2012.

The Articles give details of the circumstances in which Directors will be treated as having automatically vacated their office and also state that the Company's shareholders may remove a Director from office by passing an ordinary resolution.

The powers of the Directors are determined by Cayman Islands Company Law, Cayman Islands common law, the provisions of the Company's Memorandum and Articles and by any valid directions given by shareholders by way of special resolution.

The Directors have been authorised to allot and issue securities and grant options over or otherwise dispose of shares under Article 14.

At the Company's AGM held on 13 May 2011, shareholders granted the Company authority to purchase up to 10% of its issued ordinary shares. Any ordinary shares purchased under the authority would, subject to the Cayman Islands Companies Law (as amended), either be cancelled or held in treasury. These authorities were not used during the year or up to the date of this report.

Subject to obtaining shareholder approval for the renewal of this authority at the forthcoming AGM, the Company is authorised to make purchases of its own shares under Article 20 and make payment for the redemption or purchase of its own shares in any manner permitted by the Cayman Islands Companies Law (as amended), applicable law or regulation, including without limitation, out of capital, profits, share premium or the proceeds of a new issue of shares. The Company held no treasury shares during the year or up to the date of this report.

Directors' remuneration and interests
A report on Directors' remuneration is presented on pages 72 to 82 including details of their interests in shares and share options or any rights to subscribe for shares in the Company.

Directors' indemnities
Following shareholder approval on 15 March 2010, the Company has entered into a deed of indemnity by way of deed poll with its Directors whereby the Company has agreed to indemnify each Director against all losses incurred by them in the exercise,

execution or discharge of their powers or duties as a Director of the Company, provided that the indemnity shall not apply to the extent prohibited by any applicable law.

The deed of indemnity remains in force as at the date of signature of this Directors' report.

Directors' conflicts of interest
The Board has established procedures for handling conflicts of interest in accordance with Cayman Islands company law and the Company's Articles.

On an ongoing basis, Directors are responsible for informing the Company Secretary of any new, actual or potential conflicts that may arise.

All Directors and employees of the Company and its subsidiaries are subject to the Group conflicts of interest policy which has been established to provide a clear framework for an effective system of internal control to manage conflicts of interest throughout the Group.

Directors' and Officers' liability insurance
The Company maintains Directors' and Officers' liability insurance cover which is renewed annually.

Governance

Going concern
The Board has followed the UK Financial Reporting Council's 'Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009' when performing its going concern assessment. As part of its comprehensive assessment of whether the Group and the Company are a going concern, the Board has undertaken a review of the valuation and liquidity of its investments as at the date of preparation of the statement of consolidated financial position. The Board has also reviewed solvency and cash flow projections under both normal and stressed conditions. The cash and solvency projections include the potential impact of the contingent liabilities stated in note 47 to the IFRS financial statements.

Having thoroughly considered the going concern assessment, including a detailed review of the regulatory capital and cash flow positions of each subsidiary company and the availability across the Group of a range of management actions, the Board has concluded that there are no material uncertainties that may cast significant doubt about the Group and the Company's ability to continue as a going concern. The Directors have a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. Thus, they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Corporate governance statement
The disclosures required by section 7.2 of the FSA's Disclosure and Transparency Rules can be found in the Corporate Governance report on pages 65 to 71 which is incorporated by reference into this Directors' report.

Financial controls
The Group operates a financial controls policy for the internal control and risk management systems relating to the process of preparing consolidated accounts. The policy incorporates minimum control standards for operating within risk appetite.

Memorandum and Articles of Association
Changes to the Company's Memorandum and Articles of Association require prior shareholder approval and in some cases, approval of the Group's main lenders.

The Memorandum and Articles of Association are available on the Company's website at www.thephoenixgroup.com/about-us/corporate-governance/articles-of-association.aspx.

Re-appointment of the Auditors
Ernst & Young Accountants LLP has indicated its willingness to continue in office and a resolution that it be re-appointed will be proposed at the AGM. There is a liability cap in place in relation to audit work that is carried out by Ernst & Young Accountants LLP on the consolidated IFRS financial statements. For the MCEV supplementary information and the Group's UK subsidiaries' individual financial statements, which are audited by Ernst & Young LLP, there is no cap on auditor liability.

Details of fees paid to Ernst & Young Accountants LLP during 2011 for audit and non audit work are disclosed in note 11 to the IFRS financial statements.

Disclosure of information to Auditors
The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are aware, there is no relevant audit information of which the Company's auditor is unaware and that each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Company Secretary
The Company Secretary throughout the period was Gerald Watson.

Contractual/Other

Significant agreements impacted by a change of control of the Company
Details of the change of control provisions contained in the amended contingent rights agreements dated 22 June 2010 are set out in note 15 to the IFRS financial statements.

There are change of control clauses contained in certain of the Group's financing agreements. Upon a change of control of the Company, the principal amounts outstanding and the accrued interest under the Pearl and Impala facility agreements, the Pearl loan notes, the Royal London PIK facility and Royal London PIK notes would become immediately repayable or be required to be immediately redeemed.

In addition, certain provisions of the Articles relating to the City Code on Takeovers and Mergers apply in connection with a takeover bid. The Articles are available on the Company's website at www.thephoenixgroup.com/about-us/corporate-governance/articles-of-association.aspx.

All of the Company's employee share and incentive plans contain provisions relating to a change of control. Outstanding awards and options would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions and pro rata reduction as may be applicable under the rules of the employee share incentive plans.

Apart from the aforementioned, there are a number of agreements that take effect, alter or terminate upon a change of control of the Company, such as commercial contracts and joint venture agreements. None is considered to be significant in terms of their potential impact on the business of the Group.

Essential contracts or arrangements
There are a number of relationships with third parties which are of significant value to the Group. Apart from the two main credit facilities, no single relationship is considered to be essential to the Group.

Supplier payment policy
The Company and its subsidiaries do not follow any code or standard on payment practice, but it is the policy to pay suppliers within 30 days of the invoice date or, if different, in accordance with any terms agreed with suppliers.

Employees
The Company is committed to achieving equality of opportunity and the equal treatment of all our people and those applying to join us. To this end, all our people share an obligation to their colleagues, customers and business partners to provide a safe, fair and equitable working environment in which every individual can seek, obtain and continue employment without experiencing any unfair or unreasonable discrimination.

The Company recognises the need to treat people with disabilities fairly and equally. Full and fair consideration is given to applications for employment by people with a disability. Applicants are asked if they have any special requirements when invited to attend an interview and reasonable provisions are made to meet the applicant's request. Applicants are considered on the basis of the job requirements and the individual's ability and competencies, also taking into consideration any appropriate reasonable workplace adjustments.

Political donations
No political donations were made during the year ended 31 December 2011. The Company and its subsidiaries do not intend to make donations to political parties or independent election candidates nor have they made or do they intend to make any donations to EU political organisations or incur EU political expenditure.

Charitable contributions
During the year the Group made charitable donations of £98,083 details of which are presented in the Corporate Responsibility section on pages 44 to 51.

Clive Bannister
Group Chief Executive Officer

Alastair Lyons
Audit Committee Chairman

St Helier, Jersey
22 March 2012

CORPORATE GOVERNANCE REPORT

Introduction

The Company is a member of the FTSE 250 Index, having achieved a Premium Listing on the London Stock Exchange in July 2010. The Board is committed to high standards of corporate governance and supports the UK Corporate Governance Code (‘the Code’) which sets standards of good practice for UK listed companies. The Code has applied to the Company from 1 January 2011 and the Company has implemented those new aspects of the Code which were not included in its predecessor, the Combined Code on Corporate Governance. In particular, in relation to the more notable new provisions of the Code, all Directors of the Company are subject to annual re-election by shareholders and evaluation of the Board will be externally facilitated at least every three years.

It is the Board’s view that the Company has been fully compliant during 2011 with the provisions set down in the Code with the one exception that not all Directors were able to attend the AGM (Code provision E.2.3). This did not impact the AGM as there were no questions posed at the meeting. It is the Board’s intention to comply with this provision in 2012.

This report sets out details of how the Company has applied the principles and complied with the provisions of the Code during the period from 1 January 2011 to 31 December 2011.

The Board

The Board comprises the Non-Executive Chairman, the Group Chief Executive Officer and 11 other Non-Executive Directors, seven of whom are independent. Biographical details of all Directors are provided on pages 54 to 57. The Board considers that the following Directors are independent as they do not have any interest or business and other relationship which could, or could be perceived to, interfere materially with their ability to act in the best interests of the Company: David Barnes, Charles Clarke, Ian Cormack, Tom Cross Brown, Isabel Hudson, Alastair Lyons and David Woods. The Board has considered the criteria proposed by the Code in assessing the independence of the Directors.

The remuneration of the Directors is shown in the Remuneration report on pages 72 to 82. The terms and conditions of appointment of Non-Executive Directors are on the Group’s website. In accordance with the provisions of the Articles of Association and the Code, all Directors will submit themselves for election or re-election at the Company’s AGM on 3 May 2012.

All the Directors of the Company are FSA Approved Persons in respect of the Company’s FSA-regulated subsidiaries.

The Board is responsible to the shareholders for the overall governance and performance of the Group. Overall, the Board’s role is to provide entrepreneurial leadership within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board has a schedule of matters reserved for its consideration and approval supported by a set of operating principles. These matters include:

- Group strategy and business plans
- Major acquisitions, investments and capital expenditure
- Financial reporting and controls
- Dividend policy
- Capital structure
- The constitution of Board Committees
- Appointments to the Board and Board Committees
- Senior executive appointments
- Key Group policies.

The schedule of matters reserved for the Board is available from the Group Company Secretary. Matters which are not reserved for the Board and also its Committees under their terms of reference (which are available on the Group website), or for shareholders in general meetings, are delegated to the Executive Management under a schedule of delegated authorities approved by the Board.

During 2011, the steps taken by the Board to improve its governance arrangements included:

- Adopting annual re-election of all Directors in accordance with the Code
- Undertaking an externally facilitated Board, Board Committee and individual Director evaluation
- Undertaking a successful AGM at which all resolutions were passed by a majority of at least 96% of votes cast
- Establishing a Board Investment Committee in response to the Board evaluation undertaken at the end of 2010
- Enhancing the Board education programme in response to the Board evaluation undertaken at the end of 2010, in particular including site visits to operational business units and presentations from management in those units
- Publishing a Chairman’s statement on “Women on Boards” in accordance with the Lord Davies Review

• Holding a two-day event to review and debate strategy.

The head office of the Company is in Jersey and, as such, the Board and its Committees hold their meetings in Jersey.

The Chairman, Group Chief Executive Officer and Senior Independent Director

There is a division of responsibility, approved by the Board, between the Chairman, Ron Sandler, who is responsible for the leadership and effective operation of the Board and the Group Chief Executive Officer, Clive Bannister, who is responsible to the Board for the overall management and operation of the Group. The Chairman's other significant commitments are set out in his biographical details on page 54.

The Senior Independent Director, appointed by the Board, is Alastair Lyons. His role is to be available to shareholders whose concerns are not resolved through the normal channels or when such channels are inappropriate. He is also responsible for leading the annual appraisal of the Chairman's performance by the Non-Executive Directors (which was undertaken in the latter part of 2011) and for leading the process for appointment of a new Chairman, when appropriate.

Board effectiveness

In accordance with the Code, an evaluation of the performance of the Board and that of its Committees and individual Directors was undertaken in the latter part of 2011 and was externally facilitated by Egon Zehnder International ('EZI') who is independent of the Company.

The process involved completion by Directors of a questionnaire covering various aspects of Board and Director effectiveness, followed by individual meetings between EZI and each Director, concluding in a Board report which was discussed by the Board in November 2011. The process and report covered the following areas:

• Board structure and composition

• Board dynamics and relationship

• Board processes

• Board committees

• People and people processes

• Company strategy and performance

• Capital, risk and tracking board effectiveness

• Strategic and operational issues.

An action list, with senior executive accountability, has been established to address the recommendations from the evaluation. The EZI review concluded as follows:

"Phoenix has a well functioning Board and has made substantial steps to improve the quality of Directors and the level of debate over the past two years. Overall, this Board effectiveness review concurs with Phoenix's own tracking process that most of the previous recommendations have been implemented with a few minor exceptions."

A review of each Director's individual performance took place as part of the evaluation and the output from this will be used in revising the training programme for Directors.

The output from the Board and individual Director reviews informed the review of the Board composition and structure undertaken by the Board Nomination Committee in January 2012.

All Directors receive a tailored induction on joining the Board in accordance with a process approved by the Board. To ensure that the Directors maintain up-to-date skills and knowledge of the Company, all Directors receive regular presentations on different aspects of the Company's business and on financial, legal and regulatory issues.

Operation of the Board

The terms of appointment for the Directors state that they are expected to attend in person regular (at least six per year) and emergency Board meetings of the Company and to devote appropriate preparation time ahead of each meeting. The Board met seven times during 2011 and is scheduled to meet seven times in 2012 including a two day strategy-setting meeting. Additional meetings will be held as required and the Non-Executive Directors will hold meetings with the Chairman, without the Executive Directors being present, as they did on several occasions in 2011.

Attendance by each of the Directors at Board meetings and at Committee meetings for Committees of which they were a member during 2011 was:

	Board Meetings		Nomination Committee		Audit Committee		Remuneration Committee		Risk Committee		Investment Committee	
	Maximum	Actual	Maximum	Actual	Maximum	Actual	Maximum	Actual	Maximum	Actual	Maximum	Actual
Chairman												

Ron Sandler	7	7	4	4	–	–	–	–	–	–	–	–
Executive Directors												
Clive Bannister[1]	6	6	–	–	–	–	–	–	–	–	–	–
Jonathan Yates	7	7	–	–	–	–	–	–	–	–	–	–
Non-Executive Directors												
Alastair Lyons	7	7	–	–	7	7	–	–	–	–	–	–
Ian Ashken	7	7	–	–	–	–	–	–	–	–	–	–
René-Pierre Azria	7	7	–	–	–	–	–	–	6	5	2	2
David Barnes	7	7	–	–	7	7	8	8	–	–	–	–
Charles Clarke	7	7	–	–	7	7	–	–	–	–	2	2
Ian Cormack	7	7	4	4	–	–	8	8	–	–	–	–
Tom Cross Brown	7	7	4	3	–	–	–	–	6	6	2	2
Manjit Dale	7	6	–	–	–	–	–	–	–	–	2	1
Isabel Hudson	7	7	–	–	–	–	8	7	6	6	–	–
Hugh Osmond	7	7	–	–	–	–	–	–	6	6	2	2
David Woods	7	6	–	–	–	–	–	–	6	5	–	–

1 Clive Bannister was appointed to the Board on 28 March 2011.

Jonathan Moss resigned from the Board on 7 February 2011, having attended one Board meeting during 2011.

Board Committees
The Board has delegated specific responsibilities to five standing committees of the Board. The terms of reference of the Committees can be found on the Company's website.

Audit Committee

Alastair Lyons, Chairman
David Barnes
Charles Clarke

The Audit Committee has recent and relevant financial experience. The composition of the Committee is in accordance with the requirements of the Code that the Audit Committee should consist of at least three independent Non-Executive Directors of whom at least one has recent and relevant financial experience. The Audit Committee met seven times during 2011.

The Audit Committee is responsible for making recommendations to the Board on such matters as the appointment of the external auditors and their terms of engagement and for reviewing the performance, objectivity and independence of the external auditors. The Audit Committee is also responsible for assessing the effectiveness of the internal audit function. The Audit Committee receives and reviews the Annual Report and Accounts and other related financial disclosures, the ultimate responsibility for these matters remaining with the Board. It monitors the overall integrity of the financial reporting by the Company and its subsidiaries and reviews compliance with legal and regulatory requirements and the effectiveness of the Group's internal controls. The terms of reference of the Audit Committee state that it shall meet the external auditor at least once a year without management being present.

The Company has adopted a Charter of Statutory Auditor Independence, which requires both the Company and the external auditors to take measures to safeguard the objectivity and independence of the external auditors. These measures include a prohibition regarding non-audit services in respect of specific areas, such as secondments to management positions, or those which could create a conflict or perceived conflict. It also includes details of the procedures for the rotation of the external audit engagement partner. The Charter can be found on the Company's website.

Audit Committee's principal activities during 2011
- Reviewed the Company's 2010 Annual Report and Accounts, 2011 interim financial statements and 2011 interim management statements, recommending their approval to the Board, as well as related disclosures and the financial reporting process, supported by reports from management and the external auditors
- Reviewed the financial forecasts prepared by management, supported by the sensitivity analysis on the key assumptions underpinning the forecasts, in support of the assumption that the Group will continue as a going concern and in support of dividend payments

- Assessed the effectiveness of both the external auditors and the internal audit function, the latter supported by an external effectiveness review
- Approved the Group Internal Audit Charter and the Group Internal Audit Plan (including its link to the Risk Management Framework), receiving regular reports to monitor progress against the plan
- Reviewed the engagement and remuneration of the external auditors, recommending their re-appointment to the Board and thence to shareholders
- Reviewed and monitored the independence of the external auditors including their provision of non-audit services
- Reviewed arrangements for whistleblowing should an employee wish to raise concerns, in confidence, about any possible improprieties
- Reviewed the internal controls effectiveness report prior to its consideration by the Board.

Nomination Committee

Ron Sandler, Chairman
Ian Cormack
Tom Cross Brown

The composition of the Nomination Committee is in accordance with the requirements of the Code that a majority of its members should be independent Non-Executive Directors. The Nomination Committee is responsible for considering the size, composition and balance of the Board; the retirement and appointment of Directors; succession planning for the Board and senior management and making recommendations to the Board on these matters. The Nomination Committee met four times in 2011.

The standard process used by the Committee for Board appointments involves the use of an external search consultancy to source candidates external to Phoenix (and may in the case of executive appointments also consider internal candidates). Detailed assessments of short-listed candidates are undertaken by the search consultancy, followed by interviews with Committee members and other Directors and the sourcing of references before the Committee recommends the appointments to the Board.

Nomination Committee's principal activities during 2011

- Delivery of recommendations to the Board in connection with the appointments of the Group Chief Executive Officer and Group Finance Director
- Review of the balance of skills, knowledge and experience of the Board, taking account of the Board evaluation report
- Review of the structure, size and composition of the Board, taking account of the Board evaluation report
- Given the above, delivery of recommendations to the Board to approve the AGM notice stating that the performance of each director continues to be effective and demonstrates commitment to the role
- Assessment of Board succession planning with the agreement that a further review, to include senior management succession planning, would be undertaken by the Committee in January 2012 utilising the results of the external Board evaluation undertaken at the end of 2011
- Consideration of the Lord Davies Review of 'Women on Boards' and the Chairman's statement as follows which was released on the Phoenix Group website:

"The Nomination Committee, which I chair, will continue to review on a regular basis the experience, skills, knowledge and independence of the Board. This encompasses, and will continue to encompass, the recommendations of the Lord Davies Review titled 'Women on Boards'. Phoenix Group supports the recommendations in principle and we believe that it is appropriate for FTSE 350 companies to set out clear targets for female representation on their Boards. We are a recently listed FTSE 250 Company (from July 2010) and none of our Directors was appointed to the Board prior to September 2009. As we already have a large Board of 14 Directors (including one female director) and are unlikely to want to increase its size, it is difficult at this stage to commit to firm percentages regarding the number of women on our Board in 2013 and 2015. Nonetheless, we have set targets of two female directors by 2013 and a further female director by 2015. Our overriding aim remains the appointment of the most appropriate candidates to the Board.

We embrace equality of opportunity in all parts of our organisation and I am pleased to say that we have three female members out of nine on our Executive Committee."

Remuneration Committee

Ian Cormack, Chairman
David Barnes
Isabel Hudson

The composition of the Remuneration Committee accords with the requirements of the Code that the Remuneration Committee should consist of at least three independent Non-Executive Directors. The Remuneration Committee met eight times during 2011.

The Remuneration Committee is responsible for making recommendations to the Board on the Company's remuneration and compensation plans, policies and practices and for determining, within agreed terms of reference, specific remuneration packages for the Executive Directors. These include pension rights and executive incentive schemes to encourage superior performance. Details of the remuneration structure and the Committee's activities in 2011 are provided in the Remuneration report on pages 72 to 82.

Hewitt New Bridge Street (up to August 2011) and FIT Remuneration Consultants (from August 2011) provided advice to the Remuneration Committee and are independent of the Company.

Risk Committee

David Woods, Chairman
René-Pierre Azria
Tom Cross Brown
Isabel Hudson
Hugh Osmond

The establishment of a Risk Committee is not a requirement of the Code. However, the Board believes such a Committee is important to ensure the robust oversight of the management of risk within the Group. The composition of the Committee, with a majority of independent Non-Executive Directors, is in accordance with the final recommendations of the report by Sir David Walker titled 'A review of corporate governance in UK banks and other financial industry entities'.

The Risk Committee met six times in 2011.

The Risk Committee advises the Board on risk appetite and tolerance in setting the future strategy, taking account of the Board's overall degree of risk aversion, the current financial situation of the Company and, drawing on assessment by the Audit Committee, the Company's capacity to manage and control risks within the agreed strategy. It advises the Board on all high-level risk matters. Details of the Risk Management Framework, for which the Risk Committee has oversight, are provided in the Risk Management section on pages 38 to 43.

Risk Committee's principal activities during 2011

- Recommending to the Board approval of the Group's risk appetite
- Recommending to the Board the Group's overall risk management strategy
- Recommending to the Board the Group's principal risk policies
- Approval of the Group Risk function's 2011 plan
- Consideration of any breaches of the Group's risk appetite
- Monitoring of compliance and satisfying itself that action plans to address significant breaches of the Group's principal risk policies are sufficient
- Reviewing the Group's risk profile and monitoring it against the FSA risk categories of Market, Insurance, Credit, Liquidity and Operational with particular attention to risk appetite, risk trends, risk concentrations, provisions, experience against budget and key performance indicators for risk
- Consideration of risks, issues and matters that were escalated from principal business unit risk committees to ensure adequate coverage of the Group's significant business risks and systems of internal control
- Oversight of and challenge to, the design and execution of the Group's stress and scenario testing, including any changes of assumptions.

Investment Committee

Tom Cross Brown, Chairman
René-Pierre Azria
Charles Clarke
Manjit Dale
Hugh Osmond

The Investment Committee was formed in May 2011 in response to a recommendation from the Board evaluation undertaken at the end of 2010 to provide greater focus on investment strategy and performance. The Committee reviews investment performance and strategic asset allocation across the Group. It held its first two meetings in 2011 and is scheduled to meet four times in 2012.

Communication with shareholders

The Company places considerable importance on communication with shareholders and regularly engages with them on a wide range of issues.

The Company's Investor Relations department is dedicated to facilitating communication with investors and analysts and an active investor relations programme is maintained. The Company continued to increase its communication and engagement with the investment community during 2011. The Chairman, Senior Independent Director and Executive Directors are available to meet investors and analysts when required. At these meetings a wide range of relevant issues including strategy, performance, management and governance are discussed. Should major shareholders wish to meet newly appointed Directors, or any of the Directors generally, they are welcome to do so.

The Directors consider it important to understand the views of the market and in particular any issues which concern them. Board members regularly receive copies of the latest analysts' reports on the Company and the sector, as well as market feedback to further develop their knowledge and understanding of external views about the Company. The Chairman and the Non-Executive Directors provide feedback to the Board on topics raised with them by major shareholders. In addition, an independent investor perception study is conducted periodically. The Company held two investor days in 2011 and going forward, it plans to hold these on a recurring basis.

The Company's AGM provides another opportunity to communicate with its shareholders. At the 2011 meeting, the Company complied with the Code provisions relating to voting and the separating of resolutions. Shareholders were invited to ask questions during the meeting. It is intended that the same processes will be followed at the 2012 AGM and that shareholders will have an opportunity to meet with the Directors following the conclusion of the formal part of the meeting. In line with the Code, details of proxy voting by shareholders will be made available at the meeting and will be posted on the Company's website following the meeting.

The Company's Annual Report and Accounts, together with the Company's interim report, interim management statements and other public announcements and presentations are designed to present a balanced and understandable view of the Group's activities and prospects. These are available on the Company's website at www.thephoenixgroup.com, along with a wide range of relevant information for private and institutional investors, including the Company's financial calendar.

Financial reporting and going concern

The Directors have acknowledged their responsibilities in the Statement of Directors' Responsibilities in relation to the IFRS financial statements for the year ended 31 December 2011 (as noted on page 84).

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business and strategy and Business review sections on pages 8 to 17 and 18 to 43 respectively.

The financial position of the Group, its cash flows and liquidity position are described in the financial statements and notes.

The Board's going concern assessment is included within the Directors' report on page 62.

Review of system of internal controls

The Code requires Directors to review the effectiveness of the Company's risk management and internal control systems which includes financial, operational and compliance controls. The Board has overall responsibility for the Group's risk management and internal control systems and for reviewing their effectiveness. The Group's systems of internal controls are designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss. The Board's review of the period covered by this report, which was undertaken with the assistance of the Audit and Risk Committees, was completed on 22 March 2012. Where any significant weaknesses were identified, the actions required to address them have been taken, or are being taken and monitored.

The Board (and its subsidiary company boards) monitor internal controls on a continual basis, in particular through Audit and Risk Committees. There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group, which has been in place throughout the period covered by this report and up to the date of approval of the Annual Report and Accounts for 2011, in accordance with the 'Internal Control: Guidance to Directors' published by the Financial Reporting Council.

Additional assurance is provided by the internal audit function, which operates and reports independently of management. The internal audit function provides objective assurance on risk mitigation and control to the Audit Committee.

REMUNERATION REPORT

Phoenix Group – Directors' Remuneration report

for the year ended 31 December 2011

Dear Shareholder

I am pleased to introduce the Remuneration report for 2011. Following the changes to the senior executive remuneration arrangements made last year as a result of the Company's Premium Listing, the Remuneration Committee ('the Committee') has determined that these arrangements remain appropriate for 2012.

In considering the remuneration arrangements, the Committee has been mindful of the intense scrutiny to which executive remuneration is currently subject including through the Financial Services Authority ('FSA') Remuneration Code and through the Department for Business, Innovation and Skills review into executive remuneration more generally. The Committee seeks to have regard to the highest levels of governance and to reflect developments in best practice.

The main elements of the Executive Directors' packages, which are set out in more detail in the report which follows, are:

- Base salary levels are appropriate for the size and complexity of the business, given relevant market data
- Annual incentive maximum potential remains appropriate at 150% of base salary with 20% of potential based on personal and strategic measures and 80% of potential based on corporate embedded value, cash generation and expense management targets, with one-third of any incentive deferred into shares for three years. The only changes for 2012 are to increase the weighting of the expense management target, given the Board's continued focus on expense management, and to extend the deferral provisions to a wider population
- Consistent with best practice, the Committee operates a claw-back provision which will operate for any annual incentive amounts subsequently found to have been based on materially inaccurate results
- The structure of the long-term incentive arrangement and the use of embedded value and cash generation performance metrics remain appropriate and in line with the Group's strategy. The current expectation is that awards to be granted in April 2012 will be at similar levels and be based on similar performance metrics to those granted in April 2011 (with Total Shareholder Return ('TSR') also being considered) with the precise targets set just prior to the awards being granted
- Consistent with best practice, the Committee operates share ownership guidelines. Executive Directors are required to build and maintain a specified shareholding in the Company (200% of salary for the Group Chief Executive Officer and 100% of salary for the Group Finance Director) through the retention of all post-tax shares which vest under the Long-Term Incentive Plan ('LTIP') (or any other discretionary long-term arrangement introduced in the future) until target holdings have been achieved.

The Committee considers that the current arrangements are appropriate to the Group and its commercial situation and reflect UK best practice. I encourage shareholders to support the arrangements.

Ian Cormack
Remuneration Committee Chairman

22 March 2012

Introduction

Although not required for a non-UK incorporated company, this report has been prepared in accordance with the requirements of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. The report also meets the relevant requirements of the FSA's Listing Rules and describes how the Board has complied with the provisions set out in the UK Corporate Governance Code relating to remuneration matters. This report sets out the policy for the financial year just ended, for the forthcoming financial year and, subject to ongoing review, for subsequent financial years.

The auditors have reported on certain parts of the Directors' Remuneration Report and stated whether in their opinion those parts of the report have been properly prepared in accordance with the Companies Act 2006. The report has therefore been divided into separate sections for unaudited and audited information.

Unaudited information

Remuneration Committee

The Group established the Committee on 18 February 2010. The terms of reference of the Committee are available at www.thephoenixgroup.com. During 2011, the Committee's main responsibilities were to:

- Establish and operate a framework for remuneration throughout the Group, with particular emphasis on aligning the remuneration policy with the overall aims and risk appetite of the Group
- Determine and recommend to the Board the remuneration policy and the approval of all elements of pay for each of the following categories: the Chairman of the Board; Executive Directors; Executive Committee members; those individuals receiving a base salary greater than £200,000 or who have total target pay or receive an award on joining to buy-out value from a former employer which warrants the attention of the Committee even if their salary is below £200,000; and those individuals who perform a significant influence function and/or undertake activities which could have a material impact on the risk profile of the Group

- Review the design of, and agree targets for, any performance-related incentive schemes operated by the Group and approve the total annual payments made under such schemes
- Review the design of all share-based plans (or other plans requiring shareholder approval) for approval by the Board and shareholders, including the overall level of awards in any year, the individual award levels for Executive Directors and senior executives and performance targets
- Select, appoint and determine the terms of reference for independent remuneration consultants to advise the Committee
- Approve remuneration practices within Ignis, applying similar overall principles as applied to the rest of the Group but relating these to an appropriate peer group of asset managers.

The table below shows the independent Non-Executive Directors who served on the Committee during 2011 and their date of appointment:

Member	From	To
Ian Cormack (Committee Chairman)	18 February 2010	To date
David Barnes	18 February 2010	To date
Isabel Hudson	18 February 2010	To date

The Committee meets at least twice a year but more frequently if required. During 2011, eight Committee meetings were held and details on attendance at these meetings are set out in the Corporate Governance report on page 67.

None of the Committee members have any personal financial interest (other than as shareholders), conflicts of interests arising from cross-directorships, or day-to-day involvement in running the business.

The Committee makes recommendations to the Board. No Director plays a part in any discussion about his or her own remuneration.

The Board has agreed that from 2012, certain responsibilities of the Committee should be assumed by a Committee of the Board of Phoenix Life Holdings Limited, the highest EEA insurance holding company within the Group. In particular, that Committee will oversee remuneration relating to UK based employees other than Executive Directors. The initial members of the two Committees will be the same. This will not impact the governance of remuneration from an external perspective, but it will simplify the oversight of remuneration matters affecting UK based employees.

Advice

The Committee received independent remuneration advice during the year from its appointed adviser, Hewitt New Bridge Street ('HNBS'), part of Aon Hewitt (up to August 2011) and FIT Remuneration Consultants ('FIT') (from August 2011). A separate team within Aon Hewitt also provided advice to the Group in respect of actuarial pension services. The Committee did not believe that the independence of its adviser was compromised by this appointment. Both HNBS and FIT are members of the Remuneration Consultants Group (the professional body for consultants) and adhere to its code of conduct.

The Committee also consulted with the Group Chief Executive Officer, Group HR Director and General Counsel who attended, by invitation, various Committee meetings during the year although no Executive is permitted to participate in discussions or decisions regarding his or her own remuneration. Input is also sought from the Chief Risk Officer.

Remuneration policy

General policy

Executive remuneration packages are structured so that they:

- Are aligned to the Group's strategy
- Are aligned with the interests of shareholders, with a significant proportion being performance-related to areas which impact value
- Are competitive but not excessive, in relation to the UK life assurance and asset management markets
- Do not promote unacceptable behaviours or encourage unacceptable risk taking. In particular, the Committee recognises the interdependence of colleagues within an insurance business and so focuses the annual incentive targets for senior executives on the delivery of corporate financial targets. Within Ignis, consistent with standard industry practice, targets are more focused on individual objectives (but subject to a pool linked to overall Ignis profitability)
- Take into account Group-wide pay and employment conditions. The Committee reviews the average Group-wide base salary increase and bonus costs and is responsible for all discretionary and all employee share-based arrangements.

There are five main elements of the remuneration package for Executive Directors and senior executives:

- Base salary
- Benefits

- Pension
- Annual incentives
- Long-term incentives.

The policy for Executive Directors for 2011 is described in more detail below.

Base salary and benefits

Executive Directors' base salaries are reviewed annually by the Committee by reference to median data taking into account the responsibilities, skills and experience of each individual and salary levels within listed companies of a similar size and complexity. Base salary levels are as follows:

Name	Role	**From 1 January 2012**	From 1 January 2011
Clive Bannister[1]	Group Chief Executive Officer	**£700,000**	£700,000
Jonathan Yates[2]	Group Finance Director	**£415,000**	£415,000

1 Joined the Phoenix Group on 7 February 2011 and was appointed to the Board as a Director on 28 March 2011.

2 Resigned from the Board on 21 December 2011 but remained in the Group's employment to the end of February 2012.

Benefits received by Executive Directors comprise a car allowance, private medical insurance, relocation assistance and life assurance.

Pension

The Executive Directors (as at the date of this report) receive a contribution equal to 20% of base salary to a defined contribution pension arrangement.

Annual incentives

For 2011, annual incentive potential ('AIP') was capped at 150% of base salary for Executive Directors. Performance targets were based on the achievement of personal and strategic objectives for 20% of the bonus opportunity and, for the other 80%, financial targets based on a sliding scale as follows:

Performance metric	% of 80% of incentive potential based on financial measures
Group MCEV Operating Earnings after Tax ('GMCEVOEaT')	30%
Group Market Consistent Embedded Value ('GMCEV')	30%
Operating Companies' Cash Generation ('OCCG')	30%
Expense Management ('EM')	10%

In addition to the above targets and in order for any incentive payment to be paid, the Committee confirmed that it was satisfied that management had identified and managed material business risks in an appropriate manner.

Details of the actual incentive payments awarded in respect of the 2011 financial year (to be paid in March 2012) are presented in the emoluments table and notes on page 78. In summary, the AIP corporate out-turn was 75% of maximum. The table below shows the actual out-turn against the annual incentive maximum.

	AIP earned (as a % of maximum)						
Name	GMCEVOEaT	GMCEV	OCCG	EM	Personal	Total	Maximum
Clive Bannister	20.25	12.75	22.50	4.50	12.50	72.50	100%
Jonathan Yates	20.25	12.75	22.50	4.50	14.01	74.01	100%

For Mr C Bannister, one-third of annual incentive awards for 2011 awarded (compared with any award above target operated in 2010) will be deferred into shares for three years. The shares comprising the deferred element will vest three years from the date of award and will normally be forfeited if the individual leaves the Group prior to vesting (unless designated as a good leaver).

For 2012, the on-target and maximum incentive potential remains at 75% and 150% respectively of base salary for Executive Directors and the measures remain as set out above, but with an increase in the weighting of the expense management target by 10% (with corresponding 10% reduction in GMCEV), given the Board's continued focus on expense management.

Consistent with best practice, the Committee operates a claw-back provision which will operate for any annual incentive amounts subsequently found to have been based on materially inaccurate results.

Long-term incentives

The LTIP is designed to retain executives and align their interests to the Group's long-term goals and, through those goals, to the delivery of superior returns to shareholders. Each year, approximately 50 participants receive contingent awards of shares in the Group which will permit the participant to receive shares three years after they were awarded, but only if both suitably stretching performance conditions measured over the three-year period are met and they remain employed (or are designated as a good leaver).

The Committee's policy is to award Executive Directors shares with an initial face value equal to no more than 200% of their respective base salaries. This is below the formal plan limits of 300% of base salary or 400% in exceptional circumstances.

Consistent with the awards in May 2010, for LTIP awards granted in April 2011, the performance measures are 50% based on MCEV growth and 50% based on net cumulative cash generation (i.e. after taking into account certain recurring costs), with both targets measured over the three financial years commencing 1 January 2011 and underpinned by a debt management assessment. A summary of the targets is set out below:

MCEV growth (50% of awards)	25% of the MCEV related component of the award will vest for MCEV growth in excess of the risk free rate by 2.5% per annum rising on a pro rata basis until 100% vests for MCEV growth in excess of the risk-free rate by 6% per annum.
Cash generation (50% of awards)	25% of the cash generation component of the award will vest for cumulative cash generation of £1.217 billion rising on a pro rata basis until 100% vests for cash generation of £1.517 billion.
Debt underpin	Notwithstanding the MCEV and cash generation performance targets, if the Committee determines that the Group's debt levels and associated interest costs have not remained within parameters acceptable to the Committee over the performance period and that the Group has not made progress considered to be reasonable by it in executing any strategy agreed by the Board on debt management and capital structuring, the level of awards vesting will either be reduced or lapse in full.

The Committee selected these performance metrics as they are directly linked to the objectives set out in the Group's strategy and there is a clear line of sight for participants between performance and reward.

The current expectation is that MCEV and cash generation performance metrics will continue to be used for the 2012 awards (with TSR also being considered for part of the 2012 awards), with performance targets (which will be no less challenging than those presented above) set in advance of the awards being granted.

Shareholding guidelines

The Company operates share ownership guidelines for Executive Directors. Under the guidelines, Executive Directors are expected to retain all shares (net of tax) which vest under the LTIP (or any other discretionary long-term incentive arrangement introduced in the future) until such time that they hold a specified value of shares (200% of salary for the Chief Executive Officer, 100% of salary for other Executive Directors). Once shareholding guidelines have been met, individuals are expected to retain these levels as a minimum. The Committee will review shareholdings annually in the context of this policy.

All employee share plans

The Group operates a Sharesave scheme which is approved by HM Revenue & Customs. All eligible employees, including Executive Directors, are invited to participate on similar terms to save up to a maximum of £250 each month for a fixed period of three or five years. At the end of the savings period, individuals may use their savings plus a tax-free bonus to buy ordinary shares in the Company at a discount currently set at 15% of the market price set at the launch of each scheme.

In addition for 2012, the Committee has approved the launch of an HM Revenue & Customs approved Share Incentive Plan. This offers all eligible employees, including Executive Directors, the opportunity to purchase, out of their pre-tax salary, shares in the Company (up to a value of £125 per month) and receive one matching share for every six shares purchased.

Ignis

The Committee is responsible for approving the remuneration practices within Ignis, the Group's asset management business. In structuring remuneration arrangements within Ignis, the Committee applies similar overall principles to those used in the rest of the Group, but relating these to an appropriate peer group of asset managers.

Directors' service contracts

Executive Directors

Executive Director service contracts, which do not contain expiry dates, provide that compensation provisions for termination without notice will only extend to 12 months of salary, fixed benefits and pension (which may be payable in instalments and subject to mitigation). By excluding any entitlement to compensation for loss of the opportunity to earn variable pay, the Committee believes the contracts to be consistent with best practice. The Committee also has discretion to mitigate further by paying on a phased basis with unpaid instalments ceasing if the executive finds alternative employment. Contracts do not contain change of control provisions.

Name	Date of Contract	Notice period from either party (months)
Clive Bannister	7 February 2011	12

Jonathan Yates[1]	6 May 2010	12

1 Resigned from the Board on 21 December 2011.

Subject to Board approval, Executive Directors are permitted to accept outside appointments on external boards or committees as long as these are not deemed to interfere with the business of the Group. Neither Director was an outside director during 2011.

Former Executive Directors

Jonathan Moss left the role of Group Chief Executive Officer on 7 February 2011 and left the Group on 29 March 2011. As reported last year, he received a payment in lieu of notice of £690,000 in aggregate, reflecting both his base salary and benefits in line with his contractual entitlements. In addition, a contribution of £857,188 was made to the Company's Employee Benefit Trust ('EBT') subject to a recommendation that it was allocated to a sub-trust for the benefit of Jonathan Moss' family in lieu of any annual incentive for 2010. Jonathan Moss also received £50,000 by way of compensation for loss of statutory employment rights and £4,800 in respect of his legal expenses and outplacement services. His long-term incentive awards continue to vest until the normal vesting date (with performance conditions and time pro-rating applying for the 2010 LTIP awards) with the exception of his 112,500 Bonus Share Plan shares which, consistent with the rules, vested on 29 March 2011.

In December 2011, the Company announced that Jonathan Yates would leave the Group at the end of February 2012. He remained employed throughout 2011 and his remuneration has been reported in the normal way. For 2012, he will receive his normal salary and benefits for the period he continued to be employed. He will not be eligible for a bonus for any part of 2012 and will not receive any termination payment in respect of his departure. However, the Committee has confirmed that he will be treated as a good leaver and therefore, will be entitled to early release, on departure, of the 16,259 shares held under the Deferred Bonus Share Scheme (being the deferred element of prior bonuses). He will retain his 2010 and 2011 LTIP awards which continue to vest until the normal vesting date (with performance conditions and time pro-rating applying).

Non-Executive Directors' contracts

The Non-Executive Directors, including the Group Chairman, have letters of appointment which set out their duties and responsibilities. Appointment is for a fixed term of three years, terminable by one month's notice on either side. Non-Executive Directors are not eligible to participate in incentive arrangements or receive pension provision or other benefits such as private medical insurance ('PMI') and life assurance.

Name	Date of Letter of Appointment	Appointment end date	Unexpired term (Months)
Ian Ashken	2 September 2009	2 September 2012	5
René-Pierre Azria	2 September 2009	2 September 2012	5
David Barnes	2 September 2009	2 September 2012	5
Charles Clarke	18 February 2010	18 February 2013	10
Ian Cormack	2 September 2009	2 September 2012	5
Tom Cross Brown	24 September 2009	24 September 2012	6
Manjit Dale	2 September 2009	2 September 2012	5
Isabel Hudson	18 February 2010	18 February 2013	10
Alastair Lyons	29 March 2010	29 March 2013	12
Hugh Osmond	2 September 2009	2 September 2012	5
Ron Sandler	24 September 2009	24 September 2012	6
David Woods	18 February 2010	18 February 2013	10

The remuneration of the Non-Executive Directors is a matter for the Chairman and Executive members of the Board and the remuneration of the Non-Executive Chairman is a matter for the Board. Fees for both the Non-Executive Directors and the Non-Executive Chairman are reviewed from time to time with regard to the complexity of the Group, the time commitment required and the level of fees paid by comparable companies.

In 2011, fee levels were set at £450,000 for the Chairman of the Board, £90,000 for the role of Non-Executive Director with additional fees of: (i) £5,000 payable for the role of Senior Independent Director; and/or (ii) £10,000 payable where an individual also Chairs the Audit, Investment, Remuneration or Risk Committee; and/or (iii) £20,000 payable where a Non-Executive Director also sits on the Board of a subsidiary company. Non-Executive Directors in place in 2011, who are not paid for serving on subsidiary company Boards, had their fees unchanged at £100,000. In addition, David Woods receives a temporary fee (starting 1 July 2011) of £10,000 per annum for being a member of the Solvency II Model Governance Committee. No changes to these fee levels are proposed for 2012.

Audited information

Directors' emoluments

The emoluments of the Directors for 2011 were as follows:

Name	Directors salaries/fees £	Benefits[1] £	Annual Incentive[2] £	Compensation for loss of office £	Contribution to EBT £	**Total 2011 £**	Total 2010 £
Non-Executive Chairman							
Ron Sandler	450,000	–	–	–	–	**450,000**	450,000
Executive Directors							
Clive Bannister[3]	533,050	13,057	681,954	–	–	**1,228,061**	–
Non-Executive Directors							
Ian Ashken	100,000	–	–	–	–	**100,000**	100,000
René-Pierre Azria	100,000	–	–	–	–	**100,000**	100,000
David Barnes	110,000	–	–	–	–	**110,000**	113,295
Charles Clarke[4]	100,000	–	–	–	–	**100,000**	86,026
Ian Cormack	120,000	–	–	–	–	**120,000**	120,000
Tom Cross Brown	120,000	–	–	–	–	**120,000**	115,000
Manjit Dale	100,000	–	–	–	–	**100,000**	100,000
Isabel Hudson[4]	100,000	–	–	–	–	**100,000**	86,026
Alastair Lyons[5]	125,000	–	–	–	–	**125,000**	82,500
Hugh Osmond	100,000	–	–	–	–	**100,000**	100,000
David Woods[4]	125,000	–	–	–	–	**125,000**	94,628
Former Directors							
Jonathan Moss[6]	67,708	1,270	–	744,800	857,188	**1,670,966**	662,393
Simon Smith[7]	–	–	–	–	–	**–**	736,958
Jonathan Yates[8]	402,414	16,381	460,750	–	–	**879,545**	546,230
Total	**2,653,172**	**30,708**	**1,142,704**	**744,800**	**857,188**	**5,428,572**	3,493,056

1 Benefits comprise car allowance, private medical insurance and life insurance.

2 Annual incentive amounts are presented inclusive of any amounts which must be deferred in shares for three years (i.e. one-third of the 2011 incentive award). Of the amounts presented above, £227,318 of Clive Bannister's incentive payment will be deferred in shares for a period of 3 years. Full details of the number of shares under award will be disclosed in the 2012 Remuneration report.

3 Clive Bannister joined Phoenix Group on 7 February 2011 and was appointed to the Board as a Director on 28 March 2011. The detail shown only relates to the period from his appointment as a Director to 31 December 2011, except for the AIP which includes the amount earned in respect of the period 7 February 2011 to 28 March 2011.

4 Appointed to the Board on 18 February 2010.

5 Appointed to the Board on 29 March 2010.

6 Resigned from the Board on 7 February 2011.

7 Simon Smith resigned from the Board on 23 June 2010. The details shown for 2010 only relate to the period from the 1 January 2010 to 23 June 2010.

8 Jonathan Yates resigned from the Board on 21 December 2011.

Pensions

Clive Bannister and Jonathan Yates received a Company contribution of 20% of base salary. Jonathan Moss received a Company contribution of 11.7% of salary (up to a maximum earnings limit of £123,600) to a defined contribution pension arrangement.

During the year to 31 December 2011, the Group has made the following contributions to the defined contribution arrangements:

	£
Clive Bannister	105,000
Jonathan Yates	83,000
Jonathan Moss	1,205

Share-based awards

As at 31 December 2011, Directors' interests under long-term share-based arrangements were as follows:

	Date of grant	Share price on grant	As at 1 Jan 2011	Shares granted	Shares vested	Shares lapsed	**As at 31 Dec 2011**	Vesting date
Clive Bannister								
LTIP[3]	12 April 2011	657.5p	–	212,927	–	–	**212,927**	12 April 2014

	Date of grant	Share price on grant	As at 1 Jan 2011	Shares granted	Shares vested	Shares lapsed	**As at 31 Dec 2011**	Vesting date
Jonathan Yates								
LTIP[3,4]	28 May 2010	627.5p	127,490	–	–	–	**127,490**	28 May 2013
LTIP[3,4]	12 April 2011	657.5p	–	126,235	–	–	**126,235**	12 April 2014
			127,490	**126,235**	**–**	**–**	**253,725**	
Jonathan Moss								
BSP[1,5]	21 Sep 2009	842.0p	112,500	–	112,500	–	**–**	29 Mar 2011
Phantom[2]	02 Sep 2009	818.0p	73,350	–	–	–	**73,350**	02 Sep 2012
LTIP[3,4,5]	28 May 2010	627.5p	207,171	–	–	–	**207,171**	28 May 2013
			393,021	**–**	**112,500**	**–**	**280,521**	

1 The Bonus Share Plan ('BSP') was introduced to reward a small number of senior executives upon completion of the September 2009 refinancing. BSP awards vested on the second anniversary of grant, subject to continued service. In line with the BSP rules, Jonathan Moss' BSP awards vested in full on the termination of his employment on 29 March 2011. No further BSP awards will be granted. The share price at vesting was 668p.

2 In March 2010, the Group confirmed the operation of a phantom share award to a small number of senior executives. Individuals were granted a notional number of shares based on a multiple of salary at the time of grant (150% of base salary for the Group Chief Executive Officer). Awards (including those granted to Jonathan Moss who was treated as a good leaver) will vest on the third anniversary of grant generally subject to continued employment, with the value delivered in cash based on the prevailing share price at that time.

3 The performance conditions for the 2010 and 2011 awards are set out in the Remuneration policy section of this report (except that for the 2010 grant, the cash generation targets were £1.375 billion rising to £1.655 billion). Jonathan Moss' award was pro-rated with the 207,171 shares presented in the table reduced to 57,547 shares.

4 In addition to the shares awarded under the LTIP presented above, participants received an additional number of shares (based on the number of LTIP awards which actually vest) to reflect the dividends paid during the vesting period.

5 On vesting, the shares awarded under the 2009 LTIP were appointed into sub-trusts of the Phoenix Group Holdings Employee Benefit Trust, for the benefit of Jonathan Moss' family. On vesting the shares to be awarded under the BSP were also appointed into this sub-trust.

Deferred Bonus Shares	Date of Award	Shares awarded	Share price on award	Lapsed	Outstanding	Vesting Date
Clive Bannister	–	–	–	–	–	–
Jonathan Yates	6 April 2011	16,259	672.7p	–	16,259	6 April 2013

Notes:

This is the arrangement pursuant to which part of the annual incentive for any year is deferred into the Company's shares.

Sharesave

At the end of the year, the Executive Directors' Sharesave share options were as follows:

	As at 1 Jan 2011	Options granted	Options vested	Options exercised	Options lapsed	**As at 31 Dec 2011**	Exercise price	Exercisable from	Date of expiry
Clive Bannister	–	1,577	–	–	–	**1,577**	£5.72	01 June 2014	30 Nov 2014
Jonathan Moss	1,611	–	–	–	1,611	**–**	£5.63	01 Mar 2013	31 Aug 2013
Jonathan Yates	–	–	–	–	–	**–**	–	–	–

Sharesave options held by Jonathan Moss lapsed on 29 March 2011.

During the year ended 31 December 2011, the highest mid-market price of the Company's shares was 688p and the lowest mid-market price was 451.1p. At 31 December 2011, the Company's share price was 525p.

Directors' interests

Name	As at 1 January 2011 or date of appointment if later	As at 31 December 2011 and as at 22 March 2012
Clive Bannister	–	–
Jonathan Yates	–	–
Ian Ashken[1]	1,260,759	1,263,698
René-Pierre Azria	16,866	27,812

David Barnes	2,300	2,300
Charles Clarke	2,000	2,000
Ian Cormack	–	–
Tom Cross Brown	1,615	1,664
Manjit Dale[2]	–	–
Isabel Hudson	1,587	3,249
Alastair Lyons	7,500	7,500
Hugh Osmond[3]	9,714,015	9,849,533
Ron Sandler	182,133	195,666
David Woods	–	–
Jonathan Moss	162,505	275,005

1 Ian Ashken holds 1,113,698 shares in his own name. Tasburgh LLC, of which Ian Ashken is a managing member, holds 150,000 shares and is considered a connected person to Mr Ashken.

2 Manjit Dale is a director of TDR Capital Nominees Limited, Jambright Limited and O-Re Holdings UK Limited and as such these companies are all considered as connected persons. Total interests held by these entities amount to 33,763,900.

3 Hugh Osmond is a director of Xercise2 Limited, Xercise Limited and O-Re Holdings UK Limited and as such these are considered as connected persons. Hugh Osmond has a total interest in 30,095,410 shares of which he has beneficial interest over 9,849,533.

Additional FSA Disclosures

Code Staff

The Remuneration Committee has identified the Group's asset management subsidiary, Ignis Asset Management, as a Code firm. By virtue of its influence over Ignis, the Committee has determined that Phoenix Group Holdings is also a Code firm. Both companies have been identified as Tier 4 Code firms. The Committee has determined that 23 staff within Ignis qualify as Code Staff. The Committee has also determined that a further 23 Group employees, who have sufficient supervisory responsibility over Ignis' activities, qualify as Code Staff.

Whilst not all of Phoenix Group's activities are covered by the FSA Remuneration Code, the Committee anticipates broadly equivalent provisions will apply, in due course, via Solvency II. The Committee considers the FSA Code to reflect best practice and has due regard to it across the Group.

Code Staff criteria

The following groups of employees have been identified within the Code firms as meeting the FSA's criteria for Code Staff:

- Certain members of the Group Board and Executive Management Committee
- Employees performing a Significant Influence Function in relation to the Code firm
- Key control function roles.

Design and structure of remuneration

The individual elements of employees' remuneration packages at Phoenix Group comprise fixed pay (base salary, retirement and other benefits) and performance-related pay (consisting of annual incentives, deferred awards and long-term incentives).

Taking into account the expected value of long-term incentives, the performance-related elements of the package make up a significant proportion of the total remuneration of Code Staff, while maintaining an appropriate balance between fixed and variable elements.

Base salary and fees

All Code Staff receive either a base salary (employees) or fees (Non-Executive Directors) to reflect their experience, skills, competencies and contribution to the Group relative to the market for comparable roles. Phoenix Group ensures that fixed remuneration is sufficient to cover employees' key financial needs while generally seeking to pay base salary around a mid-market range.

Phoenix Group also operates a fully flexible bonus policy which allows zero bonus payments to be made when appropriate.

Benefits

Code Staff receive benefits in line with other employees that include pension provision, and may include car allowance, private medical insurance and life assurance. Non-Executive Directors who are listed as Code Staff do not receive any benefits.

Annual incentives

Rationale and eligibility criteria

All executive Code Staff are eligible to receive an annual incentive. Annual incentives are designed to reward good financial and non-financial performance that supports the business strategy, taking into account the Group's risk appetite and personal contribution.

Non-executive Code Staff are not eligible to receive annual incentives.

Performance measurement/assessment

For Group and life company employees, performance assessment is normally based upon a balanced scorecard of measures related to Group and/or life company and individual targets. These targets typically include financial performance, risk, people and customer measures. Overall bonus costs are reviewed by the Committee at the year end having regard to the Group KPIs and non-financial measures.

Ignis employees' bonuses are financed from a defined profit pool (subject to discretion being reserved to the Committee to adjust the percentage available). Distribution of the pool has due regard to objectives similar to those in the Group and life companies.

For senior staff in control functions (Internal Audit, Regulatory Compliance and Risk) reward will, from 1 January 2012, be linked to individual achievement against personal objectives and will exclude any direct link to financial performance.

In each case, target levels of individual reward have regard to market levels for comparable roles internally and externally.

All incentive awards to Code Staff are subject to the review and support of the Committee.

Deferral and vesting

The Committee requires that one-third of annual incentives awarded to the Group's senior employees are deferred into Phoenix Group Holdings shares. Equivalent rules apply to Ignis employees who are required to defer part of their bonus into phantom shares where the value of the outcome is determined by Ignis' financial performance.

These deferral arrangements extend to the majority of Code Staff.

Long-term incentives

Group

To encourage the creation of value over the long-term and to align the rewards of the participants with the returns to shareholders, the Group provides employees in senior roles (executive level and selected senior management) the opportunity to receive annual awards of long-term incentives. Details of the LTIP are given on page 75 of this report.

Ignis

Selected employees are eligible to receive awards subject to the rules of the Ignis Long-Term Phantom Option Plan ('LTOP'). Awards may be made annually but are typically one-off in nature and reward the growth in the notional value of Ignis over a six year period (with one-third of the award vesting on the fourth, fifth and sixth anniversaries of the grant date). Awards take the form of a cash settled option. Awards with a grant date of 2010 reward growth over an initial value of £1 per notional share, whilst awards granted in respect of 2011 reward growth over an initial value of £1.15 per notional share. The value per notional share at the end of the year was £1.16. Where it has been necessary and as a part of the recruitment process, the Committee has provided an underpin to the value of the award to reflect the value forfeited by employees due to leaving previous employers.

Risk adjustment

To manage the risk aspects of the remuneration policy, the Committee considers the performance of the Group and individual businesses against risk objectives in determining the bonus pool and requires the Chief Risk Officer to report to the Committee on this.

Quantitative Remuneration Disclosure

The Group is required to disclose aggregate quantitative remuneration information for Code Staff.

There were 23 Code Staff that have been classified as Group and 23 as Ignis. Aggregate remuneration expenditure is broken down as follows:

	Number of staff	£m
Non-executive Director	17	4.18
Senior Management	9	14.33
Other	20	12.38

Total	**46**	**30.89**

	Number of staff	£m
Ignis	23	18.30
Group	23	12.59
Total	**46**	**30.89**

Approval
This report in its entirety has been approved by the Committee and the Board of Directors and signed on its behalf by

Ian Cormack
Remuneration Committee Chairman

22 March 2012

IFRS FINANCIAL STATEMENTS

The IFRS operating profit of £387 million reflects a strong performance from both the Group's operating segments.

In this section

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Board Responsibility Statement according to section 5:25c(2)(c) of the Dutch Financial Markets Supervision Act.[1]

The Board of Directors of Phoenix Group Holdings hereby declares that, to the best of its knowledge:

1. The IFRS financial statements for the year ended 31 December 2011 give a true and fair view of the assets, liabilities, financial position and results of Phoenix Group Holdings and its consolidated subsidiaries taken as a whole;
2. The Annual Report gives a true and fair view of the state of affairs of Phoenix Group Holdings and its consolidated subsidiaries as at 31 December 2011 and their development in the financial year to which the Annual Report and Accounts relate; and
3. The Annual Report describes the principal risks facing Phoenix Group Holdings.

Clive Bannister
Group Chief Executive Officer

Alastair Lyons
Audit Committee Chairman

St Helier, Jersey
22 March 2012

[1] The Company's home member state is the Netherlands as a result of its original listing on Euronext Amsterdam and is therefore governed by the Dutch Financial Markets Supervision Act.

INDEPENDENT AUDITOR'S REPORT

To: The Meeting of Shareholders of Phoenix Group Holdings

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements 2011 of Phoenix Group Holdings, Cayman Islands, and its subsidiaries (the 'Group'), which comprise the statement of consolidated financial position as at 31 December 2011, the consolidated income statement, the statement of consolidated comprehensive income, the pro forma reconciliation of Group operating profit to result attributable to owners, the statement of consolidated changes in equity and the statement of consolidated cash flows for the year then ended, and notes, comprising a summary of the significant accounting policies and other explanatory information.

Directors' responsibility
The Directors are responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code, and for the preparation of the Directors' Report in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore the Board of Directors is

responsible for such internal control as it determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. This requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the Group's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion with respect to the consolidated financial statements

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2011, and of its result and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code.

Report on other legal and regulatory requirements

Directors' Report in accordance with Dutch Civil Code

Pursuant to the legal requirement under section 2:393 sub 5 at e and f of the Dutch Civil Code, we have no deficiencies to report as a result of our examination as to whether the Directors' Report, to the extent we can assess, has been prepared in accordance with Part 9 of Book 2 of this Code, and whether the information as required under section 2:392 sub 1 at b–h has been annexed. Further we report that the Directors' report, to the extent we can assess, is consistent with the consolidated financial statements as required by section 2:391 sub 4 of the Dutch Civil Code.

Requirements of the Listing Rules

We have nothing to report in respect of the following items that we are required to review under the Listing Rules:

- the Directors' statement, set out on page 62, in relation to going concern;
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

Matters on which we report by exception because of voluntary compliance with the UK Companies Act 2006

We have nothing to report in respect of the following items that we are required to report to you under the UK Companies Act 2006 if, in our opinion:

- adequate accounting records have not been kept by the Group, or returns adequate for our audit have not been received from branches not visited by us; or
- the Directors' Remuneration report to be audited is 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;

The Hague, 22 March 2012

Ernst & Young Accountants LLP

was signed by
S. B. Spiessens

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2011

	Notes	**2011 £m**	2010 £m
Gross premiums written		**1,473**	1,534
Less: premiums ceded to reinsurers		**(85)**	(85)
Net premiums written		**1,388**	1,449
Fees	6	**170**	162

Net investment income	7	**4,920**	5,907
Total revenue, net of reinsurance payable		**6,478**	7,518
Other operating income	8	**12**	25
Net income		**6,490**	7,543
Policyholder claims		**(4,968)**	(5,260)
Less: reinsurance recoveries		**224**	210
Change in insurance contract liabilities		**(1,338)**	(252)
Change in reinsurers' share of insurance contract liabilities		**222**	89
Transfer from/(to) unallocated surplus	21	**16**	(143)
Net policyholder claims and benefits incurred		**(5,844)**	(5,356)
Change in investment contract liabilities		**260**	(964)
Acquisition costs	9	**(13)**	(12)
Change in present value of future profits	33	**(19)**	7
Amortisation of acquired in-force business	33	**(134)**	(147)
Amortisation of customer relationships	33	**(18)**	(18)
Administrative expenses	10	**(606)**	(676)
Net income/(expense) attributable to unitholders		**131**	(97)
Total operating expenses		**(6,243)**	(7,263)
Profit before finance costs and tax		**247**	280
Finance costs	12	**(251)**	(269)
(Loss)/profit for the year before tax		**(4)**	11
Tax attributable to policyholders' returns	13	**(173)**	(5)
(Loss)/profit before the tax attributable to owners		**(177)**	6
Tax (charge)/credit	13	**(94)**	69
Add: tax attributable to policyholders' returns	13	**173**	5
Tax credit attributable to owners	13	**79**	74
(Loss)/profit for the year attributable to owners		**(98)**	80
Attributable to:			
Owners of the parent		**(131)**	30
Non-controlling interests	19	**33**	50
		(98)	80
Earnings per ordinary share			
Basic and diluted earnings per ordinary share	15	**(76.2p)**	20.1p

STATEMENT OF CONSOLIDATED COMPREHENSIVE INCOME

For the year ended 31 December 2011

	Notes	2011 £m	2010 £m
(Loss)/profit for the year		**(98)**	80
Other comprehensive income:			
Actuarial gains of defined benefit pension schemes	32	**251**	45
Contribution in respect of actuarial losses of defined benefit pension scheme by the with-profit funds	32	**–**	27
		251	72
Tax credit on actuarial gains of defined benefit pension schemes	13	**1**	4
		252	76
Total comprehensive income for the year		**154**	156
Attributable to:			
Owners of the parent		**121**	106
Non-controlling interests		**33**	50
		154	156

PRO FORMA RECONCILIATION OF GROUP OPERATING PROFIT TO RESULT ATTRIBUTABLE TO OWNERS

For the year ended 31 December 2011

	Notes	2011 £m	2010 £m
Operating profit			
Phoenix Life		**395**	388
Ignis Asset Management		**46**	46
		441	434
Group costs		**(54)**	(61)
Total operating profit before adjusting items		**387**	373
Investment return variances and economic assumption changes on long-term business	5	**(338)**	18
Variance on owners' funds	5	**9**	19
Amortisation of acquired in-force business		**(121)**	(132)
Amortisation of customer relationships		**(18)**	(18)
Non-recurring items	4.2	**14**	(139)
(Loss)/profit before finance costs attributable to owners		**(67)**	121
Finance costs attributable to owners		**(110)**	(115)
(Loss)/profit before the tax attributable to owners	4.2	**(177)**	6
Tax credit attributable to owners		**79**	74
(Loss)/profit for the year attributable to owners		**(98)**	80

STATEMENT OF CONSOLIDATED FINANCIAL POSITION

As at 31 December 2011

	Notes	**2011 £m**	2010 Restated £m
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	16	**–**	–
Share premium		**1,054**	1,109
Other reserves		**5**	5
Shares held by employee trust and Group entities	17	**(11)**	(13)
Foreign currency translation reserve		**93**	93
Retained earnings		**511**	386
Total equity attributable to owners of the parent		**1,652**	1,580
Non-controlling interests	19	**714**	720
Total equity		**2,366**	2,300
Liabilities			
Pension scheme deficit	32	**–**	77
Insurance contract liabilities			
Liabilities under insurance contracts	20	**51,800**	50,479
Unallocated surplus	21	**848**	864
		52,648	51,343
Financial liabilities			
Investment contracts		**7,978**	8,849
Borrowings	22	**3,152**	4,028
Deposits received from reinsurers	23	**472**	419
Derivatives	24	**4,292**	2,431
Net asset value attributable to unit holders		**3,209**	1,937
Obligations for repayment of collateral received	25	**13,005**	10,160
	26	**32,108**	27,824
Provisions	27	**59**	73
Deferred tax	28	**673**	607
Reinsurance payables		**33**	25
Payables related to direct insurance contracts	29	**707**	713
Current tax	28	**105**	99

Accruals and deferred income	30	**175**	214
Other payables	31	**627**	327
Total liabilities		**87,135**	81,302
Total equity and liabilities		**89,501**	83,602

	Notes	**2011 £m**	2010 Restated £m
ASSETS			
Pension scheme surplus	32	**314**	59
Intangible assets			
Goodwill		**115**	115
Acquired in-force business		**1,882**	2,016
Customer relationships		**402**	420
Present value of future profits		**23**	42
	33	**2,422**	2,593
Property, plant and equipment	34	**28**	34
Investment property	35	**1,816**	1,732
Financial assets			
Loans and receivables		**3,529**	2,293
Derivatives	24	**6,099**	3,197
Equities		**11,078**	12,460
Fixed and variable rate income securities		**42,010**	40,899
Collective investment schemes		**6,251**	7,144
	36	**68,967**	65,993
Insurance assets			
Reinsurers’ share of insurance contract liabilities	20	**3,153**	2,939
Reinsurance receivables		**257**	263
Insurance contract receivables		**14**	19
		3,424	3,221
Current tax	28	**8**	5
Prepayments and accrued income		**599**	603
Other receivables	39	**200**	174
Cash and cash equivalents	40	**11,723**	9,188
Total assets		**89,501**	83,602

STATEMENT OF CONSOLIDATED CASH FLOWS

For the year ended 31 December 2010

	Notes	2011 £m	2010 £m
Cash flows from operating activities			
Cash generated by operations	41	**3,692**	3,392
Taxation (paid)/recovered		**(16)**	3
Net cash flows from operating activities		**3,676**	3,395
Cash flows from investing activities			
Purchase of property, plant and equipment		**(7)**	(3)
Net cash flows from investing activities		**(7)**	(3)
Cash flows from financing activities			
Gross proceeds from issue of share capital		**–**	33
Proceeds from issuing shares in subsidiaries to non-controlling interests		**1**	96
Partial buy back of non-controlling interests		**–**	(4)
Proceeds of new policyholder borrowings		**98**	–
Ordinary share dividends paid		**(55)**	(43)
Coupon on Perpetual Reset Capital Securities paid		**(26)**	(62)
Dividends paid to non-controlling interests		**(21)**	(18)
Repayment of policyholder borrowings		**(825)**	(38)
Repayment of shareholder borrowings		**(174)**	(127)
Interest paid on policyholder borrowings		**(21)**	(12)
Interest paid on shareholder borrowings		**(111)**	(110)
Net cash flows from financing activities		**(1,134)**	(285)
Net increase in cash and cash equivalents		**2,535**	3,107
Cash and cash equivalents at the beginning of the year		**9,188**	6,081
Cash and cash equivalents at the end of the year	40	**11,723**	9,188

STATEMENT OF CONSOLIDATED CHANGES IN EQUITY

For the year ended 31 December 2011

	Share capital (note 16) £m	Share premium £m	Other reserves £m	Shares held by the employee trust and group entities (note 17) £m	Foreign currency translation reserve £m	Retained earnings £m	Total £m	Non-controlling interests (note 19) £m	Total £m
At 1 January 2011	**–**	**1,109**	**5**	**(13)**	**93**	**386**	**1,580**	**720**	**2,300**
(Loss)/profit for the year	**–**	**–**	**–**	**–**	**–**	**(131)**	**(131)**	**33**	**(98)**
Other comprehensive income for the	**–**	**–**	**–**	**–**	**–**	**252**	**252**	**–**	**252**

year									
Total comprehensive income for the year	**–**	**–**	**–**	**–**	**–**	**121**	**121**	**33**	**154**
Dividends paid on ordinary shares	**–**	**(72)**	**–**	**–**	**–**	**–**	**(72)**	**–**	**(72)**
Dividends paid to non-controlling interests	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(21)**	**(21)**
Coupon paid to non-controlling interests, net of tax relief	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(19)**	**(19)**
Shares issued in lieu of dividends	**–**	**17**	**–**	**–**	**–**	**–**	**17**	**–**	**17**
Credit to equity for equity-settled share-based payment	**–**	**–**	**–**	**–**	**–**	**6**	**6**	**–**	**6**
Shares in subsidiaries subscribed for by non-controlling interests	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**1**	**1**
Shares distributed by employee trust	**–**	**–**	**–**	**2**	**–**	**(2)**	**–**	**–**	**–**
At 31 December 2011	**–**	**1,054**	**5**	**(11)**	**93**	**511**	**1,652**	**714**	**2,366**

STATEMENT OF CONSOLIDATED CHANGES IN EQUITY

For the year ended 31 December 2010

	Share capital (note 16) £m	Share premium £m	Other reserves £m	Shares held by the employee trust and group entities (note 17) £m	Foreign currency translation reserve £m	Retained earnings £m	Total £m	Non-controlling interests (note 19) £m	Total £m
At 1 January 2010	–	859	257	(4)	93	207	1,412	728	2,140
Profit for the year	–	–	–	–	–	30	30	50	80
Other comprehensive income for the year	–	–	–	–	–	76	76	–	76
Total comprehensive income for the year	–	–	–	–	–	106	106	50	156
Dividends paid on ordinary shares	–	(34)	(20)	–	–	–	(54)	–	(54)
Dividends paid to non-controlling interests	–	–	–	–	–	–	–	(18)	(18)
Coupon paid to non-controlling interests, net of tax relief	–	–	–	–	–	–	–	(47)	(47)
Issue of share capital	–	33	–	–	–	–	33	–	33
Shares issued in lieu of dividends	–	11	–	–	–	–	11	–	11
Issue of ordinary shares – Chairman’s shares	–	1	–	–	–	(1)	–	–	–
Conversion of contingent rights over shares	–	230	(230)	(3)	–	–	(3)	–	(3)
Credit to equity for equity-settled share-based payment	–	–	–	–	–	8	8	–	8
Conversion of warrants into ordinary shares	–	9	(2)	–	–	–	7	–	7
Shares in subsidiaries subscribed for by non-controlling interests	–	–	–	–	–	–	–	96	96
Partial buy back of non-controlling	–	–	–	–	–	–	–	(19)	(19)

interest									
Restructure of non-controlling interests	–	–	–	–	–	70	70	(70)	–
Shares acquired by employee trust	–	–	–	(10)	–	–	(10)	–	(10)
Shares distributed by employee trust	–	–	–	4	–	(4)	–	–	–
At 31 December 2010	–	1,109	5	(13)	93	386	1,580	720	2,300

Phoenix Group Holdings is subject to Cayman Islands Companies Law. Under Cayman Islands 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.

Retained earnings comprise the owners' interest in the post-acquisition retained earnings of the subsidiary companies and the retained earnings of the Company. Distribution of the retained earnings held within the long-term business funds and surplus assets held within the owners' funds of the life companies is subject to retaining sufficient funds to protect policyholders' interests.

There is a restriction on the ability of certain subsidiary companies to distribute funds to Phoenix Group Holdings as a result of restrictions imposed by the Group's two main credit agreements, namely the Pearl Facility and the Impala Facility (note 22).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting policies

(a) Basis of preparation

The consolidated financial statements for the year ended 31 December 2011 comprise the financial statements of Phoenix Group Holdings ('the Company') and its subsidiaries (together referred to as 'the Group').

The consolidated financial statements have been prepared on a historical cost basis except for investment property, owner-occupied property and those financial assets, financial liabilities and insurance and investment contracts with discretionary participation features ('DPF') that have been measured at fair value.

Statement of compliance

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

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

Assets and 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 IFRS 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. 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 recognised in the consolidated income statement. Directly attributable acquisition costs are included within administrative expenses, except for acquisitions undertaken prior to 2010 when they are included within the cost of the acquisition. Costs directly related to the issuing of debt or equity securities 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 share of net assets attributed to the non-controlling interest holder, adjusted for the relevant share of subsequent changes in equity.

(b) Critical accounting estimates and judgements

The preparation of financial statements 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 43.

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. 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. Further details of the estimates made are included in note 37.

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. Further details of estimates made are included in note 33.

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 the carrying value of deferred tax in the financial statements are discussed in note 28.

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

Pension benefit assets and liabilities

The valuation of pension benefit assets and liabilities is determined using actuarial valuations using a number of assumptions. 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, expenses and cash flows denominated in foreign currencies are translated at average exchange rates; and
- all resulting exchange differences are recognised through the statement of consolidated comprehensive income.

Foreign currency transactions are translated into the functional currency of the transacting Group entity using exchange rates prevailing at the date of translation. 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 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 FSA Handbook for Insurers. The liability for insurance contracts 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 on 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 43.

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 in accordance with the FSA's realistic capital regime. The key aspects of this methodology are:

- liabilities to policyholders arising from the with-profit 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 43.

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 ('PVFP') 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. This 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 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 43.

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 *Insurance Contracts*, 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 this represents amounts which have yet to be allocated to owners since the unallocated surplus attributable to policyholders has been included within liabilities under insurance contracts.

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 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 accounting mismatches 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 and managed 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 meet the definition of 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, it is recognised as a 'financial asset' and the collateral repayable is recognised as 'deposits received from reinsurers' within the statement of consolidated financial position.

(j) Net asset value attributable to unitholders
The net asset value attributable to unitholders represents the non-controlling interest in collective investment schemes which are consolidated by the Group. 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 and derivative transactions, usually in the form of cash or marketable securities. Where cash collateral is available to the Group for investment purposes, it is recognised as a 'financial asset' and the collateral repayable is recognised as 'obligations for repayment of collateral received' in the statement of consolidated financial position. 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 pension plans
Obligations for contributions to defined contribution pension plans are recognised as an expense in the consolidated income statement as incurred.

Defined benefit pension 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. As required by IFRIC 14, to the extent that the economic surplus will be available as a refund, the scheme assets are stated after a provision for tax that would be borne by the scheme administrators when the refund is made.

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, past service cost, curtailments and settlements (recognised within administrative expenses in the consolidated income statement), the interest cost on the liabilities less the expected return on assets, including any reimbursement assets (recognised within net investment income in the consolidated income statement), actuarial gains and losses (recognised in other comprehensive income) and employer contributions. All actuarial gains and losses are recognised in full.

Part of the cost of changes in the longevity assumptions of the PGL pension scheme is recoverable from certain with-profit funds to the extent that cash contributions are made to the pension scheme. Recoveries are recognised when the related cash contributions are agreed with the Trustee of the pension scheme and are accounted for as a transfer to other comprehensive income from insurance contract liabilities.

(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 less than the 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
Intangible assets include vesting pension premiums and investment management contracts as detailed in note 33. These 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 on a straight-line basis over their useful economic lives and assessed for impairment whenever there is an indication that the recoverable amount 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 50 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*. 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 derivative assets 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 this is reflective of the manner in which they are managed and the risks are evaluated.

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. 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 applicable 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 contractual cash flows using current market conditions and market calibrated discount rates and interest rate assumptions for similar instruments.

For units in unit trusts and shares in open-ended investment companies, fair value is determined 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 in 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.

(s) Reinsurance
The Group cedes insurance risk in the normal course of business. Reinsurance assets represent balances due from reinsurance providers. Reinsurers' share of insurance contract liabilities is 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 period. 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 recognised in the consolidated income statement. The reinsurers' share of investment contract liabilities is measured on a basis that is consistent with the valuation of the liability to policyholders to which the reinsurance applies.

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 payables 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 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 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 in issue during the year.

For the diluted earnings per share, the weighted average number of 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. As permitted by Cayman Islands Companies Law, dividends have been charged within equity against the share premium account and other reserves account. Where shareholders exercise a scrip dividend option, the amount of the related dividend is credited to share premium in the statement of consolidated changes in equity and an amount equal to the nominal value of the shares issued is transferred from share premium to share capital.

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 payment 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.

Fair value 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 claims payable on death are recognised 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 payable is recognised in the consolidated income statement as it accrues and is calculated using the effective interest method.

(z) Share capital and shares held by the employee trust and Group entities

Ordinary share capital
The Group has issued ordinary shares which are 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 the employee trust and Group entities
Where an employee trust or a Group entity acquires shares in the Company 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 the employee trust and Group entities are charged or credited to the own shares account in equity.

(aa) General business
The general insurance business has been closed to new business for a number of years and is in run-off. The results are included within other operating income in 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.

2. Financial information
The consolidated financial statements for the year ended 31 December 2011, set out on pages 84 to 164, were authorised on 22 March 2012 by the Board of Directors for issue.

In preparing the financial statements the Group has adopted the following standards, interpretations and amendments which have been issued by the International Accounting Standards Board ('IASB') and have been adopted for use by the EU. None of these have a material effect on the results of the Group.

- IAS 32 *Financial Instruments Presentation* (Amendment). The amendment alters the definition of a financial liability in IAS 32 to enable entities to classify rights issues and certain options or warrants as equity instruments.
- IFRIC 14 *Prepayments of a Minimum Funding Requirement* (Amendment). The amendment permits a prepayment of future service costs in accordance with a minimum funding requirement to be recognised as a pension asset.
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*. This addresses the accounting by an entity when the terms of a financial liability are renegotiated and result in its equity instruments being issued to extinguish all or part of the financial liability.
- Annual improvements 2010. This makes a number of minor improvements to existing standards and interpretations.

The IASB has issued the following standards, interpretations and amendments which, subject to adoption for use by the EU, apply from the dates shown. The Group has decided not to early adopt any of these standards, interpretations or amendments where this is permitted. The impact on the Group of adopting them is subject to evaluation:

- IFRS 9 *Financial Instruments* (2015). This is the first two parts of a replacements standard for IAS 39 *Financial Instruments: Recognition and Measurement* and deals with the classification and measurement of financial assets and financial liabilities, including some hybrid contracts.
- Deferred tax: Recovery of Underlying Assets (Amendments to IAS 12) (2012). This provides a practical approach to the measurement of deferred tax liabilities and assets when investment property is measured at fair value, according to whether the entity expects to recover an asset by using or selling it.
- Disclosure – Transfer of Financial Assets (Amendments to IFRS 7) (2012). This revises the required disclosures to help users of financial statements evaluate the risk exposures relating to transfers of financial assets and the effect of those risks on an entity's financial position.
- IFRS 11 *Joint Arrangements* (2013) establishes principles for financial reporting by parties to a joint arrangement.
- IFRS 12 *Disclosure of Interests in Other Entities* (2013) combines, enhances and replaces the disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities.
- IFRS 13 *Fair Value Measurement* (2013) defines fair value and sets out in a single IFRS a framework for measuring fair value.
- Presentation of Items of Other Comprehensive Income (Amendments to IAS 1) (2013). The amendment requires companies to group together items within other comprehensive income that may be reclassified to the profit or loss section of the income statement.

- IAS 19 *Employee Benefits* (Amendment) (2013). The IASB has issued numerous amendments to IAS 19. These range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording.
- IAS 28 *Investments in Associates and Joint Ventures* (Revised) (2013). This standard supersedes IAS 28 Investments in Associates and prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.
- Disclosures – Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7) (2013). The new disclosure requirements are intended to help users of financial statements better assess the effect or potential effect of offsetting arrangements on an entity's financial position.
- Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32) (2014). The amendments address inconsistencies in current practice when applying the offsetting criteria in IAS 32.

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

- Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (Amendments to IFRS 1) (2012).
- IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* (2013).
- IAS 27 *Separate Financial Statements* (Revised) (2013).

3. Prior period adjustment

During the Group's review of the recoverability of its deferred tax assets, it was identified that a deferred tax asset of £38 million should have been written off at the date of, and as a consequence of, the 2009 acquisition of the then Pearl businesses by the Company. The consequence of this is a prior year understatement of deferred tax liabilities and goodwill of £38 million. The impact of the correction on the prior year statement of consolidated financial position is to increase goodwill and deferred tax liabilities by £38 million. The correction of this classification error has no impact on operating profit, profit attributable to owners, retained earnings or net assets. A statement of consolidated financial position as at 31 December 2009 has not been presented as it would not add any further clarity to the information presented above.

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 operating 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 presented 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 are sourced in the UK.

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

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

4.1 Segmental result

2011

	Phoenix Life £m	Ignis Asset Management £m	Unallocated group £m	Eliminations £m	Total £m
Net premiums written from:					
External customers	**1,388**	–	–	–	**1,388**
Other segment	–	–	–	–	–
	1,388	–	–	–	**1,388**
Fees from:					

External customers	**94**	**76**	**–**	**–**	**170**
Other segment	**–**	**69**	**–**	**(69)**	**–**
	94	**145**	**–**	**(69)**	**170**
Net investment income:					
Recurring	**4,911**	**1**	**8**	**–**	**4,920**
Offset interest income on interest swaps against interest expenses[1]	**–**	**–**	**(19)**	**–**	**(19)**
	4,911	**1**	**(11)**	**–**	**4,901**
Other operating income:					
Recurring	**12**	**–**	**–**	**–**	**12**
Net income	**6,405**	**146**	**(11)**	**(69)**	**6,471**
Net policyholder claims and benefits incurred:					
Recurring	**(5,879)**	**–**	**–**	**–**	**(5,879)**
Non-recurring	**35**	**–**	**–**	**–**	**35**
	(5,844)	**–**	**–**	**–**	**(5,844)**
Depreciation, impairment and amortisation:					
Depreciation of property, plant and equipment	**–**	**(3)**	**–**	**–**	**(3)**
Impairment losses on property, plant and equipment	**(8)**	**–**	**–**	**–**	**(8)**
Amortisation of acquired in-force business	**(134)**	**–**	**–**	**–**	**(134)**
Amortisation of customer relationships	**(13)**	**(5)**	**–**	**–**	**(18)**
	(155)	**(8)**	**–**	**–**	**(163)**
Other operating expenses:					
Recurring	**(136)**	**(97)**	**(51)**	**69**	**(215)**
Non-recurring	**(50)**	**(2)**	**31**	**–**	**(21)**
	(186)	**(99)**	**(20)**	**69**	**(236)**
Total operating expense	**(6,185)**	**(107)**	**(20)**	**69**	**(6,243)**
Profit/(loss) before finance costs and tax	**220**	**39**	**(31)**	**–**	**228**
Finance costs	**(122)**	**–**	**(129)**	**–**	**(251)**
Offset interest income on interest swaps against interest expense[1]	**–**	**–**	**19**	**–**	**19**
	(122)	**–**	**(110)**	**–**	**(232)**
Profit/(loss) before tax	**98**	**39**	**(141)**	**–**	**(4)**
Tax attributable to policyholders' returns	**(173)**	**–**	**–**	**–**	**(173)**
Segmental result before the tax attributable to owners	**(75)**	**39**	**(141)**	**–**	**(177)**

[1] The Group has entered into derivatives to protect its net exposure to interest rate fluctuations and this reallocation reflects the net economic interest exposure of the Group.

2010

	Phoenix Life £m	Ignis Asset Management £m	Unallocated group £m	Eliminations £m	Total £m
Net premiums written from:					
External customers	1,449	–	–	–	1,449
Other segment	–	–	–	–	–
	1,449	–	–	–	1,449

Fees from:					
External customers	100	62	–	–	162
Other segment	–	82	–	(82)	–
	100	144	–	(82)	162
Net investment income:					
Recurring	5,877	–	35	–	5,912
Offset interest income on interest swaps against interest expenses[2]	–	–	(53)	–	(53)
Non-recurring	(5)	–	–	–	(5)
	5,872	–	(18)	–	5,854
Other operating income:					
Recurring	25	–	–	–	25
Net income	7,446	144	(18)	(82)	7,490
Net policyholder claims and benefits incurred:					
Recurring	(5,292)	–	–	–	(5,292)
Non-recurring	(64)	–	–	–	(64)
	(5,356)	–	–	–	(5,356)
Depreciation, and amortisation:					
Depreciation of property, plant and equipment	–	(3)	–	–	(3)
Amortisation of acquired in-force business	(147)	–	–	–	(147)
Amortisation of customer relationships	(15)	(3)	–	–	(18)
	(162)	(6)	–	–	(168)
Other operating expenses:					
Recurring	(1,616)	(95)	(40)	82	(1,669)
Non-recurring	(38)	–	(32)	–	(70)
	(1,654)	(95)	(72)	82	(1,739)
Total operating expense	(7,172)	(101)	(72)	82	(7,263)
Profit/(loss) before finance costs and tax	274	43	(90)	–	227
Finance costs	(101)	–	(168)	–	(269)
Offset interest income on interest swaps against interest expense[2]	–	–	53	–	53
	(101)	–	(115)	–	(216)
Profit/(loss) before tax	173	43	(205)	–	11
Tax attributable to policyholders' returns	(5)	–	–	–	(5)
Segmental result before the tax attributable to owners	168	43	(205)	–	6

2 The Group has entered into derivatives to protect its net exposure to interest rate fluctuations and this reallocation reflects the net economic interest exposure of the Group.

4.2 Reconciliation of operating profit/(loss) before adjusting items to the segmental result
2011

	Phoenix Life £m	Ignis Asset Management £m	Unallocated Group £m	Total £m
Operating profit/(loss) before adjusting items	**395**	**46**	**(54)**	**387**
Investment return variances and economic assumption changes on long-term business	**(338)**	**–**	**–**	**(338)**

Variance on owners' funds	**17**	**–**	**(8)**	**9**
Amortisation of acquired in-force business	**(121)**	**–**	**–**	**(121)**
Amortisation of customer relationships	**(13)**	**(5)**	**–**	**(18)**
Non-recurring items	**(15)**	**(2)**	**31**	**14**
Financing costs attributable to owners	**–**	**–**	**(110)**	**(110)**
Segment result before the tax attributable to owners	**(75)**	**39**	**(141)**	**(177)**

Non-recurring items include:

- restructuring costs of £37 million;
- regulatory change and systems transformation costs of £21 million;
- a gain of £37 million arising from closing the Group's pension schemes to future accrual and implementing a pension increase exchange programme; and
- a £35 million recovery of historic costs under the management services agreements with the life division.

2010

	Phoenix Life £m	Ignis Asset Management £m	Unallocated Group £m	Total £m
Operating profit/(loss) before adjusting items	388	46	(61)	373
Investment return variances and economic assumption changes on long-term business	18	–	–	18
Variance on owners' funds	16	–	3	19
Amortisation of acquired in-force business	(132)	–	–	(132)
Amortisation of customer relationships	(15)	(3)	–	(18)
Non-recurring items	(107)	–	(32)	(139)
Financing costs attributable to owners	–	–	(115)	(115)
Segment result before the tax attributable to owners	168	43	(205)	6

Non-recurring items include:

- premium listing and other restructuring costs, including site rationalisation and outsourcer transformation, of £80 million;
- regulatory change and systems transformation costs of £36 million; and
- an increase in the expense reserves of Phoenix Life of £23 million following the new fee arrangement between Phoenix Life and Ignis Asset Management. Ignis Asset Management will recognise the benefit of this new arrangement as it is earned and so this charge will reverse over time.

4.3 Segmental total assets and total liabilities

	Assets 2011 £m	**Liabilities 2011 £m**	Assets restated 2010 £m	Liabilities restated 2010 £m
Phoenix Life	**88,848**	**83,967**	83,187	78,158
Ignis Asset Management	**339**	**95**	356	128
Unallocated Group	**314**	**3,073**	59	3,016
	89,501	**87,135**	83,602	81,302

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 reflect the impact of the increase in credit spreads on corporate bonds and movements in equities, properties and yields.

5.2 Owners' funds

For non-long-term business including owners' funds, the total investment income, including fair value 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:

	2011 £m	2010 £m
Variances on owners' funds of:		
Subsidiary undertakings	**7**	7
The Company	**2**	12
	9	19

The variances on owners' funds of the Company comprise fair value gains arising from movements in the fair value of warrants in issue over the Company's shares.

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:

	2011 %	2010 %
Equities	**7.1**	7.6
Properties	**6.1**	6.6
Gilts (15 year gilt)	**4.0**	4.5
Other fixed interest (15 year gilt plus 0.6%)	**4.6**	5.1

6. Fees

	2011 £m	2010 £m
Fund management based fees	**75**	62
Investment contract income	**95**	100
	170	162

7. Net investment income

	2011 £m	2010 £m

Investment income		
Interest income on loans and receivables	**49**	57
Interest income on impaired financial assets	**7**	5
Interest income on financial assets designated at fair value through profit or loss on initial recognition	**2,554**	1,911
Dividend income	**679**	492
Rental income	**86**	78
Net expected return on pension assets	**(11)**	(18)
	3,364	2,525
Impairment losses on loans and receivables	**(3)**	(12)
Fair value gains/(losses)		
Financial assets at fair value through profit or loss		
Held for trading – derivatives	**960**	(17)
Designated upon initial recognition	**595**	3,324
Investment property	**4**	87
	1,556	3,382
Net investment income	**4,920**	5,907

8. Other operating income

	2011 £m	2010 £m
General business result	**2**	–
Income received from outsourcer	**–**	14
Income under Royal London transitional services agreement	**–**	5
Other income	**10**	6
	12	25

9. Acquisition costs

	2011 £m	2010 £m
Acquisition costs paid	**13**	12

10. Administrative expenses

	2011 £m	2010 £m
Employee costs	**128**	158
Outsourcer expenses	**160**	183
Investment management expenses and transaction costs	**99**	142
Professional fees	**73**	61
Office costs	**45**	53
Impairment of property, plant and equipment	**8**	–
Operating expenses in respect of investment properties	**6**	4
Depreciation of property, plant and equipment	**3**	3
Other	**84**	72
	606	676

Certain prior year disclosures in note 10 have been amended to conform to current year presentation.

Employee costs comprise:

	2011	2010

	£m	£m
Wages and salaries	**137**	134
Social security contributions	**12**	13
Other pension costs	**(21)**	11
	128	158

Included with other pension costs are the benefits associated with liability management exercises undertaken on the Group's defined benefit pension schemes as detailed in note 32.

	2011 Number	2010 Number
Average number of persons employed		
Phoenix Life	**804**	758
Ignis Asset Management	**551**	520
	1,355	1,278

11. Auditors' remuneration

The remuneration of the Company's auditors, including their associates, in respect of services supplied to members of the Group was £6.7 million (2010: £13.6 million). No services were provided by the Company's auditors to the Group's pension schemes.

	2011 £m	2010 £m
Audit of the consolidated financial statements	**0.5**	0.7
The auditing of accounts of subsidiaries of the Company pursuant to legislation	**2.9**	3.5
Other services supplied pursuant to such legislation:		
Audit related	**0.4**	0.7
Services as reporting accountants	**0.1**	6.6
Other services:		
Audit of MCEV supplementary information	**0.6**	0.8
Other	**2.2**	1.3
	6.7	13.6

The total remuneration of the Company's auditors for services as reporting accountants during the prior year mainly comprised services provided in respect of the Premium Listing.

12. Finance costs

	2011 £m	2010 £m
Interest expense		
On borrowings at amortised cost	**215**	196
On borrowings at fair value through profit or loss	**36**	73
	251	269
Attributable to:		
– policyholders	**122**	101
– owners	**129**	168
	251	269

13. Tax charge/(credit)

13.1 Current year tax charge/(credit)

	2011 £m	2010 £m

Current tax:		
UK Corporation tax	**68**	30
Overseas tax	**16**	7
	84	37
Adjustment in respect of prior years	**(57)**	16
	27	53
Deferred tax:		
Reversal/origination of temporary differences		
On non-profit surpluses	**(9)**	(32)
On amortisation of acquired in-force business	**(44)**	(50)
On amortisation of customer relationship intangible	**(5)**	(5)
Capital allowances in excess of depreciation	**6**	–
On accrued interest	**7**	(38)
Losses on group restructuring not matched in accounts	**–**	(33)
Tax losses arising in the current year carried forward	**–**	(17)
Pension scheme movements	**30**	19
On provisions for future expenditure	**2**	(6)
Other temporary differences	**3**	–
Utilisation of tax losses	**131**	57
Change in the rate of corporation tax	**(41)**	(19)
Write (up)/down of deferred tax assets	**(13)**	2
	67	(122)
Total tax charge/(credit)	**94**	(69)
Attributable to:		
– policyholders	**173**	5
– owners	**(79)**	(74)
	94	(69)

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 charge attributable to policyholder earnings was £173 million (2010: £5 million).

13.2 Tax credited to other comprehensive income

	2011 £m	2010 £m
Deferred tax on actuarial gains of defined benefit schemes	**(1)**	(4)

13.3 Reconciliation of tax charge/(credit)

	2011 £m	2010 £m
(Loss)/profit before tax	**(4)**	11
Policyholder tax charge	**(173)**	(5)
(Loss)/profit before the tax attributable to owners	**(177)**	6
Tax at standard UK[1] rate of 26.5% (2010: 28%)	**(47)**	2
Net tax losses on group restructuring not matched in accounts	**–**	(110)
Untaxed income and gains	**(7)**	(61)

Disallowable expenses	**3**	18
Adjustment to tax charge in respect of prior years	**(57)**	16
Movement in non-profit surplus taxed at less than 26.5% (2010: 28%)	**13**	20
Movement on acquired in-force amortisation at less than 26.5% (2010: 28%)	**3**	1
Profits taxed at rates other than 26.5% (2010: 28%)	**19**	(3)
Tax losses not previously valued	**(11)**	(8)
Prior year deferred tax	**20**	12
Deferred tax rate change	**(41)**	(19)
Current year losses not valued	**3**	41
Temporary differences not valued	**27**	11
Other	**(4)**	6
Owners' tax credit	**(79)**	(74)
Policyholder tax charge	**173**	5
Total tax charge/(credit) for the year	**94**	(69)

1 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 0% which is applicable to Phoenix Group Holdings.

14. Dividends on ordinary shares

	2011 £m	2010 £m
Dividends declared and paid in 2011	**72**	54

On 30 March 2011, the Board recommended a final dividend of £0.21 per share in respect of the year ended 31 December 2010. A scrip dividend option was available to shareholders and the total dividend that was settled on 17 May 2011, following shareholders' approval at the AGM, amounted to £36 million of which £7 million was settled via the scrip dividend option.

On 24 August 2011, the Board declared an interim dividend of £0.21 per share for the half year ended 30 June 2011. A scrip dividend option was available to shareholders and the total dividend that was settled on 7 October 2011 amounted to £36 million of which £10 million was settled via the scrip dividend option.

15. Earnings per share

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

	2011 £m	2010 £m
(Loss)/profit for the year	**(98)**	80
Share of result attributable to non-controlling interests	**(33)**	(50)
(Loss)/profit attributable to owners	**(131)**	30

The basic earnings per share of (76.2p) (2010: 20.1p) has been based on the loss of £131million (2010: profit £30 million) and a weighted average number of ordinary shares outstanding during the year of 172 million (2010: 149 million), calculated as follows:

	2011 Number million	2010 Number million
Issued ordinary shares at beginning of the year	**171**	130
Effect of ordinary shares issued/redeemed	**1**	19
Weighted average number of ordinary shares	**172**	149

The diluted earnings per share of (76.2p) (2010: 20.1p) has been based on the loss of £131 million (2010: profit £30 million) and a diluted weighted average number of ordinary shares outstanding during the year of 172 million (2010: 149 million) calculated as follows:

	2011 Number million	2010 Number million
Weighted average number of ordinary shares	**172**	149
Effect of warrants in issue	**–**	–
Weighted average number of ordinary shares (diluted)	**172**	149

The IPO warrants were not dilutive in either 2011 or 2010 due to the exercise price of the warrants being significantly higher than the share price of the Company. The Founders' and Sponsors' warrants were converted into ordinary shares during 2010.

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, due to their exercise price, they did not have a dilutive effect 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; and
- 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.

There are 3,600,000 remaining contingent rights over ordinary shares which will result in the issue of ordinary shares on a one-for-one basis if before 22 June 2013 (i) an offer is made to acquire all or a majority of the Company's issued ordinary share capital or substantially all of the Company's assets (in each case such transaction having become unconditional in all respects); or (ii) any party or parties acting in concert becomes interested in more than 50% of the ordinary shares of the Company through the issue of shares by the Company. As the conditions for this conversion were not met in the reporting period, these additional shares have not been included in the diluted earnings per share figures.

16. Share capital

	2011 £	2010 £
Authorised:		
410 million (2010: 410 million) ordinary shares of €0.0001 each	**31,750**	31,750
Issued and fully paid:		
174.5 million (2010: 171.5 million) ordinary shares of €0.001 each	**14,165**	13,904

The holders of ordinary shares 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. Movements in issued share capital during the year:

2011

	Number	**£**
Shares in issue at 1 January	**171,455,610**	**13,904**
Ordinary shares issued for scrip dividend (note 14)	**3,005,093**	**260**
Other ordinary shares issued in the year	**12,112**	**1**
Shares in issue at 31 December	**174,472,815**	**14,165**

During the year, the Company issued 12,112 shares at a premium of £68,190 in order to satisfy its obligation to employees under the Group's share schemes.

2010

	Number	£
Shares in issue at 1 January	130,200,732	10,450
'B' ordinary shares issued on conversion of warrants	2,085,123	177
'B' ordinary shares issued to the Chairman	177,000	16
Ordinary shares issued on conversion of contingent rights over shares	32,400,000	2,677
Ordinary shares issued for scrip dividend	1,567,416	138
Ordinary shares issued in connection with Alternative Coupon Satisfaction Mechanism	5,020,000	445
Other ordinary shares issued in the year	5,339	1

Shares in issue at 31 December	171,455,610	13,904

17. Shares held by the employee trust and group entities

	2011 £m	2010 £m
At 1 January	**13**	4
Purchased in year	**–**	10
Vested to employees in year	**(2)**	(4)
Shares issued to group entity on conversion of contingent rights over ordinary shares	**–**	3
At 31 December 2011	**11**	13

This reserve represents the value of the shares held by the Phoenix Group Holdings Employee Benefit Trust ('PGH EBT') to satisfy awards granted to employees under the Group's share-based payment schemes and shares issued to Pearl Assurance Limited following the restructuring of the contingent rights over ordinary shares of the Company which occurred during 2010. During the year nil (2010: 1,580,671) further shares were purchased on market and 306,250 (2010: 595,740) shares were awarded to employees (see note 18). The number of shares held by the PGH EBT at 31 December 2011 was 1,245,509 (2010: 1,484,931).

18. Share-based payment

18.1 Share-based payment expense

The expense recognised for employee services receivable during the year is as follows:

	2011 £m	2010 £m
Expense arising from equity-settled share-based payment transactions	**6**	8
Expense arising from cash-settled share-based payment transactions	**1**	1
Total expense arising from share-based payment transactions	**7**	9

The carrying amount of the liability relating to the cash-settled options at 31 December 2011 is £2 million (2010: £1 million) and is included within other payables.

18.2 Share-based payment schemes in issue

Long-term incentive plan ('LTIP')

In 2009, the Group implemented a long-term incentive plan to retain and motivate its senior management group. The awards under this plan are in the form of nil-cost options to acquire an allocated number of ordinary shares. Assuming no good leavers or other events which would trigger early vesting rights, these awards will be subject to performance conditions tied to the Company's financial performance in respect of growth in embedded value and cumulative cash generation over a three year period. There are no cash settlement alternatives. The 2009 LTIP awards vested in 2010. Further awards were made in 2010 which will vest on 28 May 2013 and in 2011 which will vest on 12 April 2014.

The fair value of these awards is estimated at the share price at the grant date, taking into account the terms and conditions upon which the instruments were granted.

Save As You Earn ('SAYE')

The SAYE scheme allows participating employees to save up to £250 each month over a period of either 3 or 5 years.

Under the SAYE arrangement, participants remaining in the Group's employment at the end of the 3 or 5 year saving period are entitled to use their savings to purchase shares at an exercise price at a discount to the share price on the date of grant. Employees leaving the Group for certain reasons are able to use their savings to purchase shares if they leave less than six months before the end of their 3 or 5 year periods.

The fair value of the awards has been determined using a Black-Scholes valuation model. Key assumptions within this valuation model included expected share price volatility and expected dividend yield.

The following information was relevant in the determination of the fair value of the 2010 SAYE and 2011 SAYE awards in the year:

	2011 SAYE	2010 SAYE
Share price (p)	**669.5**	650.0
Exercise price (£)	**5.72**	5.63

Expected life (years)	**3.25 and 5.25**	3.25 and 5.25
Risk-free rate (%)	**1.8 (for 3.25 year scheme) and 2.6 (for 5.25 year scheme) based on UK Government Gilts with a term commensurate with the expected term for each award**	2.0 (for 3.25 year scheme) and 2.8 (for 5.25 year scheme) based on UK Government Gilts with a term commensurate with the expected term for each award.
Expected volatility (%)	**30.0 which is based on the Company's share price volatility to date**	30.0 which is based on the Company's share price volatility to date.
Dividend yield (%)	**6.3**	0

Bonus share plan ('BSP')

In 2009, certain employees were granted nil-cost options to acquire an allocated number of ordinary shares. There were no performance criteria associated with these awards and no cash settlement alternatives. The contractual life of the awards is two years. The fair value of these awards is estimated at the share price at the grant date, taking into account the terms and conditions upon which the options were granted. The majority of awards vested in 2011.

Deferred cash plan

With effect from 2 September 2009, a number of executives were given deferred cash awards the value of which will be equal to a fixed number of Phoenix Group Holdings shares on 2 September 2012 and will be payable on this date provided the executive remains in employment by the Group.

The fair value of the awards has been determined assuming that all granted shares vest. As the award is a cash settled scheme, the fair value of the expense is updated at every period end to reflect movements in Phoenix Group Holdings' share price.

Deferred bonus share plan ('Deferred BSP')

With effect from 31 December 2010, part of the annual incentive for certain executives, for any year, is deferred into Phoenix Group Holdings' shares. This grant of shares is conditional on the employee remaining in employment with the Group for a period of three years. The 2010 Deferred BSP shares are expected to vest on 6 April 2014.

The fair value of these awards is estimated at the share price at the grant date, taking into account the terms and conditions upon which the options were granted.

18.3 Movements in the year

The following tables illustrate the number of, and movements in, share options during the year:

	No of share options 2011				
	LTIP Schemes	**SAYE Schemes**	**2009 BSP**	**Deferred cash plan**	**2010 Deferred BSP**
Outstanding at the beginning of the year	**1,424,549**	**1,037,214**	**326,250**	**229,370**	**–**
Granted during the year	**1,405,116**	**310,366**	**–**	**–**	**88,729**
Forfeited during the year	**(271,185)**	**(206,851)**	**–**	**–**	**–**
Exercised during the year	**–**	**(12,112)**	**(306,250)**	**–**	**–**
Outstanding at the end of the year	**2,558,480**	**1,128,617**	**20,000**	**229,370**	**88,729**

	No of share options 2010				
	LTIP Schemes	SAYE Schemes	2009 BSP	Deferred cash plan	2010 Deferred BSP
Outstanding at the beginning of the year	403,750	–	403,750	–	–
Granted during the year	1,601,087	1,163,948	40,000	229,370	–
Forfeited during the year	(106,241)	(121,395)	–	–	–
Exercised during the year	(474,047)	(5,339)	(117,500)	–	–
Outstanding at the end of the year	1,424,549	1,037,214	326,250	229,370	–

The weighted average fair value of options granted during the year was £5.65 (2010: £4.95).

The weighted average share price at the date of exercise for the rewards exercised is £5.84 (2010: £6.77).

The weighted average remaining contractual life for the rewards outstanding as at 31 December 2011 is 2.0 years (2010: 2.5 years).

19. Non-controlling interests

2011

	Perpetual Reset Capital Securities £m	**UK Commercial Property Trust Limited £m**	**Total £m**
At 1 January	**411**	**309**	**720**
Profit for the year	**15**	**18**	**33**
Dividends paid	**–**	**(21)**	**(21)**
Coupon paid, net of tax relief	**(19)**	**–**	**(19)**
Shares in subsidiaries subscribed for by non-controlling interests	**–**	**1**	**1**
At 31 December	**407**	**307**	**714**

2010

	Perpetual Reset Capital Securities £m	UK Commercial Property Trust Limited £m	Total £m
At 1 January	527	201	728
Profit for the year	20	30	50
Dividends paid	–	(18)	(18)
Restructure of non-controlling interest	(70)	–	(70)
Coupon paid, net of tax relief	(47)	–	(47)
Partial buyback of non-controlling interest	(19)	–	(19)
Shares in subsidiaries subscribed for by non-controlling interests	–	96	96
At 31 December	411	309	720

19.1 Perpetual Reset Capital Securities

On 1 January 2010, Pearl Group Holdings (No. 1) Limited ('PGH1') had 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. Following amendments made to the Notes in 2010, the principal amount outstanding is now £425 million.

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 coupon payments may be deferred at the option of PGH1; accordingly the Notes meet the definition of equity for financial reporting purposes. Under the rules of the FSA, the Notes also meet the conditions to be included in Tier 1 capital in the calculation of the Group's Capital Resources. As the Notes are not 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.

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 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. These restrictions would also apply to the Company until the deferred coupon payment is satisfied.

On 25 April 2011, the 2011 coupon was settled in full.

19.2 UK Commercial Property Trust Limited

UK Commercial Property Trust Limited ('UKCPT') is a property investment subsidiary which is domiciled in Guernsey and is admitted to the Official List of the UK Listing Authority and to trading on the LSE.

20. Liabilities under insurance contracts

	Gross liabilities 2011 £m	**Reinsurers' share 2011 £m**	Gross liabilities 2010 £m	Reinsurers' share 2010 £m
Life assurance business:				
Insurance contracts	**40,517**	**3,153**	38,770	2,939
Investment contracts with DPF	**11,283**	**–**	11,709	–
	51,800	**3,153**	50,479	2,939
Amounts due for settlement after 12 months	**46,759**	**2,792**	42,376	2,719

	Gross liabilities 2011 £m	**Reinsurers' share 2011 £m**	Gross liabilities 2010 £m	Reinsurers' share 2010 £m
At 1 January	**50,479**	**2,939**	50,291	2,860
Premiums	**1,473**	**85**	1,534	85
Claims	**(4,968)**	**(224)**	(5,260)	(210)
Other changes in liabilities	**4,833**	**361**	3,978	214
Foreign exchange adjustments	**(17)**	**(8)**	(37)	(10)
Transfer to statement of consolidated comprehensive income in respect of actuarial losses of defined benefit pension scheme	**–**	**–**	(27)	–
At 31 December	**51,800**	**3,153**	50,479	2,939

21. Unallocated surplus

	2011 £m	2010 £m
At 1 January	**864**	721
Transfer (to)/from income statement	**(16)**	143
At 31 December	**848**	864

22. Borrowings

	Carrying value		**Fair value**	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Limited recourse bonds 2012 7.39% (note a)	**11**	29	**11**	29
Limited recourse bonds 2022 7.59% (note a)	**90**	94	**102**	97
£779 million loan (note b)	**–**	757	**–**	766
£15 million loan (note b)	–	14	–	15
£4 million loan (note b)	–	4	–	4
Property Reversions loan (note c)	**217**	234	**217**	234
£80 million facility agreement (note d)	**80**	42	**80**	42
£150 million term facility (note e)	**60**	–	**60**	–

Total policyholder borrowings	**458**	1,174	**470**	1,187
£200 million 7.25% unsecured subordinated loan (note f)	**135**	127	**154**	170
Unsecured loan notes (note g)	**7**	12	**7**	12
£2,260 million syndicated loan (note h)	**1,993**	2,138	**1,993**	2,138
£100 million PIK notes and facility (note i)	**111**	106	**111**	106
£75 million secured loan note (note j)	**73**	72	**73**	72
£425 million loan facility (note j)	**375**	399	**375**	399
Total shareholder borrowings	**2,694**	2,854	**2,713**	2,897
Total borrowings	**3,152**	4,028	**3,183**	4,084
Amount due for settlement after 12 months	**2,983**	3,838		

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 £11 million (2010: £27 million) mature in 2012. A principal repayment of £16 million was made in September 2011 as per the terms of the agreement. The £120 million 7.59% limited recourse bonds with an outstanding principal of £120 million (2010: £120 million) have an average remaining life of 7 years maturing in 2022. NPLL has provided collateral of £65 million (2010: £77 million) to provide security to the holders of the NPLL recourse bonds in issue.

b. On 21 March 2011, the £779 million loan, £15 million loan and £4 million loan were all settled for consideration of £782 million as part of the restructure of a £1.2 billion portfolio of corporate loans.

c. The Property Reversions loan from Abbey National Property Investments was brought into the consolidated financial statements at fair value. It relates to the sale of Extra-Income Plan policies that Abbey National Property Investments finances to the value of the associated property reversions. As part of the arrangement Abbey National Property Investments receive an amount calculated by reference to the movement in the Halifax House Price Index and NPLL and NPI Limited have undertaken to indemnify Abbey National Property Investments 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. During the year, a repayment of £27 million was made. Note 35 contains details of the assets that support this loan.

d. In 2008, UKCPT entered into an £80 million revolving loan facility agreement. This loan accrues interest at LIBOR plus a variable margin of 0.50% to 0.60% 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. This facility was fully utilised during 2011 in order to increase UKCPT's property portfolio.

e. On 19 May 2011, UKCPT entered into a £150 million investment term loan facility agreement. The £150 million investment term loan facility agreement accrues interest at LIBOR plus a variable margin of 1.60% to 2.00% per annum. The lender holds security over the assets of UK Commercial Property Estates Holdings Limited and UK Commercial Property Estates Limited, both of which are subsidiaries of UKCPT. The repayment date for this facility is 19 May 2018. As at 31 December 2011 the amount drawn down was £60 million.

f. Scottish Mutual Assurance Limited 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'). 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 assumed these subordinated loan notes as a result of the acquisition of the Pearl businesses at their fair value and as such, the outstanding principal of these subordinated loan notes differs from the carrying value in the statement of financial position. The fair value adjustments which were recognised on acquisition will unwind over the remaining life of these subordinated loan notes.

g. 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 which are due to mature at the end of 2012. During the year £5 million (2010: £6 million) of these loan notes have been repaid and £7 million (2010: £12 million) were outstanding.

h. 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. The terms of this facility are:

- 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.

During 2011, a repayment of £145 million (2010: £122 million) was made.

i. On 14 May 2008, PGH (MC1) Limited issued PIK notes to the value of £154.5 million to Royal London and PGH (MC2) Limited obtained a £154.5 million PIK facility from Royal London. The PIK notes and facility were subsequently amended on 2 September 2009, leaving a total of £100 million outstanding. At 31 December 2009, interest of £2 million had been capitalised, leaving an outstanding balance of £102 million. 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%. During 2011, interest of £5 million (2010: £4 million) was capitalised on the PIK notes and facility. The final maturity date on the PIK notes and facility is 30 June 2019.

j. 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 (the 'Pearl Facility'). This loan was subsequently amended on 2 September 2009, leaving £425 million outstanding on this facility and £75 million of secured C loan notes.

The £425 million 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 £75 million secured C loan notes are repayable 15 years after amendment and attract interest at LIBOR plus a margin of 1.00%.

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).

During the year a scheduled repayment of £24 million was made on the £425 million loan facility and interest of £1 million (£2010: £2 million) was capitalised on the £75 million secured C loan notes.

23. Deposits received from reinsurers

	2011 £m	2010 £m
Carrying value and fair value:		
At 31 December	**472**	419
Amount due for settlement after 12 months	**439**	384

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:

	Assets 2011 £m	**Liabilities 2011 £m**	Assets 2010 £m	Liabilities 2010 £m
Warrants over shares in Phoenix Group Holdings	**–**	**3**	–	5
Forward currency	**771**	**794**	641	692
Credit default options	**33**	**–**	3	11
Interest rate swaps	**4,600**	**3,473**	2,064	1,709
Swaptions	**396**	**–**	241	–
Inflation swaps	**33**	**2**	26	2
Equity options	**216**	**–**	186	–
Stock index futures	**46**	**16**	36	12
Fixed income futures	**4**	**4**	–	–
	6,099	**4,292**	3,197	2,431

The amount recoverable after one year is £4,320 million (2010: £2,247 million). The amount payable after one year is £3,368 million (2010: £1,517 million).

Warrants over shares

On 1 January 2010, the Company had in issue 7.5 million Founders' warrants, 8.2 million IPO warrants, 12.4 million warrants held by Royal London and 5 million held by the Lenders. The table below shows a reconciliation of the outstanding number of these warrants:

2011

	IPO warrants Number	**Founders' warrants Number**	**Lenders' warrants Number**	**Royal London warrants Number**
At 1 January and 31 December	**8,169,868**	**–**	**5,000,000**	**12,360,000**

2010

	IPO warrants Number	Founders' warrants Number	Lenders' warrants Number	Royal London warrants Number
At 1 January	8,169,868	7,468,200	5,000,000	12,360,000
Conversion of Founders' warrants into new ordinary shares (January 2010)	–	(7,468,200)	–	–
At 31 December	8,169,868	–	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. At 31 December 2011, the terms of the IPO warrants entitle the holder to purchase 1.0272 (2010: 1.009507) ordinary shares per IPO warrant, for an exercise price of €10.71 (2010: €10.90).

During January 2010, the remaining Founders' warrants in issue were converted into ordinary shares. On 5 July 2010, the IPO warrants were admitted to trading on the LSE. The IPO warrants were subsequently delisted from Euronext on 17 November 2010.

The exercise period for the IPO warrants commenced on the later of:

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

The IPO warrants will expire at the close of trading on the LSE on 3 September 2014 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 and was subsequently amended to €16.34 on 15 October 2010.

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 to do so on a cashless basis.

The IPO warrants are listed and were previously valued using the warrant price quoted on the LSE for the Company. Due to the relatively low number of IPO warrants in issue, they are thinly traded and the quoted price is not considered to be the best indicator of their fair value. As a result the IPO warrants have been valued using an extended Black-Scholes valuation model. The key assumptions used to ascertain a value as at 31 December 2011 are as follows:

- share price as at 31 December 2011 of £5.25;
- volatility of 30%;
- the warrants are not adjusted for dividends; and
- the valuation incorporates the impact of amending some of the terms of the warrants on 15 October 2010.

At 31 December 2011 the IPO warrants were valued at £1 million (2010: £2 million).

Lenders' warrants

On 2 September 2009, the Company issued 5 million warrants over its shares to the Lenders. These warrants entitled the holder to purchase one 'B' ordinary share at a price of £15 per share, subject to adjustment. Following the achievement of the Company's Premium Listing on 5 July 2010, the Lenders' warrants relate to ordinary shares rather than 'B' ordinary shares. On 15 October 2010, following an issue of ordinary shares by the Company under a scrip dividend, the terms of the warrants were amended to entitle the holder to purchase 1.009507 ordinary shares per warrant.

The exercise period 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.

All outstanding Lenders' 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. On 15 October 2010, this threshold of £19.50 was amended to £19.32. 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 an extended Black-Scholes valuation model to capture the embedded barrier feature. The key assumptions used to ascertain a value are the same as for the IPO warrants (see above). The value of the warrants at the year end was £250,000 (2010: £280,000).

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 entitled the holder to purchase one 'B' ordinary share at a price of €11 per share, subject to adjustment. Following the achievement of the Company's Premium Listing, the Royal London warrants relate to ordinary shares rather than 'B' ordinary shares. On 15 October 2010, following an issue of ordinary shares by the Company under a scrip dividend, the terms of the warrants were amended to entitle the holder to purchase 1.009507 ordinary shares per warrant.

The exercise period 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.

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. On 15 October 2010, this threshold of €16.50 was amended to €16.34. 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 an extended Black-Scholes valuation model.

The key assumptions used to ascertain a value as at 31 December 2011 are as for the IPO warrants (see above). The value of the warrants at the year end was £2 million (2010: £3 million).

25. Obligations for repayment of collateral received

	2011 £m	2010 £m
Carrying value and fair value:		
At 31 December	**13,005**	10,160
Amount due for settlement after 12 months	**1,552**	628

26. Financial liabilities

	Carrying value		Fair value	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Financial liabilities at fair value through profit or loss:				
Designated upon initial recognition	**11,404**	11,020	**11,404**	11,020
Held for trading – derivatives	**4,292**	2,431	**4,292**	2,431
Financial liabilities measured at amortised cost	**16,412**	14,373	**16,442**	14,376
	32,108	27,824	**32,138**	27,827
Amount due for settlement after 12 months	**8,343**	6,366		

27. Provisions

2011

	Leasehold properties £m	**Staff related £m**	**Known incidents £m**	**Other £m**	**Total £m**
At 1 January	**37**	**21**	**1**	**14**	**73**
Additions in the year	**11**	**7**	**4**	**2**	**24**
Utilised during the year	**(4)**	**(4)**	**–**	**(4)**	**(12)**
Released during the year	**(16)**	**(3)**	**–**	**(7)**	**(26)**
At 31 December	**28**	**21**	**5**	**5**	**59**

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 5.46% and it is expected that the provision will be utilised over the next 10 years.

Staff related provisions primarily relate to costs associated with restructuring across the Group. These include provisions for unfunded pensions of £5 million (2010: £5 million) and private medical insurance costs for former employees of £3 million (2010: £4 million). These provisions have been calculated on a realistic basis.

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 are litigation and onerous contract provisions.

28. Tax assets and liabilities

	2011 £m	2010 Restated £m
Current tax receivables	**8**	5
Net deferred tax assets	**–**	–
Total tax assets	**8**	5

	2011 £m	2010 Restated £m
Current tax payables	**105**	99
Net deferred tax liabilities	**673**	607
Total tax liabilities	**778**	706

Deferred tax assets comprise

	2011 £m	2010 Restated £m
Trading losses	**37**	82
Expenses and deferred acquisition costs carried forward	**14**	86
Provisions and other temporary differences	**11**	20
Pension scheme deficit	**–**	21
Accelerated capital allowances	**18**	25
Unpaid interest	**34**	44
Gross deferred tax assets	**114**	278
Less: offset against deferred tax liabilities	**(114)**	(278)
Net deferred tax assets	**–**	–

Deferred tax liabilities comprise

	2011 £m	2010 Restated £m
Acquired in-force business	**593**	670
Customer relationships	**100**	114
Surplus within the non-profit funds	**62**	64
Provisions and other temporary differences	**8**	17
Adjustment for insurance policies held with related parties in respect of the PGL Pension Scheme	**24**	20
Gross deferred tax liabilities	**787**	885
Less: offset against deferred tax assets	**(114)**	(278)
Net deferred tax liabilities	**673**	607

Movements in net deferred tax liabilities comprise

	2011 £m	2010 Restated £m
At 1 January	**(607)**	(695)
Write off to goodwill	**–**	(38)
Amounts (charged)/credited to the income statement	**(67)**	122
Amounts credited to the statement of other comprehensive income	**1**	4
At 31 December	**(673)**	(607)

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.

A gradual reduction in the UK corporation tax rate from 28% to 24% over four years was announced in the Emergency Budget of 22 June 2010 with further 1% reductions being announced in each of the Budgets of 23 March 2011 and 21 March 2012. The Finance (No. 2) Act 2010 included the first of the 1% rate reductions with effect from April 2011, a further 1% reduction was substantively enacted on 29 March 2011 under the Provisional Collection of Taxes Act 1968 and a further 1% reduction (effective from April 2012) was included in Finance Act 2011. Consequently a rate of 25% has been used for the purposes of providing deferred tax in these financial statements. Further reductions are to be introduced by future legislation. The benefit to the Group's net assets arising from the further 3% reduction of rate is estimated as £64 million in total and will be recognised as the legislation is substantively enacted.

On 23 March 2011, HMRC issued a technical note on "Solvency II and the Taxation of Insurance Companies", outlining changes to the taxation of UK insurance companies with effect from 2013. The Group has been actively involved in consulting with HMRC and HM Treasury on the detail of the new rules, including providing comments on proposed draft legislation, with the aim of ensuring that the Group's policyholders and shareholders are, as far as possible, not adversely affected by the changes.

The Group is still assessing the likely impact of the new rules (subject to the final legislation which will be introduced following the March 2012 Budget). The Group's view, at this stage, is that transition to the new rules is likely to result in the acceleration of some taxable profits (which will be recognised over a 10-year period under transitional provisions in the new rules), but this is not expected to have a material impact on its overall tax position.

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

	2011 £m	2010 £m
Deferred tax assets have not been recognised in respect of:		
Tax losses carried forward	**102**	103
Excess expenses and deferred acquisition costs carried forward	**22**	22
Provisions and other temporary differences	**14**	7
Deferred tax assets not recognised on capital losses[1]	**262**	165

[1] These can only be recognised against future capital gains and have no expiry date.

29. Payables related to direct insurance contracts

	2011 £m	2010 £m
Payables related to direct insurance contracts	**707**	713
Amount due for settlement after 12 months	**39**	40

Payables relating to direct insurance contracts include claims outstanding on general insurance and life assurance. The general insurance element amounts to £240 million (2010: £263 million).

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 Limited

Within Pearl Assurance Limited 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.

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

	2011 £m	2010 £m

Accruals	**175**	214
Amount due for settlement after 12 months	**6**	9

31. Other payables

	2011 £m	2010 £m
Investment broker balances	**487**	187
Other payables	**140**	140
	627	327
Amount due for settlement after 12 months	**–**	–

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.

	2011 £m	2010 £m
Pearl Group Staff Pension Scheme		
Economic surplus/(deficit) (including £56 million (2010: nil) available as a refund on a winding-up of the scheme	**56**	(77)
Provision for tax on that part of the economic surplus available as a refund on a winding-up of the scheme	**(19)**	–
Reported surplus/(deficit)	**37**	(77)
PGL Pension Scheme		
Economic surplus (including £471 million (2010: £92 million) available as a refund on a winding-up of the scheme)	**520**	165
Adjustment for insurance policies held with related parties and eliminated on consolidation	**(94)**	(74)
Net economic surplus	**426**	91
Provision for tax on that part of the economic surplus available as a refund on a winding-up of the scheme	**(149)**	(32)
Reported surplus	**277**	59
Total reported pension scheme surplus/(deficit)	**314**	(18)

The total net actuarial gains recognised in the statement of consolidated comprehensive income is set out below.

	2011 £m	2010 £m
Pearl Group Staff Pension Scheme	**81**	38
PGL Pension Scheme	**170**	7
Total actuarial gains	**251**	45

Information on each of these schemes is set out below.

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

Contributions in the year amounted to £1 million (2010: £2 million).

Defined benefit scheme

The defined benefit scheme is funded by payment of contributions to a separately administered trust fund. A Group company, Pearl Group Holdings (No. 2) Limited ('PGH2') is the principal employer of the Pearl Scheme. 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 2011, 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.

In June 2011, following formal consultation, the trustees of the Pearl Scheme signed a deed of amendment to the defined benefit scheme, which closed the scheme to future accrual by active members with effect from 1 July 2011. Thus, the active members become deferred members of the scheme and their future service will not qualify for benefits under the scheme. As a result of this, the Group has recognised a curtailment gain, relating to a release from future liabilities, of £3 million, which has been recognised in the consolidated income statement during the year.

In November 2011, following formal consultation, the Group carried out a pension increase exchange ('PIE') exercise where existing in-scope pensioners were offered the option to exchange future non-statutory pension increases for benefits accrued before 6 April 1997 for a higher, non increasing pension, thereby reducing longevity and inflation risk for the Group. The offer period for this exercise ended on 3 January 2012. The financial effect of all acceptances received up to 31 December 2011 has been recognised in the consolidated financial statements and the reduction in scheme liabilities of £16 million is shown as a negative past service cost.

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

	2011 %	2010 %
Rate of general long-term increase in salaries	**n/a**	4.45
Rate of increase for pensions in payment (5% per annum or RPI if lower)	**3.10**	3.45
Rate of increase for deferred pensions (CPI)	**2.10**	2.95
Discount rate	**4.90**	5.40
Inflation – RPI	**3.10**	3.45
Inflation – CPI	**2.10**	2.95
Expected rate of return on scheme assets	**3.70**	4.80

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 each of 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 a scheme-specific table which was derived from the actual mortality experience in recent years, performed as part of the actuarial valuation as at 30 June 2009, based on the standard tables PMA92 for males and PFA92 for females and based on year of use. This includes medium cohort projections for future mortality improvements, subject to a minimum annual improvement of 1.25% at each age. Under these assumptions, the average life expectancy from retirement for a member currently aged 40 retiring at age 60 is 29.6 years and 31.7 years for male and female members respectively.

A triennial funding valuation of the Pearl Scheme as at 30 June 2009 was completed in June 2010. This showed a deficit on the funding basis as at 30 June 2009 of £755 million.

The principal employer and the Trustees of the Pearl Scheme have entered into an agreement, the principal terms of which provide for the following:

- Cash payments into the scheme 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 payments due between 2020 and 2027 are calculated from projected scheme deficits, on a funding basis, as follows: £2 million payable on or before 30 June 2020, £39 million payable on or before 30 June 2021; £35 million payable on or before each of 30 June 2022, 30 June 2023 and 30 June 2024, and £41 million payable on each of 30 June 2025, 30 June 2026 and 30 June 2027. The amounts payable on and from 30 June 2021 may alter in light of any funding shortfall disclosed as at the triennial funding valuation immediately preceding their date of payment.
- The Trustees being granted a first charge over shares in Pearl Assurance Limited, National Provident Life Limited, 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 main 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 National Provident Life Limited 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 amounts recognised in the income statement are as follows:

	2011 £m	2010 £m
Current service cost	**(1)**	(1)
Interest cost	**(95)**	(100)
Expected return on scheme assets	**81**	82
Past service cost	**16**	–
Curtailment gain	**3**	–
	4	(19)

The net actuarial gains recognised in other comprehensive income comprise the following:

	2011 £m	2010 £m
Actual return less expected return on scheme assets	**110**	19
Experience (losses)/gains arising on scheme liabilities	**(22)**	70
Gain/(loss) due to changes in assumptions underlying scheme liabilities	**12**	(51)
	100	38
Change in provision for tax on the economic surplus available as a refund	**(19)**	–
	81	38

The cumulative net actuarial gains recognised in other comprehensive income amount to £148 million (2010: £67 million).

The surplus/(deficit) recognised in the statement of financial position is as follows:

	2011 £m	2010 £m
Fair value of scheme assets	**1,846**	1,725
Present value of defined benefit obligation	**(1,809)**	(1,802)
	37	(77)

The actual return on the scheme assets comprises the following:

	2011 £m	2010 £m
Expected return on scheme assets	**81**	82
Actual return less expected return on scheme assets	**110**	19
	191	101

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

	2011 £m	2010 £m
At 1 January	**1,802**	1,805
Current service cost	**1**	1
Interest cost	**95**	100
Past service cost	**(16)**	–
Curtailment gain	**(3)**	–
Actuarial losses/(gains)	**9**	(19)

Benefits paid	**(79)**	(85)
At 31 December	**1,809**	1,802

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:

	2011 £m	2010 £m
At 1 January	**1,725**	1,684
Expected return on scheme assets	**81**	82
Actual return less expected return on scheme assets	**110**	19
Provision for tax on the economic surplus available as a refund	**(19)**	–
Contributions by the employer	**28**	25
Benefits paid	**(79)**	(85)
At 31 December	**1,846**	1,725

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

	2011 £m	2010 £m
Equities	**165**	203
Bonds	**1,385**	1,228
Properties	**166**	119
Cash and other	**149**	175
Provision for tax on the economic surplus available as a refund	**(19)**	–
	1,846	1,725

Contributions totalling £27 million are expected to be paid into the scheme in 2012 in accordance with the agreement with the Trustee of the Pearl Scheme.

Table of historical information:

	2011 £m	2010 £m	2009 £m
Fair value of scheme assets	**1,846**	1,725	1,684
Defined benefit obligation	**(1,809)**	(1,802)	(1,805)
Surplus/(deficit)	**37**	(77)	(121)
Experience gains on scheme assets	**110**	19	36
Experience (losses)/gains on scheme liabilities	**(22)**	70	58

32.2 PGL Pension Scheme
The PGL Pension Scheme comprises a final salary section and a defined contribution section.

Defined contribution scheme
Contributions in the year amounted to £2 million (2010: £4 million).

Defined benefit scheme
The defined benefit section of the PGL Pension Scheme is a final salary arrangement which is closed to new entrants.

The valuation has been based on an assessment of the liabilities of the PGL Pension Scheme as at 31 December 2011, undertaken by independent qualified actuaries.

In June 2011, as outlined for the Pearl Scheme, the PGL Pension Scheme signed a deed of amendment to the defined benefit scheme, which closed the scheme to future accrual by active members with effect from 1 July 2011. A curtailment gain of £7 million, has been recognised in the consolidated income statement during the year.

In November 2011, following formal consultation, the Group carried out a PIE exercise, the same as outlined for the Pearl Scheme, although its offer period ended on 30 December 2011. The financial effects of the exercise were treated in the same way as for the Pearl Scheme. The financial effects of all acceptances received up to 31 December 2011 have been reflected as a negative past service cost of £11 million in the current year. The effect has been to reduce the Scheme liabilities by £11 million.

The present values of the defined benefit obligation and the related current service costs have been measured using the projected unit credit method.

A triennial funding valuation of the PGL Pension Scheme as at 30 June 2009 was completed in September 2010. This showed a deficit on the funding basis as at 30 June 2009 of £255 million. Following discussions with the Trustee of the PGL Pension Scheme it was agreed that new cash contributions to the scheme amounting to £160 million would be paid over the period from September 2010 to August 2017. Together with the outstanding contributions of £28 million, due to the scheme as at the end of August 2010 following the previous triennial valuation, the total future contributions amount to £188 million.

In accordance with an agreement dated November 2005, certain of the Group's with-profit funds have indemnified the Group's owners in respect of contribution calls equal to their share of the costs of changes in longevity assumptions. Completion of the triennial valuation in 2010 resulted in a recovery from the with-profit funds of £37 million, together with interest, in respect of the balance due in relation to the cost of changes in longevity assumptions determined by the previous triennial valuation. Accordingly a contribution in respect of actuarial losses was made by the with-profit funds of this amount, less tax, resulting in £27 million being recognised in the consolidated statement of comprehensive income in 2010.

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

	2011 %	2010 %
Rate of general long-term increase in salaries	**n/a**	4.45
Rate of increase for pensions in payment	**3.00**	3.30
Rate of increase for deferred pensions ('CPI')	**2.10**	2.95
Discount rate	**4.90**	5.40
Inflation – RPI	**3.10**	3.45
Inflation – CPI	**2.10**	2.95
Expected rate of return on scheme assets	**3.90**	5.10

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 each of 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 60 is 31.2 years and 32.3 years for male and female members respectively.

The economic value of the PGL Pension Scheme assets as at 31 December 2011 amounted to £1,589 million (2010: £1,326 million) and the economic value of the surplus amounted to £355 million (2010: £133 million). For financial reporting purposes the carrying value of the insurance policies effected by the PGL Pension Scheme with the Group have been eliminated on consolidation, resulting in reported assets of the PGL Pension Scheme as at 31 December 2011 of £1,511 million (2010: £1,252 million) and a reported surplus of £277 million (2010: £59 million).

The amounts recognised in the income statement are as follows:

	2011 £m	2010 £m
Current service cost	**(3)**	(4)
Interest cost	**(63)**	(63)
Expected return on scheme assets	**66**	63
Past service cost	**11**	–
Gain on curtailment	**7**	–
	18	(4)

The net actuarial gains recognised in other comprehensive income comprise the following:

	2011 £m	2010 £m
Actual return less expected return on scheme assets	**327**	81
Experience loss arising on scheme liabilities	**(15)**	(23)
Loss due to changes in assumptions underlying scheme liabilities	**(25)**	(19)
	287	39
Change in provision for tax on the economic surplus available as a refund	**(117)**	(32)
	170	7

The cumulative net actuarial gains recognised in other comprehensive income amounted to £253 million (2010: £83 million).

The surplus recognised in the statement of financial position is as follows:

	2011 £m	2010 £m
Fair value of scheme assets	**1,511**	1,252
Present value of defined benefit obligation	**(1,234)**	(1,193)
	277	59

The actual return on the scheme assets comprises the following:

	2011 £m	2010 £m
Expected return on scheme assets	**66**	63
Actual return less expected return on scheme assets	**327**	81
	393	144

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

	2011 £m	2010 £m
At 1 January	**1,193**	1,130
Current service cost	**3**	4
Interest cost	**63**	63
Past service cost	**(11)**	–
Curtailment gain	**(7)**	–
Actuarial losses	**40**	42
Benefits paid	**(47)**	(46)
At 31 December	**1,234**	1,193

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:

	2011 £m	2010 £m
At 1 January	**1,252**	1,126
Expected return on scheme assets	**66**	63
Actual return less expected return on scheme assets	**327**	81
Provision for tax on the economic surplus available as a refund	**(117)**	(32)
Contributions by the employer	**30**	60
Benefits paid	**(47)**	(46)
At 31 December	**1,511**	1,252

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

	2011 £m	2010 £m
Bonds	**1,443**	1,128
Properties	**117**	123

Cash and other	**100**	33
Provision for tax on the economic surplus available as a refund	**(149)**	(32)
	1,511	1,252

Contributions totalling £23 million are expected to be paid into the scheme in 2012.

Table of historical information:

	2011 £m	2010 £m	2009 £m
Fair value of scheme assets	**1,511**	1,252	1,126
Defined benefit obligation	**(1,234)**	(1,193)	(1,130)
Surplus/(deficit)	**277**	59	(4)
Experience gains on scheme assets	**327**	81	23
Experience (losses)/gains on scheme liabilities	**(15)**	(23)	18

33. Intangible assets

2011

	Goodwill £m	**Acquired in-force business £m**	**Customer relationships £m**	**Present value of future profits £m**	**Total £m**
Cost or valuation					
At 1 January	**115**	**2,213**	**445**	**42**	**2,815**
Revaluation	**–**	**–**	**–**	**(19)**	**(19)**
At 31 December	**115**	**2,213**	**445**	**23**	**2,796**
Amortisation					
At 1 January	**–**	**197**	**25**	**–**	**222**
Charge for the year	**–**	**134**	**18**	**–**	**152**
At 31 December	**–**	**331**	**43**	**–**	**374**
Carrying amount					
At 31 December	**115**	**1,882**	**402**	**23**	**2,422**
Amount recoverable after 12 months	**115**	**1,755**	**384**	**23**	**2,277**

2010 (restated)

	Goodwill Restated £m	Acquired in-force business £m	Customer relationships £m	Present value of future profits £m	Total Restated £m
Cost or valuation					
At 1 January – as restated	115	2,213	445	35	2,808
Revaluation	–	–	–	7	7
At 31 December	115	2,213	445	42	2,815
Amortisation					
At 1 January	–	50	7	–	57
Charge for the year	–	147	18	–	165
At 31 December	–	197	25	–	222

Carrying amount					
At 31 December	115	2,016	420	42	2,593
Amount recoverable after 12 months	115	1,881	402	42	2,402

Goodwill

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 2016 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% (2010: 9.5%) for the Ignis Asset Management business and a discount rate of 6.7% (2010: 9.5%) for the management services business of the Phoenix Life segment.

Impairment tests have been performed using assumptions which management consider reasonable. Given the magnitude of the excess of the value in use over carrying value, management believes that it is unlikely that there would be a change in key assumptions such that carrying value would exceed value in use.

The carrying amount of goodwill allocated to the Phoenix Life segment is £58 million (2010: £58 million) and to the Ignis Asset Management segment is £57 million (2010: £57 million).

Acquired in-force business

Acquired in-force business 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 Group's accounting policies for such contracts. This intangible is being amortised in accordance with the run-off of the book of business within the Phoenix Life segment.

The acquired in-force business is allocated to the Phoenix Life segment.

Customer relationships

The first part of the customer relationships intangible relates to 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 10.0% (2010: 9.6%). 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 have been allocated to the Ignis Asset Management segment.

The amortisation charge for customer relationships is presented separately in 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 43.5.1. Revaluation of PVFP is charged or credited to the consolidated income statement as appropriate.

34. Property, plant and equipment

	2011 £m	2010 £m
Cost or valuation		
At 1 January	**39**	36

Additions	**7**	3
Disposals	**(2)**	–
At 31 December	**44**	39

Depreciation and impairment		
At 1 January	**(5)**	(2)
Charge for the year	**(3)**	(3)
Impairment	**(8)**	–
At 31 December	**(16)**	(5)

Carrying amount		
At 31 December	**28**	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 Group's main operating site in Wythall is owned by one of the Group's with-profit funds. During 2011, an agreement in principle was reached for the purchase of that site by one of the Group's management services companies. A valuation was undertaken in connection with the sale and has resulted in an impairment of £8 million being recognised in the Phoenix Life segment.

35. Investment property

	2011 £m	2010 £m
At 1 January	**1,732**	1,915
Additions	**102**	139
Improvements	**9**	12
Disposals	**(31)**	(421)
Gains on adjustments to fair value	**4**	87
At 31 December	**1,816**	1,732

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 £221 million (2010: £235 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. The acquisition of these investment properties was financed by the Property Reversions loan as detailed in note 22.

Direct operating expenses (included within administrative expenses) in respect of investment properties that generated rental income during the year amounted to £4 million (2010: £2 million). The direct operating expenses arising from investment property that did not generate rental income during the year amounted to £2 million (2010: £2 million).

36. Financial assets

	2011 £m	2010 £m
Loans and receivables at amortised cost	**3,529**	2,293
Financial assets at fair value through profit or loss		
Held for trading – derivatives	**6,099**	3,197
Designated upon initial recognition		
Equities	**11,078**	12,460
Fixed and variable rate income securities	**42,010**	40,899
Collective investment schemes	**6,251**	7,144
	68,967	65,993

Amount recoverable after 12 months	**40,303**	39,758

The fair value of loans and receivables at amortised cost amounted to £3,494 million (2010: £2,320 million).

37. Financial instrument fair value hierarchy

37.1 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.

37.2 Fair value hierarchy of financial instruments measured at fair value
2011

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial assets at fair value				
Derivatives	**–**	**6,038**	**61**	**6,099**
Financial assets designated at fair value through profit or loss upon initial recognition				
Equities	**10,222**	**42**	**814**	**11,078**
Fixed and variable rate income securities	**31,592**	**9,556**	**862**	**42,010**
Collective investment schemes	**4,976**	**1,043**	**232**	**6,251**
	46,790	**10,641**	**1,908**	**59,339**
Total financial assets at fair value	**46,790**	**16,679**	**1,969**	**65,438**

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial liabilities at fair value				
Derivatives	**–**	**4,292**	**–**	**4,292**
Financial liabilities designated at fair value through profit or loss upon initial recognition				
Investment contract liabilities	**–**	**7,978**	**–**	**7,978**
Borrowings	**–**	**217**	**–**	**217**

Net asset value attributable to unitholders	**3,040**	**–**	**169**	**3,209**
	3,040	**8,195**	**169**	**11,404**
Total financial liabilities at fair value	**3,040**	**12,487**	**169**	**15,696**

2010

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial assets at fair value				
Derivatives	24	3,084	89	3,197
Financial assets designated at fair value through profit or loss upon initial recognition				
Equities	11,667	–	793	12,460
Fixed and variable rate income securities	34,336	5,816	747	40,899
Collective investment schemes	5,786	1,042	316	7,144
	51,789	6,858	1,856	60,503
Total financial assets at fair value	51,813	9,942	1,945	63,700

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial liabilities at fair value				
Derivatives	1	2,419	11	2,431
Financial liabilities designated at fair value through profit or loss upon initial recognition				
Investment contract liabilities	–	8,849	–	8,849
Borrowings	–	234	–	234
Net asset value attributable to unitholders	1,769	–	168	1,937
	1,769	9,083	168	11,020
Total financial liabilities at fair value	1,770	11,502	179	13,451

37.3 Level 3 financial instrument sensitivities

Included in Level 3 investments are two property investment structures with a value of £66 million (2010: £96 million) and £102 million (2010: £117 million) 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 £36 million (2010: £36 million) and in the worst case scenario the fair value would decrease by £38 million (2010: £63 million).

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 £23 million (2010: £23 million) and a reduction in yields of 25bps would increase the value by £25 million (2010: £25 million).

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.

37.4 Significant transfers of financial instruments between Level 1 and Level 2

2011

	From Level 1 to	**From Level 2 to**

	Level 2 £m	Level 1 £m
Financial assets at fair value		
Financial assets designated at fair value through profit or loss upon initial recognition		
Fixed and variable rate income securities	**1,181**	**186**

2010

	From Level 1 to Level 2 £m	From Level 2 to Level 1 £m
Financial assets at fair value		
Financial assets designated at fair value through profit or loss upon initial recognition		
Fixed and variable rate income securities	96	573

There were no transfers of financial liabilities at fair value between Level 1 and Level 2 and between Level 2 and Level 1.

All the Group's Level 2 assets have been valued using standard market pricing sources, which have not changed during 2011. However, following consultation with our investment managers and pricing providers, we have updated our criteria for an active market, particularly with reference to corporate bonds, and hence have classified some assets as Level 2 when they would have been Level 1 in previous periods.

The Group saw an improvement in the liquidity of the fixed and variable rate securities market throughout 2011, 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 Level 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.

37.5 Movement in Level 3 financial instruments measured at fair value

2011

	At 1 January 2011 £m	Total gains/ (losses) in income statement £m	Purchases and sales £m	Transfers from Level 1 and Level 2 £m	At 31 December 2011 £m	Unrealised losses on assets held at end of year £m
Financial assets						
Derivative assets	**89**	**(17)**	**(11)**	**–**	**61**	**(243)**
Financial assets designated at fair value through profit or loss upon initial recognition						
Equities	**793**	**29**	**(10)**	**2**	**814**	**(2)**
Fixed and variable rate income securities	**747**	**9**	**(3)**	**109**	**862**	**(1)**
Collective investment schemes	**316**	**(2)**	**(82)**	**–**	**232**	**(1)**
	1,856	**36**	**(95)**	**111**	**1,908**	**(4)**
Total financial assets	**1,945**	**19**	**(106)**	**111**	**1,969**	**(247)**

	At 1 January 2011 £m	Total gains/(losses) in income statement £m	Purchases and sales £m	Transfers from Level 1 and Level 2 £m	At 31 December 2011 £m	Unrealised gains on liabilities held at end of year £m
Financial liabilities						
Derivative liabilities	**11**	**(11)**	**–**	**–**	**–**	**–**
Financial liabilities designated at fair value through profit or loss upon initial recognition						
Net asset value attributable to unitholders	**168**	**1**	**–**	**–**	**169**	**44**
Total financial liabilities	**179**	**(10)**	**–**	**–**	**169**	**44**

2010

	At 1 January 2010 £m	Total gains/ (losses) in income statement £m	Purchases and sales £m	Transfers (to)/from Level 1 and Level 2 £m	At 31 December 2010 £m	Unrealised gains/(losses) on assets held at end of year £m
Financial assets						
Derivative assets	–	(22)	111	–	89	(202)
Financial assets designated at fair value through profit or loss upon initial recognition						
Equities	1,494	64	(766)	1	793	19
Fixed and variable rate income securities	819	(43)	32	(61)	747	150
Collective investment schemes	235	97	152	(168)	316	214
	2,548	118	(582)	(228)	1,856	383
Total financial assets	2,548	96	(471)	(228)	1,945	181

	At 1 January 2010 £m	Total gains/(losses) in income statement £m	Purchases and sales £m	Transfers from Level 1 and Level 2 £m	At 31 December 2010 £m	Unrealised gains on liabilities held at end of year £m
Financial liabilities						
Derivative liabilities	–	(5)	–	16	11	11
Financial liabilities designated at fair value through profit or loss upon initial recognition						
Net asset value attributable to unitholders	154	14	–	–	168	43
Total financial liabilities	154	9	–	16	179	54

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.

Level 3 financial instruments are transferred to Level 1 or Level 2 as and when the conditions of each Level are met. During 2011 the Group saw a decrease in observable inputs leading to an increase in Level 3 financial instruments.

38. Stock lending and collateral

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 2011 that have not been derecognised amounted to fixed and variable rate income securities of £10,924 million (2010: £9,994 million).

It is the Group's practice to obtain collateral in stock lending transactions, usually in the form of cash or marketable securities.

Where the Group receives collateral in the form of marketable securities which it is not permitted to sell or re-pledge except in the case of default, such collateral is not recognised in the statement of consolidated financial position. The fair value of financial assets accepted as such collateral amounts to £255 million (2010: £648 million).

Where the Group receives collateral in the form of cash it is recognised in the statement of consolidated financial position along with a corresponding liability to repay the amount of the collateral received. The amount recognised as a financial asset and a financial liability at 31 December 2011 is £10,823 million (2010: £9,222 million) and £10,916 million (2010: £9,339 million) respectively.

The maximum exposure to credit risk in respect of stock lending transactions is £10,924 million (2010: £9,994 million) of which credit risk of £10,913 million (2010: £9,714 million) is mitigated through the use of collateral arrangements.

Collateral and pledges

Assets accepted

It is the Group's practice to obtain collateral to mitigate the counterparty risk related to over-the-counter ('OTC') derivatives and reinsurance transactions, usually in the form of cash or marketable securities.

Where the Group receives collateral in the form of marketable securities which it is not permitted to sell or re-pledge except in the case of default, it is not recognised in the statement of consolidated financial position. The fair value of financial assets accepted as collateral for OTC derivatives and reinsurance transactions but not recognised in the statement of consolidated financial position amounts to £371 million and £2,089 million respectively (2010: £313 million and £1,898 million).

Where the Group receives collateral on OTC derivatives and reinsurance transactions in the form of cash it is recognised in the statement of consolidated financial position along with a corresponding liability to repay the amount of collateral received, disclosed as 'Obligations for the repayment of collateral received' and 'Deposits received from reinsurers' respectively. The amounts recognised as financial liabilities from cash collateral received at 31 December 2011 are set out below.

	OTC derivatives		**Reinsurance transactions**	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Financial liability	**2,089**	821	**472**	419

The maximum exposure to credit risk in respect of OTC derivative assets is £6,045 million (2010: £3,154 million) of which credit risk of £5,871 million (2010: £2,893 million) is mitigated by use of collateral arrangements (which are settled net after taking account of any OTC derivative liabilities owed to the counterparty).

Credit risk on exchange traded derivative assets of £54 million (2010: £43 million) is mitigated through regular merging and the protection offered by the exchange.

Assets pledged

Where the Group pledges collateral in the form of cash or marketable securities and retains all the risks and rewards of the transferred assets, they continue to be recognised in the statement of consolidated financial position. The value of assets pledged at 31 December 2011 in respect of OTC derivative liabilities of £4,268 million (2010: £2,411 million) amounted to £236 million (2010: £500 million).

Collateral has also been pledged and charges granted in respect of certain of the Group's borrowings as set out in note 22. In addition, the Trustees of the Pearl Group Staff Pension Scheme have been granted certain charges as set out in note 32.

39. Other receivables

	2011 £m	2010 £m
Investment broker balances	**95**	69
Other debtors	**105**	105
	200	174
Amount recoverable after 12 months	**–**	–

40. Cash and cash equivalents

	2011 £m	2010 £m
Bank and cash balances	**1,713**	2,101
Short-term deposits (including demand and time deposits)	**10,010**	7,087
	11,723	9,188

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 £11,387 million (2010: £8,545 million) are primarily held for the benefit of policyholders and so are not generally available for use by the owners.

41. Cash flows from operating activities

	2011 £m	2010 £m
(Loss)/profit for the year before tax	**(4)**	11
Non-cash movements in profit for the year before tax		

Fair value gains on:		
Investment property	**(4)**	(87)
Financial assets	**(1,572)**	(3,324)
Change in fair value of borrowings	**20**	12
Depreciation of property, plant and equipment	**3**	3
Impairment of owner occupied property	**8**	–
Amortisation of intangible assets	**152**	165
Change in present value of future profit	**19**	(7)
Change in unallocated surplus	**(16)**	143
Share-based payment charge/(income)	**4**	(3)
Interest expense on borrowings	**251**	269
Net expected return on pension assets	**11**	18
Other gains on pension schemes	**(37)**	–
Foreign currency exchange gains	**–**	(10)
Decrease/(increase) in investment assets	**1,400**	(1,308)
Increase in reinsurance assets	**(201)**	(69)
Increase in insurance contract and investment contract liabilities	**450**	423
Increase/(decrease) in deposits received from reinsurers	**53**	(12)
Increase in obligation for repayment of collateral received	**2,845**	6,054
Net decrease in working capital	**310**	1,114
Cash generated by operations	**3,692**	3,392

42. 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
- optimise the overall gearing to ensure an efficient capital base.

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 ensures sufficient liquidity to meet creditor obligations through the combination of cash buffers and cash flows from the Group's operating companies.

The capital policy of each life company is set and monitored by each life company Board. 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 and the Group 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.

An alternative test to the RCR 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, called 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% 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 capital adequacy 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 life assurance businesses 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 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-profit 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.

The primary source of capital used by the Group is equity shareholders' funds and borrowings. The capital statement and movement analysis that follows presents information about the capital resources for the Group's UK life businesses.

2011

	With-profit (see below) £m	Non-participating £m	Phoenix Life owners' funds £m	Total Phoenix Life business £m	Other activities and consolidation adjustments (note 4) £m	Group total £m
Owners' funds held outside long-term fund	–	–	**1,688**	**1,688**	**(763)**	**925**
Owners' funds held in long-term fund	–	**727**	–	**727**	–	**727**
Total owners' funds at 31 December 2011	–	**727**	**1,688**	**2,415**	**(763)**	**1,652**
Adjustments onto a regulatory basis:						
Unallocated surplus	**843**	**5**	–	**848**		
Adjustments to assets (note 1)	**(34)**	**(251)**	**(535)**	**(820)**		
Adjustments to liabilities (note 2)	**3,667**	**(141)**	**33**	**3,559**		
Other qualifying capital:						
Subordinated debt (note 3)	–	–	**645**	**645**		

Contingent loans	**412**	**(73)**	**(209)**	**130**
Total available capital resources at 31 December 2011	**4,888**	**267**	**1,622**	**6,777**

With-profit
2011

	Pearl WPF £m	**PLL PWP £m**	**PLL BWP £m**	**SMA WPF £m**	**SPL WPF £m**	**Other £m**	**Total £m**
Owners' funds held outside long-term fund	–	–	–	–	–	–	–
Owners' funds held in long-term fund	–	–	–	–	–	–	–
Total owners' funds at 31 December 2011	–	–	–	–	–	–	–
Adjustments onto a regulatory basis:							
Unallocated surplus	**280**	**148**	**218**	**52**	**57**	**88**	**843**
Adjustments to assets (note 1)	**(1)**	**(1)**	**(4)**	**–**	**(1)**	**(27)**	**(34)**
Adjustments to liabilities (note 2)	**841**	**710**	**782**	**275**	**655**	**404**	**3,667**
Other qualifying capital:							
Contingent loans	–	–	–	–	–	**412**	**412**
Total available capital resources at 31 December 2011	**1,120**	**857**	**996**	**327**	**711**	**877**	**4,888**

2010

	With-profit (see below) £m	Non-participating £m	Phoenix Life owners' funds £m	Total Phoenix Life business £m	Other activities and consolidation adjustments (note 4) £m	Group total £m
Owners' funds held outside long-term fund	–	–	2,194	2,194	(1,329)	865
Owners' funds held in long-term fund	–	715	–	715	–	715
Total owners' funds at 31 December 2010	–	715	2,194	2,909	(1,329)	1,580
Adjustments onto a regulatory basis:						
Unallocated surplus	853	11	–	864		
Adjustments to assets (note 1)	(93)	(319)	(422)	(834)		
Adjustments to liabilities (note 2)	3,526	(120)	54	3,460		
Other qualifying capital:						
Subordinated debt (note 3)	–	–	645	645		
Contingent loans	736	216	(772)	180		
Allocation of Group capital	52	206	(258)	–		
Total available capital resources at 31 December 2010	5,074	709	1,441	7,224		

With-profit
2010

	Pearl WPF £m	PLL PWP £m	PLL BWP £m	SMA WPF £m	SPL WPF £m	Other £m	Total £m
Owners' funds held outside long-term fund	–	–	–	–	–	–	–
Owners' funds held in long-term fund	–	–	–	–	–	–	–
Total owners' funds at 31 December 2010	–	–	–	–	–	–	–

Adjustments onto a regulatory basis:							
Unallocated surplus	294	153	273	34	62	37	853
Adjustments to assets (note 1)	(7)	(2)	(11)	–	(1)	(72)	(93)
Adjustments to liabilities (note 2)	761	812	770	261	652	270	3,526
Other qualifying capital:							
Contingent loans	–	–	–	–	–	736	736
Allocation of Group capital	–	–	–	–	–	52	52
Total available capital resources at 31 December 2010	1,048	963	1,032	295	713	1,023	5,074

Notes

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.

2 Regulatory adjustments to liabilities primarily reflect differences between the realistic valuation basis for the with-profit business used in calculating owners' funds on an IFRS basis, and the regulatory valuation basis used to calculate the FSA peak 1 capital resources.

3 Of the £645 million (2010: £645 million) subordinated debt attributed to the Phoenix Life segment of the Group £445 million (2010: £445 million) is internal to the Group, comprising £250 million (2010: £250 million) provided to Pearl Assurance Limited and £195 million provided to Phoenix & London Assurance Limited which was transferred to PLL on 1 January 2011 following a Part VII transfer. The remaining £200 million (2010: £200 million) is external subordinated debt, see note 22 for details.

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.

An analysis of the movement in available capital resources for the period 1 January 2011 to 31 December 2011 is shown below:

	With-profit								
	Pearl WPF £m	**PLL PWP £m**	**PLL BWP £m**	**SMA WPF £m**	**SPL WPF £m**	**Other £m**	**Non-participating £m**	**Phoenix Life owners' funds £m**	**Total Phoenix Life business £m**
Total available capital resources at 1 January 2011	**1,048**	**963**	**1,032**	**295**	**713**	**1,023**	**709**	**1,441**	**7,224**
Regular surplus	**44**	**54**	**(12)**	**56**	**7**	**51**	**137**	**–**	**337**
Investment return	**554**	**302**	**178**	**217**	**130**	**705**	**5**	**69**	**2,160**
Cost of bonus	**(119)**	**(184)**	**(83)**	**(55)**	**(74)**	**(81)**	**–**	**51**	**(545)**
Changes in methodology and assumptions:									
Longevity	**2**	**33**	**(2)**	**3**	**3**	**11**	**(32)**	**–**	**18**
Expenses	**22**	**5**	**3**	**1**	**(46)**	**24**	**1**	**–**	**10**
Persistency	**–**	**–**	**–**	**–**	**–**	**(13)**	**(1)**	**–**	**(14)**
Other	**–**	**15**	**–**	**12**	**(1)**	**69**	**12**	**–**	**107**
Management actions:									
Dividends paid by Phoenix Life	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(585)**	**(585)**
New business and other factors:									
Intragroup capital movement	**–**	**–**	**(31)**	**–**	**–**	**(222)**	**(581)**	**834**	**–**
Valuation rate of interest	**(441)**	**(331)**	**(89)**	**(201)**	**(88)**	**(690)**	**–**	**–**	**(1,840)**
Adjustment for internal loans in excess of counterparty limits	**–**	**–**	**–**	**–**	**–**	**–**	**(2)**	**(182)**	**(184)**
Other	**10**	**–**	**–**	**(1)**	**67**	**–**	**19**	**(6)**	**89**
Total available capital resources at 31 December 2011	**1,120**	**857**	**996**	**327**	**711**	**877**	**267**	**1,622**	**6,777**

An analysis of the movement in available capital resources for the period 1 January 2010 to 31 December 2010 is shown below:

	With-profit								
	Pearl WPF	PLL PWP	PLL BWP	SMA WPF	SPL WPF	Other	Non-participating £m	Phoenix Life owners'	Total Phoenix Life

								funds	business
	£m	£m	£m	£m	£m	£m		£m	£m
Total available capital resources at 1 January 2010	984	927	803	294	643	819	586	1,919	6,975
Regular surplus	75	64	(15)	49	8	30	167	–	378
Investment return	585	261	375	105	184	379	(76)	77	1,890
Cost of bonus	(93)	(124)	(85)	(55)	(58)	(66)	–	39	(442)
Changes in methodology and assumptions:									
Longevity	–	–	4	3	1	1	40	–	49
Expenses	(6)	21	–	(3)	(1)	10	3	–	24
Other	(1)	(4)	–	(5)	(3)	(26)	16	–	(23)
Management actions:									
Dividends paid by Phoenix Life	–	–	–	–	–	–	–	(433)	(433)
New business and other factors:									
Intragroup capital movement	(205)	–	–	–	–	179	(4)	(225)	(255)
Valuation rate of interest	(254)	(140)	(15)	(170)	(118)	(270)	–	–	(967)
Adjustment for internal loans in excess of counterparty limits	–	–	–	–	–	–	(15)	64	49
Other	(37)	(42)	(35)	77	57	(33)	(8)	–	(21)
Total available capital resources at 31 December 2010	1,048	963	1,032	295	713	1,023	709	1,441	7,224

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 2011 generally comprise payment of dividends to Group entities.

43. Risk management

The Group's overall approach to risk management is described in the Performance section of the Annual Report and Accounts

43.1 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 its various cash flow requirements. Subject to this, the Group seeks to use available capital to achieve increased 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.

43.2 Asset liability management ('ALM') framework

The use of financial instruments naturally exposes the Group to the risks associated with them, mainly, market risk, credit risk and financial soundness risk. Financial soundness risk is a broad risk category encompassing financial control and reporting risk, capital management risk, liquidity and funding risk, and tax risk. Liquidity and funding risk are the most relevant of the financial soundness risks for financial instruments.

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 actuarial function holder 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 actuarial function holder 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, including the activities of the Group's Treasury function.

More detail on the Group's exposure to financial risk is provided in note 43.3 below.

The Group is also exposed to insurance risk arising from its Phoenix Life segment. Life insurance 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 are provided in note 43.5 below.

The Group's overall exposure to market and credit 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.

43.3 Financial risk analysis

Transactions in financial instruments may result in the Group assuming financial risks. These include credit risk, market risk and financial soundness risk. Each of these are described below, together with a summary of how the Group manages them.

43.3.1 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 and variable rate income securities, equities, derivatives, collective investment schemes 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.

The impact of non-government fixed and variable rate income securities and, inter alia, the change in market credit spreads during the year is 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.

There is an exposure to spread changes affecting the prices of corporate bonds and derivatives. This exposure applies to with-profit funds, non-profit funds (where risks and rewards fall wholly to shareholders), shareholders' funds and to unit-linked funds to the extent of management fees generated by the Group.

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 £249 million (2010: £223 million).

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 £292 million (2010: £246 million).

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 credit risk tolerances. In certain cases, protection against exposure to particular credit risk types may be achieved through the use of derivatives. The credit risk borne by the shareholder on with-profit policies is dependent on the extent to which the underlying 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 (the S&P rating is used in deriving the table below):

2011

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Non-rated £m	Unit-linked £m	Total £m
Loans and receivables	**–**	**–**	**3,008**	**–**	**11**	**454**	**51**	**5**	**3,529**
Derivatives	**–**	**73**	**5,665**	**–**	**–**	**–**	**183**	**178**	**6,099**
Fixed and variable rate income securities	**28,722**	**2,478**	**5,015**	**4,107**	**492**	**425**	**603**	**168**	**42,010**
Reinsurers' share of insurance contract liabilities	**–**	**759**	**2,374**	**20**	**–**	**–**	**–**	**–**	**3,153**
Cash and cash equivalents	**8,509**	**1,574**	**1,474**	**19**	**8**	**6**	**1**	**132**	**11,723**
	37,231	**4,884**	**17,536**	**4,146**	**511**	**885**	**838**	**483**	**66,514**

2010

	AAA £m	AA £m	A m	BBB £m	BB £m	B and below £m	Non-rated £m	Unit-linked £m	Total £m
Loans and receivables	–	–	1,619	13	145	467	44	5	2,293
Derivatives	–	2,372	630	–	–	–	94	101	3,197
Fixed and variable rate income securities	25,694	4,872	5,369	3,145	343	511	828	137	40,899
Reinsurers' share of insurance contract liabilities	–	599	2,199	20	–	–	109	12	2,939
Cash and cash equivalents	2,371	5,634	912	81	–	–	1	189	9,188
	28,065	13,477	10,729	3,259	488	978	1,076	444	58,516

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 credit quality of the underlying debt securities within these vehicles is managed by the safeguards built into the investment mandates for these vehicles.

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.

2011

	Neither past due nor impaired £m	Less than 30 days £m	30–90 days £m	Greater than 90 days £m	Impaired £m	Unit-linked £m	Carrying value £m
Loans and receivables	**3,468**	**–**	**–**	**–**	**56**	**5**	**3,529**
Derivatives	**5,921**	**–**	**–**	**–**	**–**	**178**	**6,099**
Fixed and variable rate income securities	**41,842**	**–**	**–**	**–**	**–**	**168**	**42,010**
Reinsurers' share of insurance contract liabilities	**3,153**	**–**	**–**	**–**	**–**	**–**	**3,153**
Reinsurance receivables	**257**	**–**	**–**	**–**	**–**	**–**	**257**
Prepayments and accrued income	**599**	**–**	**–**	**–**	**–**	**–**	**599**
Other receivables	**200**	**–**	**–**	**–**	**–**	**–**	**200**
Cash and cash equivalents	**11,591**	**–**	**–**	**–**	**–**	**132**	**11,723**

2010

	Neither past due nor	Less than 30 days	30–90 days	Greater than 90 days	Impaired £m	Unit-linked £m	Carrying value

	impaired £m	£m	£m	£m			£m
Loans and receivables	2,284	–	–	–	4	5	2,293
Derivatives	3,096	–	–	–	–	101	3,197
Fixed and variable rate income securities	40,762	–	–	–	–	137	40,899
Reinsurers' share of insurance contract liabilities	2,927	–	–	–	–	12	2,939
Reinsurance receivables	263	–	–	–	–	–	263
Prepayments and accrued income	603	–	–	–	–	–	603
Other receivables	173	–	–	–	1	–	174
Cash and cash equivalents	8,999	–	–	–	–	189	9,188

Please refer to page 166 for additional life company asset disclosures which include the life companies' exposure to peripheral Eurozone debt securities. Peripheral Eurozone is defined as Portugal, Spain, Italy, Ireland and Greece.

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 statement of consolidated financial position. Shareholder credit exposure on unit-linked assets is limited to the level of asset manager fee which is dependent on the underlying assets.

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 partners. 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 (and is not carried at fair value).

43.3.2 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 influences. Market risk comprises interest rate risk, currency risk and other price risk (comprising equity risk, property risk, inflation risk and alternative asset class 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 and within 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 rate risk
Interest rate 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 rate risk is managed by matching assets and liabilities where practicable and by entering into derivative arrangements for hedging purposes 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 rate 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 (but excludes the impact on the Group's defined benefit pension schemes).

With-profit business and non-participating business within the with-profit funds are exposed to interest rate 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 dependent on the existence of policyholder guarantees. 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 and variable rate income securities, with the result that sensitivity to changes in interest rates is very low. For unit-linked funds the risk is limited to the extent of the management fees generated by the Group.

An increase of 1% in interest rates[1], 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 £2 million (2010: a decrease of £103 million). A decrease of 1% in interest rates[1], with all other variables held constant, would result in a decrease in profit after tax in respect of a full financial year, and in equity, of £6 million (2010: an increase of £78 million).

Equity, property and inflation risk
The Group has exposure 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 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, whilst the Group also has exposure to the value of guarantees provided to with-profit policyholders. In addition some equity investments are held in respect of shareholders' 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 and within the Group's ALM framework through the holding of derivatives or physical positions in relevant assets where appropriate.

1 55bps is assumed to relate to default risk, after allowing for additional prudence on an IFRS basis.

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 (but excludes the impact on the Group's defined benefit pension schemes).

A 10% decrease in equity prices, with all other variables held constant, would result in a increase in the profit after tax in respect of a full financial year and, in equity, of £16 million (2010: a decrease of £22 million).

A 10% increase in equity prices, with all other variables held constant, would result in an decrease in the profit after tax in respect of a full financial year, and in equity, of £16 million (2010: an increase of £21 million).

A 10% decrease in 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 £43 million (2010: £52 million).

A 10% increase in 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 £45 million (2010: £51 million).

The Group is exposed to inflation risk through certain contracts, such as annuities, which may provide for future benefits to be paid taking account of changes in the level of inflation, and also through the Group's cost base. The Group seeks to manage inflation risk within the ALM framework through the holding of derivatives, such as inflation swaps, or physical positions in relevant assets, such as index-linked gilts, where appropriate.

Currency risk

The Group's principal transactions are carried out in sterling and therefore its exchange risk is limited principally to historic business that was written in the Republic of Ireland, where the assets are generally held in the same currency denomination as their liabilities, therefore, any foreign currency mismatch is largely mitigated. Consequently, the foreign currency risk relating to this business mainly arises when the assets and liabilities 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 certain holdings in overseas assets are hedged against currency risks.

Sensitivity of profit after tax and equity to fluctuations in currency exchange rates is not considered significant at 31 December 2011, since unhedged exposure to foreign currency was relatively low. (2010: not considered significant)

43.3.3 Financial soundness risk

Financial soundness risk is a broad risk category encompassing financial control and reporting risk, capital management risk, liquidity and funding risk, and tax risk.

Financial control and reporting risk is defined as the failure of the Group to appropriately record, report or disclose financial information. The Group has exposure to financial control and reporting risk through the production of its Interim and Annual Report and Accounts. The Group's subsidiaries have exposure to financial control and reporting risk through the annual entity report and accounts and annual regulatory reporting.

Liquidity and funding 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.

Tax risk is defined as the failure of the Group to appropriately record, report or disclose taxation information. The Group has exposure to tax risk through the production of its Interim and Annual Report and Accounts. The Group's subsidiaries have exposure to tax risk through the annual entity report and accounts, annual regulatory reporting and through the processing of policyholder tax 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 company 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 including, where appropriate, by having 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 collective investment schemes which are either managed or overseen by Ignis Asset Management. The collective investment schemes have the power to restrict and/or suspend withdrawals, which would, in turn, affect liquidity. To date, the collective investment schemes have continued to process both investments and realisations in a normal manner and have not imposed any restrictions or delays.

Some of the Group's cash and cash equivalents are held through collective investment schemes. The collective investment schemes have the power, in an extreme stress, to restrict and/or suspend withdrawals, which would, in turn, affect liquidity. To date, the collective investment schemes have continued to process both investments and realisations in a normal manner and have 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:

2011

	1 year or less or on demand £m	**1–5 years £m**	**Greater than 5 years £m**	**No fixed term £m**	**Total £m**
Liabilities under insurance contracts	**5,041**	**14,279**	**29,932**	**2,548**	**51,800**
Investment contracts	**7,978**	**–**	**–**	**–**	**7,978**
Borrowings	**169**	**2,345**	**520**	**216**	**3,250**
Deposits received from reinsurers	**33**	**124**	**458**	**–**	**615**
Derivatives	**924**	**385**	**5,859**	**–**	**7,168**
Net asset value attributable to unitholders	**3,209**	**–**	**–**	**–**	**3,209**
Obligations for repayment of collateral received	**11,453**	**255**	**1,297**	**–**	**13,005**
Reinsurance payables	**33**	**–**	**–**	**–**	**33**
Payables related to direct insurance contracts	**668**	**39**	**–**	**–**	**707**
Accruals and deferred income	**169**	**4**	**–**	**2**	**175**
Other payables	**623**	**4**	**–**	**–**	**627**

2010

	1 year or less or on demand £m	1–5 years £m	Greater than 5 years £m	No fixed term £m	Total £m
Liabilities under insurance contracts	8,103	14,556	25,882	1,938	50,479
Investment contracts	8,849	–	–	–	8,849
Borrowings	190	2,751	2,153	234	5,328
Deposits received from reinsurers	35	130	492	1	658
Derivatives	914	343	2,801	–	4,058
Net asset value attributable to unitholders	1,937	–	–	–	1,937
Obligations for repayment of collateral received	9,532	122	506	–	10,160
Reinsurance payables	25	–	–	–	25
Payables related to direct insurance contracts	673	40	–	–	713
Accruals and deferred income	205	9	–	–	214
Other payables	327	–	–	–	327

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.

43.4 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.

43.5 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;
Options	– unanticipated changes in policyholder option exercise rates giving rise to increased claims costs; and
General insurance	– higher than expected number of non-life claims on general insurance policies and occurrence of one or more large claims.

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 Directors 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.

The Group has a number of small books of general insurance. These have been closed to new business for a number of years and are in run-off.

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.

This general insurance business is managed by an experienced team of specialists who are responsible for all aspects of claims management, reserving and oversight of any activities undertaken by third parties. All such activity is carried out in accordance with the relevant regulations and industry standards.

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 £24 million (2010: £23 million).

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 £24 million (2010: £24 million).

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 £191 million (2010: £164 million).

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 £186 million (2010: £162 million).

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 £56 million (2010: £61 million).

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 £51 million (2010: £49 million).

43.5.1 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 was as follows:

	Increase/ (decrease) in insurance liabilities 2011 £m	Increase/ (decrease) in insurance liabilities 2010 £m
Change in longevity assumptions	**(72)**	(43)
Change in persistency assumptions	**18**	35
Change in expenses assumptions	**(25)**	10

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:

	2011 %	2010 %
Life policies	**1.82 – 3.41**	2.32 – 3.64
Pension policies	**1.72 – 3.80**	2.67 – 4.46

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 partners. 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 43.5.2 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 £2,248 million (2010: £1,541 million) and £59 million (2010: £20 million) 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 £409 million (2010: £329 million) and £22 million (2010: £20 million) respectively.

With-profit 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.

43.5.2 Managing product risk
The following sections give an assessment of the risks associated with the Group's main life assurance products, as shown below, and the ways in which the Group manages those risks.

2011

	Gross		Reinsurance	
	Insurance contracts £m	**Investment contracts with DPF £m**	**Insurance contracts £m**	**Investment contracts with DPF £m**
With-profit funds:				
Pensions:				

Deferred annuities – with guarantees	**9,823**	**79**	**795**	**–**
Deferred annuities – without guarantees	**1,930**	**105**	**–**	**–**
Immediate annuities	**3,651**	**–**	**688**	**–**
Unitised with-profit	**1,202**	**9,033**	**3**	**–**
Total pensions	**16,606**	**9,217**	**1,486**	**–**
Life:				
Immediate annuities	**101**	**–**	**6**	**–**
Unitised with-profit	**859**	**832**	**2**	**–**
Life with-profit	**6,083**	**–**	**11**	**–**
Total life	**7,043**	**832**	**19**	**–**
Other	**1,992**	**7**	**135**	**–**
Non-profit funds:				
Deferred annuities – with guarantees	**75**	**–**	**–**	**–**
Deferred annuities – without guarantees	**643**	**6**	**–**	**–**
Immediate annuities	**11,351**	**–**	**1,195**	**–**
Protection	**663**	**–**	**279**	**–**
Unit-linked	**1,801**	**1,220**	**12**	**–**
Other	**343**	**1**	**27**	**–**
	40,517	**11,283**	**3,153**	**–**

2010

	Gross		Reinsurance	
	Insurance contracts £m	Investment contracts with DPF £m	Insurance contracts £m	Investment contracts with DPF £m
With-profit funds:				
Pensions:				
Deferred annuities – with guarantees	8,660	73	469	–
Deferred annuities – without guarantees	1,593	107	–	–
Immediate annuities	4,450	–	705	–
Unitised with-profit	1,291	9,143	102	–
Total pensions	15,994	9,323	1,276	–
Life:				
Immediate annuities	95	–	9	–
Unitised with-profit	965	936	38	–
Life with-profit	7,209	–	2	–
Total life	8,269	936	49	–
Other	1,820	7	67	–
Non-profit funds:				
Deferred annuities – with guarantees	132	–	56	–
Deferred annuities – without guarantees	1,013	6	477	–
Immediate annuities	8,592	–	701	–
Protection	636	–	282	–
Unit-linked	2,078	1,435	12	–

Other	236	2	19	–
	38,770	11,709	2,939	–

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-participating 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 and other asset classes 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. 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. 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 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.

Market and credit risk is influenced by the extent to which the cash flows 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.

Market and credit risk is influenced by the extent to which the cash flows 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.

44. Operating leases

Operating lease rentals charged within administrative expenses amounted to £16 million (2010: £7 million).

The Group has commitments under non-cancellable operating leases as set out below:

	2011 £m	2010 £m
Not later than 1 year	**15**	11
Later than 1 year and no later than 5 years	**56**	41
Later than 5 years	**35**	47

The principal operating lease commitments concern office space located at Bothwell Street, Glasgow; St Vincent Street, Glasgow; Juxon House, London and Cheapside, London.

45. Commitments

	2011 £m	2010 £m
To subscribe to private equity funds and other unlisted assets	**356**	409
To purchase, construct or develop investment property	**61**	80
For repairs, maintenance or enhancements of investment property	**1**	2
To acquire property, plant and equipment	**–**	2

46. Related party transactions

The Group has related party transactions with its pension schemes and its key management personnel.

Transactions with pension schemes

During the year the Group entered into the following transactions with its pension schemes:

	Transactions 2011 £m	**Balances outstanding 2011 £m**	Transactions 2010 £m	Balances outstanding 2010 £m
Pearl Group Staff Pension Scheme				
Investment management fees	**0.6**	**0.2**	0.5	0.7
Payment of administrative expenses	**(4.0)**	**–**	(3.0)	–
	(3.4)	**0.2**	(2.5)	0.7
PGL Pension Scheme				
Investment management fees	**2.4**	**0.8**	2.2	0.8

The Pearl Scheme has invested in collective investment schemes that are controlled by the Group. At 31 December 2011 the Pearl Scheme held 1,118,197 units (2010: 1,118,197 units) in the Ignis Systematic Strategies Fund and 53,243,341 units (2010: 147,928,525 units) in the Ignis Liquidity Fund. The value of these investments at 31 December 2011 was £169 million (2010: £168 million) and £53 million (2010: £148 million) respectively.

Information on other transactions with the pension schemes is included in note 32.

Transactions with key management personnel

The total compensation of key management personnel, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the Executive and Non-Executive Directors, are as follows:

	2011 £m	2010 £m
Salary and other short-term benefits	**4.8**	4.1
Equity compensation plans	**2.2**	3.1
Termination payments	**0.7**	0.5

Details of the shareholdings and emoluments of individual Directors are provided in the Remuneration report.

47. Contingent liabilities

During the year, the FSA completed its review of the categorisation of working capital to owners' funds relating to a transaction in 2006 by London Life Limited. The FSA concluded that no changes to the categorisation were required.

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 an immaterial contingent liability in this regard.

48. Group entities

As at 31 December 2011, 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 (life assurance company)	UK	Ordinary shares of £1
National Provident Life Limited (life assurance company	UK	Ordinary shares of £1
NPI Limited (life assurance company	UK	Ordinary shares of £1
Pearl Assurance Limited (life assurance company)	UK	'A' ordinary shares of £0.05 'B' ordinary shares of £1
PA (GI) Limited (general insurance company)	UK	Ordinary shares of £0.01 deferred shares of £0.25
Phoenix Life Limited (life assurance company)	UK	Ordinary shares of £1
Scottish Mutual International Limited (life assurance company)	ROI	Ordinary shares of €1.25
Non-insurance companies		
Ignis Asset Management Limited (investment management company)	UK	Ordinary shares of £1
Ignis Fund Managers Limited (unit trust management company)	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 'C' 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 (reassurance company)	Bermuda	'A' ordinary shares of £1 'B' ordinary shares of £1 and Preference 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 and

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned unless otherwise indicated)
		Preference shares of £1
PGH (LC2) Limited (finance company)	UK	Ordinary shares of £1 and Preference shares of £1
PGH (MC1) Limited (finance company)	UK	Ordinary shares of £1 and Preference shares of £1

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned unless otherwise indicated)
PGH (MC2) Limited (finance company)	UK	Ordinary shares of £1 and Preference shares of £1
PGH (TC1) Limited (holding company)	UK	'A' ordinary shares of £1 and Preference shares of £1
PGH (TC2) Limited (holding company)	UK	'A' ordinary shares of £1 and Preference shares of £1
Pearl Group Holdings (No. 1) Limited (finance company)	UK	Ordinary shares of £0.05
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 (management services company)	UK	Ordinary shares of £1
PGS 2 Limited (finance company)	UK	Ordinary shares of £1
Pearl Group Management Services Limited (management services 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	66% of ordinary shares of £0.25

The information disclosed above is only in respect of those undertakings which materially 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.

49. Events after the reporting period

On 22 March 2012 the Board recommended a final dividend of £0.21 per share (2010: £0.21 per share) for the year ended 31 December 2011. Payment of the final dividend is subject to compliance with the processes set out in the Group's main credit facilities and shareholder approval at the AGM. The cost of this dividend has not been recognised as a liability in the financial statements for 2011 and will be charged to the statement of changes in equity in 2012.

R Sandler
C Bannister
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, Jersey

22 March 2012

ASSET DISCLOSURES

In this section

ADDITIONAL LIFE COMPANY ASSET DISCLOSURES

Additional life company asset disclosures The analysis of the asset portfolio provided below comprises the assets held by the Group's life companies including stock lending collateral. It excludes other Group assets such as cash held in the holding and service companies and Ignis; the assets held by the non-controlling interest in collective investment schemes and UKCPT; and are net of derivative liabilities.

The following table provides an overview of the exposure by asset category of the Group's life companies' shareholder and policyholder funds:

31 December 2011

Carrying value	**Shareholder and non-profit funds[1] £m**	**Participating[1] supported £m**	**Participating[2] non-supported £m**	**Unit-linked[2] £m**	**Total[3] £m**
Cash and cash equivalents	**3,280**	**965**	**7,493**	**1,035**	**12,773**
Debt securities – gilts	**3,202**	**1,883**	**12,093**	**886**	**18,064**
Debt securities – bonds	**7,570**	**2,279**	**10,099**	**870**	**20,818**
Equity securities	**390**	**17**	**6,631**	**7,436**	**14,474**
Property investments	**153**	**184**	**759**	**306**	**1,402**
Other investments[4]	**1,687**	**(79)**	**4,173**	**35**	**5,816**
As at 31 December 2011	**16,282**	**5,249**	**41,248**	**10,568**	**73,347**

1 Includes assets where shareholders of the life companies bear the investment risk.

2 Includes assets where policyholders bear most of the investment risk. In the second half of 2011 two with-profit funds moved from 'Participating supported' to 'Participating non-supported' as they no longer require shareholder support.

3 This information is presented on a look through basis to underlying funds where available.

4 Includes repurchase loans of £3,003 million, policy loans of £15 million, other loans of £41 million, net derivatives of £1,797 million and other investments of £960 million.

30 June 2011

Carrying value	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
Cash and cash equivalents	2,650	2,144	5,441	1,007	11,242
Debt securities – gilts	2,974	4,632	7,742	891	16,239
Debt securities – bonds	7,127	5,355	7,783	885	21,150
Equity securities	401	818	6,621	8,438	16,278
Property investments	153	132	887	339	1,511
Other investments[1]	799	586	1,895	12	3,292
As at 30 June 2011	14,104	13,667	30,369	11,572	69,712

1 Includes repurchase loans of £1,772 million, policy loans of £17 million, other loans of £30 million, net derivatives of £509 million and other investments of £964 million.

31 December 2010 comparatives have not been provided. It was considered more relevant to instead provide an update on the exposures disclosed at 30 June 2011, which were detailed in the Group's 2011 Interim Report.

The following table analyses by type the debt securities of the life companies:

31 December 2011

Analysis by type of debt securities	**Shareholder and non-profit funds £m**	**Participating supported £m**	**Participating non-supported £m**	**Unit-linked £m**	**Total £m**
Gilts	**3,202**	**1,883**	**12,093**	**886**	**18,064**
Other government and supranational[1]	**1,460**	**670**	**2,151**	**169**	**4,450**

Corporate – financial institutions	**2,230**	**666**	**3,603**	**206**	**6,705**
Corporate – other	**3,547**	**481**	**3,112**	**480**	**7,620**
Asset backed securities ('ABS')	**333**	**462**	**1,233**	**15**	**2,043**
As at 31 December 2011	**10,772**	**4,162**	**22,192**	**1,756**	**38,882**

1 Includes debt issued by governments; public and statutory bodies; government backed institutions and supranationals.

30 June 2011

Analysis by type of debt securities	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
Gilts	2,974	4,632	7,742	891	16,239
Other government and supranational	1,438	1,259	1,531	197	4,425
Corporate – financial institutions	2,088	2,025	2,745	251	7,109
Corporate – other	3,358	1,338	2,163	424	7,283
Asset backed securities	243	733	1,344	13	2,333
As at 30 June 2011	10,101	9,987	15,525	1,776	37,389

The life companies' debt portfolio was £38.9 billion at 31 December 2011. Shareholders had direct exposure to £14.9 billion of these assets (including supported participating funds), of which 95% of rated securities were investment grade. The shareholders' credit risk exposure to the non-supported participating funds is primarily limited to the shareholders' share of future bonuses. Shareholders' credit risk exposure to the unit-linked funds is limited to the level of asset manager fee which is dependent on the underlying assets.

Sovereign and supranational debt represented 48% of the debt portfolio in respect of shareholder exposure, or £7.2 billion, at 31 December 2011. The vast majority of the life companies' exposure to sovereign and supranational debt holdings is to UK gilts.

The following table sets out a breakdown of the life companies' sovereign and supranational debt security holdings by country:

31 December 2011

Analysis of sovereign and supranational debt security holdings by country	**Shareholder and non-profit funds £m**	**Participating supported £m**	**Participating non-supported £m**	**Unit-linked £m**	**Total £m**
UK	**3,211**	**1,884**	**12,112**	**887**	**18,094**
European Investment Bank	**525**	**365**	**862**	**57**	**1,809**
USA	**35**	**16**	**34**	**30**	**115**
Germany	**673**	**245**	**936**	**29**	**1,883**
France	**119**	**–**	**72**	**5**	**196**
Netherlands	**27**	**–**	**24**	**3**	**54**
Portugal	**–**	**–**	**–**	**–**	**–**
Italy	**1**	**–**	**93**	**6**	**100**
Ireland	**–**	**–**	**2**	**–**	**2**
Greece	**–**	**–**	**–**	**–**	**–**
Spain	**–**	**8**	**36**	**2**	**46**
Other – non-Eurozone	**10**	**25**	**34**	**30**	**99**
Other – Eurozone	**61**	**10**	**39**	**6**	**116**
As at 31 December 2011	**4,662**	**2,553**	**14,244**	**1,055**	**22,514**

30 June 2011

Analysis of sovereign and supranational debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	2,974	4,632	7,742	891	16,239
European Investment Bank	524	573	612	78	1,787

USA	40	134	89	28	291
Germany	636	431	591	32	1,690
France	56	10	35	4	105
Netherlands	33	10	31	5	79
Luxembourg	–	–	–	4	4
Portugal	–	–	10	–	10
Italy	89	24	90	9	212
Ireland	2	–	–	–	2
Greece	–	–	–	–	–
Spain	22	24	21	2	69
Other	36	53	52	35	176
As at 30 June 2011	4,412	5,891	9,273	1,088	20,664

At 31 December 2011, the life companies had £9 million shareholder exposure to sovereign debt of the Peripheral Eurozone, defined as Portugal, Italy, Ireland, Greece and Spain. This exposure has been reduced from £161 million at 30 June 2011. This reduction of £152 million reflects a decision to dispose of Peripheral Eurozone sovereign debt in certain funds and also includes £40 million arising from the reclassification of two with-profit funds from 'Participating supported' to 'Participating non-supported'.

All of the life companies' debt securities are held at fair value through profit or loss under IAS 39, and therefore already reflect any reduction in value between the date of purchase and the balance sheet date.

The life companies have in place a comprehensive database that consolidates credit exposures across counterparties, geographies and business lines. This database is used for credit monitoring, stress testing and scenario planning. The life companies continue to manage their balance sheets prudently and have taken extra measures to ensure their market exposures remain within risk appetite. With effect from 31 December 2011, the European government bond benchmarks have been strengthened for funds with non-discretionary mandates.

The following table sets out a breakdown of the life companies' financial institution corporate debt security holdings by country:

31 December 2011

Analysis of financial institution corporate debt security holdings by country	**Shareholder and non-profit funds £m**	**Participating supported £m**	**Participating non-supported £m**	**Unit-linked £m**	**Total £m**
UK	**1,171**	**504**	**1,962**	**126**	**3,763**
USA	**326**	**73**	**447**	**18**	**864**
Germany	**46**	**1**	**58**	**–**	**105**
France	**143**	**20**	**287**	**12**	**462**
Netherlands	**313**	**46**	**559**	**40**	**958**
Portugal	**–**	**–**	**–**	**–**	**–**
Italy	**5**	**3**	**16**	**–**	**24**
Ireland	**68**	**1**	**9**	**–**	**78**
Greece	**–**	**–**	**–**	**–**	**–**
Spain	**10**	**1**	**23**	**1**	**35**
Other – non-Eurozone	**90**	**14**	**147**	**5**	**256**
Other – Eurozone	**58**	**3**	**95**	**4**	**160**
As at 31 December 2011	**2,230**	**666**	**3,603**	**206**	**6,705**

30 June 2011

Analysis of financial institution corporate debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	944	1,208	1,290	123	3,565
USA	307	272	385	22	986
Germany	78	7	51	–	136

France	195	75	219	25	514
Netherlands	228	121	306	57	712
Portugal	–	–	–	–	–
Italy	35	24	38	–	97
Ireland	12	81	16	–	109
Greece	–	–	–	–	–
Spain	102	65	138	10	315
Other	187	172	302	14	675
As at 30 June 2011	2,088	2,025	2,745	251	7,109

The life companies had £88 million shareholder exposure to financial institution corporate debt of the Peripheral Eurozone at 31 December 2011. This exposure has been reduced from £319 million at 30 June 2011, a reduction of £231 million, of which £70 million is accounted for by the reclassification of certain holdings from Spain to the UK to better reflect the geographical exposure and £48 million by the reclassification of two with-profit funds from 'Participating supported' to 'Participating non-supported'. The £2,896 million total shareholder exposure comprised £2,148 million senior debt, £261 million Tier 1 debt and £487 million Tier 2 debt.

Indirect exposure

The £2,896 million shareholder exposure to financial institution corporate debt comprised £1,554 million bank debt and £1,342 million non-bank debt.

For each of the life companies' significant financial institution counterparties, industry and other data has been used to assess the exposure of the individual counterparties to Peripheral Eurozone markets. As part of the Group's risk appetite framework and analysis of shareholder exposure to a worsening of the Eurozone situation, this assessment has been used to identify counterparties considered to be most at risk from Peripheral Eurozone sovereign defaults. The financial impact on these counterparties, and the contagion impact on the rest of the shareholder corporate bond portfolio, is assessed under various Eurozone scenarios and assumptions. This analysis is regularly reviewed to reflect the latest Eurozone outlook, economic data and changes to asset portfolios. The results are used to inform the Group's views on whether any management actions are required.

The following table sets out a breakdown of the life companies' corporate – other debt security holdings by country:

31 December 2011

Analysis of corporate – other debt security holdings by country	**Shareholder and non-profit funds £m**	**Participating supported £m**	**Participating non-supported £m**	**Unit-linked £m**	**Total £m**
UK	**1,391**	**244**	**1,556**	**381**	**3,572**
USA	**787**	**70**	**357**	**15**	**1,229**
Germany	**56**	**2**	**65**	**6**	**129**
France	**408**	**82**	**342**	**18**	**850**
Netherlands	**403**	**56**	**374**	**24**	**857**
Portugal	**–**	**–**	**–**	**–**	**–**
Italy	**67**	**3**	**71**	**6**	**147**
Ireland	**10**	**–**	**9**	**–**	**19**
Greece	**8**	**–**	**2**	**–**	**10**
Spain	**105**	**3**	**80**	**6**	**194**
Other – non-Eurozone	**95**	**19**	**129**	**10**	**253**
Other – Eurozone	**217**	**2**	**127**	**14**	**360**
As at 31 December 2011	**3,547**	**481**	**3,112**	**480**	**7,620**

30 June 2011

Analysis of corporate – other debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	969	496	891	296	2,652

USA	650	195	289	28	1,162
Germany	287	170	181	18	656
France	392	176	253	14	835
Netherlands	102	19	41	1	163
Luxembourg	173	3	13	5	194
Portugal	–	–	–	–	–
Italy	97	35	82	8	222
Ireland	30	9	16	3	58
Greece	7	–	–	–	7
Spain	100	50	98	15	263
Other	551	185	299	36	1,071
As at 30 June 2011	3,358	1,338	2,163	424	7,283

The following table sets out a breakdown of the life companies' ABS holdings by country:

31 December 2011

Analysis of ABS holdings by country	**Shareholder and non-profit funds £m**	**Participating supported £m**	**Participating non-supported £m**	**Unit-linked £m**	**Total £m**
UK	**273**	**321**	**802**	**15**	**1,411**
USA	**29**	**–**	**35**	**–**	**64**
Germany	**5**	**44**	**139**	**–**	**188**
France	**–**	**10**	**25**	**–**	**35**
Netherlands	**3**	**36**	**98**	**–**	**137**
Portugal	**–**	**–**	**2**	**–**	**2**
Italy	**–**	**10**	**31**	**–**	**41**
Ireland	**18**	**19**	**48**	**–**	**85**
Greece	**–**	**–**	**–**	**–**	**–**
Spain	**5**	**18**	**33**	**–**	**56**
Other – non-Eurozone	**–**	**4**	**20**	**–**	**24**
Other – Eurozone	**–**	**–**	**–**	**–**	**–**
As at 31 December 2011	**333**	**462**	**1,233**	**15**	**2,043**

30 June 2011

Analysis of ABS holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	211	585	1,002	13	1,811
USA	19	21	17	–	57
Germany	–	–	–	–	–
France	–	8	19	–	27
Netherlands	13	44	121	–	178
Portugal	–	–	–	–	–
Italy	–	9	28	–	37
Ireland	–	31	95	–	126
Spain	–	14	38	–	52
Other	–	21	24	–	45
As at 30 June 2011	243	733	1,344	13	2,333

The following table sets out the credit rating analysis of the debt portfolio at 31 December 2011:

Credit rating analysis of debt portfolio	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
AAA	**5,067**	**2,977**	**15,190**	**768**	**24,002**
AA	**701**	**264**	**1,005**	**89**	**2,059**
A	**1,997**	**638**	**2,612**	**148**	**5,395**
BBB	**1,615**	**211**	**2,236**	**197**	**4,259**
BB	**127**	**29**	**230**	**17**	**403**
B and below	**544**	**1**	**77**	**1**	**623**
Non-rated	**721**	**42**	**842**	**536**	**2,141**
As at 31 December 2011	**10,772**	**4,162**	**22,192**	**1,756**	**38,882**

30 June 2011

Credit rating analysis of debt portfolio	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
AAA	4,869	6,158	8,563	712	20,302
AA	511	549	798	80	1,938
A	1731	1,427	1,822	145	5,125
BBB	1,374	708	1,336	164	3,582
BB	337	40	110	6	493
B and below	710	10	78	2	800
Non-rated	569	1,095	2,818	667	5,149
As at 30 June 2011	10,101	9,987	15,525	1,776	37,389

97% of rated securities were investment grade at 31 December 2011 (96%: 30 June 2011). The percentage of rated securities that were investment grade in relation to the shareholder and policyholder exposures were 95% and 99% respectively (94% and 99% respectively: 30 June 2011).

MCEV SUPPLEMENTARY INFORMATION

The Group’s primary measure of long-term shareholder value is MCEV. MCEV remained resilient in the period, growing by £14 million.

In this section

STATEMENT OF DIRECTORS’ RESPONSIBILITIES

For the year ended 31 December 2011

When compliance with the CFO Forum MCEV principles published in October 2009 is stated those principles require the Directors to prepare supplementary information in accordance with the MCEV principles and to disclose and provide reasons for any non-compliance with the principles.

The MCEV methodology adopted by the Group is in accordance with these MCEV principles with the exception of:

- risk-free rates have been defined as the annually compounded UK Government bond nominal spot curve plus 10 basis points rather than as the swap rate curve;
- the value of asset management and the management service companies has been included on an IFRS basis; and
- no allowance for the costs of residual non-hedgeable risk has been made.

Further detail on these exceptions is included in note 1, Basis of preparation.

Specifically, the Directors have:

- determined assumptions on a realistic basis, having regard to past, current and expected future experience and to relevant external data, and then applied them consistently;
- made estimates that are reasonable and consistent; and
- provided additional disclosures when compliance with the specific requirements of the MCEV principles is insufficient to enable users to understand the impact of particular transactions, other events and conditions and the Group's financial position and financial performance.

Clive Bannister Group Chief Executive

Alastair Lyons Audit Committee Chairman

St Helier, Jersey
22 March 2012

INDEPENDENT AUDITOR'S REPORT TO THE DIRECTORS OF PHOENIX GROUP HOLDINGS ON THE CONSOLIDATED PHOENIX GROUP MARKET CONSISTENT EMBEDDED VALUE ('MCEV')

We have audited the Consolidated Phoenix Group MCEV ('Phoenix Group MCEV') supplementary information for the year ended 31 December 2011, which comprises the Summarised consolidated income statement – Group MCEV basis, MCEV earnings per ordinary share, Statement of consolidated comprehensive income – Group MCEV basis, Reconciliation of movement in equity – Group MCEV basis, Group MCEV analysis of earnings, Reconciliation of Group IFRS equity to Group MCEV net worth and related notes. The Phoenix Group MCEV supplementary information has been prepared by the Directors of Phoenix Group Holdings in accordance with the basis of preparation set out on pages 179 to 181.

Directors' responsibilities for the Phoenix Group MCEV supplementary information

The Directors are responsible for the preparation of this Phoenix Group MCEV supplementary information in accordance with the basis of preparation set out on pages 179 to 181 and for such internal control as the Directors determine is necessary to enable the preparation of supplementary information that is free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the Phoenix Group MCEV supplementary information based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require us to comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Phoenix Group MCEV supplementary information is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Phoenix Group MCEV supplementary information. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the Phoenix Group MCEV supplementary information, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Group's preparation of the Phoenix Group MCEV supplementary information in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the Phoenix Group MCEV supplementary information.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion the Phoenix Group MCEV supplementary information, for the year ended 31 December 2011, has been prepared, in all material respects, in accordance with the basis of preparation set out on pages 179 to 181.

Basis of accounting and restriction on use

Without modifying our opinion, we draw attention to pages 179 to 181 of the Phoenix Group MCEV supplementary information, which describe the basis of preparation. The Phoenix Group MCEV supplementary information is prepared to comply with the basis of preparation set out on pages 179 to 181. As a result, the Phoenix Group MCEV supplementary information may not be suitable for another purpose. This report, including the opinion, has been prepared for and only for the Group's Directors as a body in accordance with our letter of engagement dated 15 June 2011 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other matter

Ernst & Young Accountants LLP have reported separately on the IFRS consolidated financial statements of Phoenix Group Holdings for the year ended 31 December 2011. The information contained in the Phoenix Group MCEV supplementary information should be read in conjunction with the IFRS consolidated financial statements.

Ernst & Young LLP

London

22 March 2012

SUMMARISED CONSOLIDATED INCOME STATEMENT – GROUP MCEV BASIS

For the year ended 31 December 2011

	2011 £m	2010 £m
Life MCEV operating earnings	**556**	758
Management services operating profit	**17**	20
Ignis Asset Management operating profit	**46**	46
Group costs	**(84)**	(70)
Group MCEV operating earnings before tax	**535**	754
Economic variances on life business	**(426)**	101
Economic variances on non-life business	**38**	(38)
Other non-operating variances on life business	**(12)**	(54)
Non-recurring items on non-life business	**(9)**	(75)
Finance costs attributable to owners	**(123)**	(168)
Group MCEV earnings before tax	**3**	520
Tax on operating earnings	**(141)**	(211)
Tax on non-operating earnings	**169**	(54)
Total tax	**28**	(265)
Group MCEV earnings after tax	**31**	255

MCEV EARNINGS PER ORDINARY SHARE

for the year ended 31 December 2011

	2011 £m	2010 £m
Group MCEV operating earnings after tax		
Basic[1]	**229.1p**	363.2p
Diluted[2]	**229.1p**	363.2p
Group MCEV earnings after tax		
Basic[1]	**18.0p**	170.6p
Diluted[2]	**18.0p**	170.6p

1 Based on 172 million shares (2010: 149 million) as set out in note 15 of the IFRS consolidated financial statements.

2 Based on 172 million shares (2010: 149 million), allowing for warrants in issue as set out in note 15 of the IFRS consolidated financial statements.

The earnings on life 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 26.5% (31 December 2010: 28%).

STATEMENT OF CONSOLIDATED COMPREHENSIVE INCOME – GROUP MCEV BASIS

For the year ended 31 December 2011

	2011 £m	2010 £m
Group MCEV earnings for the year after tax	**31**	255
Other comprehensive income		
Actuarial gains on defined benefit pension scheme (net of tax)[1]	**32**	27
Total comprehensive income for the year	**63**	282

1 The actuarial gain on the Pearl Group Staff Pension Scheme reflected in the MCEV does not include the IFRS surplus at 31 December 2011.

RECONCILIATION OF MOVEMENT IN EQUITY – GROUP MCEV BASIS

For the year ended 31 December 2011

	2011 £m	2010 £m
Group MCEV equity at 1 January	**2,104**	1,827
Total comprehensive income for the year	**63**	282
Issue of share capital	**–**	33
Conversion of warrants into ordinary shares	**–**	7
Movement in equity for equity-settled share-based payments	**6**	(2)
Dividends paid on ordinary shares	**(72)**	(54)
Shares issued in lieu of dividends	**17**	11
Total capital and dividend flows – external	**(49)**	(5)
Group MCEV equity at 31 December	**2,118**	2,104

GROUP MCEV ANALYSIS OF EARNINGS

For the year ended 31 December 2011

		Non-covered business			
	Covered business MCEV £m	Management services IFRS £m	Asset Management IFRS £m	Other Group companies[1] IFRS £m	Group MCEV £m
Group MCEV at 1 January 2011	**4,517**	**80**	**54**	**(2,547)**	**2,104**
Operating MCEV earnings (after tax)	**409**	**13**	**34**	**(62)**	**394**
Non-operating MCEV earnings (after tax)	**(322)**	**15**	**(1)**	**(55)**	**(363)**
Total MCEV earnings	**87**	**28**	**33**	**(117)**	**31**
Other comprehensive income	–	–	–	**32**	**32**

Capital and dividend flows – internal	**(800)**	**(26)**	**(19)**	**845**	**–**
Capital and dividend flows – external	**–**	**–**	**–**	**(49)**	**(49)**
Closing value at 31 December 2011	**3,804**	**82**	**68**	**(1,836)**	**2,118**

1 Comprises the Group holding companies that do not form part of the Phoenix Life and Ignis Asset Management divisions.

For the year ended 31 December 2010

		Non-covered business			
	Covered business MCEV £m	Management services IFRS £m	Asset Management IFRS £m	Other Group companies[1] IFRS £m	Group MCEV £m
Group MCEV at 1 January 2010	4,731	56	39	(2,999)	1,827
Operating MCEV earnings (after tax)	546	14	33	(50)	543
Non-operating MCEV earnings (after tax)	34	(54)	–	(268)	(288)
Total MCEV earnings	580	(40)	33	(318)	255
Other comprehensive income	–	–	–	27	27
Capital and dividend flows – internal[2]	(794)	64	(18)	748	–
Capital and dividend flows – external	–	–	–	(5)	(5)
Closing value at 31 December 2010	4,517	80	54	(2,547)	2,104

1 Comprises the Group holding companies that do not form part of the Phoenix Life and Ignis Asset Management divisions.

2 Includes a re-allocation of a £250 million loan asset from Covered business to Other Group companies. This does not affect the closing Group MCEV or MCEV earnings

RECONCILIATION OF GROUP IFRS EQUITY TO MCEV NET WORTH

	2011 £m	2010 £m
Group net assets attributable to owners of the parent as reported under IFRS	**1,652**	1,580
Goodwill and other intangibles in accordance with IFRS removed (net of tax)	**(440)**	(391)
Value of in-force business in accordance with IFRS removed (net of tax)	**(1,289)**	(1,345)
Adjustments to IFRS reserving	**(47)**	(138)
Tax adjustments	**8**	(90)
Revalue listed debt to market value	**161**	94
Eliminate value of contingent loan asset[1]	**(160)**	(276)
Fair value adjustments[2]	**(43)**	5
Eliminate pension scheme surpluses[3] (net of tax)	**(380)**	(112)
Other adjustments	**27**	30
MCEV net worth attributable to owners of the parent	**(511)**	(643)
MCEV value of in-force business included (net of tax) as set out in note 2	**2,629**	2,747
Closing Group MCEV	**2,118**	2,104

1 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.

2 Investments carried at amortised cost under IFRS are revalued at market value.

3 The pension scheme surpluses removed are the economic surpluses of the Pearl Group Staff Pension Scheme and PGL Pension Scheme net of tax, as described in note 32 to the IFRS consolidated financial statements.

NOTES TO THE MCEV FINANCIAL STATEMENTS

1. Basis of preparation

Overview
The supplementary information on pages 175 to 187 has been prepared on a Market Consistent Embedded Value ('MCEV') basis except for the items described further below.

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 10 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 focused 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); and
- the asset management and management service companies' values are calculated on an IFRS basis. 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 holding companies at their IFRS net asset value.

A gradual reduction in the UK corporation tax rate from 28% to 24% over four years was announced in the Emergency Budget of 22 June 2010 with further 1% reductions being announced in each of the Budgets of 23 March 2011 and 21 March 2012. The Finance (No. 2) Act 2010 included the first of the 1% rate reductions with effect from April 2011, a further 1% reduction was substantively enacted on 29 March 2011 under the Provisional Collection of Taxes Act 1968 and a further 1% reduction was included in the Finance Act 2011. Further reductions are to be introduced by future legislation. The 2011 MCEV includes the impact of the tax rate being reduced to 25%. The impact of the further 3% reduction of rate is not expected to be material.

On 23 March 2011, HMRC issued a technical note on 'Solvency II and the Taxation of Insurance Companies', outlining changes to the taxation of UK insurance companies with effect from 2013. The Group has been actively involved in consulting with HMRC and HM Treasury on the detail of the new rules, with the aim of ensuring that the Group's policyholders and shareholders are, as far as possible, not adversely affected by the changes.

The consultation process is still ongoing in relation to certain aspects of the new rules, and as a consequence of this and the complexity of the proposed changes it has not been possible to estimate their potential future impact on the Group MCEV.

Covered business
The MCEV calculations cover all long-term insurance business written by the Group, but exclude Ignis Asset Management and the management service companies.

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.

The key components of MCEV are net worth plus the value of in-force covered business.

a) Net worth
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 or 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.

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.

Required capital is defined as the minimum regulatory capital requirement, which is the greater of Pillar1 and Pillar 2 capital requirements, plus the capital required under the Group's capital management policy.

This equates to 128% (2010: 119%) of the minimum regulatory capital requirement.

Solvency II will introduce a new capital regime for insurers from the end of 2013. These disclosures do not take account of the impact of the change in regime as this is still under development.

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 CNHR has been made, as in the opinion of the Directors, the CNHR 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 CNHR calculated in accordance with the CFO Forum principles and guidance, and therefore without anticipating further risk management actions, has been disclosed below.

For with-profit business the CNHR would increase the TVFOGs by £46 million (2010: £64 million).

For other business the cost would be £130 million (2010: £137 million). This equates to an equivalent average cost of capital charge of 1.2% (2010: 1.2%). 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 Limited recourse bonds are backed by surpluses that are expected to emerge on blocks of its unit linked and unitised with-profit 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-profit 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-profit 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

	2011 £m	2010 £m
Net worth	**1,175**	1,770
PVFP	**2,846**	3,022
TVFOG	**(108)**	(113)
COC	**(109)**	(162)
Total VIF	**2,629**	2,747
	3,804	4,517

The net worth of covered business of £1,175 million at 31 December 2011 (2010: £1,770 million) consists of £11 million of free surplus in excess of required capital which includes the capital required under the Group's capital management policy (2010: £670 million). This does not include the IFRS net assets of management services of £82 million (2010: £80 million) as shown in the free surplus reconciliation for Phoenix Life on page 25.

3. Analysis of covered business MCEV earnings (after tax)

	Net worth £m	**VIF £m**	**Total Life MCEV £m**
Life MCEV at 1 January 2011	**1,770**	**2,747**	**4,517**

New business value	**7**	**6**	**13**
Expected existing business contribution (reference rate)[1]	**65**	**115**	**180**
Expected existing business contribution (in excess of reference rate)[2]	**33**	**41**	**74**
Transfer from VIF to net worth	**212**	**(212)**	**–**
Experience variances	**122**	**59**	**181**
Assumption changes	**(28)**	**10**	**(18)**
Other operating variances	**8**	**(29)**	**(21)**
Life MCEV operating earnings	**419**	**(10)**	**409**
Economic variances	**(272)**	**(41)**	**(313)**
Other non-operating variances	**(4)**	**(5)**	**(9)**
Total Life MCEV earnings	**143**	**(56)**	**87**
Capital and dividend flows	**(738)**	**(62)**	**(800)**
Life MCEV at 31 December 2011	**1,175**	**2,629**	**3,804**

1 Expected existing business contribution (reference rate) represents the expected return on the opening MCEV at the long-term risk-free rate.

2 Expected existing business contribution (in excess of reference rate) represents the additional expected return above the risk-free rate arising from long-term risk premiums on equities, property and corporate bonds.

	Net worth £m	VIF £m	Total Life MCEV £m
Life MCEV at 1 January 2010	2,234	2,497	4,731
New business value	16	3	19
Expected existing business contribution (reference rate)	102	122	224
Expected existing business contribution (in excess of reference rate)	43	39	82
Transfer from VIF to net worth	145	(145)	–
Experience variances	35	229	264
Assumption changes	53	(91)	(38)
Other operating variances	(28)	23	(5)
Life MCEV operating earnings	366	180	546
Economic variances	(94)	167	73
Other non-operating variances	58	(97)	(39)
Total Life MCEV earnings	330	250	580
Capital and dividend flows	(794)	–	(794)
Life MCEV at 31 December 2010	1,770	2,747	4,517

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.

	Premium £m	MCEV £m	MCEV/ Premium
Year ended 31 December 2011	**274**	**13**	**5%**
Year ended 31 December 2010	388	19	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					
Present value of future profits (PVFP)	1-5 £m	6-10 £m	11-15 £m	16-20 £m	20+ £m	Total £m
31 December 2011	**1,135**	**683**	**455**	**291**	**282**	**2,846**
31 December 2010	1,147	848	488	271	268	3,022

6. 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:

	2011		2010	
Term	**Gilt Yield +10bps**	**Swap yield**	Gilt Yield +10bps	Swap yield
1 year	**0.32%**	**1.09%**	0.73%	0.88%
5 years	**1.14%**	**1.61%**	2.51%	2.69%
10 years	**2.20%**	**2.32%**	3.79%	3.70%
15 years	**2.85%**	**2.79%**	4.37%	4.08%
20 years	**3.21%**	**3.02%**	4.58%	4.17%

The swaps rates above are only applicable to sensitivity (16) as disclosed in note 7.

(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 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. The additional yield above risk-free rates implied by the calculated liquidity premium is as follows:

	2011	2010
Additional yield over risk-free rates	**0.90%**	0.48%

Inflation

For purposes of the MCEV calculation, the rate of increase in the UK Retail Price Index (‘RPI’) as at 31 December 2011 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 2011 (2010: RPI + 100 basis points).

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 2011. The scenario generator and calibration are consistent with those 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 10 basis points, consistent with the deterministic projections. Interest rate volatility is calibrated to swaption implied volatilities, as per the sample below.

	Option term (years)					
Interest rate volatility	**5**	**10**	**15**	**20**	**25**	**30**
2011 Swap term (years)						
5	**28.1%**	**19.5%**	**17.6%**	**16.1%**	**16.4%**	**16.2%**
10	**24.1%**	**18.0%**	**16.2%**	**15.3%**	**15.4%**	**14.9%**
20	**21.2%**	**16.1%**	**14.8%**	**13.8%**	**13.5%**	**13.0%**
30	**20.0%**	**15.0%**	**13.4%**	**12.3%**	**12.0%**	**11.5%**

	Option term (years)					
Interest rate volatility	5	10	15	20	25	30
2010 Swap term (years)						
5	17.5%	13.3%	13.6%	13.9%	14.7%	15.1%
10	15.8%	13.5%	13.6%	13.9%	14.5%	14.3%
20	15.2%	13.2%	13.2%	13.0%	13.0%	12.6%
30	14.6%	12.6%	12.2%	11.7%	11.5%	11.2%

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)					
Equity implied volatility (ATM)	**5**	**10**	**15**	**20**	**25**	**30**
2011	**25.8%**	**27.2%**	**27.5%**	**27.7%**	**27.8%**	**27.9%**
2010	24.3%	26.1%	26.4%	26.7%	26.8%	27.0%

Best estimate levels of volatility are assumed for directly held property. The model implied volatility for 2011 is 15% (2010: 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
The Group uses normalised investment returns in calculating the expected existing business contribution. The Group considers that an average return over the remaining term of our in-force business is more appropriate than using a short-term rate and is more consistent with the Group's expectation of longer term rates of return. Therefore, the Group calculates the expected contribution on existing business using a 15-year gilt rate at the beginning of the reporting period plus 10 basis points and long-term expectations of excess investment returns.

The table below sets outs the asset risk premiums used:

	2011	2010
Equities	**3.0%**	3.0%
Property	**2.0%**	2.0%
Gilts	**0.0%**	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 management 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 2011 includes Perpetual Reset Capital Securities with principal outstanding of £425 million (2010: £425 million) and subordinated debt with a face value of £200 million (2010: £200 million). 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:

	2011		2010	
	Face value (including accrued interest) £m	**Market value £m**	Face value (including accrued interest) £m	Market value £m
Listed debt and non-controlling interests				
Perpetual Reset Capital Securities	**444**	**256**	444	304
Subordinated debt	**211**	**139**	211	170

Unlisted debt has been included at face value:

	2011 Face value £m	2010 Face value £m
Unlisted debt		
Pearl and Impala facilities	**2,471**	2,639
Royal London PIK notes and facility	**111**	106

7. Sensitivity to assumptions

The table below summarises the key sensitivities of the MCEV of covered business at 31 December 2011:

	2011 Life MCEV £m	2010 Life MCEV £m
(1) Base	**3,804**	4,517
(2) 1% decrease in risk-free rates	**153**	183
(3) 1% increase in risk-free rates	**(157)**	(167)
(4) 10% decrease in equity market values	**(75)**	(105)
(5) 10% increase in equity market values	**71**	102
(6) 10% decrease in property market values	**(72)**	(77)
(7) 10% increase in property market values	**72**	76
(8) 100bps increase in credit spreads[1]	**(241)**	(267)
(9) 100bps decrease in credit spreads	**277**	250
(10) 25% increase in equity/property implied volatilities	**(20)**	(35)
(11) 25% increase in swaption implied volatilities	**(11)**	(23)
(12) 25% decrease in lapse rates and paid-up rates	**(43)**	(21)
(13) 5% decrease in annuitant mortality	**(203)**	(166)
(14) 5% decrease in non-annuitant mortality	**27**	35
(15) Required capital equal to the minimum regulatory capital[2]	**32**	31
(16) Swap curve as reference rate, retaining appropriate liquidity premiums	**(50)**	(272)

1 44bps is assumed to relate to default risk.

2 Minimum regulatory capital is defined as the greater of Pillar 1 and Pillar 2 capital requirements without any allowance for the Group's capital management policy.

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.

ADDITIONAL INFORMATION

In this section

SHAREHOLDER INFORMATION

Annual General Meeting

Our Annual General Meeting will be held on 3 May 2012 at 1pm.

The voting results for our 2012 AGM, including proxy votes and votes withheld, will be available on the Group's website shortly after the meeting.

Shareholder profile as at 31 December 2011

Analysis of shareholders	No. of shareholders	%	No. of shares	%
Individual	110	22.04	3,542,735	2.03
Banks and nominee companies	343	68.74	116,405,042	66.72
Insurance companies	7	1.40	9,828,198	5.63
Other entities	39	7.82	44,696,840	25.62
Total	499	100.00	174,472,815	100.00

Range of shareholdings	No. of shareholders	%	No. of shares	%
1–1,000	127	25.45	65,077	0.04
1,001–5,000	82	16.43	217,305	0.12
5,001–10,000	46	9.22	328,569	0.19
10,001–250,000	155	31.06	10,522,777	6.03
250,001–500,000	24	4.81	8,605,215	4.93
500,001 and above	65	13.03	154,733,872	88.69
Total	499	100.00	174,472,815	100.00

Shareholder services

Managing your shareholding

Our registrar, Computershare, maintains the Company's Register of Members. Shareholders may request a hard copy of this Annual Report from our registrar and if you have any further queries in respect of your shareholding, please contact them directly using the contact details set out below.

Registrar details

Computershare Investor Services (Jersey) Limited
Queensway House
Hilgrove Street
St Helier
Jersey JE1 1ES

Shareholder helpline number	+44 (0) 870 707 4040
Fax number	+44 (0) 870 873 5851
Shareholder helpline e-mail address	info@computershare.co.je

Dividend mandates

Shareholders may find it convenient to have their dividends paid directly to their bank or building society account. If you wish to take advantage of this facility please call Computershare and request a 'Dividend Mandate' form.

Scrip dividend alternative

The Company will be offering a scrip dividend alternative in relation to the recommended final dividend. Shareholders will be sent an information booklet which provide details of the terms of the scrip dividend alternative on or around 2 April 2012. The information booklet will also be made available on the Group's website within the investor relations section.

The information booklet will give guidance regarding how shareholders may elect to take up the scrip dividend alternative. Such elections must be received by the Company's registrar by 5pm on 25 April 2012.

Warning to shareholders

Over recent years, many companies have become aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters. These are typically from overseas-based 'brokers' who target UK shareholders, offering to sell them what often turn out to be worthless or high-risk shares in US or UK investments. These operations are commonly known as 'boiler rooms'.

Shareholders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free reports about the Company.

If you receive any unsolicited investment advice:

- Make sure you get the correct name of the person and organisation
- Check that they are properly authorised by the FSA before getting involved by visiting www.fsa.gov.uk/register/home.do
- Report the matter to the FSA by calling 0845 606 1234
- If the calls persist, hang up.

If you deal with an unauthorised firm, you would not be eligible to receive payment under the Financial Services Compensation Scheme. The FSA can also be contacted by completing an online form available at www.fsa.gov.uk/pages/doing/Regulated/Law/Alerts/form.shtml.

Details of any share dealing facilities that the Company endorses will be included in Company mailings.

More detailed information on this or similar activity can be found on the FSA website available at www.fsa.gov.uk/pages/consumerinformation.

Share price

You can access the current share price of Phoenix Group Holdings on the Group's website.

Group financial calendar for 2012

Annual General Meeting	3 May 2012
Announcement of first quarter interim management statement	4 May 2012
Announcement of unaudited six months' interim results	23 August 2012
Announcement of third quarter interim management statement	31 October 2012
Ordinary shares – 2011 final dividend	
Scrip mandate forms issued	2 April 2012
Ex-dividend date	4 April 2012
Scrip calculation period	4–12 April 2012
Record date	10 April 2012
Scrip election date	25 April 2012
Payment date for the recommended final dividend	8 May 2012

Forward-looking statements

The 2011 Annual Report and Accounts contains, and we may make other statements (verbal or otherwise) containing, forward-looking statements about the Group's current plans, goals and expectations relating to future financial conditions, performance, results, strategy and/or objectives.

Statements containing the words: 'believes', 'intends', 'expects', 'plans', 'seeks', 'targets', 'continues' and 'anticipates' or other words of similar meaning are forward-looking. Forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group's control. For example, certain insurance risk disclosures are dependent on the Group's choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that we have estimated. Other factors which could cause actual results to differ materially from those estimated by forward-looking statements include but are not limited to:

- Domestic and global economic and business conditions
- Asset prices
- Market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally
- The policies and actions of governmental and/or regulatory authorities, including, for example, new government initiatives related to the financial crisis and the effect of the European Union's 'Solvency II' requirements on the Group's capital maintenance requirements
- The impact of inflation, and deflation
- Market competition
- Changes in assumptions in pricing and reserving for insurance business (particularly with regard to mortality and morbidity trends, gender pricing and lapse rates)
- The timing, impact and other uncertainties of future acquisitions or combinations within relevant industries
- Risks associated with arrangements with third parties, including joint ventures
- Inability of reinsurers to meet obligations or unavailability of reinsurance coverage
- 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.

As a result, the Group's actual future financial condition, performance and results may differ materially from the plans, goals and expectations set out in the forward-looking statements within the 2011 Annual Report and Accounts. The Group undertakes no obligation to update any of the forward-looking statements contained within the 2011 Annual Report and Accounts or any other forward-looking statements it may make.

The 2011 Annual Report and Accounts has been prepared for the members of the Company and no one else. The Company, its Directors or agents do not accept or assume responsibility to any other person in connection with this document and any such responsibility or liability is expressly disclaimed. Nothing in the 2011 Annual Report and Accounts should be construed as a profit forecast.

GLOSSARY

ABI — Association of British Insurers – A trade association for the UK's insurance industry

ABS — Asset Backed Securities – A collateralised security whose value and income payments are derived from a specified pool of underlying assets

ACSM — Alternative Coupon Satisfaction Mechanism – The process through which the deferred coupon on certain securities is settled

AGM — Annual General Meeting – a meeting which companies with shareholders are required by law to hold

ALM — Asset Liability Management – Management of mismatches between assets and liabilities within risk appetite

Annuity policy — A policy that pays out regular benefit amounts, either immediately and for the remainder of a policyholder's lifetime (immediate annuity), or deferred to commence at some future date (deferred annuity)

Asset management — The management of assets using a structured approach to guide the act of acquiring and disposing of assets, with the objective of meeting defined investment goals and maximising value for investors, including policyholders

AST — Actuarial Systems Transformation – A project set up to rationalise and streamline the Group's actuarial systems, models and processes into a single actuarial modelling platform that is state of the art, scalable and able to meet our future demands

Black-Scholes — A mathematical model used to calculate the value of an option

BREEAM — Building Research Establishment Environmental Assessment Method – a voluntary measurement rating for green buildings that was established in the UK by the Building Research Establishment

BSP — Bonus Share Plan – A share incentive legacy plan which operated before the Company's

	shares were admitted to the LSE. No further awards will be made under this plan
CFO Forum	A high-level discussion group formed of the Chief Financial Officers of major European listed and non-listed insurance companies. Its aim is to discuss and influence the development of accounting, financial reporting and related regulatory developments in the insurance industry on behalf of its members
Closed life fund	A fund that no longer accepts new business. The fund continues to be managed for the existing policyholders
COC	Frictional Cost of Capital – 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
CNHR	Cost of residual non-hedgeable risk – The expected cost of non-hedgeable risks that can have an asymmetric impact on shareholder value to the extent these risks have not already been reflected in the PFVP or TVFOG. These can include both financial risks and non-financial risks such as mortality, persistency and expense risk
DPF	Discretionary Participation Feature – A contractual right under an insurance contract to receive, as a supplement to guaranteed benefits, additional benefits whose amount or timing is contractually at the discretion of the issuer
EBT	Employee Benefit Trust – A trust set up to enable its Trustee to purchase and hold shares to satisfy employee share-based incentive plan awards
Economic assumptions	Assumptions related to future interest rates, inflation, market value movements and tax
EEA	European Economic Area – Established on 1 January 1994 and is an agreement between Norway, Iceland, Liechtenstein and the European Union. It allows these countries to participate in the EU's single market without joining the EU
EIOPA	European Insurers and Occupational Pensions Authority – the Committee is composed of high-level representatives from the insurance and occupational pensions supervisory authorities of European Union member states and is currently consulting with the industry on the technical requirements of Solvency II
Euronext	A pan-European Stock Exchange based in Amsterdam, Holland
EV	Embedded Value – The value to equity shareholders of the net assets and expected future profits of a life company
Expense risk	The risk of financial or reputational losses arising from unexpected timing or value of expenses incurred
Experience variances	Current period differences between the actual experience incurred and the assumptions used in the calculation of embedded value or IFRS insurance liabilities
Financial Reporting Council	The UK's independent regulator responsible for promoting confidence in corporate governance and reporting
Free surplus	The amount of capital held in life companies in excess of that needed to support their minimum regulatory capital requirement, which is the greater of Pillar 1 and Pillar 2 capital requirements, plus the capital required under the Group's capital management policy
FSA	Financial Services Authority – The regulatory authority for the UK financial services industry
GAR	Guaranteed Annuity Rate – A rate available to certain pension policyholders to acquire an annuity at a contractually guaranteed conversion rate
GCO	Guaranteed Cash Option – An option through which exercise is accomplished by a payment in cash, rather than by delivering the underlying security
GCR	Group Capital Resources – In accordance with the UK capital adequacy regime for insurance groups, this is the aggregate of the individual capital resources for each of the regulated related undertakings less the book value of investments by the Group in those capital resources
GCRR	Group Capital Resource Requirement – In accordance with the UK's capital adequacy regime for insurance groups, it is the sum of the individual capital resource requirements for each of the regulated undertakings in the insurance group
Gearing	Net shareholder debt as a percentage of the sum of Group MCEV, net shareholder debt and the

	PVFP of Ignis
Group AUM	Group assets under management – This represents life company assets (excluding collateral on stock lending arrangements), Holding Company cash and third party assets managed by Ignis
HMRC	Her Majesty's Revenue and Customs
Holding Companies	Refers to Phoenix Group Holdings, Phoenix Life Holdings Limited, Pearl Group Holdings (No. 2) Limited, Impala Holdings Limited, Pearl Group Holdings (No. 1) Limited, PGH (TC1) Limited, PGH (TC2) Limited, PGH (MC1) Limited, PGH (MC2) Limited, PGH (LCA) Limited, PGH (LCB) Limited, PGH (LC1) Limited, PGH (LC2) Limited and Pearl Life Holdings Limited
ICA	Individual Capital Assessment – A life company's assessment of its capital requirements to ensure that assets exceed liabilities 99.5% of the time over a 1-year period or (in other words) to be able to withstand a one in 200 year event
IFRS	International Financial Reporting Standards – Accounting standards, Interpretations and the Framework adopted by the International Accounting Standards Board
IGD	Insurance Groups Directive – The European Directive setting out the current capital adequacy regime for insurance groups
IGD Excess Capital	IGD surplus plus policyholder and certain shareholder capital currently excluded under FSA rules from the calculation of the IGD surplus. The excluded capital relates to the surplus estate of the with-profit funds and other restricted surplus
IGD surplus	An FSA regulatory measure which calculates surplus capital at a group level. IGD surplus is defined as Group Capital Resources less the Group Capital Resource Requirement
IMC	Investment Management Contract – A contract between an investor and an investment manager
In-force	Long-term business written before the period end and which has not terminated before the period end
Inherited estate	The assets of the long-term with-profit funds less the realistic reserves for non-profit policies written into the non-profit fund, less asset shares aggregated across the with-profit policies and any additional amounts expected at the valuation date to be paid to in-force policyholders in the future in respect of smoothing costs and guarantees
IPO	Initial Public Offering
LDI	Liability Driven Investment – Refers to investing in assets which move in line with the value of liabilities. Ignis LDI strategies typically involve purchasing a mix of government bonds and other instruments which have similar sensitivity to interest rates and inflation as the liabilities, to protect against changes in the deficit between asset and liability values
LIBOR	London Interbank Offer Rate – The average interbank interest rate at which a selection of banks on the London money market are prepared to lend to one another
Longevity risk	The risk of financial or reputational losses arising from lower than expected number of deaths experienced on annuity products or greater than expected improvements in annuitant mortality
LSE	London Stock Exchange
LTICR	Long-Term Insurance Capital Requirement – Capital required to be held by life companies for regulatory purposes in respect of investment, expense and insurance risks on a Pillar 1 base
LTIP	Long-Term Incentive Plan – The part of an executive's remuneration designed to incentivise long-term value for shareholders through an award of shares with vesting contingent on employment and the satisfaction of stretching performance conditions linked to Group strategy
MCEV	Market Consistent Embedded Value – A measure of the consolidated value of shareholders' interests calculated using the Group's MCEV methodology as described in note 1 of the MCEV supplementary information
MG ALFA	An asset liability modelling system developed by Milliman that forms the foundation platform for actuarial modelling and is uniquely capable of meeting Solvency II requirements for enhanced stochastic modelling capability
Morbidity risk	The risk of financial or reputational losses arising from higher than expected number of inceptions on critical illness or income protection policies and lower than expected termination

	rates on income protection policies
Mortality risk	The risk of financial or reputational losses arising from higher than expected death claims on assurance products
MSA	Management Services Agreement – Contracts that exists between either Phoenix Life and management services companies or between management services companies and their outsourced partners
Net shareholder debt	Shareholder debt (including hybrid debt) less Holding Company cash and cash equivalents
Non-economic assumptions	Assumptions related to future levels of mortality, morbidity, persistency and expenses
Non-profit fund	A fund which is not a with-profit fund (see below)
Open Ended Investment Companies	A type of company or a fund in the UK that is structured to invest in other companies with the ability to adjust its investment criteria and fund size
Operating companies	Refers to the trading companies within Phoenix Life (which includes Opal Reassurance Limited) and all trading companies within Ignis Asset Management
Part VII transfer	The transfer of insurance policies under Part VII of FSMA 2000. The insurers involved can be in the same corporate group or in different groups. Transfers require the consent of the High Court, which will consider the views of the FSA and of an Independent Expert
Participating business	These are policies for which the premiums are paid into a separate fund and the policyholder has an entitlement to share in the profits of that fund
Pearl businesses	PGH (LCA) Limited, PGH (LCB) Limited, PGH (TC1) Limited, PGH (TC2) Limited and Opal Reassurance Limited, together with their subsidiaries, being the five companies acquired by Phoenix Group Holdings on 2 September 2009
Peripheral Eurozone	Refers to Portugal, Ireland, Italy, Greece and Spain
Persistency risk	The risk of financial or reputational losses arising from adverse movements in either surrender rates or persistency rates on policies with guaranteed benefits leading to losses. This includes the risk of greater than expected policyholder option exercise rates giving rise to increased claims costs
PIK	Payment-in-kind. Interest on a bond is paid other than in cash, most commonly by increasing the principal
Pillar 1 surplus	The excess of available capital resources over regulatory capital resource requirements as mandated by the FSA for individual insurance companies
Pillar 2 surplus	The excess of available capital resources over capital calculated on an economic basis required to ensure entities can meet their liabilities. It is based on a self-assessment methodology called the ICA (Individual Capital Assessment) which is reviewed by the FSA
PPFM	Principles and Practices of Financial Management – A publicly available document which explains how a company's with-profit business is run. As part of demonstrating that customers are treated fairly, the Board certifies that the PPFM has been complied with
Protection policy	A policy which provides benefits payable on certain events. The benefits may be a single lump sum or a series of payments and may be payable on death, serious illness or sickness
Public warrant	Warrants of the Company currently listed on the London Stock Exchange
PVFP	Present Value of Future Profits – The present value of profits attributable to shareholders arising from the in-force business
RCR	Resilience Capital Requirement – Additional amounts of capital required to be held by certain life companies for regulatory purposes as a result of two stress tests under Pillar 1
Scrip issue	The issue of new shares to existing shareholders in lieu of a cash dividend
Solvency II	A fundamental review of the capital adequacy regime for the European insurance industry. Solvency II aims to establish a set of EU-wide capital requirements and risk management standards that will replace the current Solvency I requirements
TCF	Treating Customers Fairly – A central FSA principle that aims to ensure fair outcomes for customers
Total Shareholder Return	The total return, over a fixed period, to an investor in terms of both share price growth

	and dividends (assuming that any dividends paid are re-invested, on the ex-dividend date, in acquiring further shares)
UEL	Useful economic life – The period over which future economic benefits are expected to be derived from an asset
UK Corporate Governance Code	Standards of good corporate governance practice in the UK relating to issues such as board composition and development, remuneration, accountability, audit and relations with shareholders
UKCPT	UK Commercial Property Trust Limited – A property subsidiary of the Group which is domiciled in Guernsey and listed on the London Stock Exchange
UKLA	UK Listing Authority – The FSA acting as the competent authority for listing, and which maintains the official list
UK GAAP	Generally Accepted Accounting Principles adopted within the UK
Unit-linked policy	A policy where the benefits are determined by the market value of the underlying assets in the unit linked fund
VIF	The Value of In-Force business – The Present Value of Future Profits (PVFP) plus the Time Value of Financial Options and Guarantees (TVFOG) less the Frictional Cost of Required Capital (COC)
With-profit fund	A fund where policyholders are entitled to a share of the profits of the fund. Normally, policyholders receive their share of the profits through bonuses, which reflect both the investment return from the assets which premiums are invested in and other profits the fund makes. Also known as a participating fund as shareholders have a participating interest in the with-profit funds and any declared bonuses. Generally, policyholder and shareholder participation in the with-profit funds in the UK is split 90:10
WPICC	With-Profit Insurance Capital Component. The WPICC is the amount by which the regulatory surplus exceeds the realistic surplus

REDUCING OUR ENVIRONMENTAL IMPACT

In line with our Corporate Responsibility programme and as part of our desire to reduce our environmental impact, you can view key information on our website at www.thephoenixgroup.com.

Our Investor Relations section includes information such as our most recent news items, results presentations, annual and interim reports, share-price performance, AGM and EGM information, FSA returns and contact information.

To stay up-to-date with Phoenix Group news and other changes with our site's content, you can sign up for e-mail alerts, which will notify you when content is added. To sign up visit www.thephoenixgroup.com/investor-relations/email-alerts.aspx

For mobile phone users we also have a useful mini-site at http://m.thephoenixgroup.com which contains links to our latest news items, share price, financial calendar and contact details.