



**Phoenix Life Limited
100% With-Profits Fund**

**Annual report to with-profits policyholders by the Board of Phoenix Life Limited
for the period 1 January 2009 to 31 December 2009**

Purpose

We set out how we manage the Phoenix Life Limited with-profits funds in our Principles and Practices of Financial Management (PPFM). In this report we give details of how we have complied with the PPFM for 2009 for our 100% With-Profits Fund ('the fund').

Phoenix Life Limited has discretion in a number of areas, such as setting bonuses, policy payouts and surrender values, and in addressing any competing or conflicting rights of policyholders and shareholders. This report deals with how Phoenix Life Limited has exercised its discretion in these areas.

Background

The Phoenix Life Limited 100% With-Profits Fund consists of:

- former Phoenix Assurance Limited (PAL) policies;
- former Bradford Insurance Limited (Bradford) policies;
- former Swiss Life UK (SLUK) With Profit Fund policies; and
- until 6 February 2009, former Swiss Life UK (SLUK) Pension With-Profits Fund unitised with-profits pension policies.

Phoenix Life Limited has eight with-profits funds including the 100% With-Profits Fund. We manage each with-profits fund in accordance with its own subset of our PPFM. The with-profits bonuses, policy returns and payouts for each with-profits fund reflect the financial position of that fund. The performance of each with-profits fund reflects the historic performance of the original with-profits funds and companies up to their respective transfer to Phoenix Life Limited, and then their performance within Phoenix Life Limited since that time.

The 100% With-Profits Fund is part of Phoenix Life Limited, along with seven other with-profits funds and a non-profit fund. The 100% With-Profits Fund is run as a separate ring fenced fund within Phoenix Life Limited but with the additional security that comes from being part of a large well capitalised company. In extreme circumstances one fund may have to provide financial assistance to another. However there are internal arrangements to ensure that Phoenix Life Limited holds assets in excess of the requirements of our regulator and, because of this, it is extremely unlikely that a with-profits policy in one fund will be affected by losses from another fund.

We have produced separate reports for our other with-profits funds.

Our PPFM is available on our website at www.phoenixlifegroup.co.uk, or you can ask us for a copy. We have produced a shorter guide called 'How we manage the Phoenix Life Limited 100% With-Profits Fund' and this can be obtained in the same way.

Independent review

The company formally consulted with, and took into account the opinions of the With-Profits Actuary and the With-Profits Committee (a committee which is independent by virtue of its majority of independent members) in respect of all material changes during 2009. This included consultation on the changes to bonus rates, surrender values and the estate.

The funds merger was subject to independent actuarial review and review by the Financial Services Authority. The funds merger was also subject to a court scheme.

Summary

Payouts for with-profits policies depend on the discretion exercised by Phoenix Life Limited. The interests of with-profits policyholders are protected by the PPFM of the company.

Each year the Board will produce a report to you, the with-profits policyholders, summarising compliance with the PPFM and how any discretion has been used over the previous year.

The PPFM guiding principles cover the following areas:

- Legal requirements, that is, Phoenix Life Limited and its with-profits funds are managed in accordance with Phoenix Life Limited's then current understanding of all legal and regulatory requirements.
- Basic fund concept, that is, subject only to the legal requirements guiding principle, the interests of with-profits policyholders extend to, but are also limited to, the assets of the fund to which the policy belongs.
- Fair treatment, that is, Phoenix Life Limited aims to treat its with-profits policyholders fairly.

The guiding principles are presented here at a high level rather than in the full detail of the PPFM. These guiding principles are applied in managing Phoenix Life Limited and all of its with-profits funds. Guiding principles are considered when applying the other fund specific principles and practices set out in the PPFM. In the event of a conflict with other principles these guiding principles take priority.

In the Board's opinion, the guiding principles were applied in accordance with the PPFM.

The principles for the 100% With-Profits Fund cover:

- Amounts payable under a with-profits policy
- Annual bonus rates
- Final bonus rates
- Smoothing
- Surrender values
- Investment strategy
- Business risks
- Expenses and charges
- Estate management
- New business
- Equity between the fund and shareholders

These are expanded on in the sections below. In addition, there is a commentary on any changes to the PPFM, other significant events and communications to with-profits policyholders during the year.

Amounts payable under a with-profits policy

We aim to pay all policyholders their fair share of the profits which the fund has earned over the time they have held their policy. We pay the share of profits in the form of annual and final bonuses. When deciding what is a fair share we consider the underlying value of representative specimen policies (sometimes called the 'asset share') as a guide. The underlying value of policies reflects the premiums paid and the investment performance of the fund over the lifetime of the policies, after allowing for factors such as our costs, the tax we have to pay, charges for death benefits, charges for guarantees and other profits and losses. This was the approach we used over 2009.

The outcomes we describe below relating to bonus rates, smoothing, surrender values and investment strategy are all measured by reference to representative specimen policies rather than to each actual policy.

In the Board's opinion, the methodology used to calculate the underlying value of policies has been in line with the PPFM. Further, in the Board's opinion, the discretion applied to the methods used to determine payouts on all policies during 2009 has been in line with the PPFM.

Annual bonus rates

We declared annual bonus rates for 2008 in March 2009 as part of the 2008 year end valuation. We maintained the same rates as those for 2007. For former Swiss Life unitised with-profits pensions where we declare annual bonus rates in advance, we maintained the same rates from January 2009 as those from January 2008.

We reviewed annual bonus rates for 2009 in December 2009. We subsequently declared annual bonus rates in March 2010 as part of 2009 year end valuation. We maintained the same annual bonus rates as those for 2008. The annual bonus rates for 2009 are shown in the table below.

Type of with-profits policy and bonus series	Annual bonus rate for 2009	
	On the basic sum assured	On previously added bonuses
Former PAL life	5.00%	8.00%
Former SLUK With Profit Fund life	3.00%	3.00%
Former SLUK With Profit Fund pension deferred annuity	4.50%	4.50%
Former Bradford life	4.50%	4.50%

We declared interim annual bonus rates for 2009 and 2010 at the same rates as the 2008 and 2009 annual bonus rates respectively.

The Board is satisfied that the approach taken in determining annual bonuses during the year was in line with the PPFM.

Final bonus rates

We changed final bonus rates on 1 January 2009 and 1 July 2009.

We also reviewed final bonus rates to apply from 1 January 2010.

For former Swiss Life With Profit Fund policies and former Bradford policies, we set final bonuses on an individual policy basis at the date of claim.

The Board is satisfied that the changes to final bonus rates resulted in changes to payouts that were consistent with the PPFM and were consistent with treating customers fairly.

Smoothing

We do not apply smoothing for former Swiss Life With Profit Fund policies and former Bradford policies, as we set final bonuses for these on an individual policy basis at the date of claim.

For former Phoenix Assurance Limited policies, when smoothing is applied to maturity or retirement values it is done by limiting the change in final bonus rates. We generally limit the changes in final bonuses to restrict differences in total maturity payouts (sum assured, annual bonus and final bonus) on similar maturing policies to 7.5% at each half yearly final bonus review and to 15% from one year to the next.

However, if it is necessary to enable the fund to continue to meet the objectives set out in the guiding principles, sometimes larger changes are made in final bonus rates. For example in recent years, payouts for former Phoenix Assurance Limited traditional life

policies have been increased and latterly reduced by more than 15% to reflect increases and latterly decreases made to the enhancement applied to asset shares on account of the fund's estate and changes in the estate. We do not smooth changes in final bonuses due to the changes in the level of estate distribution. These changes are in addition to the normal changes in final bonus rates due to investment returns which are smoothed.

In light of the exceptional investment conditions, for the January 2009 final bonus changes, we allowed an additional 5% reduction in total maturity payouts before smoothing applied. This meant that we generally limited reductions in total maturity payouts to 12.5% compared to similar maturity payouts in July 2008. The reduction in the estate distribution reduced payouts by 4%, meaning that the total reduction in total maturity payouts was up to 16.5% compared to similar payouts in July 2008.

We also allowed an additional 5% reduction in total maturity payouts for the 1 July 2009 final bonus changes. This generally limited reductions in total maturity payouts to 12.5% compared to similar maturity payouts in January 2009. The reduction in the estate distribution reduced payouts by 14%, meaning that the total reduction in total maturity payouts was up to 24% compared to similar maturity payouts in January 2009.

We allowed an additional 5% increase in total maturity payouts for the 1 January 2010 final bonus changes. This generally limited increases in total maturity payouts to 12.5% compared to similar maturity payouts in July 2009. The reduction in the estate distribution reduced payouts by 13% compared to similar maturity payouts in July 2009.

The Board is satisfied that these movements in final bonuses and maturity payouts in 2009, were necessary to keep payouts reasonably in line with the underlying value of policies, to ensure fairness between groups of policyholders and to protect the financial position of the fund, and were in line with the PPFM.

Surrender values

During 2009, we broadly set surrender values with the aim of paying 100% of the underlying value. For former Phoenix Assurance Limited traditional with-profits policies, the underlying value allows for the enhancements due to the estate distribution. We reviewed the way we calculate surrender values at the end of 2009 with revised surrender values applying from 1 January 2010. Surrender values include an allowance for final bonus and these final bonus allowances were revised from 1 January 2009, 1 July 2009 and 1 January 2010 in line with changes in final bonus rates. However, unlike changes in final bonuses and maturity payouts, the changes in the final bonus allowances for surrender values and surrender values are not smoothed.

In the Board's opinion, the methodology used to determine surrender values has been in line with the PPFM.

Investment strategy

During 2009, we invested the fund in a mix of assets such as company shares (equities), property, fixed interest stocks (bonds, types of loan usually issued by the Government or companies) and cash deposits. The expected approximate asset mixes for with-profits policies in the fund for 2010 are shown below. The asset mix depends on whether policies are former Phoenix Assurance Limited (PAL), former Bradford or former Swiss Life With Profit Fund.

Investment type	Former Phoenix Assurance Limited	Former Bradford	Former Swiss Life With Profit Fund
Company shares (equities)	39%	39%	39%
Fixed interest stocks - issued by the UK government (gilts)	27%	27%	27%
Fixed interest stocks - other (including corporate bonds)	28%	28%	28%
Property	6%	6%	6%
Cash	0%	0%	0%
Other	0%	0%	0%

Where the fund invests in corporate bonds (types of loan issued by companies) we normally only invest in bonds with a high credit rating. During 2009, the credit rating was reduced on a number of the bonds we invested in, meaning that we had a higher proportion of lower rated bonds than we would normally aim to hold. On the advice of our investment managers we continued to hold most of these bonds and, over 2009, there was a very strong recovery in the overall value of these investments following the falls in value in 2008. It is likely that in the near future our exposure to lower rated bonds will remain higher than it has been in the past. Despite these holdings, the overall quality of our bond investments remains good.

We expect the proportion in company shares (equities) for 2010 to remain at a broadly similar level to that for 2009.

For former Phoenix Assurance Limited policies, the fixed interest assets attributed to a specimen policy will reflect the term remaining to that policy's maturity date.

Any yearly statement that we send to with-profits policyholders includes information about the mix of assets for with-profits policies.

The fund also contains investments which back the cost of guarantees, the cost of smoothing and the estate.

The Board is satisfied that the approach taken in following the investment strategy during the year was broadly in line with the PPFM.

Business risks

There was an annual review by the Board of existing business risk exposure. In the opinion of the Board, appropriate measures were taken to limit the with-profits business exposure to risk to amounts which are fair.

The Board is satisfied that it has managed its business in line with the PPFM, that is, in a prudent manner, having regard to both the risks and rewards of which it is aware.

Expenses and charges

During 2009, we charged a fair share of our expenses to the fund and we made an appropriate allocation to the underlying value of with-profits policies in the fund. The main expenses we charged to the fund in 2009 were due to:

- Management services

During 2009, Pearl Group Management Services provided all the services required to operate the fund apart from investment management services. The charges are mainly expressed as an annual amount per policy which increases each year linked to the increase in the Retail Prices Index.

Pearl Group Management Services made additional charges for certain one-off activities and developments and we generally apportioned such costs in a fair and reasonable manner, taking into account the beneficiaries of the activity.

- Investment management services

During 2009, investment management services for the fund were provided by Ignis Asset Management. The charges made by Ignis Asset Management in respect of the fund's investments were attributed to the fund.

- Direct and other costs

The Board is satisfied that we apportioned a fair share of the direct and other costs we incurred to the fund and that these were in line with the PPFM.

Allocation of taxation

We allocated a share of the provisional amount of tax we incurred to the fund, in line with the PPFM. We calculated this by treating the fund as though it was our only fund and as though it was a mutual fund. Once we have agreed our tax charge with HM Revenue & Customs (HMRC), we will review the amount of tax we have allocated to the fund to ensure it is fair.

We made an appropriate allocation of tax to the underlying value of with-profits policies in the fund.

Estate management

We only distribute the fund's estate to former Phoenix Assurance Limited with-profits policies. The fund's estate provides working capital for the fund and supports the running of the fund. The estate is the excess assets that are not needed to support the fund's current and future liabilities. Profits and losses arising from policies in the fund affect the estate, including the cost of providing the guarantees and the cost of smoothing.

As the fund is closed, we aim to ensure a fair and orderly distribution of all the fund's assets including the estate, over the remaining lifetime of the former Phoenix Assurance Limited with-profits policies. While making sure that we have enough working capital to cover the risks in the fund, we expect the estate to run down to zero over time, broadly in line with the remaining lifetime of these policies in the fund.

For the last few years, we have been including a substantial distribution of the estate when we set bonuses. Unfortunately, the estate has been adversely impacted by the investment conditions in 2008 and early 2009 and other unfavourable experience, including some corrections in respect of previous years' reinsurance claims. Therefore we have had to reduce the level of estate distribution when we set bonuses. As a result we have had to make large reductions in final bonuses and policy payouts. Although we have had to make large reductions in final bonuses, policy payouts remain substantially higher than those from other with-profits companies.

We review the level of the estate distributions following each half yearly valuation. For the January 2009 final bonus review, the uplift due to the estate distribution was 630% of the underlying value of policies, making the target payout for maturity and surrender values to be 730% of the underlying value of policies. For the July 2009 final bonus review, the uplift reduced to 530% making the target payout to be 630% of the underlying value of policies. The uplift was further reduced for the January 2010 final bonus review to 450% of the underlying value of policies, making the target payout for maturity and surrender values to be 550% of the underlying value of policies.

In the Board's opinion, the methodology used to calculate the estate has been in line with the PPFM. Furthermore, in the Board's opinion, the distribution of the estate has been in line with the PPFM.

New business

The fund is no longer actively seeking new business. The Board is satisfied that this is in line with the PPFM.

Equity between the fund and shareholders

Our shareholders do not receive any share of the profits arising in the fund. The Board is satisfied that this is in line with the PPFM.

Changes to the PPFM during 2009

We include a description of the recent changes to the PPFM with any annual statement we issue to with-profits policyholders.

Funds merger

We wrote to policyholders in August / September 2008 about our proposal to transfer certain policies of our sister companies Scottish Mutual Assurance Limited and Scottish Provident Limited to Phoenix Life Limited. This transfer took place on 6 February 2009 as a result of schemes approved by the UK High Court, the Royal Court of Jersey and the Royal Court of Guernsey. The policies were transferred into two new with-profits funds or the existing Non-Profit Fund in Phoenix Life Limited. None of the transferring policies were transferred to the 100% With-Profits Fund.

At the same time the former Swiss Life UK unitised with-profits pension policies were transferred from the Phoenix Life Limited 100% With-Profits Fund to the Phoenix Life Limited 90% With-Profits Fund. Also at the end of December 2008, Phoenix & London Assurance Limited recaptured the former Phoenix Assurance Limited final salary unitised with-profits group pension policies which it had previously reassured to the 100% With-Profits Fund.

The funds merger was subject to reports by the Head of Actuarial Function and the With-Profits Actuary. It was also subject to a report by an independent actuary and the Financial Services Authority did not object.

The February 2009 PPFM for Phoenix Life Limited was updated to allow for this transfer. Changes were made to take account of the transfer, related events and to create a consistent style and presentation. Apart from these changes, the February 2009 Phoenix Life Limited PPFM reflected the existing Phoenix Life Limited PPFM and the PPFMs of Scottish Mutual Assurance Limited and Scottish Provident Limited.

Communications to with-profits policyholders

During 2009, we provided with-profits policyholders with key information concerning annual bonuses, investment mixes and changes to the PPFM with their annual statement.

Conclusion

It is the opinion of the company that Phoenix Life Limited including the 100% With-Profits Fund was, in all material respects, managed in accordance with the PPFM over 2009.

The With-Profits Committee has reviewed this annual report to with-profits policyholders and does not wish to make any additional or separate reports.

The Directors of Phoenix Life Limited

June 2010

Report to with-profits policyholders by the With-Profits Actuary of the Phoenix Life Limited 100% With-Profits Fund for the period 1 January 2009 to 31 December 2009

Purpose

The Principles and Practices of Financial Management (PPFM) for Phoenix Life Limited ('the company') is a detailed document which sets out how the company manages its with-profits business.

The company has discretion in a number of areas, such as setting bonuses, policy payouts and surrender values, and in addressing any competing or conflicting rights of policyholders and shareholders.

The purpose of my report to the company's with-profits policyholders in the 100% With-Profits Fund is to give my opinion, as required by the rules of the Financial Services Authority, as to whether the company has taken the interests of these with-profits policyholders into account in a reasonable and proportionate manner in exercising this discretion during 2009.

Conclusion

In my opinion, the company has taken the interests of the 100% With-Profits Fund with-profits policyholders into account in a reasonable and proportionate manner in exercising this discretion during 2009.

My opinion is based on the information which the company provided to me during the year.

The Board for Actuarial Standards has issued a Technical Actuarial Standard on Reporting ('TAS R') which applies to reports produced by actuaries. My report, when considered alongside the information in the company's own report to which my report is annexed, together with the other information provided to policyholders in relation to 2009, is intended to comply with TAS R.

Andrew Burke
Fellow of the Institute of Actuaries
With-Profits Actuary
June 2010