With profits changes explained

A leaflet for with profits policyholders in the SPI Fund of Scottish Provident Limited

Phoenix

Scottish Provident

We have sent you this leaflet because you have a with profits policy which is currently in the SPI Fund of Scottish Provident Limited (Scottish Provident) or a unitised with profits (UWP) policy with Scottish Provident where the with profits benefit is provided by the SPI Fund. The SPI Fund includes with profits policies and UWP policies of policyholders of Scottish Provident's Irish branch.

In this leaflet we explain how our proposals will affect your policy in particular. We recommend that you read the other material that we have sent you before reading this leaflet. The terms defined in the brochure have the same meanings in this leaflet.

Throughout this leaflet, reference to 'policy' includes UWP benefits on policies with such benefits.

Introduction
As part of our proposals, all policies within the SPI Fund of Scottish Provident will be transferred to the SPI With-Profits Fund (SPI WPF) of Phoenix Life Limited (Phoenix). This includes the relevant policies in Scottish Provident's Irish branch.

Further, as part of the Phoenix Scheme the with profit policies originally held within the Special Fund of Scottish Provident (not applicable to Irish branch policies) are going to be converted into non profit policies with guaranteed benefits and transferred to the SPI WPF together with the assets of the Special Fund. There is a separate leaflet for Special Fund policyholders explaining these changes.

Your policy benefits
Your benefits will not change as a result of the transfer. We will continue to add bonuses to your policy when appropriate in the same way as before and the SPI WPF will continue as a separate with profits fund within Phoenix.

Future bonuses on with profits policies currently in the SPI Fund will take account of the assets underlying those policies that are transferred into the SPI WPF of Phoenix and the returns earned on them. Some changes may, however, occur in the future, as described in the section below headed "Targeted Asset Allocation".

The protections for policyholders built into the 2001 Scottish Provident Demutualisation Scheme (2001 Demutualisation Scheme) will largely be carried over where they remain relevant but some important changes are explained below.

The way the fund is governed
Within Scottish Provident the investment and bonus policy of the SPI Fund is decided by the SPI Fund Supervisory Committee (SPI FSC) and the SPI FSC oversees the continuing interests of policyholders within the SPI Fund. Within Phoenix the investment and bonus policy is usually set by the Board following recommendations by the With Profits Committee.

It is proposed that the key powers of the SPI FSC will be assumed by the Phoenix With Profits Committee (WPC) as part of the Phoenix Scheme. The WPC is to be renamed the With-Profits and SPI WPF Supervisory Committee. Therefore, for the SPI WPF only, the WPC will have the additional responsibility for setting the investment and bonus policy. The WPC will do this on the basis that it will only consider the assets and liabilities of the SPI WPF as if it was a separate company. The WPC will be a committee of the Board of Phoenix, whereas the SPI FSC reports to the Scottish Provident board but is independent of it.

The SPI FSC currently has a duty to act at all times in the best interests of the holders of policies in the SPI Fund and the members who qualified for membership compensation after the demutualisation of the Scottish Provident Institution (the Qualifying Members). This obligation will also apply to the WPC which will be under a duty, when discharging its duties in respect of the SPI WPF, to act in the best interests of the holders of policies in the fund and Qualifying Members.

The membership of the WPC will differ from that of the SPI FSC. The Phoenix Scheme will require that the WPC will have a majority of non-executive members (the Non-Executive Members), of whom at least one must be an actuary who is not a non-executive director or associated with Phoenix or any group company (the Independent Member). The Independent Member under the new arrangements will be appointed and may be removed by the Board of Phoenix, but any new appointment will have to be approved by the other Non-Executive members and (except in certain limited circumstances) by the outgoing Independent Member. This differs from the current arrangements for the SPI Fund, where the independent member cannot be removed by the Scottish Provident board and any successor must be approved by the outgoing independent member. It is proposed that the first Independent Member for the WPC will be approved by the outgoing independent member of the SPI FSC.

The Independent Member is not required to attend all meetings of the WPC, but Phoenix will make all reasonable efforts to ensure that he or she is able to attend in person or by telephone or other means. Currently the independent member of the SPI FSC has a designated alternate member who can attend meetings if the independent member is unable to do so. In order to ensure continuity and emphasise the importance of attendance by the Independent Member, the requirement for an alternate to the independent member has not been carried forward into the Phoenix Scheme.

In relation to the SPI Fund, a member is independent if he or she is not and has not been employed in an executive capacity by a member of the Abbey Group. The Phoenix Scheme and WPC Terms of Reference have adopted a higher standard for the test of independence, including the criteria that a Non-Executive Member cannot have been an employee of, or had any form of material consulting or contractual relationship with (other than as a retail customer or as a non-executive director), Phoenix or the Phoenix Group within the last five years.

The arrangements outlined above concerning the membership and duties of the WPC, together with certain procedures regarding the operation of the WPC, will be set out in the Terms of Reference for the WPC. Any change to the core responsibilities and powers of the WPC remains subject to Court approval, but the Terms of Reference may be amended in other respects subject to opinions from internal and independent actuaries (where appropriate), consultation with the WPC and non-objection by the FSA.

Targeted asset allocation

As part of the Phoenix Scheme, it is proposed that in future the WPC may decide that some or all of the returns on with profits policies allocated to the SPI WPF will be determined for policies, particular policies or policy groups by reference to, or influenced by, particular assets or asset types within the SPI WPF. At present, with some limited exceptions, it is considered that this cannot be done in the context of the SPI Fund of Scottish Provident and the returns on the with profits policies allocated to the SPI Fund of Scottish Provident are determined by reference to the overall financial position of the fund.

The Phoenix Scheme provides for some formal safeguards before the WPC can decide to make a change of this kind. Therefore, subject to these safeguards, it will be possible for the WPC to make a change even if it is contrary to the terms of a policy or to commitments given to policyholders. The WPC will be required by the Phoenix Scheme to take appropriate legal, actuarial and other advice and will not be allowed to make this sort of change unless it is satisfied that it is unlikely to have a material adverse effect on the with profits policies allocated to the SPI WPF. This sort of change might be appropriate if, for example, the WPC believes that it will improve policyholder returns or reduce the volatility of payouts for those policyholders near maturity.

Principles and Practices of Financial Management

Full details of how Scottish Provident currently manages the fund have been published in its Principles and Practices of Financial Management (PPFM). This document goes into a large amount of detail regarding the management of the fund and how benefits are determined. We also produce a quick guide for different types of products which contain less detail and which will already have been sent to you.

As a result of the transfer, the PPFM of Phoenix will apply to the management of the SPI WPF. A draft version of the PPFM of Phoenix, including the SPI WPF, has been prepared. It will reflect the changes noted in this document. It is available on our website. You can also phone our helpline number or write to us to request a copy.

Drafts of the quick guide have also been prepared and are available in the same way. In addition, if our proposals are approved you will be sent a copy of the new version with your 2009 annual statement.

You will notice that the format of the documents has changed. This is to bring them in line with the format used elsewhere in Phoenix. However, apart from the changes described in this leaflet, no material changes are proposed to the way we are going to manage the fund.

Capital policy and support arrangements

Currently, the fund has adequate assets to cover its liabilities and the additional capital requirements of our regulator, the Financial Services Authority (FSA) and this will not be changed by the transfer to the SPI WPF of Phoenix.

In addition, the current PPFM specifies certain actions that will be taken if at any time the fund does not have enough money to cover its liabilities. These include a limit on any extra amount that the shareholder has agreed to provide to the fund if it does not have enough assets to cover its liabilities.

Following the transfer to Phoenix, we will:

- change the way in which asset shares, which are used to guide payout amounts, can be reduced if a deficit does arise; and
- remove the limit on the maximum amount that the shareholder will provide to the SPI WPF if its assets are insufficient to cover its liabilities.

In addition, under the Phoenix Scheme, we will implement the Phoenix Capital Policy (PCP). The PCP is part of the Phoenix Scheme and requires Phoenix to hold additional capital for all of its operations in excess of the normal regulatory requirements. This is intended to help Phoenix withstand conditions of excessive financial stress.

Under the PCP, the Non-Profit Fund or Shareholder Fund of Phoenix will make a loan (provided they have sufficient resources) to the SPI WPF if its assets are insufficient to cover its liabilities. Further, where the SPI WPF is unable to cover the additional capital requirements of the FSA, then the WPC can request the Phoenix Board for the SPI WPF to be able to rely on the Non-Profit Fund and Shareholder Fund.

In extreme circumstances the SPI

WPF may have to provide financial assistance to another fund within Phoenix. However, our proposals mean that the PCP will be in place to ensure that Phoenix holds assets in excess of the requirements of the FSA in relation to each of its funds, including the SPI WPF. Because of this it will be extremely unlikely that a with profits policy in the SPI WPF will be affected by losses from another fund within Phoenix.

Closure of the fund
If the statutory value of the with profits liabilities in the SPI WPF falls below a certain level in the future, our proposals will require us to convert all the with profits policies that then exist in the fund to non profit policies and transfer them into the Non-Profit Fund. If the conversion happens, policyholders will be given guaranteed bonuses at a guaranteed rate which will be calculated in a way that is fair to them.

Closure would only occur with the approval of our regulator the FSA. It is not expected that this would occur until around 2025.

These terms of closure are different to those that apply to the SPI Fund under the 2001 Demutualisation Scheme and no longer include a provision for the SPI WPF to merge with another with profits fund in certain circumstances.

Charges and expenses
Currently policies are charged a cost for covering the expense of the guarantees on some policies. It is proposed that in the future this charge will fall to the ‘estate’ (any assets in the SPI WPF above those needed to cover the liabilities).

The policy administration expenses that are charged to the fund will continue to be based on fixed per policy costs which are subject to inflation each year of RPI plus 0.75%. Currently, after 2011 the amount that can be charged must fall in the range of 85% to 125% of the actual expenses incurred. The Phoenix Scheme will bring forward the time when these restrictions will apply to 2009 and to reduce the upper limit to 115% which based on current charges will reduce the expenses charged to policyholders. The existing arrangements for charging a fixed amount for investment management services will continue.

Service standards
Scottish Provident is currently required to use reasonable endeavours to ensure that the service levels provided to the holders of all policies transferred under the 2001 Demutualisation Scheme are no less favourable than those provided to holders of policies in Scottish Mutual Assurance Limited (Scottish Mutual), and that the same level of skill and diligence is applied to the investment management of the assets in the SPI Fund as is applied to the assets of any fund in

the Abbey Group (other than fund managers carrying on banking business). This protection has been carried forward on the basis that the service levels provided to the holders of policies transferred from Scottish Provident under the Phoenix Scheme will be no less favourable than those provided to holders of policies transferred from Scottish Mutual, and that the level of skill and diligence applied to the management of assets in the SPI WPF is no less than that applicable to the Scottish Mutual With-Profits Fund established under the Phoenix Scheme.

Members' Account/Members' Compensation

When the Scottish Provident Institution demutualised in 2001, Qualifying Members were awarded compensation in return for the loss of membership rights. Scottish Provident was unable to contact a small minority of policyholders at the time, and so a proportion of the compensation monies was set aside to be paid out in the event that the remaining claimants came forward. Under the terms of the 2001 Demutualisation Scheme, the monies are held in a nominated "Members' Account" with Abbey National plc until July 2011, when they will be paid into the SPI Fund. The Phoenix Scheme will maintain a similar arrangement, and Qualifying Members may continue to claim compensation, where they are entitled to do so, until July 2011, when any unclaimed monies will become part of the SPI WPF within Phoenix.

Independent Actuary review of amendments to the Phoenix Scheme

At present, Scottish Provident may change the terms of the 2001 Demutualisation Scheme by applying to the Court of Session in Scotland. The application must be accompanied by a certificate from an independent actuary stating his opinion that the amendment does not affect the reasonable expectations of policyholders or reduce the protection conferred on them by the 2001 Demutualisation Scheme. This protection is carried forward by the Phoenix Scheme with respect to holders of policies within the SPI Fund, but with the reference to the High Court instead of the Scottish Court.

Conclusion of Independent Actuary under 2001 Demutualisation Scheme

As well as acting as Independent Expert for the Phoenix Scheme, Mr Tim Sheldon of Deloitte & Touche LLP has been asked, in his capacity as an independent actuary, to give an opinion on how the proposals affect the holders of policies transferred under the 2001 Demutualisation Scheme. A summary of his opinion is as follows:

"The 2001 Demutualisation Scheme states that any amendment to that scheme must be approved by the Court and must not, in the opinion of an independent actuary, adversely affect the reasonable expectations of or reduce the protection conferred by the scheme on the

holders of transferred policies.
I have been asked to provide this opinion as the 2001 Demutualisation Scheme is being discontinued and replaced by the Phoenix Scheme.

I have interpreted the replacement of the 2001 Demutualisation Scheme as an amendment for the purpose of this opinion. I do not regard any of the changes as having either a significant adverse effect or a significant beneficial effect for Scottish Provident policyholders. Overall, I am therefore satisfied that the amendments being made to the 2001 Demutualisation Scheme as a result of it being replaced by the Phoenix Scheme do not adversely affect the reasonable expectations of or reduce the protection conferred by the 2001 Demutualisation Scheme on the holders of transferred policies."

Conclusion of Independent Expert
The Independent Expert has concluded that the proposals do not have a material adverse effect on either the security of the affected policyholders' benefits or on their benefit expectations.

Summary of opinion of the SPI Fund Supervisory Committee
The SPI Fund Supervisory Committee also has reviewed the Scheme in detail, as it affects SPI with-profits policyholders and Qualifying Members. The Committee must look at this from the point of view of what is in the best interests of the policyholders, and it took detailed, independent legal advice. The Committee has been able to rely on the opinions of both the With Profits Actuary and the Independent Actuary who was appointed to consider the Scheme. The Committee accepted their views, in particular the opinion of the Independent Actuary that the new Scheme did not reduce the protection for policyholders and that it did not adversely affect their reasonable expectations. Looking at the content of Scheme overall, the Committee was satisfied that it would offer some benefit to policyholders, and the Committee has therefore accepted that it should go ahead.

Further information
If you have any questions or require further information please call our helpline. You will find the number on the letter enclosed with this leaflet.