



Phoenix Life Limited
Alba With-Profits Fund

ANNUAL REPORT TO WITH-PROFITS POLICYHOLDERS BY THE BOARD OF PHOENIX LIFE LIMITED FOR THE PERIOD 1 JANUARY 2010 TO 31 DECEMBER 2010

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 2010 for our Alba 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 Alba With-Profits Fund consists of former Alba Life Ordinary Long Term Fund policies.

Phoenix Life Limited has nine with-profits funds including the Alba With-Profits Fund. We manage each with-profits fund in accordance with its own section 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 Alba With-Profits Fund is part of Phoenix Life Limited, along with eight other with-profits funds and a non-profit fund. The Alba 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.

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

The policies in the fund originate from:

- former FS Assurance / Britannia Life Limited (FS / BLL);
- former Britannia Life Assurance / Crusader Insurance (BLA / Crusader); and
- former Life Association of Scotland (LAS).

The with-profits policies in the fund fall into two broad groupings. These are fully participating business which fully participates in profits and losses of the fund and investment smoothing business which only shares in the profits and losses arising from investment returns after allowing for smoothing.

Fully participating business comprises:

- traditional with-profits;
- unitised with-profits (started before 1 January 1994);
- deposit administration (not former FS / BLL); and
- controlled funding arrangements (not former BLA / Crusader).

Investment smoothing business comprises:

- unitised with-profits (started from 1 January 1994);
- Unitised Capital Guaranteed Fund;
- deposit administration (former FS / BLL);
- controlled funding arrangements (former BLA / Crusader).
- former BLA / Crusader With-Profits Performance Fund and With-Profits Pension Fund; and
- former BLA / Crusader Growth Bonus Series H.

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 that is independent by virtue of its majority of independent members) regarding all material changes during 2010. This included consultation on the changes to bonus rates, surrender values and the estate.

The funds transfer was subject to independent actuarial review and review by the Financial Services Authority. The funds transfer was approved by the High Court.

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 Alba With-Profits Fund cover the following areas.

- 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 that the fund has earned over the time they have held their policy. We pay the share of profits either in the form of bonuses or interest rates. 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, the shareholders' share of profits, charges for death benefits, charges for guarantees and other profits and losses. This was the approach we used over 2010.

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 2010 has been in line with the PPFM.

Annual and final bonus rates

The different product types investing in the fund receive their share of the profits earned in the fund in different forms of bonus. The form of bonus varies by type of product.

- Traditional with-profits and unitised with-profits policies receive their share of the profits in the form of annual and final bonuses.

The capital position of the fund still remains weak and hence we will not add annual bonuses for the foreseeable future, other than where they are guaranteed under the policy conditions. For traditional with-profits business, annual bonus is declared in arrears and, in March 2010 as part of the 2009 year end valuation, we declared nil annual bonuses for 2009. We reviewed the 2010 annual bonuses in December 2010 and we subsequently declared nil annual bonuses for 2010 in March 2011 as part of the 2010 year end valuation. For unitised with-profits business, we declare annual bonuses in advance and we declared a rate of nil for 2010 and to apply from 1 January 2011, other than where rates are guaranteed.

During 2010, we changed final bonus rates on 1 January and 1 July. We also reviewed final bonus rates from 1 January 2011. For some policies where the value of guaranteed benefits already exceeded the underlying value, we did not add any final bonus.

- Unitised Capital Guaranteed Fund policies, With-Profits Performance Fund and With-Profits Pension Fund policies receive their share of the profits in the form of regular bonuses added daily to the unit price.

We reviewed the bonus rates in March 2010 and also those to apply from March 2011.

- Deposit administration policies receive their share of the profits in the form of interest added to policyholders' accounts.

We reviewed the rates of interest in March 2010 and also subsequently in March 2011, or in each quarter, depending on the particular type of product.

- Controlled funding policies receive their share of the profits as:
 - a percentage of the pension benefits purchased by the scheme to date;
 - an additional contribution; or
 - a reduction in the contribution payable.

We reviewed these bonuses for 2009 in March 2010 and they were nil. We reviewed the rates for 2010 in December 2010 and subsequently declared nil rates in March 2011 as part of the 2010 year end valuation.

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

- For traditional with-profits and unitised with-profits policies, 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, due to the improved investment conditions, for the January 2010 final bonus changes, we allowed an additional 5% increase in total maturity payouts before smoothing applied. This meant that we generally limited increases in total maturity payouts to 12.5% compared to similar maturity payouts in July 2009.

We also allowed an additional 5% increase in total maturity payouts for the 1 July 2010 final bonus changes. This generally limited increases in total maturity payouts to 12.5% compared to similar maturity payouts in January 2010.

- For other types of business, we generally smooth in changes in the bonus or interest rates declared.

The Board is satisfied that these movements in final bonuses and maturity payouts in 2010, 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

- For traditional with-profits policies that are close to maturity, we set surrender values to avoid big differences between the surrender value and the maturity value. For other traditional with-profits policies, we aimed to set surrender values to be less than the underlying value of policies to protect the interests of continuing policyholders from bearing an increased share of the risks in the fund. Surrender values were generally targeted at 80% of the underlying value of policies in the first half of 2010. The 80% target had previously been reduced from 95% in July 2009 due to the deterioration in the final position of the fund during 2008. However, following an improvement in the fund's financial position in 2009, the 95% target was restored from July 2010. Over the last five years to the maturity of a policy the 80% and 95% targets are increased each year as maturity approaches, so that the surrender value produces a reasonable progression into the expected maturity value.

We reviewed surrender values at the end of 2010. To the extent that surrender values depend on final bonus rates, surrender values changed in line with final bonus changes from 1 January 2010, 1 July 2010 and 1 January 2011.

- For unitised with-profits policies, we set surrender values based on the underlying value. If the underlying value was less than the value of the units then we applied a market value reduction (MVR) so that the surrender value reflected the underlying value. We apply market value reductions to ensure fairness to all with-profits policyholders, so that surrender values are not unfairly higher than a policy's share of the underlying value of the fund's assets.

We reviewed market value reductions from 1 January 2010, from 1 July 2010 and again from 1 January 2011.

- For Unitised Capital Guaranteed Fund, With-Profits Performance Fund and With-Profits Pension Fund policies we set surrender values based on the underlying value. If the underlying value was less than the value of the units then we applied a market value reduction so that the surrender value reflected the underlying value.

We reviewed market value reductions in March 2010 (and subsequently from March 2011).

- For deposit administration policies, we set surrender value based either on the terms specified in the policy documentation or on the underlying value. If the underlying value was less than the value of the units then we applied a market value reduction so that the surrender value reflected the underlying value.

We reviewed market value reductions in March 2010 (and subsequently from March 2011) or in each quarter, depending on the particular type of product. For some policies we use scheme specific market value reductions and we review these on an individual scheme basis at the time of surrender.

- For controlled funding arrangements, we set surrender values based either on the terms specified in the policy documentation or on the underlying value.

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

Investment strategy

During 2010, we mostly invested the fund in a mix of assets such as property, fixed interest stocks (bonds, types of loan usually issued by the Government or companies) and cash deposits. We had the following asset mixes for with-profits policies on 31 December 2010.

Type of policy	Asset type				
	Fixed interest stocks issued by the UK government (gilts) %	Fixed interest stocks other (including corporate bonds) %	Property %	Company shares (equities) %	Cash %
Traditional with-profits life and pensions (former BLL Series B)	53%	21%	26%	0%	0%
Traditional with-profits pensions (other than former BLL Series B)	71%	29%	0%	0%	0%
Unitised with-profits business (started before 1 Jan 1994)	53%	21%	26%	0%	0%
Unitised with-profits business (started from 1 Jan 1994)	53%	21%	26%	0%	0%
Unitised Capital Guaranteed Fund	55%	24%	21%	0%	0%
Deposit administration - former FS/BLL	55%	24%	21%	0%	0%
Deposit administration - former Crusader	53%	11%	11%	0%	25%
Deposit administration - former LAS Laserplan	71%	29%	0%	0%	0%
Deposit administration - former LAS other	62%	27%	11%	0%	0%

Type of policy (continued)	Asset type				
	Fixed interest stocks issued by the UK government (gilts) %	Fixed interest stocks other (including corporate bonds) %	Property %	Company shares (equities) %	Cash %
Controlled funding arrangements - former Crusader (Growth Pension Fund)	53%	21%	26%	0%	0%
Controlled funding arrangements - former FS/BLL and LAS	67%	27%	6%	0%	0%
With-Profits Performance Fund	4%	5%	3%	47%	41%
With-Profits Pension Fund	4%	5%	3%	47%	41%

The mix of assets is broadly the same as that on 31 December 2009.

Generally we do not currently invest in company shares (equities) and, because of overall weakness of the fund and the high risk associated with company shares, the fund is unlikely to invest in them for the foreseeable future.

The exception to this is the With-Profits Performance Fund and With-Profits Pension Fund policies which are invested in ring-fenced notional funds and these have maintained investment in company shares (equities).

The 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 non-profit business, the cost of guarantees and the cost of smoothing.

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 2010, 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 2010 were due to the following.

- Management services

During 2010, Pearl Group Management Services and Capita 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 and Capita 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 2010, 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. 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.

Cost of guarantees and other profits and losses

Products which are described as fully participating share in all the profits and losses arising in the fund. This includes the costs of providing guarantees, the cost of guaranteed annuity options, profits and losses arising from surrenders and profits and losses arising from the non-profit business within the fund. They also share in the run-off item which is the balancing item to ensure that all of the assets of the fund will be distributed over the remaining lifetime of the policies in force. We review the level of these charges, other profits and losses and the run-off item following each half yearly valuation. We apply these items to the underlying policy values.

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

Estate management

The financial position of the fund means that there is no estate available for distribution and this was the case during 2010. However, as the financial position of the fund had generally improved, we were able to increase the surrender value target for traditional with-profits business from July 2010. We reviewed the level of the estate and considered the estate distribution position following each half yearly valuation.

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 received a share of the distributed profits which is generally a percentage of the value of bonuses we distributed to with-profits policyholders.

- In respect of traditional with-profits policies, unitised with-profits policies and controlled funding arrangements, the shareholders received one ninth of the value of bonuses distributed to policies, excluding any guaranteed bonuses or annual bonuses in respect of unitised with-profits business written from 1 January 1994.
- In respect of Unitised Capital Guaranteed Fund policies and deposit administration (former FS / BLL) policies, the shareholders did not receive any share of the value of bonuses distributed to policies.
- In respect of deposit administration (other than former FS / BLL) policies, the shareholders received one ninth or one eighteenth of the value of bonuses distributed to policies, excluding any guaranteed bonuses, depending on the type of policy.
- In respect of the With-Profits Performance Fund and With-Profits Pension Fund policies, the shareholders did not receive any share of the value of bonuses distributed to policies.

The shareholders' share of distributed profits for 2010 was £0.5m. The shareholder pays any tax that is generated as a result of this distribution to shareholders.

The Board is satisfied that the shareholders' share of the distributed profits for 2010 is in line with the PPFM.

From January 2011, when Alba With-Profits Fund pension policyholders retire, the pension will be set up in, and then paid from, the company's non-profit fund. The fund will pay the non-profit fund a fair value representing the cost of setting up and paying the pension payments. The Board reviewed the terms for the cost of setting up and paying the pension payments in 2010. The Board is satisfied that the terms agreed were in line with the requirements of the PPFM.

Changes to the PPFM during 2010

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

Funds transfer

In February 2011 we transferred the policies of our sister company Phoenix & London Assurance Limited to Phoenix Life Limited. The policies were transferred into a new with-profits fund in Phoenix Life Limited. None of the transferring policies were transferred to the Alba With-Profits Fund. This transfer has not changed the way we manage the Alba With-Profits Fund or the with-profits policies in it.

The funds transfer 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 funds transfer was approved by the High Court.

The February 2011 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 2011 Phoenix Life Limited PPFM reflected the existing Phoenix Life Limited PPFM and the PPFM of Phoenix & London Assurance Limited.

Communications to with-profits policyholders

During 2010, 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 Board that Phoenix Life Limited including the Alba With-Profits Fund was, in all material respects, managed in accordance with the PPFM over 2010.

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 2011

Report to with-profits policyholders by the With-Profits Actuary of the Phoenix Life Limited Alba With-Profits Fund for the period 1 January 2010 to 31 December 2010

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 of the Alba 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 2010.

Conclusion

In my opinion, the company has taken the interests of the with-profits policyholders of the Alba With-Profits Fund into account in a reasonable and proportionate manner in exercising this discretion during 2010.

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

The Board of Actuarial Standards has published a number of Technical Actuarial Standards (TASs). My report, when considered alongside the information in the company's own report to which my report is annexed, together with other information provided to policyholders in relation to 2010, is intended to comply with TAS R (which relates to the reporting of actuarial information), TAS M (which relates to modelling) and TAS D (which relates to data).

Geoffrey Ross
Fellow of the Institute of Actuaries
With-Profits Actuary
June 2011

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