LONDON LIFE LIMITED

Company Registration Number: 1179800

DIRECTORS' REPORT AND FINANCIAL STATEMENTS
for the year ended 31 December 2010

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Directors' report

The Directors present their report and the Financial Statements of London Life Limited Company ("the Company") for the year ended 31 December 2010

The Company is incorporated in the United Kingdom Its registration number is 1179800 and its registered office is 1, Wythall Green Way, Wythall, Birmingham B47 6WG

The financial statements of the Company have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS") and the comparative information has been restated accordingly In previous years the financial statements of the Company were prepared in accordance with applicable United Kingdom Generally Accepted Accounting Principles ("UK GAAP") Information on the effect of the transition to IFRS is given on pages 48 to 54

Business review

Principal activities
The principal activity of the Company is the transaction of various classes of insurance business covering life assurance, pension and annuity business in the form of participating, non-participating and unit-linked contracts This will continue to be the main activity for the foreseeable future

The Company has ceased to write new business but continues to accept premiums on in-force business

All business is written in the United Kingdom

Strategy
The strategy of the Phoenix Group, of which the Company is a member, is to be recognised as the best and most innovative manager of closed life assurance funds to improve returns for policyholders and deliver value for owners

Corporate activity

At 31 December 2010, the outstanding balance on the loans to Pearl Group Holdings (No 2) Limited ("PGH2"), the Company's immediate parent, were £57m (2009 £56m) and £18m (2009 £18m)

Business transacted
The Company maintains four long-term funds, together with its shareholder fund ("SHF") The long-term funds comprise a Life With-Profits fund ("LWP"), a Pensions With-Profits fund ("PWP") where, whilst operated on a 90 10 basis for discretionary payments to policyholders, the owners' are entitled to any surplus emerging due to contingent loan arrangements in place, a Life Non-Profit fund ("LNP") and a Pension Non-Profit fund ("PNP") In terms of policyholder liabilities, the PNP fund is the largest with gross policyholder liabilities of £962m at the period end

The Company writes a wide range of life and pensions business, predominantly on individual risks Business written in the Company includes unit-linked life and pensions and conventional life and pensions The LWP and PWP funds transact conventional and unitised with-profits business together with some unit linked business The PWP fund also reinsures some of its with-profits annuity business to Pearl Assurance Limited (formerly Pearl Assurance Plc) The LNP fund transacts term assurance and permanent health insurance ("PHI") business as well as immediate and deferred annuities, together with some unit linked business The PNP fund transacts immediate annuities, deferred annuities and some unit linked business

The Company has re-insured certain blocks of immediate and deferred annuities to fellow subsidiaries, Pearl Assurance Limited and Opal Reassurance Limited ("Opal") In addition, the Company has entered into a Surplus Relief Reassurance Agreement with Pearl Assurance Limited Under this arrangement Pearl Assurance Limited agrees to accept a defined level of risk in respect of all of the long-term business excluding the LWP fund

Reinsurance arrangements are also in place with parties outside the Phoenix Group to cover some PHI, endowment and whole life risks

Policy administration is outsourced to Pearl Group Services Limited ("PGS"), a fellow Group company PGS has, in turn, outsourced all administration to Diligenta Limited Under the agreements with PGS the majority of costs are levied on a per policy basis thereby mitigating the Company's expense risk Asset management is primarily outsourced to Ignis Asset Management Limited, a fellow group entity

The gross premium income of the Company for the year was £17m (2009 £24m)

The total value of assets was £3,467m compared with £3,529m a year earlier

The gross liabilities under insurance and investment contracts at 31 December 2010 were £1,886m (2009 £1,895m)

There is a provision for the Company's shareholder fund and, to a lesser extent, the non-profit funds to support any of the Company's with-profits funds in the event of a regulatory deficit in the with-profits funds

Valuation result
The Company is required to retain sufficient capital at all times to meet the regulatory capital requirements mandated by the FSA A valuation of the long-term insurance business of the Company in accordance with the FSA Handbook for Insurers issued by the Financial Services Authority was made as at 31 December 2010 FSA rules require the Company to determine its liabilities and capital requirements on two different bases which are known as the "regulatory basis" and the "realistic basis" and effectively take the higher of the two The valuation showed a surplus in excess of capital requirements of £246m (2009 £208m)

Results and dividends
The results of the Company for the year are shown in the statement of comprehensive income on page 14 The profit before tax was £19m (2009 £31m)

No dividends were paid during the year (2009 £nil)

Principal risks and uncertainties
The Company is exposed to a number of financial risks arising from its underlying assets and liabilities, in particular from falls in financial markets, the change in interest rates, the widening of credit spreads and the risk of corporate defaults

The principal owners' risk exposures during the year relate to all of the long-term funds due to the contingent loan arrangement in place with the PWP fund, the shareholder ownership of any LWP surplus and the 100% shareholder ownership of the LNP and PNP funds Life assurance, PHI, critical illness contracts are affected by mortality and morbidity risks whilst pensions business is adversely affected by improving annuitant longevity Persistency and expense inflation risks apply to most products The owners' are also exposed to the risks of meeting policyholder guarantees in the with-profits funds The funds also carry investment risk on any surplus assets and from investment performance associated with products carrying fund based charges A proportion of the business in the PNP fund is unit-linked with the investment performance risk being carried by policyholders, although owner profit is affected by fund based charges Risk exposures will reflect the wide range of business managed, with market risks and improving annuitant mortality being the principal risk exposures De-risking strategies are in place such as investment strategies matching fixed interest securities with liabilities and the purchase of interest rate swaptions to mitigate risks of guaranteed annuity options

In addition, the Company faces operational risks The outsourced policy administration arrangements which as noted above have been outsourced to Diligenta are considered secure even in extreme stresses, specifically given the letter of credit and guarantee provided by Diligenta's parent undertaking Tata Consultancy Services

As a result of the various transactions mentioned above, the Company is exposed to increased counterparty risk from the loans to PGH2

Further information on financial risks is provided in the notes to the financial statements

Key Performance Indicators ("KPIs")
The Company's performance is measured and monitored by the Board with particular regard paid to the following KPIs:

Customers
The Directors review various metrics in respect of Treating Customers Fairly ("TCF"), customer communication and complaints on a monthly basis TCF is monitored through various TCF committees and any exceptions are reported to the Board as appropriate

There is a with-profits committee comprising mostly of independent members to opine on issues of fairness to policyholders including ensuring policyholder monies are managed in accordance with the Company's Principles and Practices of Financial Management ("PPFM")

Capital resources
The aim of the Company is to maintain an appropriate margin of capital resources over capital resource requirements, both on a Pillar 1 and a Pillar 2 basis As at 31 December 2010, the Company's surplus assets on a Pillar 1 basis were £246m (2009 £208m)

Profits after taxation and distributable reserves
For the year ended 31 December 2010 the Company reported a profit after taxation of £6m (2009 £12m) As at 31 December 2010, the Company had distributable reserves amounting to £183m (2009 £177m), subject to the provisions of the 1997 Schedule 2C Scheme

Cash flows
Policyholder and owner cash flows are monitored closely by the business to ensure that all liabilities can be met as they fall due

Investment performance
The performance of the Company's invested assets is reviewed against pre-defined benchmarks by the Board, the Investment Committee and the Asset-Liability Management Committee ("ALCO")

Future developments
The Company's long-term business is in gradual run off The Company will continue to explore future business opportunities which help to secure future benefits for both policyholders and owners

Going concern
The Directors' report summarises the Company's activities, its financial performance and financial position together with any factors likely to affect its future development In addition, it discusses the principal risks and uncertainties it faces Notes 31 and 32 to the financial statements summarise the Company's risk and capital management objectives and policies together with its financial risks

The Board has followed the United Kingdom Financial Reporting Council's "*Going Concern and Liquidity Risk Guidance for Directors of UK Companies 2009*" when performing their going concern assessment As part of its comprehensive assessment of whether the Company is a going concern, the Board has undertaken a review of the valuation and liquidity of its investments at the period end The Board has also reviewed solvency and cash flow projections under normal and stressed conditions

As a result of this review, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future Accordingly, they continue to adopt the going concern basis in preparing the financial statements

Directors
The names of those individuals who served as Directors of the Company during the year or who held office as at the date of signature of this report are as follows

A B Davidson	
J P Evans	Chairman
K Luscombe	resigned on 9 February 2010
M J Merrick	
A Moss	appointed on 10 June 2010
J C Park	appointed on 1 April 2010
M D Ross	
J S B Smith	resigned on 25 March 2010
W R Treen	
M N Urmston	appointed on 18 January 2010
J J Yates	appointed on 24 June 2010

Secretary
G A Watson acted as Secretary throughout the year

Disclosure of indemnity
Qualifying third party indemnity arrangements (as defined in section 234 of the Companies Act 2006) were in force for the benefit of the Directors of the Company during the year and remain in place at the date of approval of this report

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

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

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

On behalf of the Board

A Moss
Director

22 March 2011

Statement of Directors' responsibilities

The Directors are required to prepare financial statements for each accounting period that comply with the relevant provisions of the Companies Act 2006 and International Financial Reporting Standards as adopted by the European Union ("IFRS"), and which present fairly the financial performance, financial position and cash flows of the Company, and the information on the transition to IFRS for the accounting period A fair presentation of the financial statements in accordance with IFRS requires the Directors to

- select suitable accounting policies and verify they are applied consistently in preparing the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business,
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance, and
- state that the Company has complied with applicable IFRS, subject to any material departures disclosed and explained in the financial statements

The Directors are responsible for maintaining proper accounting records which are intended to disclose with reasonable accuracy at any time the financial position of the Company They are also ultimately responsible for the systems of internal control maintained for safeguarding the assets of the Company and for the prevention and detection of fraud and other irregularities

Independent auditors' report to the members of London Life Limited

We have audited the financial statements of London Life Limited for the year ended 31 December 2010 which comprise the accounting policies, the statement of comprehensive income, the statement of financial position, the statement of cash flows, the statement of changes in equity, the related notes 1 to 36 and the information on the transition to IFRS on pages 48 to 54 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards as adopted by the European Union ("IFRS")

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

Respective responsibilities of Directors and auditor
As explained more fully in the Statement of Directors' Responsibilities set out on page 6, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

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

Opinion on the financial statements
In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2010 and of its profit for the year then ended,
- have been properly prepared in accordance with IFRS, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006
In our opinion the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements

Matters on which we are required to report by exception
We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

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

Ernst & Young LLP

James Lenton
Senior Statutory Auditor
For and on behalf of Ernst & Young LLP, Statutory Auditor
London

23 March 2011

Accounting policies

(a) Basis of preparation

The financial statements have been prepared on a historical cost basis except those financial assets and financial liabilities that have been measured at fair value

The financial statements are separate financial statements and the exemption in section 401 of the Companies Act, 2006 has been used not to present consolidated financial statements

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS")

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

The Company presents its statement of financial position broadly in order of liquidity An analysis regarding recovery or settlement more than twelve months after the period end is presented in the notes

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 statement of comprehensive income unless required or permitted by an international financial reporting standard or interpretation, as specifically disclosed in the accounting policies of the Company

(b) Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS 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 Company'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 and income taxes

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 32

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 (m) 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, without any deduction for transaction costs 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

Impairment of intangible assets

Intangible assets are subject to regular impairment reviews as detailed in accounting policy (k) Impairments are measured at the difference between the carrying value of a particular asset and its recoverable amount Impairments are recognised in the statement of comprehensive income in the period in which they occur

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 values of deferred tax assets and liabilities in the financial statements are discussed in note 19

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

(c) Foreign currency transactions
Assets and liabilities denominated in foreign currencies are translated into sterling at the closing rate at the period end Income and expenses denominated in foreign currencies are translated at the prevailing rate at the date of the transaction 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 within fair value gains and losses in the statement of comprehensive income

(d) Classification of contracts
Contracts under which the Company accepts significant insurance risk are classified as insurance contracts

Contracts under which the transfer of insurance risk to the Company from the policyholder is not significant are classified as investment contracts

Some insurance and investment contracts contain a Discretionary Participation Feature ("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 previously adopted under United Kingdom Generally Accepted Accounting Principles ("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 issued by the Financial Services Authority ("FSA"), the UK Regulator 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 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 32

For participating business, the Company 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 to comply with the requirements of the FSA realistic capital regime The key aspects of this methodology are

- liabilities to policyholders arising from the with-profits business are stated at the amount of the realistic value of the liabilities, adjusted to exclude the owners' share of projected future bonuses and the associated tax liabilities,
- 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 32

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 statement of comprehensive income

The Company'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 statement of comprehensive income

Unallocated surplus
The unallocated surplus comprises the excess of the assets over the policyholder liabilities of the with-profits business For the Company's with-profits funds, the amount included in the statement of financial position line item 'Unallocated surplus' 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 The with-

profits funds are closed to new business and as permitted by IFRS 4, the whole of the unallocated surplus has been classified as a liability (either within insurance contract liabilities or unallocated surplus)

(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 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 financial liability is measured based on the carrying value of the assets and liabilities that are held to back the contract 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 statement of comprehensive income

(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 a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch') 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 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 Company's key management personnel

(h) Deposits from reinsurers

It is the Company'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 Company for investment purposes, the investments are recognised as 'financial assets' and the collateral repayable is recognised as 'deposits received from reinsurers' within the statement of financial position

(i) Obligations for repayment of collateral received

It is the Company'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 Company for investment purposes, the investments are recognised within the statement of financial position as 'financial assets' and the collateral repayable is recognised as 'obligations for repayment of collateral The 'obligations for repayment of collateral received' are measured at amortised cost, which in the case of cash is equivalent to cost

(j) Income tax

Income tax comprises current and deferred tax Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised in the statement of changes in equity, in which case it is recognised in this statement

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 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

(k) Intangible assets

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 Company's accounting policies 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 statement of comprehensive income Acquired in-force business is also considered in the liability adequacy test for each reporting period

(l) Investment in subsidiaries

Investments in shares in subsidiaries held for strategic purposes are carried in the statement of financial position at cost less impairment Investments in shares in subsidiaries held for investment purposes are carried at fair value

The Company assesses at each reporting date whether an investment in subsidiary or group of investments in subsidiaries held at cost is impaired The Company first assesses whether objective evidence of impairment exists Evidence of impairment is obtained by comparing the carrying value of the investment in the subsidiary with the estimate of the recoverable amount of the subsidiary

There are no investments in subsidiaries held for investment purposes

(m) Financial assets

Purchases and sales of financial assets are recognised on the trade date, which is the date that the Company 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 derivatives 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 statement of comprehensive income

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 financial position at fair value They are designated at fair value through profit or loss because they are managed and evaluated on a fair value basis in accordance with the Company's stated risk management policies

Impairment of financial assets

The Company assesses at each period end whether a financial asset or group of financial assets held at amortised cost is impaired The Company first assesses whether objective evidence of impairment exists for financial assets 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 current 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 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 Company's stock lending programme do not qualify for derecognition from the statement of financial position as the Company retains substantially all the risks and rewards of the transferred assets

Collateral
The Company receives and pledges collateral in the form of cash or non-cash assets in respect of stock lending transactions and derivative contracts in order to reduce the credit risk of these transactions The amount and type of collateral required where the Company receives collateral depends on an assessment of the credit risk of the counterparty

Collateral received in the form of cash, where the Company has contractual rights to receive the cash flows generated, is recognised as an asset in the statement of financial position with a corresponding liability for its repayment Non-cash collateral received is not recognised in the statement of financial position, unless the counterparty defaults on its obligations under the relevant agreement

Cash and non-cash collateral pledged where the Company retains the contractual rights to receive the cash flows generated is not derecognised from the statement of financial position, unless the Company defaults on its obligations under the relevant agreement, and therefore continues to be recognised in the statement of financial position within the appropriate asset classification

(n) Reinsurance
The Company cedes insurance risk in the normal course of business Reinsurance assets represent balances due from reinsurance companies Reinsurers' share of insurance contract liabilities are 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 year Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the Company 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 Company will receive from the reinsurer The impairment loss is recorded in the statement of comprehensive income 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 statement of comprehensive income

Gains or losses on purchasing reinsurance are recognised in the statement of comprehensive income 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

(o) 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 Company's cash management are deducted from cash and cash equivalents for the purpose of the statement of cash flows

(p) Provisions and contingent liabilities
A provision is recognised when the Company 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 Company 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 least 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

(q) Dividends
Final dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Company's owners Interim dividends are deducted from equity when they are paid

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

(r) 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 Company 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
- 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, fair value gains and losses on financial assets and impairment losses on loans and deposits

Interest income is recognised in the statement of comprehensive income as it accrues using the effective interest method Dividend income is recognised in the statement of comprehensive income on the date the right to receive payments is established, which in the case of listed securities is the ex-dividend date

Fair value gains and losses on financial assets designated at fair value through profit or loss are recognised in the statement of comprehensive income 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

(s) 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

Finance costs
Interest payable is recognised in the income statement as it accrues and is calculated by using the effective interest method

(t) Share capital
Ordinary share capital
The Company has issued ordinary shares which are classified as equity

Statement of comprehensive income
for the year ended 31 December 2010

	Notes	2010 £m	2009 £m
Gross premiums written		17	24
Less premiums ceded to reinsurers		-	2
Net premiums written		17	26
Fees and commissions	2	3	3
Net investment income	3	173	106
Total revenue, net of reinsurance payable		193	135
Policyholder claims		(149)	(173)
Less reinsurance recoveries		44	45
Change in insurance contract liabilities		27	151
Change in reinsurers' share of insurance contract liabilities		18	(31)
Transfer from/(to) unallocated surplus	12	2	(1)
Net policyholder claims and benefits incurred		(58)	(9)
Change in investment contract liabilities		(39)	(47)
Impairment of acquired in-force business	24	(1)	-
Administrative expenses	4	(9)	(10)
Other operating expenses	7	(64)	(31)
Total operating expenses		(171)	(97)
Profit before finance costs and tax		22	38
Finance costs	8	(3)	(7)
Profit for the year before tax		19	31
Tax attributable to policyholders' returns		(1)	(2)
Profit before tax attributable to owners		18	29
Tax charge	9	(13)	(19)
Less tax attributable to policyholders' returns		1	2
Tax attributable to owners		(12)	(17)
Profit for the year attributable to owners		6	12
Other comprehensive income		-	-
Total comprehensive income for the year		6	12

Statement of financial position – equity and liabilities
as at 31 December 2010

	Notes	As at 31 December 2010 £m	As at 31 December 2009 £m	As at 1 January 2009 £m
EQUITY AND LIABILITIES				
Equity attributable to owners of the parent				
Share capital	10	19	19	19
Retained earnings		190	184	172
Total equity		209	203	191
Liabilities				
Insurance contract liabilities				
Liabilities under insurance contracts	11	1,535	1,562	1,713
Unallocated surplus	12	6	8	7
		1,541	1,570	1,720
Financial liabilities				
Investment contracts		351	333	307
Deposits received from reinsurers	13	560	545	552
Derivatives	14	73	48	117
Obligations for repayment of collateral received	15	525	664	726
Contingent loan	16	180	127	105
	17	1,689	1,717	1,807
Provisions	18	-	2	4
Deferred tax	19	2	2	2
Payables related to direct insurance contracts	20	6	9	6
Current tax	19	9	6	-
Accruals	21	2	1	3
Other payables	22	9	19	8
Total liabilities		3,258	3,326	3,550
Total equity and liabilities		3,467	3,529	3,741

Statement of financial position – assets
as at 31 December 2010

	Notes	As at 31 December 2010 £m	As at 31 December 2009 £m	As at 1 January 2009 £m
ASSETS				
Intangible assets				
Acquired in-force business	24	8	9	9
		8	9	9
Financial assets				
Loans and deposits	25	146	209	176
Derivatives	14	99	67	179
Equities		6	3	11
Fixed and variable rate income securities		1,554	1,640	1,766
Collective investment schemes		982	756	797
Reinsurers' share of investment contract liabilities		13	13	12
	26	2,800	2,688	2,941
Deferred tax assets	19	4	10	9
Insurance assets				
Reinsurers' share of insurance contract liabilities	11	607	589	620
Reinsurance receivables		-	-	1
Insurance contract receivables		4	4	4
		611	593	625
Current tax	19	-	-	2
Prepayments and accrued income		23	23	27
Other receivables	28	13	5	21
Cash and cash equivalents	29	8	201	107
Total assets		3,467	3,529	3,741

On behalf of the Board

A Moss
Director
22 March 2011

Statement of cash flows
as at 31 December 2010

	Notes	2010 £m	2009 £m
Cash flows from operating activities			
Cash (utilised)/generated by operations	30	(264)	87
Net cash flows from operating activities		(264)	87
Cash flows from investing activities			
Interest received from Group entities		6	7
Net cash flows from investing activities		6	7
Cash flows from financing activities			
Transfer of loan to fellow subsidiary	25	65	-
Net cash flows from financing activities		65	-
Net (decrease)/increase in cash and cash equivalents		(193)	94
Cash and cash equivalents at the beginning of the year		201	107
Cash and cash equivalents at the end of the year	29	8	201
Supplementary disclosures on cash flow from operating activities			
Interest received		83	98
Dividends received		4	-

Statement of changes in equity
for the year ended 31 December 2010

	Share capital (note 10) £m	Retained Earnings £m	Total £m
At 1 January 2010	19	184	203
Profit for the year	-	6	6
Other comprehensive income for the year	-	-	-
Total comprehensive income for the year	-	6	6
At 31 December 2010	19	190	209

In accordance with the terms of the 1997 Schedule 2C scheme, dividends or return of capital may only be made to owners of the company provided that the Financial Services Authority ("FSA") certifies that at that point there are sufficient assets to cover policyholders' reasonable benefit expectations, inter-fund loan amounts and solvency requirements as set out in the Schedule 2C scheme

Of the above, £183m (2009 £177m) of retained earnings is considered distributable

	Share capital (note 10) £m	Retained earnings £m	Total £m
At 1 January 2009	19	172	191
Profit for the year	-	12	12
Other comprehensive income for the year	-	-	-
Total comprehensive income for the year	-	12	12
At 31 December 2009	19	184	203

Notes to the financial statements

1 Financial information

The financial statements for the year ended 31 December 2010, set out on pages 8 to 54, were authorised by the Board of Directors for issue on 22 March 2011 The financial statements have been prepared in accordance with IFRS The comparative amounts for the year ended 31 December 2009 are based on the Company's financial statements for that year after adjustment for the transition from United Kingdom Generally Accepted Accounting Principles ("UK GAAP") to IFRS

Information on how the transition to IFRS has affected the financial position, financial performance and cash flows of the Company is set out on pages 48 to 54 This information includes reconciliations of equity and income as reported under UK GAAP to financial information reported under IFRS

In preparing the financial statements the Company has adopted all applicable standards, interpretations and amendments which have been issued by the International Accounting Standards Board and have been adopted for use by the EU in 2010

In addition, the Company has adopted the amendments to IAS 24 *Related Party Disclosures* These amend the definition of a related party, clarify its intended meaning and eliminate inconsistencies and, as permitted, have been early adopted from 2010

The International Accounting Standards Board has issued the following standards, interpretations and amendments which, subject to adoption for use by the EU, apply from the dates shown The Company has decided not to early adopt any of these standards, interpretations or amendments where this is permitted The impact of adopting them is subject to evaluation but is currently not expected to have a material effect on the results of the Company

- IFRS 9 *Financial Instruments* (2013) IFRS 9 is the first phase of the project to replace IAS 39 *Financial Instruments Recognition and Measurement* and deals with the classification and measurement of financial assets and financial liabilities, including some hybrid contracts
- Annual improvements 2010 (2011) This makes a number of minor improvements to existing standards and interpretations
- 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

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

- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* (2011)
- Classification of Rights Issues (Amendments to IAS 32) (2011)
- Prepayments of a Minimum Funding Requirement (Amendments to IFRIC 14) (2011)
- Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (Amendments to IFRS 1) (2012)

2 Fees and commissions

	2010	2009
	£m	£m
Investment contract income	3	3

3 Net investment income

	2010	2009
	£m	£m
Investment income		
Interest income on loans and deposits	8	9
Dividend income	4	-
Interest income on financial assets designated at fair value through profit or loss on initial recognition	75	87
	87	96
Fair value gains/(losses)		
Financial assets at fair value through profit or loss		
Held for trading	(22)	16
Designated upon initial recognition	108	(6)
	86	10
Net investment income	173	106

Interest income on loans and deposits includes interest of £8m (2009 £9m) on loans to Group entities

Included within held for trading financial assets is £53m of losses (2009 £22m of losses) in respect of the change in value of the contingent loan liability (see note 16)

4. Administrative expenses

	2010	2009
	£m	£m
Investment management expenses and transaction costs	5	5
Outsourcing expenses	4	5
	9	10

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

5 Directors' remuneration

	2010 £000	2009 £000
Salaries and other short term benefits	236	401
Remuneration (excluding pension contributions and awards under share option schemes arising from long term incentive schemes)	236	401
Post-employment benefits	2	27
Other long-term benefits	131	-
	133	27
Contributions to money purchase pension schemes	2	27

	2010 Number	2009 Number
Number of Directors who		
- are members of a money purchase pension scheme	1	2
- are members of a defined benefit pension scheme	2	2

	2010 £000	2009 £000
Highest paid Director's remuneration		
Remuneration (excluding pension contributions and awards under share option schemes arising from long term incentive schemes)	85	132

The Executive Directors are employed by Pearl Group Services Limited and Pearl Group Management Services Limited The Non-Executive Directors are not employed but provide their services via a letter of appointment

6. Auditors' remuneration

The remuneration of the auditors of the Company, including their associates, in respect of services supplied to entities included in the financial statements was £143,000 (2009 £187,000) No services were provided to associated pension schemes

	2010 £000	2009 £000
Audit of the financial statements	106	134
Other services supplied pursuant to such legislation		
Services as reporting accountants	37	47
Other services		
Other	-	6
	143	187

7. Other operating expenses

	2010 £m	2009 £m
Movement in deposits received from reinsurers	64	31

8 Finance costs

	2010 £m	2009 £m
Interest expense		
On borrowings at amortised cost	3	7
Attributable to		
- policyholders	3	7

Interest expense includes £3m (2009 £7m) of stock lending fees

9 Tax charge

Current year tax charge

	2010 £m	2009 £m
Current tax		
UK Corporation tax	15	21
	15	21
Adjustment in respect of prior years	(8)	(1)
	7	20
Deferred tax		
Reversal/(origination) of temporary differences		
On non-profit surpluses	-	1
On provisions for future expenditure	-	(10)
Utilisation of tax losses	-	8
Excess expenses and deferred acquisition costs	6	-
	6	(1)
Total tax charge	13	19
Attributable to		
- policyholders	1	2
- owners	12	17
	13	19

The Company, 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 benefit attributable to policyholder earnings was £1m (2009 £2m)

Reconciliation of tax charge

	2010 £m	2009 £m
Profit before tax	19	31
Policyholder tax charge	(1)	(2)
Profit before the tax attributable to owners	18	29
Tax at standard UK rate of 28%	5	8
Adjustment to tax charge in respect of prior years	(8)	(1)
Policyholder tax calculation methodology	-	10
Net taxable gains in revaluation of long-term business	15	-
Owners' tax charge	12	17
Policyholder tax charge	1	2
Total tax charge for the year	13	19

10. Share capital

	2010	2009
	£m	£m
Issued and fully paid 18,800,002 (2009 18,800,002) ordinary shares of £1 each	19	19

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

The holders of the 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

11. Liabilities under insurance contracts

	Gross liabilities 2010	Re-insurers' share 2010	Gross liabilities 2009	Re-insurers' share 2009
	£m	£m	£m	£m
Insurance contracts	1,417	607	1,439	589
Investment contracts with DPF	118	-	123	-
	1,535	607	1,562	589
Amounts due for settlement after 12 months	1,272	568	784	550

	Gross liabilities	Re-insurers' share
	£m	£m
At 1 January 2010	1,562	589
Premiums	17	-
Claims	(149)	(44)
Other changes in liabilities	105	62
At 31 December 2010	1,535	607

	Gross liabilities	Re-insurers' share
	£m	£m
At 1 January 2009	1,713	620
Premiums	24	(2)
Claims	(173)	(45)
Other changes in liabilities	(2)	16
At 31 December 2009	1,562	589

12 Unallocated surplus

	2010	2009
	£m	£m
At 1 January	8	7
Transfer (to)/from statement of comprehensive income	(2)	1
At 31 December	6	8

13. Deposits received from reinsurers

Deposits received from reinsurers are measured at fair value through profit and loss as designated upon initial recognition

	2010 £m	2009 £m
Carrying value		
At 31 December		
- Premium withheld from reinsurers	535	515
- Deposit back from Pearl Assurance Limited (formerly Pearl Assurance Plc)	25	30
	560	545
Amounts due for settlement after 12 months	560	545

The carrying value amount of these assets is a reasonable approximation of their fair value

With effect from 1 January 2007, the Company reassured certain pension annuities in payment to Opal Reassurance Limited ("Opal"), a fellow group company Under the terms of this reassurance arrangement the Company holds assets in a collateral account over which Opal has a fixed charge

Under the deposit back arrangement, premiums from London Life Limited to Pearl Assurance Limited are such that London Life Limited makes no profit of loss on the business All claims paid by London Life Limited are reassured 100% to Pearl Assurance Limited

14 Derivatives

The Company 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

	2010 Assets £m	2010 Liabilities £m	2009 Assets £m	2009 Liabilities £m
Interest rate swaps	92	69	58	45
Swaptions	3	-	6	-
Currency forwards	3	3	2	3
Credit default swap	1	1	1	-
	99	73	67	48

The amount recoverable after one year is £94m (2009 £63m) The amount payable after one year is £68m (2009 £45m)

It is the Company's practice to obtain collateral to mitigate the counterparty risk related to derivative transactions, usually in the form of cash or marketable securities

Where the Company 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 financial position The fair value of financial assets accepted as collateral but not recognised in the statement of financial position amounts to £nil (2009 £nil)

Where the Company receives collateral on derivatives in the form of cash or marketable securities which it is permitted to sell or re-pledge, the assets are recognised in the statement of financial position along with a corresponding liability to repay the amount of the collateral received, disclosed as "Obligations for the repayment of collateral received" The amount recognised as a financial asset and a financial liability at 31 December 2010 is £26m (2009 £16m) and £25m (2009 £15m) respectively

Where the Company 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 financial position The value of assets pledged at 31 December 2010 amounted to £7m (2009 £nil)

15. Obligations for repayment of collateral received

	2010 £m	2009 £m
Carrying value		
At 31 December		
- Stock lending collateral	500	649
- Derivative collateral	25	15
	525	664
Amount due for settlement after 12 months	23	15
Fair value		
At 31 December	525	664

16 Contingent loan

	2010 £m	2009 £m
At 1 January	127	105
Movement in the year	53	22
At 31 December	180	127

The contingent loan has been provided to the Company by its parent, Pearl Group Holdings (No 2) Limited ("PGH2") and the purpose is to cover the shortfall arising as a result of prudential reserves for guaranteed benefits under the relevant policies, which are expected to unwind over time as policies become claims The contingent loan is only repayable if there are sufficient assets to cover policyholders' reasonable benefit expectations, inter-fund amounts and solvency requirements No interest accrued on the loan for the period from 1 January 2007 to 31 December 2010

The inter-relationship between the contingent loan and the insurance contract liabilities will continue to be the subject of regular dialogue with the Financial Services Authority ("FSA") to ensure appropriate recognition of the need to treat customers fairly and the obligations set out in the (Principles and Practices of Financial Management ("PPFM")

17 Financial liabilities

	2010 £m	2009 £m
Carrying value		
Financial liabilities at fair value through profit or loss		
Designated upon initial recognition		
Investment contracts	351	333
Deposits received from reinsurers	560	545
Contingent loan	180	127
Held for trading – derivatives	73	48
Financial liabilities measured at amortised cost	525	664
	1,689	1,717
Amount due for settlement after 12 months	273	203

The carrying value of the financial liabilities measured at amortised cost approximates to fair value

18. Provisions

	Total £m
As at 1 January 2010	2
Released during the year	(2)
At 31 December 2010	-

19. Tax assets and liabilities

	2010 £m	2009 £m
Current tax receivables	-	-
Net deferred tax assets	4	10
Total tax assets	4	10
Current tax payables	9	6
Net deferred tax liabilities	2	2
Total tax liabilities	11	8

Deferred tax assets comprise:

	2010 £m	2009 £m
Expenses and deferred acquisition costs carried forward	4	10
Gross deferred tax assets	4	10

Deferred tax liabilities comprise:

	2010 £m	2009 £m
Intangible assets	2	2
Gross deferred tax liabilities	2	2

Movements in deferred tax assets/(liabilities) comprise:

	2010 £m	2009 £m
At 1 January	8	7
Amounts charged to the statement of comprehensive income	(6)	1
At 31 December	2	8

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

Deferred income tax assets are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable

	2010 £m	2009 £m
Deferred tax assets have not been recognised in respect of		
Tax losses carried forward	-	29
Deferred tax assets not recognised on capital losses	24	52

These can only be offset against future capital gains and have no expiry date

20 Payables related to direct insurance contracts

	2010 £m	2009 £m
Payables related to direct insurance contracts	6	9
Amount due for settlement after 12 months	-	-

21. Accruals

	2010 £m	2009 £m
Accruals	2	1
Amount due for settlement after 12 months	-	-

22. Other payables

	2010 £m	2009 £m
Investment broker balances	-	1
Other payables	9	18
	9	19
Amount due for settlement after 12 months	-	-

23. Investment in subsidiaries

The principal subsidiaries of the Company are dormant and are as follows

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned)
Trustees		
London Life Trustees Limited	UK	Ordinary shares of £1
Insurance companies		
The London Life Association Limited	UK	Membership status

24 Intangible assets – acquired in-force business

	2010 £m	2009 £m
Cost		
At 1 January and 31 December	101	101
Amortisation		
At 1 January	92	92
Charge	1	-
At 31 December	93	92
Carrying amount		
At 31 December	8	9
Amount recoverable within 12 months	1	1
Amount recoverable after 12 months	7	8

The acquired in-force business was recognised upon the demutalisation of AMP Limited in 1998 and represents the shareholders share of future bonuses arising within the with-profits fund

25 Loans and deposits

	2010 £m	2009 £m
Loans to Group entities at amortised cost		
Loans to PGH2, the Company's immediate parent	75	74
Loan to National Provident Life Limited, a fellow subsidiary	-	65
	75	139
Other loans	71	70
At 31 December	146	209

On November 2010, the loan to National Provident Life Limited was transferred from London Life Limited to Pearl Assurance Limited for a sum of £65m The movement in the loan value with PGH2 is due to capitalised interest

Included in Other loans are policy loans and a £69m loan note issued by Axial Credit Opportunities Holdings Limited, a fellow subsidiary and a holding company of another fellow subsidiary, Axial Fixed Income Opportunities S A R L to the collateral fund of London Life Limited Interest is deferrable and cumulative

26 Financial assets and financial instrument fair value hierarchy

	2010 £m	2009 £m
Loans at amortised cost	146	209
Financial assets at fair value through profit or loss		
Held for trading – derivatives	99	67
Designated upon initial recognition		
Equities	6	3
Fixed and variable rate income securities	1,554	1,640
Collective investment schemes	982	756
Reinsurers' share of investment contract liabilities	13	13
	2,800	2,688
Amount recoverable after 12 months	1,846	1,937

The fair value of loans and deposits at amortised cost amounted to £146m (2009 £209m)

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 Company'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

Fair value hierarchy of financial instruments measured at fair value

At 31 December 2010	Level 1	Level 2	Level 3	Total fair value
	£m	£m	£m	£m
Financial assets at fair value				
Derivatives	-	99	-	99
Financial assets designated at fair value through profit or loss upon initial recognition				
Equities	1	-	5	6
Fixed and variable rate income securities	1,386	90	78	1,554
Collective investment schemes	894	3	85	982
Reinsurers share of investment contract liabilities	-	13	-	13
	2,281	106	168	2,555
Total financial assets at fair value	2,281	205	168	2,654

At 31 December 2010	Level 1	Level 2	Level 3	Total fair value
	£m	£m	£m	£m
Financial liabilities at fair value				
Derivatives	-	73	-	73
Financial liabilities designated at fair value through profit or loss upon initial recognition				
Investment contract liabilities	-	351	-	351
Contingent loan	-	180	-	180
Deposits received from reinsurers	-	560	-	560
	-	1,091	-	1,091
Total financial liabilities at fair value	-	1,164	-	1,164

At 31 December 2009	Level 1	Level 2	Level 3	Total fair value
	£m	£m	£m	£m
Financial assets at fair value				
Derivatives	-	67	-	67
Financial assets designated at fair value through profit or loss upon initial recognition				
Equities	1	-	2	3
Fixed and variable rate income securities	1,540	42	58	1,640
Collective investment schemes	582	1	174	757
Reinsurers share of investment contract liabilities	-	13	-	13
Deposits received from reinsurers	-	545	-	545
	2,123	601	234	2,958
Total financial assets at fair value	2,123	668	234	3,025

At 31 December 2009	Level 1	Level 2	Level 3	Total fair Value
	£m	£m	£m	£m
Financial liabilities at fair value				
Derivatives	-	48	-	48
Financial liabilities designated at fair value through profit or loss upon initial recognition				
Investment contract liabilities	-	333	-	333
Contingent loan	-	127	-	127
	-	460	-	460
Total financial liabilities at fair value	-	508	-	508

Level 3 financial instrument sensitivities

Level 3 instruments 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

Fixed and variable rate income securities categorised as Level 3 instruments 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

Included in Level 3 instruments in collective investment schemes is an investment in a property related structure with a value of £12m (2009 £15m), which 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 £10m (2009 £3m) and in the worst case scenario the fair value would decrease by £12m (2009 £10m)

Significant transfers of financial instruments between level 1 and level 2

At 31 December 2010	From level 1 to level 2	From level 2 to level 1
	£m	£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	-	48

2010 saw an improvement in the liquidity of the fixed and variable rate income securities market which has resulted in a number of securities moving from level 2 into level 1

There were no significant movements between level 1 and level 2 investments in 2009

Movement in level 3 financial instruments measured at fair value

	At 1 Jan 2010 £m	Total losses in statement of comprehensive income £m	Purchases and sales £m	Transfers to level 1 and level 2 £m	At 31 Dec 2010 £m	Unrealised losses on assets held at end of year £m
Financial assets designated at fair value through profit or loss upon initial recognition						
Equities	2	-	3	-	5	(11)
Fixed and variable rate income securities	58	(15)	34	(8)	69	(11)
Collective investment schemes	174	(86)	-	(3)	85	(5)
	234	(101)	37	(11)	159	(27)

	At 1 Jan 2009 £m	Total losses in statement of comprehensive income £m	Sales £m	Transfers to level 1 and level 2 £m	At 31 Dec 2009 £m	Unrealised losses on assets held at end of year £m
Financial assets designated at fair value through profit or loss upon initial recognition						
Equities	11	(9)	-	-	2	(9)
Fixed and variable rate income securities	81	(13)	-	(10)	58	(13)
Collective investment schemes	230	(5)	(51)	-	174	(10)
	322	(27)	(51)	(10)	234	(32)

Gains and losses on Level 3 financial instruments are included in net investment income in the statement of comprehensive income There were no gains or losses recognised in other comprehensive income

27. Stock lending

The Company lends listed financial assets held in its investment portfolio to other institutions The Company 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 Company retains all the risks and rewards of the transferred assets except for the voting rights The carrying value of fixed and variable rate income securities lent at 31 December 2010 that have not been derecognised amounted to £478m (2009 £618m)

It is the Company's practice to obtain collateral in stocklending transactions, usually in the form of cash or marketable securities

Where the Company receives marketable securities which it is not permitted to sell or re-pledge, the collateral held in the absence of default it is not recognised on the balance sheet The fair value of financial assets accepted as collateral amounts to £nil (2009 £nil)

Where the Company receives collateral in the form of cash or marketable securities which it is permitted to sell or re-pledge, the assets are recognised in the balance sheet 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 2010 is £472m (2009 £597m) and £500m (2009 £649m) respectively

28. Other receivables

	2010 £m	2009 £m
Other receivables	13	5
Amount recoverable after 12 months	-	-

The carrying value amount of other receivables is a reasonable approximate to their fair values

29 Cash and cash equivalents

	2010 £m	2009 £m
Bank and cash balances	8	188
Short-term deposits (including demand and time deposits)	-	13
	8	201

The carrying amounts approximate to fair value at the period end

30 Cash flows

Cash flows from operating activities

	2010 £m	2009 £m
Profit for the year before tax	19	31
Non-cash movements in profit for the year before tax		
Fair value (gains)/losses on		
Financial assets	(139)	(12)
Financial liabilities	53	22
Impairment of		
Acquired value of in-force business and intangibles	1	-
Change in unallocated surplus	(2)	1
Change in deposits received from reinsurers	15	(7)
Interest income on loans	8	(9)
Changes in operating assets and assets and liabilities		
(Increase)/decrease in investment assets	(158)	140
(Increase)/decrease in net derivative assets/(liabilities)	(7)	27
(Increase)/decrease in reinsurance assets	(18)	31
Decrease in insurance contract and investment contract liabilities	(9)	(125)
(Increase)/decrease in other assets/(liabilities)	(27)	(12)
Cash (absorbed)/generated by operations	(264)	87

31. Capital management

Capital Management Framework

The Company'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
- meet the dividend expectations of owners

The framework comprises a suite of capital management policies that govern the allocation of capital throughout the Company 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 is set by the Board and monitored each month at both the executive and Board level The policies ensure sufficient liquidity to meet creditor and dividend obligations through the combination of cash buffers and cash flows Volatility in the latter is monitored at the executive and Board level through stress and scenario testing Where cash flow volatility is judged to be in excess of the Board's risk appetite, de-risking activities are undertaken

The capital policy is set by the Board and monitored on a daily basis These policies ensure there is sufficient capital to meet regulatory capital requirements under a range of stress conditions The capital policy is managed according to the risk profile and financial strength of the company

Regulatory capital requirements

The Company 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 The 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 The 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-profits 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")) The regulatory capital requirement is then deducted from the available capital resources to give the excess capital on a regulatory basis

A further test is required under Pillar 1 in respect of with-profits funds which may result in an additional capital requirement referred to as the "with-profits insurance capital component" ("WPICC")

The table below sets out the Company's capital resources position at 31 December 2010 as reported in the annual returns to the FSA and compares this with the total equity attributable to owners of the Company as reported in the statement of financial position

	2010 £m	2009 £m
Total equity attributable to owners	209	203
Differences in the valuation of assets and liabilities	163	117
Unallocated Surplus	6	8
Intangible Assets	(8)	(8)
Asset values in excess of Pillar 1 counterparty limits	(32)	(33)
Capital resources on a Pillar 1 Regulatory reporting basis	338	287

The Company has complied with externally imposed capital requirements during the year At 31 December 2010, the amount of capital that the Company was required to hold was £92m (2009 £79m) and the excess capital over that required was £246m (2009 £208m)

Pillar 2
The Pillar 2 capital requirements are based on a self-assessment methodology, the Individual Capital Assessment ("ICA") This methodology determines the capital requirement to ensure that the 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 the Company's ICA and may impose additional capital requirements if necessary in the form of Individual Capital Guidance ("ICG")

Group Capital Adequacy
In addition to the requirement to maintain individual capital resources in excess of its individual capital resources requirement, the Company is required to ensure that its capital resources are sufficient to maintain group capital resources in excess of the group capital resources requirement at all times This is calculated at the level of the Company's highest EEA insurance parent undertaking, Phoenix Life Holdings Limited

The group capital resources requirement is an aggregate of the individual capital resources requirements of each of the regulated entities within the Phoenix Group Group capital resources are based on an aggregation of the capital resources of each of the regulated entities, net of the Phoenix Group's investment in them, and net of surplus assets held in the long-term funds of the regulated entities, but without making any deduction for counterparty exposures in excess of defined limits

There are different forms and quality of capital that may be admitted to the calculation of group capital resources and there are also restrictions which limit lower quality capital to prescribed levels Lower quality capital which exceeds these levels must be excluded from group capital resources, with a corresponding effect on the excess of group capital resources over group capital resources requirements

32. Risk management

The Company is exposed to a number of risks in its business including those arising from underlying assets and liabilities The Company complies with the Group approach to risk management which is described in the Performance section of Phoenix Group Holdings annual report and accounts

Risk and capital management objectives
The risk management objectives and policies of the Company are based on the requirement to protect the Company's regulatory capital position, thereby safeguarding policyholders' guaranteed benefits whilst also ensuring the Company can meet various cash flow requirements Subject to this, the Company seeks to use available capital to achieve increased investment returns, balancing risk and reward, to generate additional value for policyholders and owners

In pursuing these objectives, the Company 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

Asset and Liability Management framework
The use of financial instruments naturally exposes the Company to the risks associated with them, chiefly market risk, credit risk and liquidity risk

Responsibility for agreeing the financial risk profile rests with the Board, given advice from investment managers, internal committees and the actuarial function In setting the risk profile, the Board will receive advice from the appointed investment managers and the relevant actuary 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 actuary will also advise the extent to which the investment risk taken is consistent with the Company's commitment to treat customers fairly

Derivatives are used in a number of the Company's funds, within policy guidelines agreed by the Board and overseen by the Investment Committee supported by the management oversight committee Derivatives are primarily used for efficient portfolio management or for risk hedging purposes

More details on the Company's exposure to financial risk are provided below

The Company is also exposed to insurance risk Life assurance risk in the Company 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 Company's exposure to insurance risk is provided below

The Company's overall exposure to investment risk is monitored by appropriate committees, which agree policies for managing each type of risk on an ongoing basis, essentially within the Asset and Liability Management ("ALM") framework that has been developed to achieve investment returns in excess of amounts due in respect of insurance contracts The effectiveness of the Company's ALM framework 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-profits business, which includes all of the Company's participating business, non-linked non-participating business and unit linked-business held within the with-profits and non-profits fund

Financial risk analysis
Transactions in financial instruments may result in the Company assuming financial risks This includes credit risk, market risk and liquidity risk Each of these is described below, together with a summary of how the Company manages them

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 financial obligations can relate to both recognised and unrecognised assets and liabilities

There are two principal sources of credit risk for the Company

- Credit risk which results from direct investment activities, including investments in fixed and variable rate income securities, equities, derivatives, collective investment schemes, hedge funds 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, and the lending of securities

The amount disclosed in the statement of financial position in respect of financial assets, together with rights secured under unrecognised collateral arrangements, and excluding those that back investment contract liabilities, represents the Company's maximum exposure to credit risk Credit risk is managed by monitoring of the Company's aggregate exposures to individual counterparties and by appropriate credit risk diversification The Company manages the level of credit risk it accepts through comprehensive credit risk tolerances In certain cases, protection against exposure to particular credit risk types may be achieved through use of derivatives

The Company's credit risk policy sets out the assessment and determination of what constitutes credit risk for the Company Compliance with the policy is monitored and significant exposures and breaches are reported to the Investment Committee The policy is regularly reviewed for pertinence and for changes in the risk environment

Quality of credit risk
An indication of the Company'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

At 31 December 2010

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Non rated £m	Unit Linked £m	Total £m
Loans	-	-	-	-	-	-	146	-	146
Denvatives	-	85	14	-	-	-	-	-	99
Fixed and vanable rate income secunties	1,022	107	245	122	24	17	17	-	1,554
Reinsurers' share of investment contract liabilities	-	-	-	-	-	-	-	13	13
Reinsurers' share of insurance contract liabilities	-	-	9	-	-	-	598	-	607
Cash and cash equivalents	-	11	(3)	-	-	-	-	-	8

At 31 December 2009

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Non rated £m	Unit Linked £m	Total £m
Loans	-	-	-	-	-	-	209	-	209
Denvatives	-	5	62	-	-	-	-	-	67
Fixed and vanable rate income secunties	698	780	93	25	11	12	21	-	1,640
Reinsurers' share of investment contract liabilities	-	-	-	-	-		-	13	13
Reinsurers' share of insurance contract liabilities	-	-	11	-	-	-	578	-	589
Cash and cash equivalents	49	56	66	-	-	-	30	-	201

Credit ratings have not been disclosed in the above tables for equities Whilst the Company is exposed to the impact of credit default on its equity holdings, this risk is not considered significant due to the spread of holdings Non-equity based denvatives are included in the credit risk table above and are subject to appropriate collateral arrangements

Credit ratings have also not been disclosed in the above tables for holdings in collective investment schemes The risk of loss to the Company due to credit default on its holdings in collective investment schemes is considered low due to the tradable nature of these investments

It is also the Company'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 vanety 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 Company's rating policy The attributable risk ratings are assessed and updated regularly and significant exposures and breaches are reported to the Board and to the investment committee

A further indicator of the quality of the Company's financial assets is the extent to which they are neither past due nor impaired The Company had no material assets which were impaired or past due (2009 £nil)

Concentration of credit risk
Concentration of credit risk might exist where the Company 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 Company counterparty risk is monitored by the counterparty limits contained within the investment guidelines and investment management agreements, overlaid by regulatory requirements

The Company is also exposed to concentration risk with individual reinsurers and outsourced service providers This is due to the nature of the reinsurance and the outsourced service market The Company operates a policy to manage reinsurance and outsourcer service counterparty exposures and the impact from default is reviewed regularly by executive committees and measured through the ICA stress and scenario testing

Reinsurance
The Company is exposed to credit risk as a result of insurance risk transfer contracts with reinsurers This also gives rise to concentration of risk with individual reinsurers, due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings The Company manages its exposure to reinsurance credit risk through the operation of a reinsurance policy and regular monitoring of exposures at the Reinsurance Management Committee The Company's largest reinsurance counterparty is Opal, a fellow group

Company, the reinsurance asset recoverable at 31 December 2010 was £535m (2009 £515m) In order to mitigate the credit risk arising from this exposure and to protect policyholders, the terms of the reinsurance arrangements provide that the initial premium payable has been withheld and placed in a collateral account

Collateral
The credit risk of the Company 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 reinsurance securities lending 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 Further details are given in notes 13, 14 and 27 above

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 prices Market risk comprises interest risk, currency risk and other price risk

The Company 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 owners' reserves yet to be distributed, surplus assets within the long-term funds and assets held to meet regulatory capital and solvency requirements, and
- the income flow of management charges from the invested assets of the Company

The Company manages the levels of market risk that it accepts through an approach to investment management policy and an approach to investment management that determines

- the constituents of market risk for the Company,
- the basis used to fair value financial assets and liabilities,
- the asset allocation and portfolio limit structure,
- diversification from 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 risk
Interest 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 risk is managed by matching assets and liabilities where practicable and by entering into swap arrangements where appropriate This is particularly the case for the non-profit funds For with-profit business, some element of investment mismatching is permitted where it is consistent with the principles of treating customers fairly The with-profits funds of the Company provide capital to allow such mismatching to be effected

In practice, the life companies of the Company maintain an appropriate mix of fixed and variable rate income securities 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 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 Company's reported profit after tax and to equity

With-profits business and non-participating business within the with-profit funds are exposed to interest risk as guaranteed liabilities are valued relative to market interest rates and investments include fixed and variable income securities 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 The contribution of these funds to the Company result is determined primarily by either the owners' share of the declared annual bonus or by the owners' interest in any change in value in the capital advanced to the Company's with-profits funds

In the non-profit funds, policy liabilities are duration matched with primarily fixed and variable income securities, with the result that sensitivity to changes in interest rates is very low An increase of 1% in interest rates, with all other variables held constant, would result in an additional profit after tax in respect of a full financial year and an increase in equity of £14m (2009 £7m) A decrease of 1% in interest rates, with all other variables held constant, would result in a decrease in profit after tax in respect of a full financial year and a decrease in equity of £16m (2009 £9m)

Price risk

The Company's price risk exposure relates 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 Company 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 financial position at fair value has exposure to price risk The Company's objective in holding these assets is to earn higher long-term returns by investing in a diverse portfolio of high quality equities and properties Portfolio characteristics are analysed regularly and price risks are actively managed in line with investment mandates The Company'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-profits 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-profits fund policyholders' future bonuses will be impacted by the investment returns achieved and hence the price risk In addition some equity investments are held in respect of owners' funds The Company 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 maintaining adequate regulatory capital and TCF This is largely achieved through asset class diversification

The impact of non-government fixed and variable rate income securities and, inter alia, the change in market credit spreads during the year are fully reflected in the values shown in these financial statements Similarly, the value of derivatives that the Company holds takes into account fully the changes in swap spreads

The sensitivity analysis for equity and property price risk illustrates how a change in the fair value of equities and properties affects the Company result It takes into account the effect of such changes in equity and property prices on all assets and liabilities that contribute to the Company's reported profit after tax and to equity

A 10% decrease in equity/property prices, with all other variables held constant, would result in a decrease in the contingent loan liability in respect of a full financial year and in equity of £8m (2009 £5m)

A 10% increase in equity/property prices, with all other variables held constant, would result in an increase in the contingent loan liability in respect of a full financial year and in equity of £9m (2009 £4m)

There is also an exposure to spread changes affecting the prices of corporate bonds and derivatives This exposure applies to the with-profits fund, unit-linked funds, non-profit funds (where risks and rewards fall wholly to owners) and in owners' funds

A 100 basis point widening of credit spreads, with all other variables held constant, would result in a decrease in the contingent loan liability in respect of a full financial year and in equity of £27m (2009 £29m)

A 100 basis point narrowing of credit spreads, with all other variables held constant, would result in an increase in the contingent loan liability in respect of a full financial year and in equity of £31m (2009 £32m)

Currency risk

The Company'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

The with-profits 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 Fluctuations in exchange rates from holdings in overseas assets are hedged against currency risks

Sensitivity of profit after tax and in equity to fluctuations in currency exchange rates is not considered significant at 31 December 2010 or 31 December 2009, since unhedged exposure to foreign currency was relatively low

Liquidity risk

Liquidity risk is defined as the failure of the Company to maintain adequate levels of financial resources to enable it to meet its obligations as they fall due The Company has exposure to liquidity risk as a result of its inability to meet its short-term cash flow requirements and to meet its obligations to policyholders

The Board has defined a number of governance objectives and principles and the liquidity risk frameworks are designed to ensure that

- liquidity risk is managed in a manner consistent with the Company's strategic objectives, risk appetite and Principles and Practices of Financial Management ("PPFM"),
- cash flows are appropriately managed and the reputation of the Company and the Phoenix Group are safeguarded, and
- appropriate information on liquidity risk is available to those making decisions

The Company's policy is to maintain sufficient liquid assets of suitable credit quality at all times and, where appropriate, to have 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 Company's commercial property investments are held through a unit trust managed by Ignis Asset Management Limited, a fellow group company This unit trust has the power to restrict and/or suspend withdrawals, which would, in turn, affect liquidity To date, the unit trust has continued to process both investments and realisations in a normal manner and has not imposed any restrictions or delays The Company has applied a 10% discount to the net asset value on certain property unit trusts to reflect their liquidity in the current market

The Company's investments in the Ignis Fundamental Solutions Fund ("IFSF") and the Ignis Strategic Solutions Fund ("ISSF") are managed by Ignis Asset Management Limited The fund managers of the underlying funds have the power to impose gates on redemptions which can restrict available liquidity within the funds

The following table provides a maturity analysis showing the remaining contractual maturities of the Company'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 financial position in accordance with the requirements of IFRS 4

At 31 December 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	263	335	641	296	1,535
Investment contracts	351	-	-	-	351
Deposits received from reinsurers	-	-	-	560	560
Derivatives	5	3	155	-	163
Obligations for repayment of collateral received	501	5	19	-	525
Contingent loan	-	-	-	180	180
Payables related to direct insurance contracts	6	-	-	-	6
Accruals	2	-	-	-	2
Other payables	9	-	-	-	9

At 31 December 2009

	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	778	218	312	254	1,562
Investment contracts	333	-	-	-	333
Deposits received from reinsurers	-	-	-	545	545
Derivatives	3	3	103	-	109
Obligations for repayment of collateral received	649	-	-	15	664
Contingent loan	-	-	-	127	127
Payables related to direct insurance contracts	9	-	-	-	9
Accruals	1	-	-	-	1
Other payables	19	-	-	-	19

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 Company does not expect all these amounts to be paid out within one year of the reporting date

A significant proportion of the Company's financial assets are held in gilts, cash, supranationals and highly rated securities which the Company considers sufficient to meet the liabilities as they fall due

Investment contracts
For investment contracts the Company matches all the liabilities with assets in the portfolio on which the unit prices are based with the exception of reinsurance exposure on certain lines of unit-linked business there is therefore no interest, price, currency or credit risk for the Company on these contracts

In extreme circumstances, the Company 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 Company 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 Company's own risk exposure

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 Company's liabilities under insurance contracts are detailed in note 11 and include the following sources of insurance risk

- Mortality – Higher than expected death claims on assurance products,
- Longevity – Lower than expected number of deaths experienced on annuity products or greater than expected improvements in life expectancy on immediate and deferred annuity products,
- Expenses – Policies cost more to administer than expected,
- Lapses – An adverse movement 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

Objectives and policies for mitigating insurance risk
The Company 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 In addition to this, mortality, longevity and morbidity risks are in certain circumstances mitigated by the use of reinsurance

The profitability of the run-off of the Company's closed long-term insurance businesses 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 Board 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

Sensitivities

Insurance liabilities are sensitive to changes in risk variables, such as prevailing market interest rates, currency rates and asset 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 Sometimes allowance must also be made for the effect on future assumptions of management or policyholder actions in certain economic scenarios 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 contingent loan liability of £4m (2009 £4m)

An increase of 5% in assurance mortality, with all other variables held constant, would result in a decrease in the contingent loan liability of £4m (2009 £5m)

A decrease of 5% in annuitant longevity, with all other variables held constant, would result in an increase in the contingent loan liability of £1m (2009 £1m)

An increase of 5% in annuitant longevity, with all other variables held constant, would result in a decrease in the contingent loan liability of £1m (2009 £1m)

A decrease of 25% in lapse rates, with all other variables held constant, would result in a decrease in the contingent loan liability of £3m (2009 £2m)

An increase of 25% in lapse rates, with all other variables held constant, would result in an increase in the contingent loan liability of £3m (2009 £2m)

Assumptions

Valuation of participating insurance and investment contracts

For participating business, which is with-profits business (insurance and investment contracts), the insurance contract liability is calculated in accordance with the FSA's realistic capital regime, adjusted to exclude the owners' 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 a gross premium valuation method

Process used to determine assumptions

For participating business the assumptions about future demographic trends are intended to be "best estimates" They are determined after considering the Company's 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 Phoenix Group The impact of material changes during the year were as follows

	Increase in insurance liabilities 2010 £m	Increase in insurance liabilities 2009 £m
Change in expenses assumptions	1	2

Valuation interest rate

For participating business 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 non-participating business, the method used to determine valuation interest rates generally follows the regulations set out in the FSA Handbook 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

Product	2010	2009
Life non-profit linked	3 40%	3 00%
Pension non-profit linked	3 40%	3 70%
Life non-profit non-linked	3 09%	3 29%
Pension non-profit non-linked	4 10%	4 35%
Life annuities	3 20%	3 41%
Term assurance	3 09%	3 29%
Pension annuities in payment	4 32%	4 56%
Deferred pension annuities	4 10%	4 35%
Index Linked Annuities	3 84%	4 16%

Expense inflation
Expenses are assumed to increase at the rate of increase in the Retail Price Index excluding mortgage payments ("RPIX") in accordance with the Management Service Agreement ("MSA") (with each increase being subject to a maximum of 5% per annum) the Company has in place with PGS For with-profits 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 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

The mortality assumptions were varying proportions of the following published tables

	Published Table 2010	Published Table 2009
Annuities in payment (UK – level)	Modified PMA00 Modified PFA00	Modified PMA00 Modified PFA00
Annuities in payment (UK – index linked)	Modified PMA00 Modified PFA00	Modified PMA00 Modified PFA00
Deferred Annuities (UK, in deferment)	A67-70	A67-70
Whole of life and endowments	A67-70	A67-70
Term assurance	A67-70	A67-70

Lapse rates
The assumed rates for surrender and voluntary premium discontinuance in the participating business depend primarily on the length of time a policy has been in force Withdrawal rates used in the valuation of with-profits 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-profits contracts will be higher on policy anniversaries on which Market Value Adjustments do not apply

Policyholder options and guarantees
Some of the Company'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-profits 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-profits bonds it is often a specified anniversary of commencement, in some cases with further dates thereafter Annual bonuses when added to with-profits 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 below for details) The total amount provided in the with-profits and non-profit funds in respect of the future costs of guaranteed annuity options are £57m (2009 £55m)

Discretionary participating bonus rate
The regular bonus rates assumed in each scenario are determined in accordance with the 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

With-profits 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

In common with other life companies in the UK which have written pension transfer and opt-out business, the Company 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 non-profit funds in respect of the review and possible redress relating to pension policies, including associated costs, are £9m (2009 £8m)

Managing product risk
The following sections give an assessment of the risks associated with the Company's main products and the ways in which the Company manages those risks

	2010 Gross Liabilities		2010 Reinsurance Share	
	Insurance contracts £m	Investment contracts with DPF £m	Insurance contracts £m	Investment contracts with DPF £m
With-profits funds				
Pensions				
Deferred annuities – with guarantees	286	-	-	-
Deferred annuities – without guarantees	7	107	-	-
Immediate annuities	156	-	66	-
Unitised with-profits	-	11	-	-
Total pensions	449	118	66	-
Life				
Immediate annuities	-	-	10	-
Unitised with-profits	7	-	-	-
Life with-profits	275	-	-	-
Total life	282	-	10	-
Other	16	-	-	-
	747	118	76	-
Non-profit funds				
Deferred annuities – without guarantees	29	-	-	-
Immediate annuities	621	-	530	-
Protection	8	-	1	-
Other	11	-	-	-
	669	-	531	-
	1,416	118	607	-

	2009 Gross Liabilities		2009 Reinsurance Share	
	Insurance contracts £m	Investment contracts with DPF £m	Insurance contracts £m	Investment contracts with DPF £m
With-profits funds				
Pensions				
Deferred annuities – with guarantees	305	-	-	-
Deferred annuities – without guarantees	8	112	-	-
Immediate annuities	145	-	-	-
Unitised with-profits	-	11	-	-
Total pensions	458	123	-	-
Life				
Unitised with-profits	8	-	-	-
Life with-profits	302	-	10	-
Total life	310	-	10	-
Other	13	-		
	781	123	10	-
Non-profit funds				
Deferred annuities – without guarantees	32	-	-	-
Immediate annuities	607	-	578	-
Protection	9	-	1	-
Other	10	-	-	-
	658	-	579	-
	1,439	123	589	-

With-profits fund (Unitised and Traditional)
The Company operates a with-profits fund in which the with-profits policyholders benefit from a discretionary annual bonus (guaranteed once added in most cases) and a discretionary final bonus The fund includes immediate annuities and deferred annuities with Guaranteed Annuity Rates ("GAR")

The investment strategy backing different blocks of policies are different, but is broadly to invest in a mixture of fixed and variable rate income securities and equities and/or property in such proportions as is appropriate to the investment risk exposure of the group of policies and its capital resources

The Company has significant discretion regarding investment policy, bonus policy and early termination values The process for exercising discretion in the management of the with-profits fund is set out in the PPFM for the with-profits fund and is overseen by with-profits committee Advice is also taken from the with-profits actuary 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-profits fund together with other elements of the experience of the fund The owners of the Company are entitled to receive one-ninth of the cost of bonuses declared

Unitised and traditional with-profits policies are exposed to equivalent risks, the main difference being that unitised with-profits policies purchase notional units in a with-profits fund whereas traditional with-profits policies do not Benefit payments for unitised policies are then dependent on the number of units held at the time of a claim, although charges may be applied The unitised with-profits unit price is fixed, bonus units are granted to policyholders in line with any discretionary bonus payments over the course of one year

Cash bonus policies
Cash Bonus policies are written as whole of life and endowment assurances where discretionary bonus for is calculated as a percentage of the premium It is intended that the rate of bonus in any year will be at least maintained throughout the term of each policy Bonus declarations are stated as an increase to the previously declared rate Once the rate of bonus exceeds 100%, the premium is extinguished and the rate of bonus reduced by 100% Actual cash bonuses, once allocated, are credited to an accumulation account which accrues with interest The accumulation account can be cashed at any time without penalty Whole of life assurances also have the option to surrender on guaranteed terms

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 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 guaranteed terms on GAR policies are more favourable than the annuity rates currently available in the market available for cash benefits Similarly, the guaranteed terms on GCO policies provide more favourable transfer values than would otherwise be the case

The option provisions on GAR and GCO 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), the Company has purchased derivatives that provide protection against an increase in liabilities and have thus reduced the sensitivity of profit to movements in interest rates

The Company 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

Investment risk depends on the extent to which the annuity payments 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

33 Related party transactions

The Company enters into transactions with related parties in its normal course of business These are at arm's length on normal commercial terms

Pearl Group Services Limited and Pearl Group Management Services Limited and provide management services to the Company, in the form of staff and other services, under a management services agreement The charge made to the Company for the year ended 31 December 2010 amounted to £4m (2009 £5m) and at the end of the year £nil (2009 £nil) remained outstanding

Ignis Investment Management Limited, a fellow group company, and it subsidiaries provide investment management services to the Company in accordance with a number of investment management agreements The charge made to the Company for the year ended 31 December 2010 amounted to £2m (2009 £2m) and at the end of the year £nil (2009 £nil) remained outstanding

In the year ended 31 December the Company received interest on loans to PGH2, the Company's immediate parent, of £2m (2009 £3m) and interest on loans to fellow subsidiary, National Provident Life Limited, of £6m (2009 £6m)

Reinsurance transactions

	2010 £m	2009 £m
Reinsurance ceded to fellow subsidiaries		
Premiums	-	2
Claims	44	45
Share of reinsurance assets	607	589

Amounts due to related parties

	2010 £m	2009 £m
Loans due to parent	180	127
Other amounts due to parents	2	6
Loans due to fellow subsidiaries	25	30
Other amounts due to fellow subsidiaries	6	11

Amounts due from related parties

	2010 £m	2009 £m
Loans due from parents	75	74
Loans due from fellow subsidiaries	78	133
Other amounts due from fellow subsidiaries	2	3

Key management compensation

The compensation payable to employees classified as key management, which comprises the Directors, is disclosed in note 5

During the year to 31 December 2010, key management and other family members contributed £2,000 (2009 £27,000) to products sold by the Company These related primarily to investment, life and pensions products

Parent and ultimate parent entity
Information on the Company's parent and ultimate parent is given in note 35

34. Contingent liabilities

In the normal course of business the Company is exposed to certain legal issues, which involve litigation and arbitration, and as at the period end, the Company has a contingent liability in this regard

Categorisation of excess working capital to shareholder funds
The Company has provided information to the FSA on its categorisation of £54m of excess working capital to shareholder funds in 2006 The Directors are confident in their treatment, which is supported by legal and actuarial advice, but note that discussions with the FSA are continuing

Reassurance arrangement with Opal
Under the terms of the reassurance arrangement between the Company and Opal the Company has a contingent liability of 80/130ths of an increase in the treaty best estimate reserves resulting from mortality improvements The maximum liability under the arrangement is £15m at 31 December 2010 (2009 £15m)

35 Other information

The Company's principal place of business is the United Kingdom The Company's immediate parent is Pearl Group Holdings (No 2) Limited and its ultimate parent undertaking is Phoenix Group Holdings, a company incorporated in the Cayman Islands and resident in Jersey A copy of the financial statements of Phoenix Group Holdings can be obtained from the Company Secretary, 1st Floor, 32 Commercial Street, St Helier, Jersey, JE2 3RU

36. Events after the reporting period

On 1 March 2011, the European Court of Justice ('ECJ') ruled that insurance companies will, with effect from 21 December 2012, no longer be allowed to use gender as a basis for calculating premiums At this time, the precise impact of this judgement is uncertain, and management is currently examining the implications Consequently, it is not yet possible to determine with any certainty what the effect of this judgement may be on the Company

Transition to International Financial Reporting Standards

Introduction

The financial statements set out on pages 8 to 54 are the Company's first annual financial statements prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS") The accounting policies set out on pages 8 to 13 have been applied in preparing the financial statements for the year ended 31 December 2010 and for preparing an opening IFRS statement of financial position as at 1 January 2009, the date of transition from United Kingdom Generally Accepted Accounting Principles ("UK GAAP") to IFRS

An explanation of how the transition from UK GAAP to IFRS has affected the Company's financial position and financial performance for 2009 is set out in the following tables and accompanying notes Under UK GAAP the Company was exempt from presenting a cash flow statement

The following information is set out below in relation to the transition from UK GAAP to IFRS

1 The selection of IFRS accounting policies that have been applied in preparing the results for 2010
2 An explanation of the principal classification changes to the assets and liabilities as at 1 January 2009 and 31 December 2009 and total comprehensive income for the year to 31 December 2009
3 An explanation of the changes to the measurement of assets and liabilities as at 1 January 2009 and 31 December 2009, together with their effect on equity and total comprehensive income for the year ended 31 December 2009
4 Summary tables showing the financial impact of the above changes on equity, liabilities and assets as at 1 January 2009 and 31 December 2009 and total comprehensive income for the year to 31 December 2009

1. Selection of accounting policies

Certain IFRS permit entities to choose between alternative accounting treatments The principal choices that have been made by the Company are set out below

Investment contracts with discretionary participation features
IFRS 4 *Insurance Contracts* permits an entity to account for investment contracts with Discretionary Participation Features ("DPF") as if they are insurance contract A decision has been taken to adopt the permitted alternative accounting treatment for these contracts

Unallocated surplus
IFRS 4 *Insurance Contracts* requires the unallocated surplus for with-profit business to be shown in the statement of financial position as either equity or as a liability or split between the two The Company has elected to show the unallocated surplus within insurance contracts liabilities

Acquired insurance contracts
IFRS 4 *Insurance contracts* permits the fair value of insurance liabilities acquired in a business combination to be split into two components, comprising (a) a liability measured in accordance with the insurer's accounting policies for insurance contracts that it issues and (b) an intangible asset, representing the difference between (i) the fair value of the contractual insurance rights acquired and (ii) the amount described in (a) The Company has taken advantage of this in recognising the fair value of insurance liabilities acquired in previous business combinations

Investments in subsidiaries
IAS 27 *Consolidated and Separate Financial Statements* permits an entity to measure its investments in subsidiaries at either cost or fair value and the Company has decided to adopt cost as its IFRS accounting policy IFRS 1 *First-time Adoption of International Financial Reporting Standards* permits a first time adopter to use its UK GAAP carrying values of investments in subsidiaries as the deemed cost on transition to IFRS Advantage has been taken of this exemption and accordingly the previous UK GAAP carrying amounts of investments in subsidiaries have been used as the deemed cost in the first IFRS financial statements Subsequently, investments in subsidiaries will be measured at cost less impairment as required by IAS 36 *Impairment of Assets* Consequently, no measurement changes have been made on transition to IFRS

Intangible assets
Intangible assets may either be recognised using the cost model or the revaluation model The Company has adopted the cost model in recognising the intangible asset "Acquired in-force business"

2 IFRS classification changes (column 1)

The principal classification changes at 1 January 2009 are as follows (see column 1 in the transition tables below) These have no effect on equity

- Assets held to cover linked liabilities of £295m (31 December 2009 £320m) have been reclassified to collective investment schemes £282m (31 December 2009 £287m), cash and cash equivalents £11m (31 December 2009 £30m) and other assets £2m (31 December 2009 £3m)

  Under UK GAAP the above items are separately disclosed whereas under IFRS the individual line items have to be presented

- The provision for linked liabilities of £307m (31 December 2009 £303m) has been reclassified to investment contract liabilities The change in provision for linked liabilities at 31 December 2009 has been reclassified to Change in investment contract liabilities

3. Measurement changes (column 3 to column 4)

The principal measurement changes are set out below These have no effect on equity

Acquired in-force business (Column 3)

IFRS requires the value of acquired in-force business to be grossed up for the related policyholder and owners' taxes, with a corresponding adjustment to deferred tax Under UK GAAP the value of acquired in-force business is presented on a net of tax basis

As at 1 January 2009 this has resulted in the carrying values of acquired in-force business and deferred tax being increased by £2m (31 December 2009 £2m) This change has no effect on equity

Current and deferred tax (Column 4)

Under UK GAAP deferred tax can be discounted to present values, this is not permitted under IAS 12 *Income Taxes*

The adjustment required to comply with IAS 12 as at 1 January 2009 are

- Removal of discounting on deferred tax has resulted in the deferred tax asset increasing by £1m (31 December 2009 £3m) and the contingent loan liability increasing by the same amount This change has no effect on equity

4. Transition tables

Statement of comprehensive income for the year ended 31 December 2009

	As previously reported under UK GAAP			IFRS	IFRS measurement changes		IFRS
	Technical account	Non-technical account	IFRS classification changes Col 1	As reclassified Col 2	Acquired in force business Col 3	Removal of discounting on deferred tax Col 4	As reported under IFRS Col 5
	£m	£m	£m	£m	£m	£m	£m
Gross premiums written	24	-	-	24	-	-	24
Less premiums ceded to reinsurers	2	-	-	2	-	-	2
Net premiums written	26	-	-	26	-	-	26
Fees and commissions	3	-	-	3	-	-	3
Net investment income	98	10	-	108	-	(2)	106
Total revenue, net of reinsurance payable	127	10	-	137	-	(2)	135
Net income	127	10	-	137	-	(2)	135
Policyholder claims	(173)	-	-	(173)	-	-	(173)
Less reinsurance recoveries	45	-	-	45	-	-	45
Change in insurance contract liabilities	151	-	-	151	-	-	151
Change in reinsurers' share of insurance contract liabilities	(31)	-	-	(31)	-	-	(31)
Transfer from unallocated surplus	(1)	-	-	(1)	-	-	(1)
Net policyholder claims and benefits incurred	(9)	-	-	(9)	-	-	(9)
Change in investment contract liabilities	-	-	(47)	(47)	-	-	(47)
Change in technical provisions for linked liabilities	(47)	-	47	-	-	-	-
Administrative expenses	(10)	-	-	(10)	-	-	(10)
Other operating expenses	(31)	-	-	(31)	-	-	(31)
Total operating expenses	(97)	-	-	(97)	-	-	(97)
Profit before finance costs and tax	30	10	-	40	-	(2)	38
Finance costs	(7)	-	-	(7)	-	-	(7)
Profit for the year before tax	23	10	-	33	-	(2)	31
Tax attributable to policyholders' returns	-	-	-	-	-	(2)	(2)
Profit before tax attributable to owners	23	10	-	33	-	(4)	29
Tax (charge)/credit	(22)	1	-	(21)	-	2	(19)
Less tax attributable to policyholders' returns	-	-	-	-	-	2	2
Tax attributable to owners	(22)	1	-	(21)	-	4	(17)
Profit for the year	1	11	-	12	-	-	12
Other comprehensive income	-	-	-	-	-	-	-
Total comprehensive income for the year	1	11	-	12	-	-	12

Statement of Financial Position - Equity and liabilities as at 01 January 2009

	UK GAAP		IFRS	IFRS Measurement changes		IFRS
	As previously reported under UK GAAP	IFRS classification changes	As reclassified	Acquired in force business	Removal of discounting on deferred tax	As reported under IFRS
		Col 1	Col 2	Col 3	Col 4	Col 5
Equity and liabilities	£m	£m	£m	£m	£m	£m
Equity attributable to owners of the parent						
Share capital	19	-	19	-	-	19
Reserves	172	-	172	-	-	172
Total equity	191	-	191	-	-	191
Liabilities						
Insurance contract liabilities						
Liabilities under insurance contracts	1,713	-	1,713	-	-	1,713
Unallocated surplus	7	-	7	-	-	7
Provision for linked liabilities	307	(307)	-	-	-	-
	2,027	(307)	1,720	-	-	1,720
Financial liabilities						
Investment contracts	-	307	307	-	-	307
Deposits received from reinsurers	552	-	552	-	-	552
Derivatives	117	-	117	-	-	117
Obligations for repayment of collateral received	726	-	726	-	-	726
Contingent loan	104	-	104	-	1	105
	1,499	307	1,806	-	1	1,807
Provisions	4	-	4	-	-	4
Deferred tax	-	-	-	2		2
Payables related to direct insurance contracts	6	-	6	-	-	6
Accruals	3	-	3	-	-	3
Other payables	8	-	8	-	-	8
Total liabilities	3,547	-	3,547	2	1	3,550
Total equity and liabilities	3,738	-	3,738	2	1	3,741

Statement of Financial Position - Assets as at 1 January 2009

	UK GAAP		IFRS	IFRS Measurement changes		IFRS
Assets	**As previously reported under UK GAAP** £m	**IFRS classification changes** Col 1 £m	**As reclassified** Col 2 £m	**Acquired in force business** Col 3 £m	**Removal of discounting on deferred tax** Col 4 £m	**As reported under IFRS** Col 5 £m
Intangible assets - Acquired in-force business	7		7	2	-	9
Financial assets						
Loans and deposits	237	(61)	176	-	-	176
Derivatives	179	-	179	-	-	179
Equities	10	1	11	-	-	11
Fixed and variable rate income securities	1,766	-	1,766	-	-	1,766
Collective investment schemes	515	282	797	-	-	797
Assets held to cover linked liabilities	295	(295)	-	-	-	-
Reinsurers share of investment contract liabilities	12	-	12	-	-	12
	3,014	(73)	2,941	-	-	2,941
Deferred tax assets	8	-	8	-	1	9
Insurance assets						
Reinsurers' share of insurance contract liabilities	620	-	620	-	-	620
Reinsurance receivables	1	-	1	-	-	1
Insurance contract receivables	4	-	4	-	-	4
	625	-	625	-	-	625
Current tax	2	-	2	-	-	2
Prepayments and accrued income	27	-	27	-	-	27
Other receivables	20	1	21	-	-	21
Cash and cash equivalents	35	72	107	-	-	107
Total assets	3,738	-	3,738	2	1	3,741

Statement of Financial Position - Equity and liabilities as at 31 December 2009

	UK GAAP		IFRS	IFRS measurement changes		IFRS
	As previously reported under UK GAAP	IFRS classification changes Col 1	As reclassified Col 2	Acquired in force business Col 3	Removal of discounting on deferred tax Col 4	As reported under IFRS Col 5
Equity and liabilities	£m	£m	£m	£m	£m	£m
Equity attributable to owners of the parent						
Share capital	19	-	19	-	-	19
Retained earnings	184	-	184	-	-	184
Total equity	203	-	203	-	-	203
Liabilities						
Insurance contract liabilities						
Liabilities under insurance contracts	1,562	-	1,562	-	-	1,562
Unallocated surplus	8	-	8	-	-	8
Provision for linked liabilities	333	(333)	-	-	-	-
	1,903	(333)	1,570	-	-	1,570
Financial liabilities						
Investment contracts	-	333	333	-	-	333
Deposits received from reinsurers	545	-	545	-	-	545
Derivatives	48	-	48	-	-	48
Obligations for repayment of collateral received	664	-	664	-	-	664
Contingent loan	124	-	124		3	127
	1,381	333	1,714	-	3	1,717
Provisions	2	-	2	-	-	2
Deferred tax	-	-	-	2	-	2
Payables related to direct insurance contracts	9	-	9	-	-	9
Current tax	6	-	6	-	-	6
Accruals	1	-	1	-	-	1
Other payables	19	-	19	-	-	19
Total liabilities	3,321	-	3,321	2	3	3,326
Total equity and liabilities	3,524	-	3,524	2	3	3,529

Statement of Financial Position - Assets as at 31 December 2009

	UK GAAP		IFRS	IFRS measurement changes		IFRS
	As previously reported under UK GAAP	IFRS classification changes Col 1	As reclassified Col 2	Acquired in force business Col 3	Removal of discounting on deferred tax Col 4	As reported under IFRS Col 5
Assets	£m	£m	£m	£m	£m	£m
Intangible assets						
Acquired in-force business	7	-	7	2	-	9
Financial assets						
Loans and deposits	222	(13)	209	-	-	209
Derivatives	67	-	67	-	-	67
Equities	2	1	3	-	-	3
Fixed and variable rate income securities	1,640	-	1,640	-	-	1,640
Collective investment schemes	469	287	756	-	-	756
Assets held to cover linked liabilities	320	(320)	-	-	-	-
Reinsurers share of investment contract liabilities	13	-	13	-	-	13
	2,733	(45)	2,688	-	-	2,688
Deferred tax assets	7	-	7	-	3	10
Insurance assets						
Reinsurers' share of insurance contract liabilities	589	-	589	-	-	589
Insurance contract receivables	4	-	4	-	-	4
	593	-	593	-	-	593
Prepayments and accrued income	23	-	23	-	-	23
Other receivables	3	2	5	-	-	5
Cash and cash equivalents	158	43	201	-	-	201
Total assets	3,524	-	3,524	2	3	3,529