PHOENIX GROUP

OPPORTUNITIES FOR GROWTH

Phoenix Group Holdings
Annual Report and Accounts 2016

PHOENIX GROUP HOLDINGS
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ABOUT US

Phoenix Group is the largest UK consolidator of closed life assurance funds, with assets under management of £76 billion, and more than six million policyholders.

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OUR MARKET

There are over £300 billion of assets held in closed life funds in the UK (excluding Phoenix).

12 Read more about the market place

"PHOENIX HAS MADE AN IMPORTANT INVESTMENT IN ITS SPECIALIST PLATFORM TO MANAGE CLOSED LIFE FUNDS, WHICH ENABLES IT TO ACQUIRE CLOSED LIFE FUNDS MORE EFFECTIVELY."

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

06 Read more in the CEO's report

PHOENIX GROUP AT A GLANCE

Phoenix is the UK's largest specialist closed life assurance fund consolidator.

c.6.1m
Policyholders

£76bn
Assets under management

OUR VISION

To be the saver-friendly 'industry solution' for the safe, innovative and profitable management of closed life funds.

OUR MISSION

To improve returns for policyholders while delivering value for shareholders.

OUR STRATEGIC PRIORITIES

IMPROVE CUSTOMER OUTCOMES

Improving customer outcomes is central to our vision of being the saver-friendly 'industry solution' for closed life funds.

DRIVE VALUE

In order to drive value, the Group looks to undertake management actions which increase and accelerate cash flows or enhance value.

MANAGE CAPITAL

The effective management of our risks and the efficient allocation of capital against them is critical in allowing us to achieve our strategic and operational objectives.

ENGAGE PEOPLE

Our people underpin everything that we do. The Group specifically targets, recruits and develops top quality people to support the achievement of its strategic and operational objectives.

18 Read more about our strategy and KPIs

OUR SPECIALIST OPERATING MODEL

Underpinned by 'The Phoenix Way', which characterises an approach and infrastructure for the efficient and effective structuring, integration and management of closed life funds and the investments they hold.

16 Read more about our operating structure

Key performance indicators

£486m
Operating companies' cash generation

£1.9bn
PLHL Solvency II surplus (pro forma)

£351m
Operating profit

170%
PLHL Shareholder Capital Coverage ratio (pro forma)

23 Read more about PLHL's pro forma Solvency II capital position

Other performance indicators

23.9p
Final dividend per share

£(100)m
IFRS loss after tax

31 Read more about our IFRS results

2016 ACQUISITIONS

In line with our strategy, we have acquired new businesses which have become part of the Phoenix Group.

The acquisitions of AXA Wealth's pension and protection businesses and Abbey Life reinforce Phoenix's position as the UK's leading closed life fund consolidator.

06 Read more about the acquisitions

Phoenix has been a well-known name in the insurance world since 1782. From its beginnings more than 200 years ago, it has grown to become the largest UK consolidator of closed life assurance funds.

2017	The Group obtains PRA's approval to incorporate AXA Wealth's pension and protection businesses into the Group's Solvency II Internal Model Issued £300 million Tier 3 bond
2016	Phoenix Group Holdings successfully completes two acquisitions – AXA Wealth's pension and protection businesses, and Abbey Life Assurance Company Limited Agreed a revised unsecured revolving credit facility offering greater flexibility to make acquisitions
2015	Investment grade credit rating achieved from Fitch Ratings Solvency II full Internal Model approved Exchange of Tier 1 bonds into new subordinated notes
2014	Divestment of Ignis Asset Management Refinanced the Group's remaining senior bank debt and PIK notes into a single £900 million facility Issued £300 million unsecured seven-year bond
2013	Successful debt re-terming and equity raising of £250 million
2012	Transferred approximately £5 billion of annuity liabilities to Guardian Assurance Transferred business of NPI Limited to Phoenix Life Limited and London Life Limited to Phoenix Life Assurance Limited
2010	Pearl Group renamed Phoenix Group Holdings and achieves Premium Listing on London Stock Exchange
2009	Liberty Acquisition Holdings (International) acquires Pearl Group
2008	Pearl Group acquires Resolution plc
2006	Resolution plc acquires Abbey National's life business
2005	Pearl Group created Resolution Life Group acquires Swiss Life (UK) plc Britannic acquires Century Group and merges with Resolution Life Group to form Resolution plc
2004	Resolution Life Group acquires UK life operations of Royal & Sun Alliance Britannic acquires life operations of Allianz Cornhill
2001	Abbey National acquires Scottish Provident
1999	Britannic acquires Alba Life
1996	Royal & Sun Alliance established
1905	Britannic Assurance Company established
1857	Pearl Loan Company established
1837	Scottish Provident established
1836	Edinburgh & Glasgow Assurance established
1835	NPI established
1806	London Life established
1782	Phoenix Assurance established

CHAIRMAN'S STATEMENT

"THE ACQUISITIONS COMPLETED BY THE GROUP IN 2016 HAVE REINFORCED PHOENIX'S POSITION AS THE UK'S LARGEST CLOSED LIFE FUND CONSOLIDATOR."

HENRY STAUNTON
CHAIRMAN

2016 was a pivotal year for Phoenix Group. The acquisitions of AXA Wealth's pension and protection businesses for £373 million and Abbey Life for £933 million have together transformed the size of the Group. Life company assets have increased to £76 billion, managed on behalf of over 6 million policyholders.

The transactions met Phoenix's strict acquisition criteria, allowing an increase in the dividend per share whilst strengthening the Group's balance sheet. The Group also received significant support from both its shareholders and its lending banks in relation to the acquisitions, with the £735 million rights issue to finance the Abbey Life acquisition achieving a 98% take-up by shareholders.

Phoenix is currently focused on the efficient integration of the acquired businesses to deliver the planned synergies whilst ensuring policyholders remain protected. The Group has already realised significant benefits, delivering £282 million of cash from the AXA Wealth acquisition to date.

This corporate activity has been undertaken against a backdrop of challenging market conditions, including a sharp decline in long-term interest rates during the year. Phoenix has shown considerable agility in navigating the volatile interest rate environment and has continued its track record of meeting publicly stated targets, successfully executing management actions and further improving customer outcomes. The interest rate hedging strategies implemented during the course of 2016 helped mitigate the adverse impacts of market movements and underpinned Phoenix's resilient capital position.

Phoenix has also remained focused on the evolving regulatory landscape. The Solvency II regime came into force on 1 January 2016 and the Group has demonstrated the benefits of our Internal Model, a key tool in assessing acquisitions that provides more accurate pricing and understanding of synergy and diversification benefits. In addition, Phoenix has navigated a number of regulatory reviews with regards to long-standing customers and annuity sales. Being able to demonstrate how the Group adds value for our customers is a critical advantage for a closed life fund consolidator and Phoenix will continue to invest in its customer proposition.

As we announced at the time of the AXA Wealth acquisition, the Board is proposing a final dividend for 2016 of 23.9p per share, an equivalent 5% increase to the 2015 level (rebased to take into account the bonus element of the rights issue completed in November 2016). The Abbey Life acquisition supports a further expected increase of 5% with respect to the 2017 interim dividend to 25.1p per share, or 50.2p per share on an annualised basis. The Directors believe this is a sustainable level at which to rebase the dividend going forward. Given the long-term run-off nature of the Group's business, the Board believes it is prudent to maintain a stable, sustainable dividend while the Group builds its financial flexibility to execute its growth strategy and meet external challenges.

During the year René-Pierre Azria left the Board of Directors and I would like to thank him on behalf of the Board and management for seven years of outstanding service. In particular, his expertise in acquisitions has been critical in helping the Group grow over the past year. We also welcomed three new Directors to the Board: Wendy Mayall, John Pollock and Nicholas Shott who all bring extensive experience and highly relevant competencies.

Looking ahead, Isabel Hudson and David Woods will both step down from the Board at the time of the 2017 AGM on 11 May. Their specialist life assurance knowledge and expertise have been invaluable to the Group over the past seven years and I would like to wish them both well for the future. The Group is undertaking a process to recruit a new non-executive Director and I am confident that the robust governance at Phoenix will continue across our enlarged Group following the acquisitions of AXA Wealth and Abbey Life.

It is likely that the uncertain market environment will prevail for a while longer. However, I believe the changing regulatory landscape and macroeconomic pressures will lead to further consolidation in the UK life industry sector. Phoenix is primed to take advantage of further opportunities as they arise.

Phoenix has delivered its growth strategy during 2016 under turbulent market conditions. I would like to thank all my colleagues for their hard work, determination and commitment in what has been a highly successful year for the Group.

HENRY STAUNTON
CHAIRMAN

17 MARCH 2017

GROUP CHIEF EXECUTIVE OFFICER'S REPORT

"PHOENIX MET ITS CASH GENERATION TARGET AND ACHIEVED TWO ACQUISITIONS IN A YEAR THAT HAS SEEN SIGNIFICANT MARKET CHALLENGES."

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

Phoenix has delivered on its strategy of closed life fund consolidation in 2016, despite the macroeconomic uncertainty seen during the year. The ability of the Group to complete two acquisitions, whilst ensuring that it continued to meet its financial targets, is a strong demonstration of the Group's capabilities.

The benefits of the acquisitions are already being realised. Phoenix will continue their integration into the Group's existing platform during the course of 2017.

Phoenix Group is well positioned to benefit from the evolving UK life insurance industry. As the largest UK specialist consolidator of closed life funds, with a scalable operating model and strong outsource partner relationships, we have demonstrated our ability to enhance value for our customers and shareholders through management actions. There remains a significant opportunity for Phoenix Group to generate further value from future acquisitions.

FINANCIAL HIGHLIGHTS

DELIVERY OF FINANCIAL TARGETS

Phoenix Group has continued its track record of meeting or exceeding its financial targets.

The Group delivered a total of £486 million of cash generation from its operating companies, against a full year cash generation target of £350 million to £450 million. Of the cash generation in 2016, £117 million was from the acquisition of the AXA businesses.

At the time of the announcement of the AXA Wealth acquisition, we stated a target to generate £250 million of cash within six months of completion of the transaction. Including an additional £165 million of cash flow that has been generated so far in 2017 following the Internal Model approval of the AXA Wealth businesses, we have already achieved £282 million from the acquisition and therefore have outperformed this target.

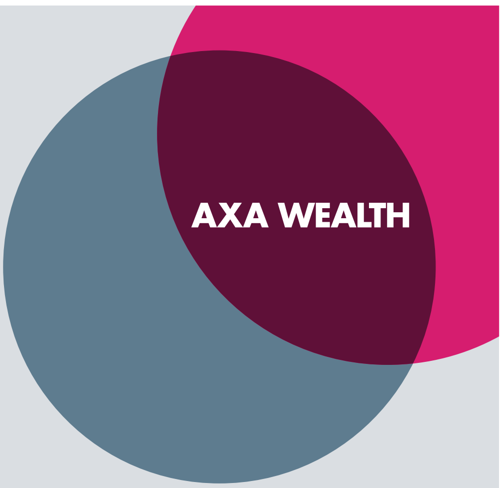
PHOENIX LIFE CAPITAL POSITION

The Phoenix Life companies hold capital management buffers, in addition to the required Solvency Capital Requirement ('SCR'), which provide the life companies with additional resilience in the event of market volatility.

Any excess over these buffers ('Free Surplus') is available for distribution to the holding companies as cash. As at the start of 2016 the Free Surplus was £0.1 billion and this has increased to £0.7 billion as at 31 December 2016, on a pro forma basis. The increase over the course of the year incorporates the benefits from the acquisitions of the AXA Wealth businesses and Abbey Life, offset in part by the cash released by the Group's life companies during the year and the impact of lower long-term interest rates.

The Group implemented further management actions during 2016 in order to increase the Free Surplus and facilitate the release of cash from the Group's life companies. These included a Part VII transfer of an annuity portfolio, a longevity swap agreement and extending Matching Adjustment portfolios.

Acquisition of AXA Wealth's pensions and protection businesses



DETAILS OF THE ACQUISITION

The acquisition comprises a pensions and investments business ('Embassy'), offering a range of propositions catering to both individual and corporate requirements and SunLife, a leader in the over 50s protection sector. The acquisition increased assets under management by £12 billion and added over 910,000 policies to the Group.

The consideration of £373 million was funded through the combination of the net proceeds of £190 million from an equity placing on 27 May and a new short-term debt facility of £182 million.

BENEFITS OF THE ACQUISITION

Phoenix now expects cost synergies of between £13 million to £15 million per annum from the acquisition, to be generated by leveraging our existing operating platform and outsourcing model. This is higher than our original expectation of £10 million of cost savings.

The Group is also investing to ensure a smooth transition of the two businesses from AXA to Phoenix and we are committed to delivering the highest level of service to both direct and IFA customers, as we do for our existing customers. The SunLife business offers additional value through its new business franchise, where it has a recognised brand and a proven track record of direct marketing.

PROGRESS MADE SO FAR

The Group has already delivered £282 million of cash flow from the acquisition, exceeding the target of £250 million within six months of completion. These benefits have been delivered from the mortality exposure of the SunLife business offsetting the Group's existing longevity exposure from its annuity liabilities and the incorporation of the acquired businesses within the Group's Solvency II Internal Model.

The cash generated from the acquired businesses facilitated the full repayment of the £182 million acquisition facility in December 2016.

GROUP CHIEF EXECUTIVE OFFICER'S REPORT
Continued

GROUP CAPITAL POSITION

The Group's surplus under Solvency II, as calculated at the level of Phoenix Life Holdings Limited ('PLHL'), is estimated to be £1.9 billion as at 31 December 2016, pro forma for the impact of the new Tier 3 bond issued in January 2017 and moving the AXA businesses onto the Group's Solvency II Internal Model. The increase in the PLHL Solvency II surplus from £1.3 billion as at 31 December 2015 also reflects the acquisitions made in 2016 together with management actions completed during the year, offset partly by the negative impact of lower long-term interest rates. The Shareholder Capital coverage ratio has increased from 154% as at 31 December 2015 to 170% as at 31 December 2016, on a pro forma basis.

The Group capital position assumes a recalculation of Transitional Measures as at 31 December 2016, to take into account the changes in interest rates over the course of the year.

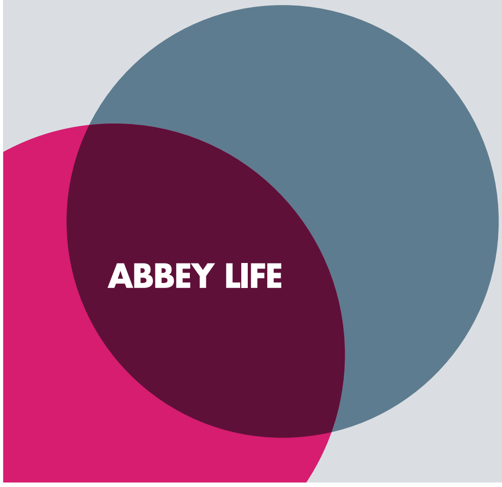
The volatility of the interest rate environment may well endure for a significant period of time. However, the Group continues to take actions to mitigate the impact of interest rates on the Group's cash generation and capital position. These include the continued hedging of market risks as well as examining options to generate additional yield on our assets by investing in alternative asset classes such as equity release mortgages.

Acquisition of Abbey Life

DETAILS OF THE ACQUISITION

Abbey Life predominantly comprises unit-linked life and pensions policies and annuities in payment, together with two small with-profit funds. Abbey Life adds 735,000 policyholders and £10 billion of assets under management to the Group. Abbey Life closed to new retail business in 2000.

Phoenix acquired Abbey Life from Deutsche Bank. The consideration of £933 million and related expenses were financed through a fully underwritten rights issue which raised a total of £735 million and a £250 million new short-term bank facility. The bank facility has since been refinanced with the Group's lending banks into an enlarged Revolving Credit Facility of £900 million, of which £550 million remains outstanding following the Group's recent Tier 3 bond issue.



BENEFITS OF THE ACQUISITION

Phoenix expects to generate capital and cost benefits through a series of management actions. These will include the migration of Abbey Life to the Phoenix Solvency II Internal Model and capital management policies, an application for Transitional Measures, implementation of changes to Abbey Life's existing asset strategy and improvements in operating efficiency (delivering approximately £7 million savings per annum).

Abbey Life already operated as a largely standalone business within Deutsche Bank. This should allow for a straightforward approach to separation with limited transitional services being required from Deutsche Bank to Abbey Life for a period following completion.

PROGRESS MADE SO FAR

Phoenix has supplemented the existing Abbey Life management and put in place new governance and oversight structures.

An integration plan has been established and the provision of customer administration and IT is expected to remain with Capita, one of the Group's existing outsource providers.

Phoenix will apply to include Abbey Life within the Group's Solvency II Internal Model in the second half of 2017.

SIMPLIFICATION OF GROUP STRUCTURE

Phoenix has taken significant steps in recent years to both reduce the level of debt within the Group and simplify its corporate structure. This progress continued in January 2017 with the issue of a £300 million subordinated Tier 3 bond, which matures in July 2022. The net proceeds from the bond issuance reduced further the amount of senior bank debt outstanding to £550 million and will allow the Group to better match its debt profile to its long-term cash flows. Furthermore, the bond provides the Group with additional Solvency II capital, assisting the rationalisation of the Group's holding company structure.

The current holding company structure was formed at the time of the Group's restructuring in 2009, with Phoenix Group Holdings being a Cayman Island-registered company domiciled in Jersey. This structure is complex for our stakeholders and imposes additional burdens on our internal governance processes. As part of the ongoing Group simplification process, Phoenix intends to put in place a new UK-registered holding company for the Group in 2018. This will provide Phoenix with a streamlined and cost efficient internal governance structure as well as greater clarity for the Group's stakeholders, including shareholders, debt investors and regulators.

OPERATING PROFIT

The Group achieved operating profits of £351 million in 2016 (2015: £324 million), reflecting an increased impact from management actions.

OPERATIONAL HIGHLIGHTS

Phoenix Group continued to undertake management actions to release cash and create value. Key actions taken during 2016 included:

- Completion of a Part VII transfer of an annuity portfolio to ReAssure Life Limited, which was previously covered by a reinsurance agreement. The transfer reduced the Group's capital requirements for counterparty credit default and released expense reserves.
- Implementation of a £2 billion longevity swap on a portfolio of immediate annuities with an external reinsurer. The attractive terms of this transaction significantly improved the capital efficiency within the Group.
- A £1 billion bulk annuity transaction under which Phoenix Life Limited insured pensions-in-payment from the PGL Pension Scheme. This transaction enhanced the Group's capital position, and gives potential for further shareholder value creation through investing the assets in line with the Group's strategic asset allocation.
- Further optimisation of Matching Adjustment portfolios, matching long-term liabilities with eligible assets in order to optimise the capital position of the Group's life companies.

These management actions have been critical in meeting the Group's cash targets in a year that has seen significant market volatility. Given the enhanced scale of the Group we believe there will be further opportunities for management actions during 2017.

CUSTOMERS

Delivering improved customer outcomes and ensuring that we provide an effective service for policyholders is critical to support our strategy of acquiring and managing closed life funds. It is essential for the Group to demonstrate that it can deliver enhanced benefits for customers by bringing them within the Phoenix Group.

The customer strategy at Phoenix Group is focused on improving customer outcomes. Security of our customer assets is foremost, followed by our aim to maximise returns wherever possible but primarily through enhanced distribution of the estate within the life funds. We delivered an additional £103 million of distributable estate through management actions, more than twice our 2016 target, and have therefore directly benefited our with-profit policyholders through increased payouts. We have improved the strength of our with-profit funds over several years which has led to an increased ability to pay bonuses. Our emphasis has been on improving final bonuses, but many funds are now strong enough to allow us to also re-introduce annual bonuses. Almost 80% of our with-profits policyholders are now receiving an annual bonus, compared to less than 40% in 2012.

Given our history of acquisitions, Phoenix has a wide range of legacy products and it is vital to us that we carry out an active programme of product governance, checking that our products continue to deliver appropriate outcomes for both customers and Phoenix.

To support our work we have created a forum for a group of our customers to provide us direct feedback on a range of topics. This has improved the clarity of our communications, including developing a more engaging web platform and digitising parts of the customer journey. Along with our significant investment in enhancing our web offering we have also joined the ABI's pension dashboard initiative. We believe this will help both existing and new customers keep track of their policies and be better prepared for their retirement as a result.

While we aim to minimise customer complaints, it is important to ensure that the complaint process is straightforward, transparent and fair to consumers while allowing us to learn for the future. Our customer-focused culture is further supported by decisions made by the independent complaints adjudicator, the Financial Ombudsman Service ('FOS'). For FOS decisions in the year, the overturn rate of 18% is significantly better than the industry average rate of 30%.

Finally, there remains the risk of fraudsters targeting our customers and we therefore continue to take action to identify possible incidences of pension fraud. Phoenix Group prevented policyholders from losing over £4 million to potentially fraudulent schemes during 2016 and we remain active in publicising the risk of pension fraud through specific campaigns in the media.

GROUP CHIEF EXECUTIVE OFFICER'S REPORT
Continued

REGULATORY AND LEGISLATIVE CHANGES

The Financial Conduct Authority ('FCA') published two separate thematic reviews during the course of 2016. The review of the fair treatment of long-standing customers in life insurance was published in March and the review into annuity sales practices was published in October. We welcome the focus that these reviews bring to the fair treatment of policyholders and the manner in which customer communication can be enhanced. Our customers and the outcomes of their policies are fundamental to our business model and we continue to seek ways to improve.

We will work closely with the FCA on the ongoing investigation into the conduct of Abbey Life in the period before the business was acquired by Phoenix. This work will continue during 2017 but Phoenix Life has already applied its own governance and customer model to the Abbey Life business and will take further action as required.

The regulator has been clear that life companies need to do more to ensure that policyholders have clear communication at the time of retirement, in particular around their options with regards to taking up an annuity. Phoenix Group currently only provides annuities for its own vesting policyholders and wrote a total of £542 million of annuities in 2016 compared with £485 million in 2015. £370 million of the annuities written in 2016 had guaranteed annuity rates ('GARs') that are often well above currently available market rates, with the remaining £172 million being non-GAR annuities. Phoenix Group aims to offer our customers an average non-GAR annuity rate that is at least 97.5% of the average of the top five open market providers.

There has been additional regulatory action on ensuring charges to policyholders are reasonable. The cap of 1% on early exit charges for pension customers aged over 55 will come into force in 2017. Over 80% of our unitised policies have no exit charge at all and we have seen no evidence that any of our customers are deterred from taking advantage of pension freedoms before their selected retirement date because of exit charges. The overall financial impact of a 1% cap on exit charges has been estimated at £26 million, including Abbey Life's business, and this has already been reflected in the Free Surplus position of the life companies.

With regards to contract-based workplace pensions, Phoenix Life's Independent Governance Committee has considered proposals to ensure that customers in our workplace pension schemes are being treated fairly. Our joint work has identified that there were some members of schemes who, if their fund was below a certain level, could be at risk of a poor outcome should they not choose some of the options available to them. For these customers we have reduced monthly charges in an effort to ensure the growth on their policy is not adversely affected by charges.

The Group will continue to work closely with the regulators as the long-term impacts of recent changes to the retirement market become clearer. This is underpinned by the actions we have taken with regards to our own customers.

PEOPLE

Phoenix Group's ability to attract, retain and motivate outstanding talent was, for the fifth year in succession, formally recognised in 2016 through our accreditation as one of the UK's Top Employers. An engaged workforce, one that feels committed to the goals of the organisation, is fundamental to the success of the Group. Our employee engagement index has increased to 81%, a 3% increase on the scores achieved in 2015.

The Group's corporate responsibility agenda plays a central part in the engagement of our people. Their commitment extends to a number of community initiatives supported by the organisation and is a critical part of our overarching objective to put the financial, physical and mental wellbeing of our employees at the heart of our people strategy.

I am pleased to report that staff-led fund raising activities in 2016 raised a total of over £212,000. This was raised primarily for our corporate partnerships with Midlands Air Ambulance Charity and London's Air Ambulance, which we will extend for a further three years. As we reach the half way mark in this six-year partnership, our employees have so far raised over £550,000.

Year on year retention and recruitment have improved our resourcing position and we are well placed to navigate the integration of the newly acquired businesses, including the combined existing management and flexible contract employees. We remain committed to developing our employees and have delivered over 16,000 hours of training in 2016.

2017 OUTLOOK AND PROSPECTS

Cash generation remains the key metric for the Group and we have set new targets which incorporate the impact of the two acquisitions made during the year.

We have updated our long-term cash generation target to £2.8 billion of cash between 2016 and 2020, up from £2.0 billion. Of this, we expect to generate £1.0 billion to £1.2 billion of cash between 2017 and 2018, in line with the expected timeframe to integrate the recent acquisitions and incorporate Abbey Life within the Group's Solvency II Internal Model. These cash generation targets include expectations of future management actions as we seek to generate value for policyholders and shareholders.

Furthermore, we expect a further £4.4 billion of cash generation from 2021 onwards. This illustrative cash generation includes the impact of the run-off of transitionals over 16 years to 2032 but does not assume any additional management actions during the period from 2021. Therefore, in total, we expect future cash generation for the existing business of £6.7 billion from the start of 2017. This is a clear demonstration of the long-term cash flow potential of the Group.

The risk remains that our business will be impacted by macroeconomic uncertainty or the evolving regulatory environment. However, in achieving its cash generation target for 2016 the Group has demonstrated its resilience and maintains a robust capital position.

CONCLUSION

I continue to believe that the impact of regulatory changes will provide Phoenix with further opportunities, as open life companies reappraise their business models and strategies for their legacy policies. During the year, the Group demonstrated how it drives value from a strategy of acquiring and integrating closed life policies and the Group is well placed to generate additional benefits from future acquisitions.

Finally, I would like to thank my colleagues for their continued hard work during a year that has seen Phoenix deliver its strategy for the benefit of both shareholders and policyholders.

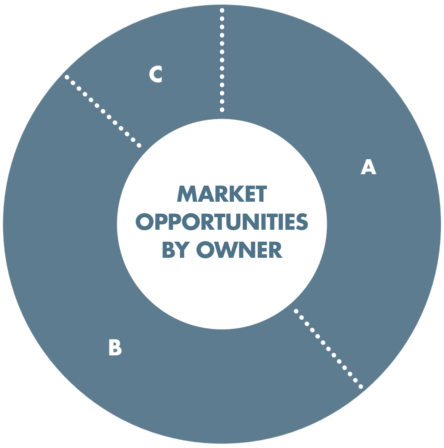
CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

17 MARCH 2017

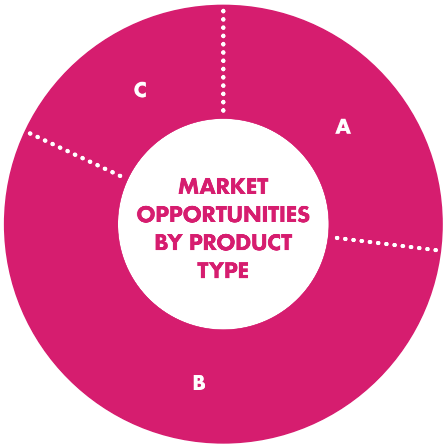
THE MARKET PLACE

The UK life and pensions market is undergoing fundamental change, driven by changes in regulation and customer behaviour. Phoenix expects further consolidation within the market and is well positioned to undertake acquisitions in future.

Phoenix estimates that the market opportunity is over £300 billion in terms of assets held within UK closed life funds (excluding Phoenix).



A	UK life companies	39%
B	Foreign owned	48%
C	Bank owned	13%



A	With-profit	27%
B	Unit-linked	55%
C	Non-profit	18%

DRIVERS FOR CONSOLIDATION

We believe there are a number of key drivers that will lead to future consolidation of closed life funds:

- Significant capital held within closed funds that owners may wish to redeploy
- More intrusive regulation is leading to pressure on owners to invest in systems and customer service
- Fixed operating costs may become an issue as closed funds decline in size over time
- Specialist skill sets are required to manage complex legacy products in closed funds
- Life companies writing new business are now focusing on a more limited range of products in future

PHOENIX'S MOTIVATION

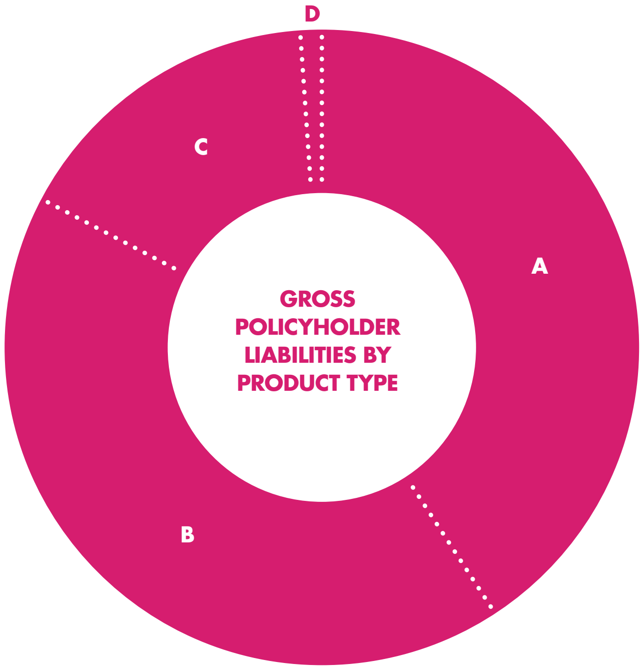
Phoenix has key competitive advantages in generating value from acquiring and managing closed life funds:

- The Group's scale provides the ability to generate capital efficiencies through the diversification of risks
- The wide range of product types that Phoenix currently manages provides a scalable platform for integrating further closed funds
- The Group's outsourcing partners provide policy administration services and allow Phoenix to run a variable cost model
- Phoenix's experienced employees are focused on closed life funds and have significant expertise in managing with-profits products
- The Group's approved Solvency II Internal Model provides greater clarity over capital requirements and the benefits of undertaking management actions

OUR KEY PRODUCTS

Phoenix has a wide range of legacy products which are written across different funds.

The features of each policy influences whether it is the policyholders or the shareholders who are exposed to the risks and rewards of a policy.



A	With-profit	41%
B	Unit-linked	42%
C	Non-profit – annuities	16%
D	Non-profit – protection and other	1%

Fund type	Gross policyholder liabilities at 31 Dec 2016	Typical characteristics	Policyholder benefits	Shareholder benefits
With-profit	£30.2 billion	– These are typically savings and investment products. – They comprise endowments, whole of life and pensions products and (some) guaranteed annuity options which guarantee the annuity that a pension pot will be able to buy. – The policyholders and shareholders share in the risks and rewards of the policy, depending on the structure of the fund. – Excess assets created over time ('estate') provide a buffer to absorb cost of guarantees and capital requirements. – In the 'supported' with-profit funds, the shareholders provide capital support to the fund.	– Policyholders benefit from discretionary annual and/or final bonuses. – The bonuses are designed to distribute to policyholders a fair share of the return on the assets in the fund, together with other elements of experience in the fund.	– In the 'supported' with-profit funds, the shareholders' capital is exposed to all economic movements until the estate is rebuilt to cover the required capital, at which point the fund becomes 'unsupported'. – In the 'unsupported' with-profit funds, typically shareholders receive 10% of declared bonuses (90:10 structure) or nil (100:0 structure).
Unit-linked	£30.9 billion	– These are insurance or investment contracts (savings and pensions) without guarantees. – The policyholders bear all of the investment risk. – Policyholders buy units with their premiums which are invested in funds. – Units are sold when a claim is made.	– Policyholders' benefits are in the form of unit price growth (based on the investment income and gains, but subject to management charges and investment transaction costs).	– Shareholders benefit from fees earned through management charges, bid/offer spreads or policy fees.
Non-profit (Annuities)	£12.4 billion	– Policyholders make fixed or variable payments in lieu of a future lump sum or a future income stream until death.	– Policyholders receive regular payments which start immediately (immediate annuity) or at some time in the future (deferred annuity).	– Shareholders earn a spread on the assets supporting the annuity payments. – The shareholders are directly exposed to all investment and demographic risks.
Non-profit (Protection and other)	£0.5 billion	– Term assurance policies which pay a lump sum on death if death occurs within a specified period. – Whole of life policies which cover the entire life and pay a lump sum on death, whenever it occurs.	– Policyholders have certainty of the benefits they will receive.	– Profits are generated from investment returns and underwriting margins. – Shareholders are exposed to the majority of the risks and benefit from 100% of the profits or losses arising.

OUR STRATEGY AND BUSINESS MODEL

We seek to generate value for all our stakeholders. The Group actively manages its assets and liabilities to help protect and enhance policyholder and shareholder returns.

OUR STRATEGIC PRIORITIES

IMPROVE CUSTOMER OUTCOMES

Improving customer outcomes is central to our vision of being the saver-friendly 'industry solution' for closed life funds.

DRIVE VALUE

In order to drive value, the Group looks to undertake management actions which increase and accelerate overall cash flows or enhance value.

MANAGE CAPITAL

The effective management of our risks and the efficient allocation of capital against them is critical in allowing us to achieve our strategic and operational objectives.

ENGAGE PEOPLE

Our people underpin everything that we do. The Group specifically targets, recruits and develops top quality people to support the achievement of its strategic and operational objectives.

OUR COMPETITIVE ADVANTAGE

CLOSED FUND FOCUS:

We specialise in the efficient management of in-force policies with limited writing of new business. This allows high visibility of cash flows over the long term due to the predictable nature and run-off profile of the Group's funds.

SCALABLE OUTSOURCER MODEL:

We operate a low cost, scalable operating model which allows us to benefit from economies of scale, diversification benefits and the ability to save costs both internally and through outsourcing arrangements.

APPLICATION OF "THE PHOENIX WAY":

"The Phoenix Way" characterises an approach and infrastructure for the efficient and effective structuring, integration and management of closed life funds and the investments they hold.

Part of "The Phoenix Way" is the application of the Group's Internal Model for effective and efficient capital management.

17 Read more on "The Phoenix Way"

PROVEN ACCESS TO DEBT AND EQUITY MARKETS:

The Group seeks a level of leverage that helps it maintain its investment grade rating and optimise its funding costs and financial flexibility for further acquisitions.

EXPERIENCED AND SKILLED MANAGEMENT TEAM:

Our management team have a proven track record of target delivery. They have the required specialist skills in regulation, operational efficiency, capital management, governance and liability customised asset management.

To maintain its competitive advantage, the Group develops specialist expertise to identify, pursue and execute suitable acquisition opportunities in the closed life space.

Our value generation strategy seeks to improve policyholders' returns and enhance shareholders' profits from participation in investment returns, charges and management fees earned on assets.

VALUE GENERATION

DISCIPLINED APPROACH TO M&A

Value accretive acquisitions generate increased cash flows and provide synergy opportunities through scale advantages. We target the following criteria when assessing acquisition opportunities:

- closed fund focus
- value accretive
- supports the dividend per share
- reinforces the Group's investment grade rating

MANAGEMENT ACTIONS AND SYNERGIES

Implementation of management actions, such as fund mergers and de-risking, optimises the Group's capital position and cash flows.

Effective management of with-profit funds facilitates estate distribution to policyholders and shareholders.

Growth through acquisitions provides opportunities for further management actions to drive operational efficiencies through the application of "The Phoenix Way".

CAPITAL MANAGEMENT

The effective management of the Group's risks and the efficient allocation of capital against them maximises value generation. The Group's Solvency II Internal Model, which has been approved by the PRA, enables us to quantify the capital and cash flow impact of specific management actions and acquisitions.

PREDICTABLE LONG TERM CASH FLOWS FROM IN-FORCE BOOK

Cash flows are generated from the build-up of Free Surplus within the life companies reflecting the emergence of shareholder profits on the in-force book and the release of capital as the risk profile reduces and the policies mature. This Free Surplus can be distributed to the Group's holding companies as cash.

OUTCOMES FOR ALL STAKEHOLDERS

POLICYHOLDERS

Optimised customer outcomes, treating customers fairly with empathy as well as respect and ensuring customer investments are secure.

91.2%
customer satisfaction

SHAREHOLDERS

A track record of creating shareholder value and delivering stable and sustainable dividends.

5%
increase in the 2016 final dividend per share

The 5% increase takes into account the bonus element of the rights issue completed in November 2016.

EMPLOYEES

Creating a challenging work environment, career development opportunities and commensurate reward and benefits.

81%
employee engagement index

SOCIETY

Reduced environmental footprint, support for local communities and our charity partners.

£212,000+
raised for a range of charities

OPERATING STRUCTURE

The Phoenix Group's operating structure is integral to its success in the closed life fund market.

PHOENIX GROUP

GROUP FUNCTIONS

Manage corporate and strategic activity

PHOENIX LIFE

LIFE COMPANIES

Hold the financial assets for our policyholders

- PHOENIX LIFE LIMITED
- PHOENIX LIFE ASSURANCE LIMITED
- ABBEY LIFE ASSURANCE COMPANY LIMITED
- AXA WEALTH LIMITED

MANAGEMENT SERVICES COMPANIES

Provide our life companies with all required management services

OUTSOURCE PARTNERS

Used by the management services companies to provide policy administration services

GROUP FUNCTIONS

The Group operates centralised functions that provide Group-wide and corporate-level services and manage corporate and strategic activity. The Group functions include Group Finance, Treasury, Group Tax, Group Actuarial, Group Risk, Legal Services, Human Resources, Corporate Communications, Strategy and Corporate Development, Investor Relations, Company Secretariat and Internal Audit. Based both in Wythall, Birmingham and Juxon House, London, the Group is led by the Group Chief Executive Officer, Clive Bannister.

PHOENIX LIFE

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

LIFE COMPANIES

The life companies are regulated entities that hold the Group's policyholder assets. Over time, the Group has reduced the number of its individual life companies through insurance business transfers. By bringing together separate life companies and funds, the Group's business model is simplified. Fund transfers enable the Group to make more efficient use of the capital and liquidity in its life companies and result in administrative expense savings and increased consistency of management practices and principles across the Group.

The Group now has four operating life companies, being Phoenix Life Limited, Phoenix Life Assurance Limited and the recently acquired AXA Wealth Limited and Abbey Life Assurance Company Limited. Together, they comprise 16 with-profit funds and 4 non-profit funds. The Group will examine the possibility of mergers to reduce the number of life companies in due course.

Investment management services are provided to the life companies by a number of external asset management companies.

MANAGEMENT SERVICES COMPANIES

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

In addition to the services above, one of the management service companies, AXA Wealth Services Limited, also provides distribution services for SunLife, the over 50s protection business.

OUTSOURCE PARTNERS

A key role of the management service companies is the management of relationships with the outsource partners on behalf of the life companies. In the absence of further acquisitions, the number of policies held by the Group gradually decline over time and the fixed cost base of our operations as a proportion of policies will increase. Our management services team manages this risk by putting in place long-term arrangements for third party policy administration. By paying a fixed price per policy to our outsource partners, we reduce this fixed cost element of our operations and convert to a variable cost structure. This allows our management services companies to generate profits by managing costs efficiently.

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

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

"The Phoenix Way" is a consistent framework applied across the Group for the efficient and effective structuring, integration and management of closed life funds. This framework reduces risk, complexity and cost, improves investment performance, enhances customer service through efficient cooperation with the Group's outsourced partners and underpins achievement of our strategic priorities.

"The Phoenix Way" comprises of four key areas:

OPERATIONAL MANAGEMENT

Standardising, streamlining and innovating the key processes and platforms across the Group improves efficiency and generates value.

RISK MANAGEMENT

Managing and mitigating risk within appetite and exercising robust governance supports policyholder security and delivers the Group's strategy.

RESTRUCTURING

Simplifying the Group's operating structure through life company consolidation and fund mergers reduces complexity and releases capital.

EFFECTIVE PARTNERSHIPS

Utilising external outsource partners and fund managers with proven track records provides access to expert knowledge and delivers a scalable cost base, maximising returns.

OUR STRATEGY AND KPIS

We have four areas of strategic focus which support the fulfilment of our mission and the realisation of our vision. Our initiatives and key performance indicators demonstrate how we have delivered against these strategic areas.

Improving customer outcomes is central to our vision of being the saver-friendly 'industry solution' for closed life funds.

IMPROVE CUSTOMER OUTCOMES

We have six key areas of focus related to our customer offering:

- Security: ensuring all policy promises and guarantees are delivered.
- Improving value and effective with-profit fund run-off: through accelerating estate distribution where possible and providing appropriate investment exposure.
- Effective service delivery: using our outsourced model to leverage expertise and ensure costs run-off in line with policy volumes.
- Clear and effective communication: recognising the importance of clarity and simplicity for what can be complex products.
- Product governance: including a rolling review of our products to ensure they continue to deliver appropriate outcomes for our customers.
- Customer journey: improving customer experience wherever possible.

KEY INITIATIVES AND PROGRESS IN 2016

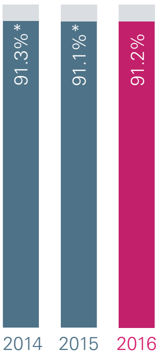
- We have implemented a full upgrade of the Phoenix Life website in order to deliver a fully responsive and engaging platform. Our changes ensure that our website adapts, resizing and rearranging itself to a customer-friendly format based on the size of the device being used.
- We have also digitised parts of the customer journey which enables those customers with funds under £10,000 to encash their small pots online.
- We have created a forum for a group of our customers to provide us direct feedback on a range of topics. This has led to improving the clarity of our communications, including input into the changes we have made to our digital offering.
- We have joined the ABI's pension dashboard initiative. We believe this important industry initiative will help both existing and new customers keep track of their policies and be better prepared for their retirement as a result.
- Our strong customer-focused culture is further supported by decisions made by the independent complaints adjudicator, the Financial Ombudsman Service ('FOS'). For FOS decisions in the year, the overturn rate of 18% is significantly below the industry average rate of 30%.
- We have again achieved a positive customer satisfaction score based on the results of the satisfaction survey managed by Ipsos MORI (an external research firm). Customers surveyed were asked to give a satisfaction rating of between 1 and 5 to a number of questions asked (with a rating of 4 or 5 regarded as satisfied) and 91.2% of all questions scored a rating of 4 or above.

PRIORITIES FOR 2017

- Making ongoing improvements to ensure that we are continuing to provide an effective service for all our policyholders, including the delivery of digital journeys in key areas.
- Despite many of our products being long term in nature, we will continue to look for options for customers who may no longer have a need for their product.
- Continue to ensure that our products deliver appropriate outcomes for our customers.
- Further improvements of customer communications with focus on ensuring that customers are provided with more information to help them in making fully informed choices.
- For the minority of customers who complain, we will continue to ensure that the process of complaining remains a straightforward, transparent and fair process, with particular focus on the speed of resolution and the quality of our responses.

How we measure delivery (KPIs exclude the acquired AXA and Abbey Life businesses)

CUSTOMER SATISFACTION SCORE



91.2%
2015: 91.1%*

WHY IS IT IMPORTANT?
This is an externally calculated measure of how satisfied customers are with Phoenix's servicing proposition.

ANALYSIS
The Group achieved a satisfaction score of 91.2% reflecting our commitment to ensuring customers are satisfied with our products and services.

TARGET
To maintain a customer satisfaction score of 90%.

* 2014 and 2015 scores have been updated to reflect only customers scoring 4 or above.

FOS OVERTURN RATE

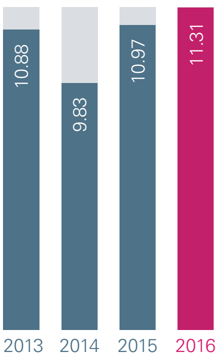
18%
2015: 18%

WHY IS IT IMPORTANT?
This is an independent view of how firms are handling complaints. It provides us with an opportunity to review and adjust our complaint handling proposition in line with best industry practice.

ANALYSIS
The FOS overturn rate of 18% is significantly below the industry average of 30%.

TARGET
To maintain a FOS overturn target of less than the industry average of 30%.

SPEED OF PENSION TRANSFER PAYOUTS – ORIGO



11.31 days
2015: 10.97 days

WHY IS IT IMPORTANT?
This is a recognised industry measure for the speed of processing Pension Transfers, Open Market Options and Immediate Vesting Personal Pensions. It allows us to benchmark performance and our overall servicing and claims proposition against our peers.

ANALYSIS
The Group's pension transfer times are better than the industry target.

TARGET
12 days in line with the industry stated target for Origo Pension Transfers.

"WE CONTINUE TO FOCUS ON IMPROVING OUTCOMES FOR OUR CUSTOMERS WITHIN A CHALLENGING AND FAST PACED EXTERNAL ENVIRONMENT. WE RECOGNISE THE IMPORTANCE OF GOOD, RELIABLE SERVICE DELIVERED IN A WAY THAT SUITS OUR CUSTOMERS. DURING 2017, WE WILL CONTINUE TO BUILD ON OUR DIGITAL PROPOSITION, ENHANCING THE SERVICES AVAILABLE TO CUSTOMERS."

OUR STRATEGY AND KPIS
Continued

In order to drive value, the Group looks to identify and undertake management actions, which increase and accelerate cash flows or enhance value.

DRIVE VALUE

These actions are undertaken across four areas: operational management, risk management, restructuring and effective partnerships. There are significant opportunities to increase and accelerate cash flows through the continued implementation of "The Phoenix Way" which reduces complexity and cost and optimises risk, which in turn maximises the potential for value creation.

With the exception of the SunLife business acquired during 2016, the life companies are closed and generally do not write new business, although they accept additional policyholder contributions on in-force policies and allow pension savings plans to be reinvested at maturity into annuities. The closed life funds provide predictable fund maturity and liability profiles, creating stable long-term cash flows for distribution to shareholders and repayment of outstanding debt.

Additional value can be generated from further acquisitions of closed life books of business.

KEY INITIATIVES AND PROGRESS IN 2016

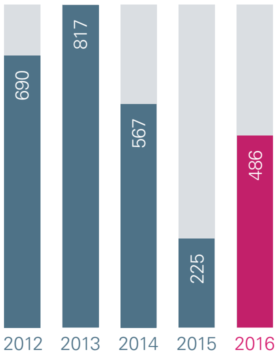
- In line with our growth and acquisition strategy, we completed the acquisition of AXA Wealth's pension and protection businesses on 1 November 2016.
- As at the end of 2016, £117 million of cash flow was delivered from the acquired AXA businesses, reflecting the benefits of offsetting effects of AXA's mortality exposure against Phoenix's existing longevity exposure on its annuity business. To date, further cash flows of £165 million have been delivered in 2017.
- On 30 December 2016, we completed the acquisition of Abbey Life from Deustche Bank.
- Despite a challenging economic climate, the Group delivered £486 million in cash generation in the period against a target of £350 million to £450 million. This includes £117 million from the acquired AXA business.
- The Group continued to explore investment opportunities which look to maximise value whilst remaining capital efficient. During 2016, this has included investment in equity release mortgages as well as more innovative ways to attract high yield assets such as total return swaps and local authority loans.
- In December 2016, the Group completed the pension buy-in under which Phoenix Life insured pensions in payment from the PGL pension scheme. This transaction provides the Group with potential for further value creation through investing assets in line with the Group's strategic asset allocation.
- We continued to streamline and simplify the Group's actuarial modelling, including the alignment of our IFRS and Solvency II reserving methodologies, in order to improve efficiency and generate value.

PRIORITIES FOR 2017

- Focus on the smooth transition and efficient integration of the acquired AXA and Abbey Life businesses to deliver planned synergies whilst providing high quality of service to policyholders.
- Deliver between £13 million and £15 million per year of cost savings from the acquired AXA businesses.
- Explore further investment opportunities in higher yielding assets for example commercial real estate and additional equity release mortgages.
- Seek further closed life fund acquisitions.

How we measure delivery

OPERATING COMPANIES' CASH GENERATION



£486m
2015: £225m

27 Read more about cash generation

WHY IS IT IMPORTANT?

Operating companies cash generation represents cash remitted by the Group's operating companies to the holding companies.

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

ANALYSIS

Cash remitted reflects the generation of Free Surplus within the life companies and the benefit of management actions implemented in the period.

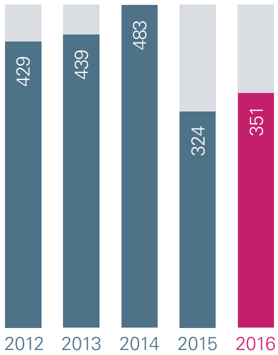
Cash generation in 2016 was £486 million, of which £117 million arose from the AXA acquisition. The Group met its full year cash generation target for 2016 of £350 million to £450 million.

TARGET

To generate cash flows of £2.8 billion between 2016 and 2020, of which £486 million has been generated in 2016.

A further £4.4 billion of cash generation, excluding the impact of management actions, is expected from 2021 onwards. More details are included in the Business Review section.

OPERATING PROFIT



£351m
2015: £324m

31 Read more about operating profit

WHY IS IT IMPORTANT?

Operating profit is a non-GAAP measure used by management and is considered a more representative measure of performance than IFRS profit or loss after tax as it provides long-term performance information unaffected by short-term economic volatility.

A reconciliation of operating profit to the IFRS loss after tax of £(100) million (2015: £249 million, profit) is included in the Business Review section.

ANALYSIS

Operating profit has increased by £27 million principally due to the impact of higher management actions compared to the previous period, partly offset by the adverse impacts of actuarial assumption strengthening in light of the continued low interest rate environment.

"THE 2016 ACQUISITIONS INCREASE THE SCALE AND STRENGTH OF THE GROUP. TOTAL CASH GENERATION FROM THE ACQUIRED AXA BUSINESS IS £282 MILLION WHICH EXCEEDS THE TARGET OF £250 MILLION OF CASH FROM THE ACQUISITION WITHIN SIX MONTHS OF COMPLETION."

OUR STRATEGY AND KPIS
Continued

MANAGE CAPITAL

We continue to focus on the effective management of our risks and the efficient allocation of capital against those risks.

We focus on optimising our capital structure while addressing the diverse needs of various stakeholders, including policyholders, shareholders, lending banks, bondholders and regulators.

We aim to ensure that unrewarded exposure to market volatility is minimised or the risks from market movements are managed through hedging.

In addition, regular re-balancing of asset and liability positions is required to ensure that only those assets which deliver appropriate risk-adjusted returns are held within life funds, taking into account any policyholder guarantees.

KEY INITIATIVES AND PROGRESS IN 2016

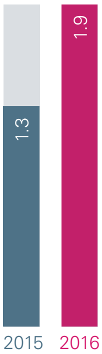
- We completed a Part VII transfer of a block of with-profit annuities to ReAssure Life Limited delivering Solvency II surplus benefits from the release of expense reserves and a decrease in capital requirements for counterparty credit default and expense risks.
- We entered into a £2.0 billion longevity swap on a portfolio of immediate annuities with an external reinsurer, realising Solvency II surplus benefits as a result of a reduction in longevity risk capital required, thereby increasing the financial resilience of the Group.
- We have continued to enhance the Group's capital position under Solvency II by further optimising our Matching Adjustment portfolios delivering Solvency II surplus benefits.
- We have actively continued hedging our market risks in response to ongoing market turbulence, with the Group's capital position remaining resilient despite the continued uncertainties.
- We agreed a revised £650 million unsecured revolving credit facility in March 2016, with no mandatory or target amortisation payments, offering the Group greater flexibility to make acquisitions.
- The AXA and Abbey Life acquisitions were financed in a capital efficient manner, balancing the debt/equity structure in line with the expected cash generation from the acquired businesses. The AXA acquisition was funded by a combination of the net proceeds from an equity placing and a new short-term debt facility that was fully repaid within two months of completion. The Abbey Life acquisition was funded through a fully underwritten rights issue and a new short-term bank facility which has since been refinanced into the £650 million unsecured revolving credit facility to create an enlarged revolving credit facility of £900 million.

PRIORITIES FOR 2017

- Incorporation of the acquired businesses within the Group's Solvency II Internal Model, including the application of Transitional Measures. We obtained the PRA's approval to incorporate the acquired AXA businesses into the Group's Internal Model in March 2017. An application to include the acquired Abbey Life business in the Group's Internal Model will be made during the second half of 2017.
- Undertaking a Funds Merger of the acquired AXA businesses into Phoenix Life Limited.
- Continued simplification of the Group's corporate structure, including the Group's intention to put in place a new UK-registered holding company for the Group during 2018. This is expected to provide the Group with a streamlined and cost efficient governance structure as well as greater clarity for the Group's stakeholders.
- Implementation of new management actions to enhance the Group's capital position.

How we measure delivery

SOLVENCY II SURPLUS (PRO FORMA)



£1.9bn
2015: £1.3bn (actual)

28 Read more about Solvency II

WHY IS IT IMPORTANT?

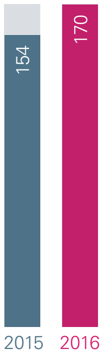
The Solvency II surplus is the regulatory assessment of capital adequacy at the PLHL level.

Cash generation is underpinned by the Phoenix Life Free Surplus, which represents the life companies' Solvency II surplus in excess of the Board approved capital management policies.

ANALYSIS

Our pro forma PLHL Solvency II surplus of £1.9 billion has increased due to surplus emergence, management actions undertaken during the period and the impact of the acquisitions, partly offset by the adverse impacts of assumptions and methodology changes and economic movements.

SHAREHOLDER CAPITAL COVERAGE RATIO (PRO FORMA)



170%
2015: 154% (actual)

29 Read more about Shareholder Capital Coverage

WHY IS IT IMPORTANT?

The Shareholder Capital Coverage Ratio demonstrates the extent to which shareholders' eligible Own Funds cover the Solvency Capital Requirements.

It is defined as the ratio of the Group Own Funds to Group SCR, after adjusting to exclude amounts relating to unsupported with-profit funds and Group pension schemes.

ANALYSIS

A pro forma coverage ratio of 170% represents a robust and resilient capital position and reflects the increase in the PLHL Solvency II surplus in the period.

PRO FORMA SOLVENCY II CAPITAL POSITION

The Group's Solvency II capital adequacy assessment is undertaken at the level of the highest EEA insurance group holding company which is Phoenix Life Holdings Limited ('PLHL').

The PLHL sub group excludes holding companies above PLHL in the Group structure whose principal activity is the issue of debt securities for the purposes of financing fellow Group undertakings.

Since the end of 2016, certain actions have been undertaken which are considered to have had a significant impact on the Group's Solvency II position. These actions comprise:

- the issuance in January 2017, of a £300 million subordinated Tier 3 bond that qualifies as Solvency II capital, the proceeds of which have been used to reduce the Group's outstanding senior bank debt; and
- receipt of the PRA's approval in March 2017 to include the acquired AXA businesses within the scope of the Group's Solvency II Internal Model.

In order to illustrate the impacts of the above, pro forma adjustments have been made to the estimated Solvency II metrics on a basis that assumes these actions took place on 31 December 2016. This pro forma position is considered to provide a more meaningful analysis of the Group's capital position and its key sensitivities.

Both the estimated and the pro forma Solvency II metrics included in the Annual Report and Accounts reflect the impact of a recalculation of the Transitional Measures on Technical Provisions ('TMTP') and the run-off of TMTP since 1 January 2016.

"WE HAVE PROGRESSED THE INTEGRATION OF THE ACQUIRED BUSINESSES AND REMAIN ON TARGET TO DELIVER THE EXPECTED SYNERGIES THAT WILL FURTHER STRENGTHEN THE GROUP'S CAPITAL POSITION, PROVIDING ADDITIONAL RESILIENCE TO FUTURE MARKET VOLATILITY."

OUR STRATEGY AND KPIS
Continued

ENGAGE PEOPLE

An engaged workforce, one that feels committed to the goals of the organisation, is fundamental to the success of the Group. In 2016, we increased our focus on ensuring our people were challenged, motivated and rewarded through opportunities for growth, both professionally and personally.

For the fifth consecutive year, we were listed as one of the UK's Top Employers, an accreditation awarded to the best companies to work for in the UK.

Our employee engagement index has increased to 81%, a 3% increase on the scores we achieved in 2014 and 2015. This index is an aggregation of scores against a number of questions considered the most important for staff engagement and was completed by 92% of employees.

KEY INITIATIVES AND PROGRESS IN 2016

We continued to grow our learning & development offering for all employees with an increased emphasis on management and leadership development.

Following the success of our Open University Executive Education programme in 2015, we supported a second cohort of 16 people who successfully completed the programme in 2016. The delegates worked on current business challenges and presented their findings and recommendations to the Executive Committee in October.

- We received and supported just over 1,000 learning requests that included professional qualifications, continuing professional development, conferences, team building and coaching/mentoring.
- We continued to utilise our Corporate Responsibility agenda to provide opportunities for skills development and team building.
- We launched a self-nominating Talent Programme within Phoenix Life. This unique self-nomination approach to talent aims to identify and develop our own talent across middle management creating a transparent and robust process.
- Our new intranet, launched in 2016, provides employees with a modern communication and collaboration platform. Our work on the intranet was rewarded with the Gold Award in the category 'Best Intranet' at the 2016 Digital Impact Awards.
- Our Corporate Responsibility agenda continued to play a central part in the engagement of our people and during 2016 the programme was re-launched with a specific focus on wellbeing. The financial, physical and mental wellbeing of our employees is at the heart of our strategy to develop initiatives that benefit our staff, policyholders and our community partners.
- Employees engaged in a large number of charitable and community initiatives this year, contributing a total of 2,840 volunteering hours, a 46% increase on 2015.
- Staff-led fund raising activities in 2016 raised over £212,000 for both our corporate partners and for other charities. The Group chose to extend our corporate charity partnership with Midlands Air Ambulance Charity and London's Air Ambulance for a further three years and, as we reach the half way mark in the six year partnership, we have so far raised over £550,000.
- Participation figures for Flexit, the Phoenix Group Flexible Benefits scheme, have increased 3% to 89% from the previous year. Our new initiative 'Pennies from Heaven', through which staff can donate their outstanding pence from monthly net salary to our corporate charity has, already seen 35% participation.
- The Group signed the HM Treasury Women in Finance Charter and has publicly committed to the following targets:
  - Minimum of 30% of our top 100 roles (as defined by base salary) to be occupied by women by end 2018.
  - Minimum of 40% of successors to be women by end 2018.
  - Group-wide gender pay gap to be less than, or equal to, 22% of the median and mean across all employees.

Go online for the Group's full Corporate Responsibility Report
www.thephoenixgroup.com/CRreport2016

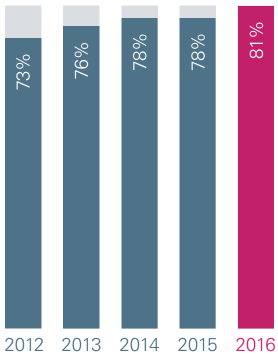
PRIORITIES FOR 2017

- Continue to attract and retain the very best talent by focusing on developing our people and strengthening our internal succession pipeline through targeted management and leadership development interventions, with particular emphasis on increasing the number of high potential female managers undertaking formal management and development activity. There is a formal review of succession plans semi-annually which ensures a continual appraisal of readiness both for emergency successors as well as longer-term strategic planning, this uses the disciplines of up to 6 months and 6-24 months readiness for internal candidates. All identified successors receive targeted development to enable them to progress.
- Prioritise our learning and development by increasing managerial strength and breadth.
- Utilise the Apprenticeship Levy to recruit Actuarial and Accountancy apprentices. We intend to work in partnership with local colleges to attract A-level individuals and graduates to Phoenix.
- Extend the Diversity and Inclusion programme, embedding changes to existing practices to deliver a diverse and inclusive workforce.
- Maintain support to our communities through employee volunteering and fund raising and engagement with our community projects.
- Support community activities through continued focus and development of our long-term partnerships with Ark Kings Academy, Midlands Air Ambulance Charity and London's Air Ambulance.

"WE WILL CONTINUE TO BUILD ON OUR STRONG MANAGERIAL CAPABILITY ALONGSIDE HIGH EXPERT SKILL."

How we measure delivery

EMPLOYEE ENGAGEMENT INDEX



81%
2015: 78%

WHY IS IT IMPORTANT?

We aim to ensure employees understand the purpose of their role and feel that their contribution is valued. The index provides an indicator of how well we are performing against these aims.

ANALYSIS

The Group has increased its employee engagement index by 3% to 81%.

TARGET

To maintain an employee engagement index above 72%.

	2016	2015
Total workforce	**1,301**[1]	741
Male	**708 (54%)**[1]	433 (58%)
Female	**593 (46%)**[1]	308 (42%)
Directors (includes Non-Executive Directors)	**11**	10
Male	**8**	8
Female	**3**	2
Executive Commitee[2]	**6**	6
Male	**5**	5
Female	**1**	1
Workforce that is of Black, Asian or Minority Ethnic background	**118**[3]	115

1 Includes 524 staff (262 male, and 262 female) in connection with the acquired AXA and Abbey Life businesses.

2 The number of Executive Committee members excludes Executive Committee members who are also members of the Board of Directors. The 2015 figures have been restated accordingly.

3 Does not include workforce from the acquired AXA and Abbey Life businesses.

BUSINESS REVIEW

"THE ACHIEVEMENT OF MANAGEMENT ACTIONS HAS DRIVEN A ROBUST SET OF FINANCIAL RESULTS IN 2016."

JAMES MCCONVILLE
GROUP FINANCE DIRECTOR

The Group has met its key financial targets during 2016.

Completion of the acquisitions of the AXA and Abbey Life businesses has strengthened the Group's capital position and offers a significant increase in the Group's cash generation capability.

Our strategy has historically focused on holding companies' cash flows and this remains the case under the new Solvency II framework, with the Group's cash generation being driven by the Free Surplus generation of Phoenix Life.

The Group has continued to meet financial targets against a backdrop of volatile market movements during 2016, reflecting political uncertainties. Swap yields fell significantly across all durations with the 15-year swap rate decreasing by c.73 bps during the period. Credit spreads narrowed across ratings and implied future inflation rates increased during the year. The FTSE All Share Index closed 16.8% ahead of the 31 December 2015 position. We continue to take management actions to mitigate the effects of market volatility to ensure that the Group maintains a stable capital position. The falling long-term interest rates in particular has meant that management actions have been important in driving cash generation during the year.

The continued low interest rate environment has also triggered changes to the Group's expectations of persistency for products with valuable guarantees and this has adversely impacted the Group's results in the period. This has been more than offset by the delivery of management actions and the positive impact of amendments to IFRS actuarial reserving estimates and assumptions to more closely align to the Solvency II requirements, leading to an increase in the Group's operating profit.

The economic volatility experienced has adversely impacted the IFRS result for the year in response to certain market factors where the Group's hedging programme is optimised to the Solvency II capital position. When combined with the one-off costs associated with acquisition and integration activities, these factors have generated an IFRS loss after tax for the year.

Cash generation

Maintaining strong cash generation delivery underpins debt servicing and repayments as well as shareholder dividends.

With cash generation of £486 million, of which £117 million is from the acquired AXA business, the Group has achieved its full year cash generation target of £350 million to £450 million.

£486m
Operating companies' cash generation

HOLDING COMPANIES' CASH FLOWS

The statement of cash flows prepared in accordance with IFRS combines cash flows relating to shareholders and cash flows relating to policyholders, but the practical management of cash within the Group maintains a distinction between the two. For this reason, the following analysis of cash flows focuses on the holding companies' cash flows which reflect cash flows relating only to shareholders and which are, therefore, more representative of the cash that could potentially be distributed as dividends or used for the prepayment of debt, the payment of debt interest, Group expenses and pension contributions (subject to the Group's liquidity policy, regulatory and other restrictions on the availability and transferability of capital). This cash flow analysis reflects the cash paid by the operating companies to the holding companies as well as the uses of those cash receipts.

	Year ended 31 December 2016 £m	Year ended 31 December 2015 £m
Cash and cash equivalents at 1 January	**706**	988
Operating companies' cash generation:		
Cash receipts from Phoenix Life	**486**	225
Total cash receipts[1]	**486**	225
Uses of cash:		
Operating expenses	**(33)**	(26)
Pension scheme contributions	**(55)**	(55)
Debt interest	**(58)**	(91)
Total recurring outflows	**(146)**	(172)
Non-recurring outflows	**(141)**	(25)
Uses of cash before debt repayments and shareholder dividend	**(287)**	(197)
Debt repayments	**(239)**	(190)
Shareholder dividend	**(126)**	(120)
Total uses of cash	**(652)**	(507)
Equity issuance (net of fees)	**908**	–
Debt issuance (net of fees)	**428**	–
Cost of acquisitions	**(1,306)**	–
Cash and cash equivalents at 31 December[2]	**570**	706

1 Includes amounts received by the holding companies in respect of tax losses surrendered to the operating companies of £84 million (2015: £71 million).

2 The required prudential cash buffer of £150 million at 31 December 2015 is no longer required.

CASH RECEIPTS

Cash remitted by the operating companies was £486 million (2015: £225 million) including £117 million generated from the acquired AXA businesses.

Of the £486 million, management actions accounted for £265 million.

RECURRING CASH OUTFLOWS

The operating expenses of £33 million (2015: £26 million) principally comprise corporate office costs, net of income earned on holding company cash and investment balances. The increase compared to prior year is due to lower interest earned on bank balances and excess cash balances being used to repay debt.

Pension scheme contributions of £55 million (2015: £55 million) are in line with the latest triennial funding agreements agreed during 2016.

Debt interest decreased to £58 million (2015: £91 million) reflecting lower principal balances following repayments made in 2015. The 2015 debt interest included payment of the £20 million coupon on the Tier 1 bonds prior to their exchange for the PGH Capital subordinated notes.

NON-RECURRING CASH OUTFLOWS

Non-recurring cash outflows of £141 million are significantly higher compared to the prior period reflecting costs associated with hedging and acquisition activity undertaken during 2016. Outflows also include £68 million of capital support provided to a subsidiary of the Group, PA (GI) Limited, with regard to the cost of providing for potential claims and associated capital requirements relating to creditor insurance underwritten prior to 2006.

DEBT REPAYMENTS AND SHAREHOLDER DIVIDEND

Total debt repayments of £239 million in 2016 were in respect of the repayment of the £182 million bank debt used to finance the acquisition of the AXA business, together with £50 million of the Group's revolving credit facility. The remaining £6 million of outstanding Tier 1 bonds were also redeemed in March 2016.

The shareholder dividend of £126 million comprises the payment of the 2015 final dividend of £60 million and the payment of the 2016 interim dividend of £66 million, reflecting the impact of shares issued in May 2016 as part of the AXA acquisition.

EQUITY ISSUANCE (NET OF FEES)

The £908 million is in relation to proceeds, net of fees of £22 million, from the equity placement and the rights issue associated with the financing of the respective acquisitions of the AXA and Abbey Life businesses.

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DEBT ISSUANCE (NET OF FEES)

£428 million of debt , net of fees of £4 million, was issued in 2016 comprising the £182 million short-term debt facility in connection with the acquisition of the AXA business, which was fully repaid during the year, and the £250 million short-term bank facility issued in connection with the Abbey Life acquisition. This facility has subsequently been refinanced with the Group's lending banks into an enlarged revolving credit facility of £900 million.

COST OF ACQUISITIONS

The £1,306 million comprise:

- £933 million in connection with the acquisition of Abbey Life; and
- £373 million for the acquisition of AXA Wealth's pensions and protection businesses.

TARGET CASH FLOWS

The five-year cumulative target cash flow for 2016 to 2020 is £2.8 billion, of which £486 million has been generated in 2016.

The resilience of the cash generation target is demonstrated by the following illustrative stress testing[1]:

	1 January 2016 to 31 December 2020 £bn
Base case five-year target	**2.8**
Following a 20% fall in equity markets	**2.8**
Following a 15% fall in property values	**2.7**
Following a 55bps interest rates rise[2]	**3.0**
Following a 80bps interest rates fall[2]	**2.6**
Following credit spread widening[3]	**2.7**
Following 6% decrease in annuitant mortality rates[4]	**2.5**
Following a 10% increase in assurance mortality rates	**2.7**
Following a 10% change in lapse rates[5]	**2.7**

1 Assumes stress occurs on 1 January 2017 and there is no market recovery during the cash generation target period.

2 Assumes recalculation of Transitionals (subject to PRA approval).

3 Credit stress equivalent to an average 150bps spread widening across ratings, 10% of which is due to defaults/downgrades.

4 Equivalent of 6 months increase in longevity applied to the annuity portfolio.

5 Assumes most onerous impact of a 10% increase/decrease in lapse rates across different product groups.

EXPECTED CASH FLOWS AFTER 2020

The expected cash generation post 2020 is expected to be £4.4 billion. This assumes no management actions after 2020 and reflects the net impact arising from the run-off of the Risk Margin and Transitionals up to 2032 (see page 31).

Capital management

£1.9bn
PLHL Solvency II surplus (pro forma)

170%
PLHL Shareholder Capital Coverage Ratio (pro forma)

CAPITAL MANAGEMENT FRAMEWORK

The Group's capital management framework is designed to achieve the following objectives:

- to provide appropriate security for policyholders and meet all regulatory capital requirements under the Solvency II regime while not retaining unnecessary excess capital.
- to ensure sufficient liquidity to meet obligations to policyholders and other creditors.
- to optimise the Fitch Rating's financial leverage ratio to maintain an investment grade credit rating.
- to support the Group's progress in putting in place a new UK-registered holding company for the Group.
- to maintain a stable and sustainable dividend policy.

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

PLHL SOLVENCY II CAPITAL POSITION (PRO FORMA)

In accordance with European Insurance and Occupational Pension Authority ('EIOPA') and PRA requirements, from 1 January 2016 the Group undertakes a Solvency II capital adequacy assessment at the level of the highest EEA insurance group holding company, which is PLHL.

This involves a valuation in line with Solvency II principles of PLHL's Own Funds and a risk-based assessment of PLHL's Solvency Capital Requirements ('SCR').

PLHL's Own Funds differ materially from the Group's IFRS equity for a number of reasons, including the exclusion of the Group's bank debt and the senior bond held outside of the PLHL sub group, the recognition of future shareholder transfers from the with-profit funds (but not the shareholder share of the estate), the treatment of certain subordinated debt instruments as capital items, and a number of valuation differences, most notably with regard to insurance contract liabilities and intangible assets.

The SCR is calibrated so that the likelihood of a loss exceeding the SCR is less than 0.5% over one year. This ensures that capital is sufficient to withstand a broadly '1 in 200 year event'.

In December 2015, the Group was granted the PRA's approval for use of its Internal Model to assess capital requirements. The capital assessment of the acquired AXA and Abbey Life businesses remained on a Standard Formula basis as at 31 December 2016. Therefore, the estimated Solvency II position of PLHL at that date is based partially on the Group's Internal Model and partially on Standard Formula.

The PLHL Solvency II surplus position at 31 December 2016 is set out in the table below. As explained in detail on page 23, a pro forma PLHL Solvency II surplus position has also been presented to illustrate the impacts of the issuance of a Solvency II qualifying Tier 3 bond in January 2017 and the receipt of the PRA's approval in March 2017 to include the acquired AXA businesses within the scope of the Group's Internal Model.

	Own Funds[1] £bn	SCR[2] £bn	Surplus[3] £bn
Estimated position[4]	**6.7**	**(5.0)**	**1.7**
Adjustments:			
Impact of the Tier 3 bond	**0.1**	**–**	**0.1**
Impact of incorporating the AXA businesses in the Group's Internal Model	**–**	**0.1**	**0.1**
Pro forma position at 31 December 2016[4]	**6.8**	**(4.9)**	**1.9**

1 Own Funds includes the net assets of the life and holding companies calculated under Solvency II rules, pension scheme surpluses calculated on an IAS19 basis not exceeding the holding companies' contribution to the Group SCR and qualifying subordinated liabilities. It is stated net of restrictions for assets which are non-transferable and fungible between Group companies within a period of nine months.

2 The SCR reflects the risks and obligations to which the PLHL Group is exposed.

3 The pro forma surplus equates to a coverage ratio of 140% as at 31 December 2016.

4 The estimated and pro forma Solvency II positions include the adverse impact of an assumed recalculation of Transitional Measures on Technical Provisions ('TMTP') and reflect the run-off of TMTP since 1 January 2016. See page 23 for more details.

5 The actual Solvency II position at 31 December 2015 comprised Own Funds of £5.7 billion and SCR of £4.4 billion equating to a coverage ratio of 130%.

PLHL SOLVENCY II SURPLUS (PRO FORMA)

The pro forma Solvency II surplus at 31 December 2016 of £1.9 billion (2015: £1.3 billion, actual) has increased by £0.6 billion as a result of:

- £0.2 billion of surplus emerging from the life companies (excluding the acquired AXA and Abbey Life businesses) and the expected run-off of capital requirements;
- achieved management actions of £0.5 billion including completion of a Part VII transfer of a portfolio of annuities, the execution of a longevity swap with an external reinsurer, and the extension of Matching Adjustment benefits to new asset classes;
- £0.3 billion impact of the acquisitions completed during the period;
- £0.1 billion pro forma benefits of including the acquired AXA businesses within the scope of the Group's Internal Model; and
- issuance of the new Tier 3 bond which contributed £0.1 billion to the Solvency II surplus on a pro forma basis; partly offset by,
- £(0.2) billion adverse impact of actuarial assumption strengthening, experience and modelling changes;
- dividend payments and financing costs of £(0.2) billion; and
- the adverse impact of market and other movements of £(0.2) billion, primarily falling yields which have had an adverse impact on risk capital in the period.

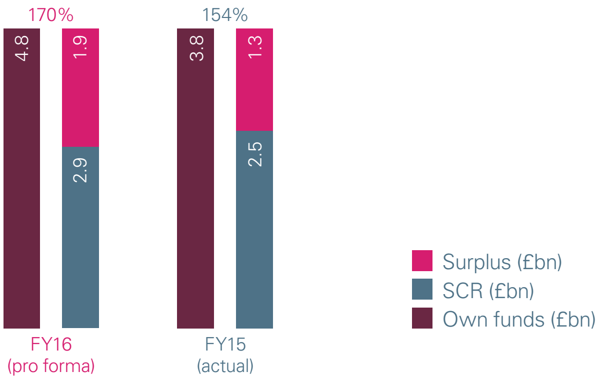
The Solvency II surplus excludes the surpluses arising in the Group's unsupported with-profit funds and the PGL Pension Scheme of £0.4 billion. In the calculation of the PLHL Solvency II surplus, the SCR of the with-profit funds and the PGL Pension Scheme is included, but the related Own Funds are recognised only to a maximum of the SCR amount. Surpluses that arise in with-profit funds and the PGL Pension Scheme, whilst not included in the PLHL Solvency II surplus, are available to absorb economic shocks. This means that the headline surplus is resilient to economic stresses.

Unsupported with-profit funds and the PGL Pension Scheme consist of £2.4 billion of Own Funds and £2.0 billion of SCR. Of the £2.4 billion of Own Funds, £1.8 billion consists of estate within the unsupported with-profit funds and £0.6 billion of Own Funds within the PGL Pension Scheme.

SHAREHOLDER CAPITAL COVERAGE RATIO (PRO FORMA)

Excluding the SCR and Own Funds relating to the unsupported with-profit funds and the PGL Pension Scheme, the pro forma Solvency II Shareholder Capital Coverage ratio is 170% as at 31 December 2016 (2015: 154%, actual). The Pearl Group Staff Pension Scheme and the Abbey Life Staff Pension Schemes did not cover their SCR as at 31 December 2016 and the related Own Funds and SCR are therefore included in the Shareholder Capital Coverage ratio calculation.

SHAREHOLDER CAPITAL COVERAGE RATIO



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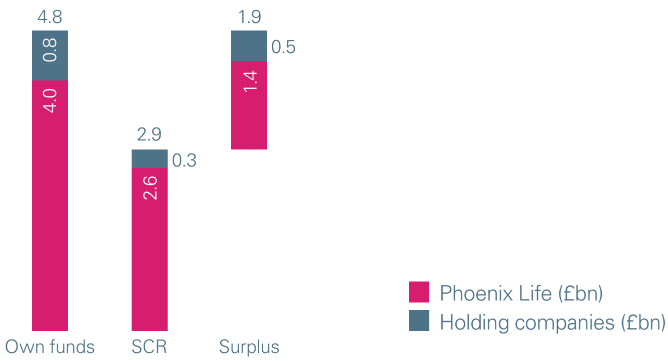
The pro forma shareholder capital position is further analysed between the contributions of the holding companies and the life companies as follows:

BREAKDOWN OF SHAREHOLDER CAPITAL POSITION



Own funds within the holding companies of £0.8 billion (2015: £1.0 billion) principally comprises cash and other financial assets held in the holding companies.

Own Funds within Phoenix Life of £4.0 billion (2015: £2.8 billion) comprise £1.1 billion (2015: £1.0 billion) in the shareholders' funds, £1.8 billion (2015: £0.7 billion) in the non-profit funds, £0.6 billion (2015: £0.7 billion) in the supported with-profit funds and future shareholder transfers of £0.5 billion (2015: £0.4 billion).

PHOENIX LIFE FREE SURPLUS (PRO FORMA)

Phoenix Life Free Surplus represents the Solvency II surplus of the life companies that is in excess of their Board-approved capital management policies.

As at 31 December 2016, the pro forma Phoenix Life Free Surplus is £0.7 billion (2015: £0.1 billion). The table below analyses the movement during the period:

	Year ended 31 December 2016 £bn
Opening Free Surplus (actual)	**0.1**
Surplus generation and expected run-off of capital requirements	**0.2**
Management actions	**0.6**
Impact of acquisitions	**0.3**
Assumptions, experience and modelling changes	**(0.1)**
Impact of economic and other variances	**(0.2)**
Free Surplus before cash remittances	**0.9**
Cash remittances to holding companies[1]	**(0.4)**
Closing Free Surplus (before pro forma adjustments)	**0.5**
Impact of incorporating the AXA businesses in the Group's Internal Model	**0.2**
Closing Free Surplus (pro forma)	**0.7**

1 The cash remittances to holding companies excludes cash receipts from Opal Re in the period of £85 million.

The pro forma Phoenix Life Free Surplus excludes £49 million of financial assets held in Opal Re as at 31 December 2016 (2015: £125 million).

SENSITIVITY AND SCENARIO ANALYSIS

As part of the Group's internal risk management processes, the regulatory capital requirements are tested against a number of financial scenarios. The results of that stress testing[1] are provided below and demonstrate the resilience of the pro forma PLHL Solvency II surplus.

	Pro forma PLHL Solvency II surplus £bn
Base: 1 January 2017	**1.9**
Following a 20% fall in equity markets	**1.9**
Following a 15% fall in property values	**1.8**
Following a 55bps interest rates rise[2]	**2.0**
Following a 80bps interest rates fall[2]	**1.8**
Following credit spread widening[3]	**1.8**
Following 6% decrease in annuitant mortality rates[4]	**1.6**
Following 10% increase in assurance mortality rates	**1.8**
Following a 10% change in lapse rates[5]	**1.8**

1 Assumes stress occurs on 1 January 2017.

2 Assumes recalculation of transitionals (subject to PRA approval).

3 Credit stress equivalent to an average 150bps spread widening across ratings, 10% of which is due to defaults/downgrades.

4 Equivalent of 6 months increase in longevity applied to the annuity portfolio.

5 Assumes most onerous impact of a 10% increase/decrease in lapse rates across different product groups.

PGH SOLVENCY II SURPLUS (PRO FORMA)

As previously noted, the Solvency II capital assessment and Group's regulatory supervision is performed at the PLHL level as this is the highest EEA insurance holding company. A waiver is currently in place which permits Group supervision to take place at the level of the ultimate parent, PGH, via other methods, as opposed to full Group supervision. This waiver is due to expire on 30 June 2017.

As part of the on going simplification of the Group structure, Phoenix intends to put in place a new UK-registered holding company for the Group. The new company will be the ultimate parent company and the highest EEA insurance Group holding company. When complete, the Solvency II capital assessment and Group supervision will only be performed at this level.

From 1 July 2017 and pending the completion of the simplification of the Group structure, regulatory supervision and the Solvency II capital adequacy assessment is expected to be performed at the PLHL and PGH level.

The key difference between the pro forma capital position of PLHL and the pro forma position at the PGH level is the inclusion of the Group's current senior debt and the revolving credit facility within the Own Funds calculation.

The table below illustrates the pro forma Solvency II position at the PGH level at 31 December 2016.

	Own funds £bn	SCR £bn	Surplus £bn
PLHL pro forma position[1]	6.8	(4.9)	1.9
Revolving credit facility	(0.5)	–	(0.5)
Senior unsecured bond	(0.3)	–	(0.3)
Net other items[2]	0.1	–	0.1
2016 final dividend	(0.1)	–	(0.1)
PGH pro forma position[3]	6.0	(4.9)	1.1

1 Details of the PLHL pro forma are set out on page 23.

2 Net other items reflect the impact of intragroup eliminations together with the recognition of cash and other assets held in companies above the PLHL sub group

3 The PGH pro forma position assumes the substitution of the issuer of the Group's shareholder borrowings from PGH Capital plc to PGH effective from 20 March 2017, as if it occurred on 31 December 2016. See note I9 to the IFRS financial statements for further details.

TRANSITIONAL MEASURES ON TECHNICAL PROVISIONS AND RISK MARGIN

The Group has obtained the PRA's approval to apply Transitional Measures on Technical Provisions ('TMTP'). This allows for a transitional deduction on technical provisions which is the difference between the net technical provisions calculated in accordance with the Solvency II rules and the net technical provisions calculated in accordance with the previous regime. The transitional deduction is expected to decrease over 16 years from 1 January 2016 to 1 January 2032 in line with business run-off.

The Solvency II technical provisions include a Risk Margin which is highly sensitive to interest rates. As a consequence, a sustained change in interest rates has a direct impact on the Risk Margin. The Solvency II rules allows for recalculation of the transitional deduction under certain circumstances, one of these being a change in the operating conditions due to external market-wide events such as changes in the risk free rate. Such a recalculation requires PRA approval.

At 31 December 2016, PLHL's Solvency II surplus includes the effects of an assumed recalculation of the transitional deduction as at that date and reflects amortisation since 1 January 2016. Accordingly the year end position includes a transitional deduction of £1.9 billion (excluding the unsupported with-profit funds), which offset £1.3 billion of Risk Margin and £0.6 billion of other technical provisions recognised in the life companies. As the acquired Abbey Life business has not recognised a transitional deduction, it is excluded from the analysis above. The run-off of the transitional deduction over time will be substantially offset by the reduction of the Risk Margin therefore mitigating any resulting impact on the Solvency II surplus.

IFRS results

£351m
Operating profit

£(100)m
IFRS loss after tax

The operating profit has increased to £351 million (2015: £324 million), primarily driven by the impact of £157 million of management actions during 2016 (2015: £68 million) and the impact of updates made to the IFRS reserving methodology to more closely align to the Solvency II requirements, partly offset by strengthening of actuarial assumptions to reflect anticipated policyholder behaviour in the continued low interest environment.

The loss after tax attributable to owners is £100 million (2015: £249 million, profit) reflecting adverse economic variances, principally yields and losses on equity hedging positions, together with the one-off impact associated with acquisition and integration activities.

	Year ended 31 December 2016 £m	Year ended 31 December 2015 £m
Phoenix Life	357	336
Group costs	(6)	(12)
Operating profit	351	324
Investment return variances and economic assumption changes on long-term business	(207)	13
Variance on owners' funds	(5)	(12)
Amortisation of acquired in-force business and other intangibles	(82)	(90)
Other non-operating items	(95)	49
Profit before finance costs attributable to owners	(38)	284
Finance costs attributable to owners	(90)	(99)
(Loss)/profit before the tax attributable to owners:	(128)	185
Tax credit attributable to owners	28	64
(Loss)/profit for the period attributable to owners	(100)	249

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PHOENIX LIFE OPERATING PROFIT

Operating profit for Phoenix Life is based on expected investment returns on financial investments backing shareholder and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities (being the release of prudential margins and the interest cost of unwinding the discount on the liabilities). The principal assumptions underlying the calculation of the long-term investment return are set out in note B2 to the IFRS consolidated financial statements.

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

Phoenix Life operating profit	Year ended 31 December 2016 £m	Year ended 31 December 2015 £m
With-profit	**81**	92
With-profit where internal capital support provided	**(72)**	84
Non-profit and unit-linked	**283**	124
One-off impact of IFRS methodology change	**31**	–
Long-term return on owners' funds	**7**	6
Management services	**27**	30
Phoenix Life operating profit before tax	**357**	336

The with-profit operating profit of £81 million (2015: £92 million). represents the shareholders' one-ninth share of the policyholder bonuses, and has reduced due to lower bonus rates.

The with-profit funds where internal capital support has been provided generated an operating loss of £72 million (2015: £84 million profit). The loss is principally driven by impact of strengthening actuarial assumptions to reflect the impact of the continued low interest rate environment on the Group's expectations of persistency for products with valuable guarantees. The 2015 comparative included the positive impact of actuarial modelling enhancements implemented in the year of £49 million.

The operating profit on non-profit and unit-linked funds increased to £283 million (2015: £124 million) primarily reflecting the outcomes of management actions of £117 million undertaken during the period, and positive experience which has more than offset some adverse one-off impacts of actuarial modelling enhancements undertaken in the period.

Following the implementation of Solvency II, certain changes have been made to the assumptions and estimates used in the valuation of insurance contract liabilities to more closely align the IFRS reserving methodology with Solvency II requirements. As the Group manages its capital on a Solvency II basis, the changes mean that the IFRS results now more closely reflect the way the business is managed. The implementation of the changes at 1 January 2016 resulted in an overall favourable impact of £31 million to Phoenix Life operating profit. The overall profile for the emergence of future operating profit is expected to be materially unchanged as a result of these updates. More details on the changes are provided in note F4 to the IFRS consolidated financial statements.

The long-term return on owners' funds of £7 million (2015: £6 million) reflects the asset mix of owners' funds, primarily cash-based assets and fixed interest securities. The investment policy for managing these assets remains prudent.

The operating profit for management services of £27 million (2015: £30 million) comprises income from the life companies in accordance with the respective management service agreements less fees related to the outsourcing of services and other operating costs. The decrease compared to the prior period reflects the impact of life company run-off and increased project costs incurred during the year.

GROUP COSTS

Group costs in the period were £6 million (2015: £12 million). The reduction compared to the prior period principally reflects an increased return on the higher opening pension scheme surpluses of both the PGL Pension Scheme and the Pearl Group Staff Pension Scheme.

INVESTMENT RETURN VARIANCES AND ECONOMIC ASSUMPTION CHANGES ON LONG-TERM BUSINESS

The negative investment return variances and economic assumption changes on long-term business of £207 million (2015: £13 million positive) are primarily driven by adverse market movements during the year.

The majority of the negative variance is driven by the adverse impact of falling yields on the life funds which has increased the margin held within insurance liabilities in respect of longevity risk.

The investment return variances have also been adversely impacted by losses arising on equity hedging positions held by the life funds following equity market gains in the period. Equity market gains in the period have resulted in an unfavourable variance as the value of the hedging instruments fall without the corresponding benefit from future profits within the life funds being recognised.

VARIANCE ON OWNERS' FUNDS

The negative variance on owners' funds of £5 million (2015: £12 million negative) is driven by losses from equity hedging positions held in the Group Holding Companies, offset by gains from interest rate hedging positions held in the life companies' shareholders' funds arising from falling yields.

AMORTISATION OF ACQUIRED IN-FORCE BUSINESS AND OTHER INTANGIBLES

Acquired in-force business and other intangibles of £2.7 billion were recognised on the acquisition of the operating companies in 2009. Following the acquisition of the AXA and Abbey Life businesses in 2016, a further £0.2 billion of acquired-in-force business and other intangibles have been recognised in the Group's balance sheet.

The acquired in-force business is being amortised in line with the run-off of the life companies. Amortisation of acquired in-force business during the period totalled £68 million (2015: £75 million). Amortisation of other intangible assets totalled £14 million in the period (2015: £15 million).

OTHER NON-OPERATING ITEMS

Other non-operating items of £(95) million (2015: £49 million positive) include a £26 million gain on the implementation of a longevity swap reassurance contract on a portfolio of the Group's annuities and a £14 million gain as a result of a premium adjustment of the 2015 reassurance arrangement with RGA International following completion of a data review.

These items have been more than offset by:

- acquisition costs of £31 million, comprising £12 million of transaction costs related to the acquisition of AXA Wealth's pensions and protection business and £19 million of transaction costs related to acquisition of Abbey Life;
- a provision for costs of £30m associated with the integration and restructuring of the acquired AXA businesses;
- the costs of providing for claims and associated costs relating to creditor insurance underwritten prior to 2016 by a subsidiary of the Group, PA (GI) Limited, of £33 million;
- recognition of costs of £10 million associated with the introduction of regulations that cap early exit charges for pension customers aged over 55 at 1%, which will come into force from 2017;
- costs of £6 million associated with the transfer of non-profit annuities from with-profit funds to non-profit matching adjustment funds;
- the costs of £4 million associated with the PGL pension scheme buy-in;
- other corporate project costs of £19 million; and
- net other one-off items totalling a cost of £2 million.

The prior period positive other non-operating result of £49 million included a gain of £49 million arising on the reassurance of a portfolio of PLAL annuities with an external reinsurer and a £17 million release of cost provisions associated with external regulatory changes, partly offset by £11 million of corporate project costs and negative £3 million of net other items.

FINANCE COSTS ATTRIBUTABLE TO OWNERS

	Year ended 31 December 2016 £m	Year ended 31 December 2015 £m
Bank finance costs	**16**	28
Other finance costs	**74**	71
Finance costs attributable to owners	**90**	99

Finance costs have decreased by £9 million, comprising a £12 million reduction in bank finance costs primarily driven by restructuring and repayments of bank debt, and a £3 million increase in other finance costs attributable to interest on the £428 million subordinated notes issued during the first half of 2015.

TAX CREDIT ATTRIBUTABLE TO OWNERS

The Group's approach to the management of its tax affairs is set out in its Tax Strategy document which will shortly be available in the governance section of the Group's website. The Group's tax affairs and tax controls are managed by an in-house tax team who report on them to the Board and the Audit Committee on a regular basis throughout the year. The Board believes that its Tax Strategy accords with the Group's approach to its wider Corporate Social Responsibility.

Implicit in the Group's Tax Strategy and the management of its tax affairs is a desire for greater transparency and openness that will help the Group's stakeholders better understand the published tax numbers. In this way the Group aims to participate in a substantive manner with HMRC and other insurance industry stakeholders on consultative documents and tax law changes that potentially impact on the insurance sector.

Following the 2015 disposal of the Group's overseas insurance interests, all of the Group's insurance operations are based in the UK and are liable to tax in accordance with applicable UK legislation. The Group derives a de-minimis level of income from non-UK sources. Although Phoenix Group Holdings is a Jersey resident holding company and subject to a 0% tax rate, its primary source of income is its UK subsidiaries. The tax residency of Phoenix Group Holdings has a negligible impact on the UK tax payable by the Group.

The Group tax credit for the period attributable to owners is £28 million (2015: £64 million) based on a loss (before tax attributable to owners) of £128 million (2015: £185 million profit). The tax credit is different from the expected tax credit (based on the UK corporation tax rate of 20%) of £26 million primarily due to the impact of disallowable expenses including £7 million relating to the provision for costs recognised in respect of the creditor insurance underwritten by PA (GI) Limited and the impact of the consolidation treatment of the PGL pension scheme buy-in agreement of £12 million. These items have been partly offset by the benefit of a 1% reduction in future corporation tax rates and the treatment of certain recurring income and expenses as either non-taxable or taxable at rates of less than 20%. See note C5 to the IFRS consolidated financial statements for further analysis.

RISK MANAGEMENT

"OUR RISK INFRASTRUCTURE HAS ENABLED THE GROUP TO DELIVER KEY STRATEGIC INITIATIVES AMIDST A VOLATILE ECONOMIC AND POLITICAL ENVIRONMENT."

WAYNE SNOW
GROUP CHIEF RISK OFFICER

THE GROUP'S RISK MANAGEMENT FRAMEWORK

The Group's Risk Management Framework ('RMF') embeds proactive and effective risk management across the Group. It seeks to ensure that all risks are identified and managed effectively and that the Group is appropriately rewarded for the risks it takes.

During the year, the Group strengthened its RMF to meet evolving regulatory requirements including Solvency II and the UK Corporate Governance Code. I was pleased to see our approach to risk management recognised in the investment grade rating reaffirmed by Fitch Ratings following our two acquisitions.

Further detail on the ten components of our RMF and the principal risks facing the Group are provided below.

The Group is now implementing its risk management approach in the AXA Wealth and Abbey Life businesses and using its framework to manage the associated integration risks.

RISK CULTURE

The Group seeks to embed a culture that is forward-looking and competent in its assessment and management of risk, a culture where everyone in the Group is aligned in their goals to deliver better risk-based decisions.

To support this goal, the Group defined a Risk Culture Statement which sets out the Group's aspirations for Risk Management:

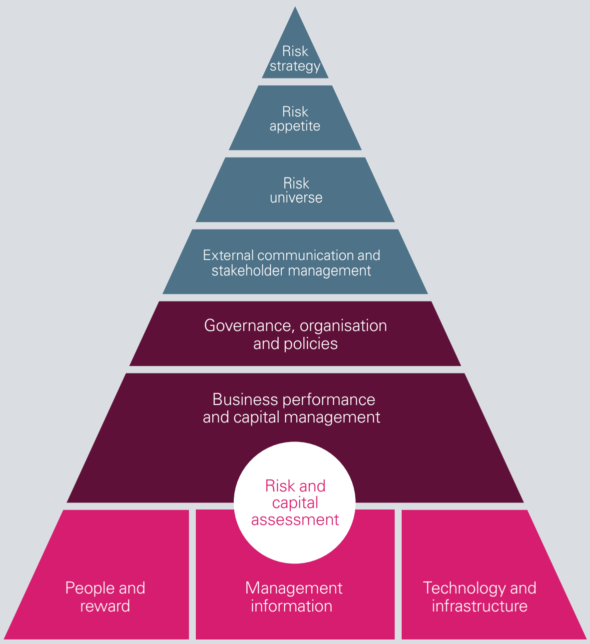
"The Group has a balanced risk culture, supportive of commercial risk-taking coupled with strong execution in line with its risk appetite."

At its core are the Group's values and behaviours, clarity of accountability and a healthy tension between the first and second lines of defence.

Collectively this means people understand the Group's approach to risk, take personal responsibility to manage risk in everything they do and encourage others to follow their example."

During 2016, Group Risk conducted its latest annual Risk Culture survey. The results of this survey enable us to assess and measure the Group's Risk Culture over time as well as being able to tailor training programmes to ensure the continued engagement and development of our employees.

RISK MANAGEMENT FRAMEWORK



OWN RISK AND SOLVENCY ASSESSMENT (ORSA)

The Group carries out an ORSA process to assess its risk profile on an ongoing basis. The ORSA considers risk, capital and return within the context of the business strategy on a forward-looking basis.

The ORSA is a fundamental part of the strategic risk and capital management processes of the business to prompt consideration of management actions and help shape strategic decision-making.

RISK STRATEGY

The Group's risk strategy provides an overarching view of how risk management is incorporated consistently across all levels of the business, from decision-making to strategy implementation.

It assists the business achieve its strategic objectives by supporting a more stable, well managed business with improved customer and shareholder outcomes.

This is achieved not by risk avoidance, but through the identification and management of an acceptable level of risk (its 'risk appetite') and by ensuring that the Group is appropriately rewarded for the risks it takes.

To ensure that all risks are managed effectively the Group is committed to:

- embedding a risk aware culture;
- maintaining a strong system of internal controls;
- enhancing and protecting customer and shareholder value by continuous and proactive risk management;
- maintaining an efficient capital structure; and
- ensuring that risk management is embedded into day-to-day management and decision-making processes.

RISK APPETITE

The Group's risk appetite is the level of risk the Group is willing to accept in pursuit of its strategic objectives. The statements below encapsulate our risk appetite for policyholder security and conduct, earnings volatility, liquidity and our control environment:

- **Capital** – The Group and each Life Company will hold sufficient capital to meet regulatory requirements in a number of asset and liability stress scenarios.
- **Cash flow** – The Group will seek to ensure that it has sufficient cash flow to meet its financial obligations and will continue to do this in a volatile business environment.
- **Shareholder Value** – The Group will take action to protect its shareholder value.
- **Regulation** – The Group and each Life Company will, at all times, operate a strong control environment to ensure compliance with all internal policies and applicable laws and regulations, in a commercially effective manner.
- **Conduct** – Phoenix has zero appetite for deliberate acts of misconduct, including omissions, that result in customer detriment, reputational damage and/or pose a risk to the Financial Conduct Authority ('FCA') statutory objectives.

The risk appetite and control framework supports the Group in operating within the boundaries of these statements by limiting the volatility of key parameters under adverse scenarios. Risk appetite limits are chosen which specify the maximum acceptable likelihood for breaching the agreed limits. Assessment against these limits is undertaken through extensive scenario and reverse stress testing.

RISK UNIVERSE

A key element of effective risk management is ensuring that the business has a complete understanding of the risks it faces. These risks are defined in the Group's risk universe.

The risk universe allows the Group to deploy a common risk language, allowing for meaningful comparisons to be made across the business. There are three levels of risk universe categories. The highest risk universe category is Level 1 and includes:

- strategic risk;
- customer risk;
- financial soundness risk;
- market risk;
- credit risk;
- insurance risk; and
- operational risk.

Embedded within these categories, and Customer risk in particular, are the conduct risks faced by the Group and its customers. These risks are separately monitored and reported on across the organisation to ensure that conduct risk receives appropriate emphasis and oversight.

The Group has developed a PGH Board-approved risk appetite statement to manage conduct risk. The appetite statement is supported by the assessment of all conduct related risks faced by the Group on a quarterly basis. This regular assessment and reporting enables us to be forward-looking and proactive in the management of conduct risk.

EXTERNAL COMMUNICATION AND STAKEHOLDER MANAGEMENT

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

GOVERNANCE, ORGANISATION AND POLICIES

GOVERNANCE

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

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

First line: Management

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

Second line: Risk Oversight

Risk oversight is provided by the Group Risk function and the Board Risk Committee. The Board Risk Committee comprises four independent Non-Executive Directors. It is supported by the Group Chief Risk Officer and met six times during 2016. During 2016, the Risk Committee of the Phoenix Life Board met five times and provided additional Board Committee focus on risk matters at Phoenix Life.

Third line: Independent Assurance

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

ORGANISATION

The Group Chief Risk Officer manages the Group Risk function and has responsibility for the implementation and oversight of the Group's RMF. The Group Risk function has responsibility for oversight over financial, operational and regulatory risk. The PRA/FCA relationship team manages the relationship and interactions with our primary regulators and reports to the Group Chief Risk Officer.

RISK MANAGEMENT
Continued

POLICIES

The Group policy framework comprises a set of policies that supports the delivery of the Group's strategy by establishing operating principles and expectations for managing the key risks to our business. The policy set contains the minimum control standards to which each business unit must adhere to and against which they report compliance.

The policies define:

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

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

The governance framework in operation throughout the Group can be found in the chart below.

BUSINESS PERFORMANCE AND CAPITAL MANAGEMENT

The Annual Operating Plan is assessed to ensure that the Group operates within our stated risk appetite. Business performance is routinely monitored with consolidated reporting against performance targets.

The Group operates a Capital Management Policy where capital is allocated across risks where capital is held as a mitigant and the amount of risk capital required is reviewed regularly.

RISK AND CAPITAL ASSESSMENT

The Group operates a standardised assessment framework for the identification and assessment of the risks to which it may be exposed and how much capital should be held in relation to those exposures. This framework is applicable across the Group and establishes a basis, not only for the approach to risk assessment, management and reporting but also for determining and embedding capital management at all levels of the Group in line with Solvency II requirements.

Risk assessment activity is a continuous process and is performed on the basis of identifying and managing the significant risks to the achievement of the Group's objectives.

Stress and scenario tests are used extensively to support the assessment of risk and provide analysis of their financial impact.

Independent reviews conducted by Group Risk provide further assurance to management and the Board that individual risk exposures and changes to our risk profile are being effectively managed.

MANAGEMENT INFORMATION

Overall monitoring and reporting against the risk universe takes place in business unit management committees and Boards. This is then reported to the Executive Committee, PLHL Board and the Group Board via regular risk reporting.

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

PEOPLE AND REWARD

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

TECHNOLOGY AND INFRASTRUCTURE

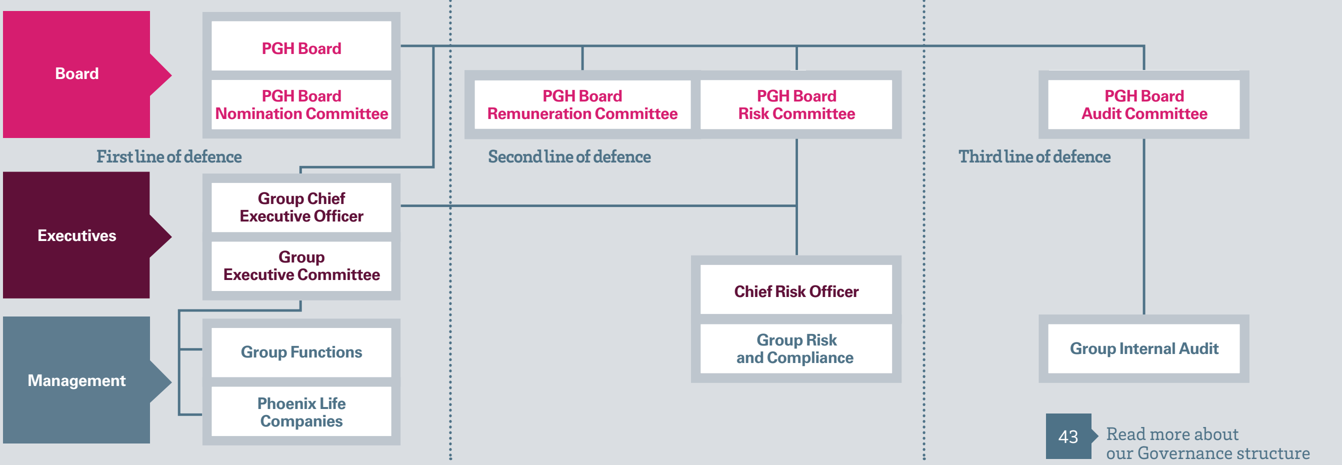
The Group employs market leading risk systems to support the assessment and reporting of the risks it faces. This enables management to document key risks and controls and evidence the assessment of them at a frequency appropriate to the operation of the control.

RISK MANAGEMENT EFFECTIVENESS

The provisions of the UK Corporate Governance Code require an annual review of the effectiveness of Risk Management.

This assessment provides assurance to management and the Boards that the RMF has been implemented consistently and is operating effectively across the Group.

GOVERNANCE FRAMEWORK



43 Read more about our Governance structure

PRINCIPAL RISKS AND UNCERTAINTIES FACING THE GROUP

The Group's top principal risks and uncertainties are detailed in the table below, together with their potential impact, mitigating actions which are in place, links to the Group's strategic objectives and changes in the risk profile from last year. As economic changes occur and the industry and regulatory environment evolves, the Group will continue to monitor their potential impact.

Further details of the Group's exposure to financial and insurance risks and how these are managed are provided in note E6 of the IFRS consolidated financial statements.

Key to Strategic objectives icons
Improve Customer outcomes
Drive Value
Manage Capital
Engage People

Change in risk from last year	Trend
Risk Improving	↑
No Change	–
Risk Deteriorating	↓

Risk	Impact	Mitigation	Strategic objectives	Change from last year
In times of severe market turbulence, the Group may not have sufficient capital or liquid assets to meet its cash flow targets or may suffer a loss in value.	The emerging cash flows of the Group may be impacted during periods of severe market turbulence by the need to maintain appropriate levels of regulatory capital. The impact of market turbulence may also result in a material adverse impact on the Group's capital position. Since the introduction of Solvency II and a swaps-based discount rate, the Group is more sensitive to movements in swap yields.	The Group undertakes regular monitoring activities in relation to market risk exposure, including limits in each asset class, cash flow forecasting and stress and scenario testing. In response to this, the Group has implemented de-risking strategies to mitigate against unwanted customer and shareholder outcomes. The Group also maintains cash buffers in its holding companies to reduce reliance on emerging cash flows. The Group's excess capital position continues to be closely monitored and managed, particularly in the low interest environment.	Improve Customer outcomes; Drive Value; Manage Capital	↓ Markets have been turbulent following the EU Referendum. Yields on UK swap rates fell markedly over the first half of the year, although they have since recovered. Phoenix prepared for this potential outcome by reducing residual interest rate exposure using a combination of interest rate swaps and swaptions. Recent currency volatility does not materially impact the Group.
Adverse changes in experience versus actuarial assumptions.	The Group has liabilities under annuities and other policies that are sensitive to future longevity, persistency and mortality rates. For example, if our annuity policyholders live for longer than expected, then their benefits will be paid for longer. The amount of additional capital required to meet those additional liabilities could have a material adverse impact on the Group's ability to meet its cash flow targets.	The Group undertakes regular reviews of experience and annuitant survival checks to identify any trends or variances in assumptions. The Group continues to actively manage its longevity risk exposures, which includes the use of reinsurance contracts to maintain this risk within appetite.	Drive Value; Manage Capital	↓ Policyholder persistency rates, rates of early and late retirement and the take-up of valuable guarantees were affected by the Pensions Freedoms legislation and the low interest rate environment. While the acquisition of the SunLife protection business exposes the Group to increased mortality and new business pricing risk, this business provides a natural hedge to our annuity business. During the year, the Group entered into a longevity swap arrangement to reinsure £2.0 billion of annuity liabilities.

RISK MANAGEMENT
Continued

Risk	Impact	Mitigation	Strategic objectives	Change from last year
Significant counterparty failure.	Assets held to meet obligations to policyholders include debt securities. Phoenix Life is exposed to deterioration in the actual or perceived creditworthiness or default of issuers. This risk is reflected in the higher expected return, or spread, over less risky assets. An increase in credit spreads on debt securities, particularly if it is accompanied by a higher level of actual or expected issuer defaults, could adversely impact the value of the Group's assets. The Group is also exposed to trading counterparties failing to meet all or part of their obligations, such as reinsurers failing to meet obligations assumed under reinsurance arrangements.	The Group regularly monitors its counterparty exposure and has specific limits relating to individual exposures, counterparty credit rating, sector and geography. Where possible, exposures are diversified through the use of a range of counterparty providers. All material reinsurance and derivative positions are appropriately collateralised and guaranteed.	£	During the year, exposure to reinsurance counterparties increased as the result of the longevity transaction referenced above. The Group also acquired reinsurance contracts with a number of external reinsurers through the AXA Wealth and Abbey Life acquisitions.
Changes in the regulatory and legislative landscape.	The conduct-focused regulator has had a greater focus on customer outcomes. This may continue to challenge existing approaches and/or may result in remediation exercises where Phoenix Life cannot demonstrate that it met the expected customer outcomes in the eyes of the regulator. Changes in legislation such as the Pension Freedoms and taxation can also impact the Group's financial position.	The Group puts considerable effort into managing relationships with its regulators so that it is able to maintain a forward view regarding potential changes in the regulatory landscape. The Group assesses the risks of regulatory and legislative change and the impact on our operations and lobbies where appropriate.		Phoenix has focused on activities identified following publication of the 'Fair Treatment of long-standing Customers' review to enhance our management of conduct risk. The Abbey Life acquisition increases the Group's regulatory risk exposure from ongoing FCA investigations. However, warranties and indemnities were agreed as part of the acquisition which mitigate against an adverse outcome. Surplus assets have been retained in life companies to mitigate any potential adverse impact of deferred tax restrictions being introduced in 2017. PGH waiver in respect of Group regulatory supervision expires at 30 June 2017.
The Group fails to effectively integrate the acquired businesses.	The challenge of integrating two new businesses into the Group could introduce structural or operational inefficiencies that results in Phoenix failing to generate the expected outcomes for policyholders or value for shareholders.	The financial and operational risks of target businesses were assessed as part of the acquisition phase. Integration plans are developed and resourced with appropriately skilled staff to ensure that the target operating models are delivered in line with expectations.		New risk.
Greater than anticipated redress cost relating to creditor insurance.	High Court ruling that PA (GI) Limited ('PAGI'), a Group company, retained liability in relation to creditor insurance originally underwritten by PAGI. Cost of redress for these complaints may be greater than provisions held, due to uncertainties with regard to the volumes of future complaints, the rates by which those complaints are upheld and the average redress value.	The Group has established efficient processes to review complaints received, and where appropriate, provide redress to the policyholder. The Group continues to monitor the level of complaints and emerging experience to ensure that the provisions remain appropriate. The Group is considering options in respect of seeking to recover incurred costs from third parties. (Further details in note G1 to the IFRS consolidated financial statements).	£	New risk.

PRINCIPAL RISKS AND UNCERTAINTIES FACING THE GROUP (CONTINUED)

The current assessment of the residual risk in respect of each of the Group's principal risks is illustrated in the chart opposite.

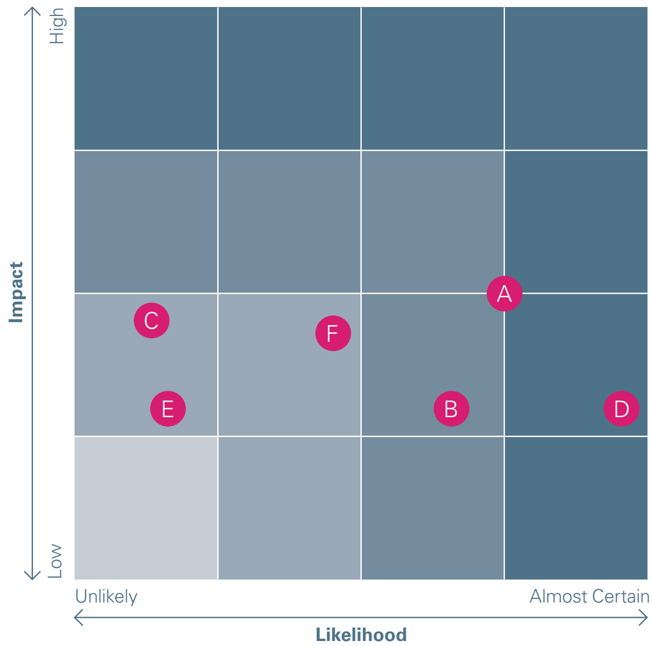
The residual risk is the remaining risk after controls and mitigating actions have been taken into account.

The Group's senior management and Board also take emerging risks into account when considering potentially adverse outcomes and appropriate management actions prior to the risk crystallising.

Some of the current emerging risks the Group considers are listed in the table below.

RISK TITLE	DESCRIPTION	RISK UNIVERSE CATEGORY
Regulatory Thematic Reviews	The unknown consequences and the potential impact, including retrospective activity, as a result of Thematic Reviews conducted by the regulators.	Customer
Voluntary Charges Cap	The FCA has noted that they are seeking a 'voluntary solution' on exit charges for legacy products.	Customer
Political Risk	Unexpected changes in the legislative environment and the impacts on financial markets driven by the political agenda following the UK's decision to leave the European Union.	Strategic
Market Disruptors	The impact of alternative providers in the market or those with more comprehensive digital propositions.	Strategic

PRINCIPAL RISKS



RISK
- A Market Volatility
- B Actuarial Assumptions
- C Counterparty Exposure
- D Regulatory and Legislative Changes
- E Acquisition Integration (new risk)
- F PAGI redress costs (new risk)

VIABILITY STATEMENT

In accordance with the provision of section C.2.2 of the 2014 revision of the UK Corporate Governance Code, the Board has completed an assessment of the prospects and viability of the Group over a five-year period to December 2021. The Board has determined that the five-year period to December 2021 is an appropriate period for the assessment, this being the period covered by the Group's Board-approved annual operating plan ('AOP').

In making the viability assessment, the Board has undertaken the following process:

— it defined what is mandatory in the context of viability;

— it reviewed the AOP which considers profits, liquidity, solvency and strategic objectives and the impacts of management actions on the Group;

— it completed stress testing to assess viability under severe but plausible scenarios, including two adverse stresses which represent the key financial risks to the Group as follows:

1. Market stress – a 1 in 10-year event combined market stress incorporating a fall in equity, property values and yields, with a widening of credit spreads.
2. Longevity stress – a 1 in 10-year event longevity and credit stress, which implies a 1.5 year increase in life expectancy for a 65 year old male alongside a widening of credit spreads.

— it considered the principal risks facing the Group which have the potential to impact on viability as discussed in the Risk report above; and

— it completed a qualitative assessment of all strategic risks to the Group and contingent actions available that could be implemented should any risk materialise that threatens the Group's resilience.

The Board has also made certain assumptions when making the assessment and these include the following:

— the stress occurs on 1 January 2017 with no allowance for any recovery, but do take into account the impact of transitionals recalculation; and

— that corporate acquisitions are not relevant, as any acquisition would only be progressed on the basis it was value accretive.

Based on the results of the procedures outlined above, the Board has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the five-year period of assessment.

ENVIRONMENTAL REPORTING

Our Corporate Responsibility programme supports our commitment to monitoring and reducing our environmental footprint.

This section includes mandatory reporting of greenhouse gas ('GHG') emissions pursuant to the Companies Act 2006 (Strategic and Directors' Reports) Regulations 2013. Emissions disclosed relate to facilities and activities where the Group has operational control.

On 1 November 2016, the Group completed the acquisition of AXA Wealth's pension and protection business from AXA UK plc. The acquisition resulted in two additional properties transferring to our operational control and being included in our carbon footprint.

In addition, on 30 December 2016 the Group completed the acquisition of Abbey Life Assurance Company Limited, Abbey Life Trustee Services Limited and Abbey Life Trust Securities Limited from Deutsche Bank Holdings No. 4 Ltd resulting in one property in Bournemouth transferring to our operational control and being included in our carbon footprint on a pro-rata basis.

In 2016 emissions have dropped principally through a reduction in the emission factor for consumption of purchased electricity (Scope 2) and the closure of one property. Approximately 0.4% of 2016 emissions are estimated as full year data is not yet available for all facilities. A sample of emissions from fuel use for company owned transport and back-up generation and fugitive emissions from refrigerants were calculated and were determined to be non-material to the overall footprint, so have not been included.

The data reported is based on the main requirements of the ISO14064 Part 1 and the GHG Protocol Corporate Standard (revised edition). Data was gathered at facility level to compile the carbon footprint. The Government's 2016 Conversion Factors for GHG Company Reporting have been used to convert energy data into carbon dioxide equivalent (CO_2e) emissions.

2016 marks the first time Phoenix Group is reporting Scope 2 emissions using the GHG Protocol dual-reporting methodology. This updated approach states that organisations should provide two figures to reflect the GHG emissions from purchased electricity, using both:

- A location-based method that reflects the average emissions intensity of the electricity grids from which consumption is drawn; and
- A market-based method that reflects emissions from electricity specific to each supply/contract

For market-based emissions there is a reporting quality hierarchy and Phoenix Group have used residual mix factors in the absence of contractual instruments.

Go online for the Group's full Corporate Responsibility Report
www.thephoenixgroup.com/CRreport2016

GREENHOUSE GAS EMISSIONS

GLOBAL GHG EMISSIONS DATA IN TONNES OF CO_2e

	2016		
	(location-based)	(market-based)	2015[1]
Combustion of fuel and operation of facilities (Scope 1)	**1,078**	**1,078**	986
Electricity, heat, steam and cooling purchased for own use (Scope 2)	**2,286**	**2,679**	2,874
Total Carbon Footprint (Scopes 1 + 2)	**3,364**	**3,757**	3,860

PHOENIX GROUP'S CHOSEN INTENSITY MEASUREMENT[2]

	2016 (location-based)	2015
Emissions reported above on a per floor area intensity	**81 kg CO_2e/m^2**	88 kg CO_2e/m^2
Emissions reported above on a per full-time equivalent employee (FTE) intensity	**4.3 tonnes CO_2e/FTE**	5.3 tonnes of CO_2e/FTE

1 Carbon footprint was restated to account for closure of a property mid-year that had previously been reported for a full 12 month period.

2 Our intensity measurement calculations exclude the newly acquired AXA and Abbey Life subsidiaries to avoid skewed intensity results.

GOVERNANCE

The Directors of Phoenix Group Holdings support the high standards of corporate governance contained in the UK Corporate Governance Code.

IN THIS SECTION

CHAIRMAN'S INTRODUCTION

"ALL WE DO MUST BE BASED ON STRONG GOVERNANCE STRUCTURES TO PROVIDE PROTECTION FOR OUR SHAREHOLDERS AND CUSTOMERS. I AM CONFIDENT IN THE ROBUST GOVERNANCE AT PHOENIX WHICH WE WILL ENSURE CONTINUES ACROSS OUR ENLARGED GROUP FOLLOWING THE ACQUISITION OF THE AXA AND ABBEY LIFE BUSINESSES."

HENRY STAUNTON
CHAIRMAN

SHAREHOLDERS

I am grateful for the strong support of our shareholders in 2016.

- Shareholders supported us at our AGM held on 11 May 2016 with a vote of at least 91% of votes cast for each resolution. The resolution which received the lowest support (91.5%) was in respect of the authority to disapply pre-emption rights of up to 10% of issued share capital. The negative voting reflected the stance being taken by certain shareholders at AGMs generally, pending clarity around the wording of this resolution, and specifically the part of the resolution for the use of 5% of issued share capital for acquisition purposes or a specified capital investment. I am pleased that our use of this resolution in 2016 was as intended – for our share placing in connection with the acquisition of the AXA Wealth businesses. At our May 2017 AGM, we will follow the new guidance from the Pre-Emption Group in respect of the authority to disapply pre-emption rights.
- Shareholders supported us at our EGM held on 24 October 2016 for approval of our acquisition of Abbey Life and the rights issue underpinning the acquisition, with a 99.9% vote in favour of both resolutions.
- Shareholders supported us by taking up 97.65% of the shares offered through the rights issue for the Abbey Life acquisition with the remaining 2.35% of shares being placed quickly at a modest discount.

BOARD OF DIRECTORS

Our Board of Directors comprises the Chairman, eight independent Non-Executive Directors and two Executive Directors. The Board considers that our optimum number of Directors is nine or ten and that number will occasionally be higher as the Board is gradually renewed.

The appointment of three new Non-Executive Directors (Wendy Mayall, John Pollock and Nicholas Shott) from 1 September 2016 was the culmination of a thorough search started at the beginning of 2016, intended to respond to our 2015 Board skills audit and address the skills being lost as Directors retire from the Board. In 2016 we lost the experience of Tom Cross Brown and Rene-Pierre Azria, both after long periods of excellent service to Phoenix. However, I was pleased to see our Board succession working so well with the enhancement to the Board dynamic provided by our three new Non-Executive Directors with their mix of experience bringing skills very relevant to our future needs as follows:

- Wendy Mayall – Asset management.
- John Pollock – Insurance, customer, FTSE 100 financial services board experience.
- Nicholas Shott – M&A, corporate finance.

Our gradual Board renewal will continue in 2017, with the retirements from the Board of Isabel Hudson and David Woods at our AGM in May 2017, both after over seven years on our Board. We are currently in the process of recruiting a further Non-Executive Director, which will bring the Board back to ten Directors.

I would like to thank Isabel and David for their outstanding service to the Board since their appointments in 2010.

We responded to the Board's desire, stated in our previous year's 2015 Board evaluation review, to spend more time on strategy, which supported the Board's focus in achieving the AXA and Abbey Life acquisitions in 2016. Our most recent Board Evaluation Review, undertaken towards the end of 2016, revealed a continued desire to keep strategy high up the agenda at each Board meeting, particularly given our growth ambitions. The review also stressed the Board's desire to provide strong oversight of the operations of our business, especially the importance of the integration of the acquired AXA and Abbey Life businesses, and to ensure that we continue to drive value as best as possible for our shareholders and customers. We are fortunate to have a strong Board for our regulated life and pensions subsidiaries, chaired by Mike Urmston and with a majority of Independent Non-Executive Directors who are not on the Board of our holding company, Phoenix Group Holdings. This extra level of independence is an important aspect of our governance.

UK CORPORATE GOVERNANCE CODE

As detailed in the Corporate Governance Report on pages 47 to 57, we complied in 2016 with all the provisions of the UK Corporate Governance Code ('the Code'), such that in the last five years we have had only one matter of non-compliance with the Code.

The following sections provide more detail on our Board of Directors, Executive Management team, operation of governance and remuneration practices as follows:

- Board and committee structure.
- Board of Directors.
- Executive Management Team.
- Corporate Governance Report.
- Directors' Remuneration Report.
- Directors' Report.

BOARD STRUCTURE

Phoenix Group Holdings Board and Committees

The main focus of the Phoenix Group Holdings Board is on Group strategy and performance, with input from Board committees. The chart below sets out the composition and main activities of the Phoenix Group Holdings Board and its committees. More detailed operational and customer-focused matters are addressed at the subsidiary board and committee level.

PHOENIX GROUP HOLDINGS BOARD

Henry Staunton (Chair)
Ian Cormack – SID
Clive Bannister*
James McConville*
Alastair Barbour
Isabel Hudson
Wendy Mayall
John Pollock
Nicholas Shott
Kory Sorenson
David Woods

AUDIT COMMITTEE

Alastair Barbour (Chair)
Isabel Hudson
Kory Sorenson
David Woods

REMUNERATION COMMITTEE

Ian Cormack (Chair)
Isabel Hudson
Nicholas Shott
Kory Sorenson

RISK COMMITTEE

David Woods (Chair)
Alastair Barbour
Wendy Mayall
John Pollock

NOMINATION COMMITTEE

Henry Staunton (Chair)
Ian Cormack
Alastair Barbour
David Woods

AUDIT COMMITTEE

- Financial Reporting
- Internal Controls
- External Audit
- Internal Audit

PHOENIX GROUP HOLDINGS BOARD

- Group Strategy
- Group Budget
- Group Risk Appetite
- Performance Monitoring
- External/Shareholder Reporting
- External Debt
- Major transactions

REMUNERATION COMMITTEE

- Group remuneration framework
- Executive Director remuneration
- Employee share schemes

RISK COMMITTEE

- Risk appetite and high-level risk matters
- The Group's Risk Management Framework

NOMINATION COMMITTEE

- Board appointments
- Senior executive appointments
- Board and senior executive succession planning

* Executive Directors

BOARD OF DIRECTORS

The Group is governed by our Board of Directors.
Biographical details of all Directors are shown below.

HENRY STAUNTON
CHAIRMAN

Committee membership
(Chairman)

Appointed to the Board
1 September 2015

Experience
Henry Staunton was appointed Chairman of the Board of Directors with effect from 1 September 2015. Mr Staunton is Non-Executive Chairman of WH Smith plc, the leading FTSE 250 retail group, and a Non-Executive Director of Capital & Counties Properties plc. He is also Non-Executive Chairman of the privately owned BrightHouse Group, the rent-to-own company. From 2004 until 2013, Mr Staunton was a Non-Executive Director, Chairman of the Audit Committee and latterly Senior Independent Director and Vice Chairman of Legal & General Group plc, where he gained significant insight into the life and pensions industry. From 2008 to 31 December 2014 he was a Non-Executive Director of Merchants Trust plc, where he was the Senior Independent Director. He was also a Non-Executive Director of Ashtead Group from 1997 to 2004 including as Chairman from 2001. During his executive career he was Finance Director of ITV plc from 2003 to 2006, and Finance Director of Granada plc from 1993 to 2003. Prior to that he joined Price Waterhouse as a graduate trainee, rising to become a Senior Partner of the audit practice.

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

Appointed to the Board
28 March 2011

Experience
Clive Bannister joined the Group in February 2011 as Group Chief Executive Officer. Prior to this, Mr Bannister was Group Managing Director of Insurance and Asset Management at HSBC Holdings plc. He joined HSBC in 1994 and held various leadership roles in planning and strategy in the Investment Bank (USA) and was Group General Manager and CEO of HSBC Group Private Banking. He started his career at First National Bank of Boston and prior to working at HSBC was a partner in Booz Allen Hamilton in the Financial Services Practice providing strategic support to financial institutions including leading insurance companies, banks and investment banks. Mr Bannister is also Chairman of the Museum of London.

JAMES MCCONVILLE
GROUP FINANCE DIRECTOR

Appointed to the Board
28 June 2012

Experience
Between April 2010 and December 2011, Mr McConville was Chief Finance Officer of Northern Rock plc. Prior to that, between 1988 and 2010, he worked for Lloyds Banking Group plc (formerly Lloyds TSB Group plc) in a number of senior finance and strategy related roles, latterly as Finance Director of Scottish Widows Group and Director of Finance for the Insurance and Investments Division. During 2011 and 2012, Mr McConville was a Non-Executive Director of the life businesses of Aegon UK. In 2014, Mr McConville joined the board of Tesco Personal Finance plc as Non-Executive Director. Mr McConville qualified as a Chartered Accountant whilst at Coopers and Lybrand.

ALASTAIR BARBOUR
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership
(Chairman – Audit Committee)

Appointed to the Board
1 October 2013

Experience
Alastair Barbour has over 30 years audit experience with KPMG where he worked across the full spectrum of financial services clients from large general insurers and reinsurers to the life insurance and investment management sector, working on a range of operational and strategic issues. Mr Barbour is the former Head of Financial Services, Scotland for KPMG. He retired from KPMG in 2011 to build a Non-Executive career. He is a Director and Audit Committee Chairman of RSA Insurance Group plc, Standard Life Private Equity Trust plc and Liontrust Asset Management plc (all London Stock Exchange listed companies). He is also a Director and Audit Committee Chairman of CATCo Reinsurance Opportunities Fund Ltd, a Bermuda-based investment company listed on the London Stock Exchange and of The Bank of N. T. Butterfield & Son Limited, a company listed in both Bermuda and New York.

IAN CORMACK
SENIOR INDEPENDENT DIRECTOR

Committee membership
(Chairman – Remuneration Committee)

Appointed to the Board
2 September 2009

Experience
Ian Cormack was appointed to the Board of Directors of the Company on 2 September 2009 and was appointed Senior Independent Director on 1 October 2013. Mr Cormack is Non-Executive Chairman of Maven Income & Growth VCT 4 plc and a Non-Executive Director of JRP Group plc and Hastings Group Holdings plc. Mr Cormack was Chief Executive Officer of AIG, Inc. in Europe from 2000 to 2002 and prior to that he spent 32 years at Citibank where he was Chairman of Citibank International plc and Co-Head of the Global Financial Institutions Client Group at Citigroup.

Nomination Committee
Risk Committee
Audit Committee
Remuneration Committee

ISABEL HUDSON
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership

Appointed to the Board
18 February 2010

Experience
Isabel Hudson is Chairman of the National House Building Council and a Non-Executive Director of BT Group plc and RSA Insurance Group plc. Ms Hudson is a former Non-Executive Director of MGM Advantage, The Pensions Regulator, QBE Insurance and Standard Life PLC. Other roles previously held by Ms Hudson include Chief Financial Officer at Eureko BV and Executive Director of Prudential Assurance Company. Ms Hudson is an ambassador to Scope, a UK charity, and has 35 years of experience in the insurance industry in the UK and mainland Europe.

WENDY MAYALL
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership

Appointed to the Board
1 September 2016

Experience
Wendy Mayall has over thirty years of asset management experience, including as Group Chief Investment Officer and later consultant at Liverpool Victoria from 2012 to 2015, having previously been Chief Investment Officer for Unilever's UK pension fund from 1996 to 2011 and holding management responsibility for Unilever's pension funds globally. From 2006 to 2009, Mrs Mayall was the Chair of the Investment Committee of the Mineworkers Pension Scheme, a British government appointment to one of the largest government backed pension schemes in the UK. Mrs Mayall is the non-executive Senior Independent Director of the Aberdeen UK Tracker Trust plc.

JOHN POLLOCK
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership

Appointed to the Board
1 September 2016

Experience
John Pollock had a career in life assurance at the Legal & General Group from 1980 to 2015, including as an Executive Director of Legal & General Group plc from 2003 to 2015. Mr Pollock held numerous senior roles, gaining wide strategic and technical experience, finally as Chief Executive Officer of LGAS (L&G Assurance Society), one of Legal and Generals' three primary business units. Prior to Mr Pollock's retirement from Legal and General in 2015, he held positions as Deputy Chair of the FCA Practitioner Panel, Chairman of investment platform Cofunds, and as a Non-Executive Director of the Cala Homes Group.

NICHOLAS SHOTT
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership

Appointed to the Board
1 September 2016

Experience
Nicholas Shott is an investment banker, who has been European Vice Chairman of Lazard since 2007 and Head of UK Investment Banking at Lazard since 2009. Mr Shott joined Lazard in 1991 and became a partner in 1997.

KORY SORENSON
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership

Appointed to the Board
1 July 2014

Experience
Kory Sorenson is currently a Non-Executive Director of SCOR SE and its US subsidiaries, Pernod Ricard SA, Uniqa Insurance Group AG and Aviva Insurance Limited. Ms Sorenson has over 20 years of experience in the financial services sector, most of which has been focused on insurance and banking. She was Managing Director, Head of Insurance Capital Markets of Barclays Capital from 2005 to 2010, and also held senior positions in the financial institutions divisions of Credit Suisse, Lehman Brothers and Morgan Stanley.

DAVID WOODS
INDEPENDENT NON-EXECUTIVE DIRECTOR

Committee membership
(Chairman – Risk Committee)

Appointed to the Board
18 February 2010

Experience
David Woods is a Fellow of the Institute of Actuaries, Non-Executive Chairman of Standard Life UK Smaller Companies Trust plc and a Non-Executive Director of Murray Income Trust plc. He is also Chairman of the pension fund trustee companies responsible for the governance of all the UK defined benefits/pension schemes in the Sopra Steria Group.

EXECUTIVE MANAGEMENT TEAM

Executive management of the Group is led by the Group Chief Executive Officer, Clive Bannister, who is supported by the Executive Committee ('ExCo').

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

Roles and responsibilities
- Leads the development of the Group's strategy for agreement by the Board
- Leads and directs the Group's businesses in delivery of the Group's strategy and business plan
- Leads the Group to safeguard returns for policyholders and grow shareholder value
- Embeds a risk-conscious Group culture which recognises policyholder obligations in terms of service and security
- Manages the Group's key external stakeholders.

JAMES MCCONVILLE
GROUP FINANCE DIRECTOR

Roles and responsibilities
- Develops and delivers the Group's financial business plan in line with strategy
- Ensures the Group's finances and capital are managed and controlled
- Develops and delivers the Group's debt capital strategy and other treasury matters
- Ensures the Group has effective processes in place to enable all reporting obligations to be met
- Supports the Group Chief Executive Officer in managing the Group's key external stakeholders
- Maximises shareholder value through clear, rigorous assessment of business opportunities.

FIONA CLUTTERBUCK
HEAD OF STRATEGY, CORPORATE DEVELOPMENT AND COMMUNICATIONS

Roles and responsibilities
- Supports the Group Chief Executive Officer in the formulation of the strategy and the business planning for the Group
- Leads implementation of the Group's strategy as regards any potential acquisitions or disposals
- Leads external Group Communications in liaison with the Group Finance Director and Head of Investor Relations.

STEPHEN JEFFORD
GROUP HUMAN RESOURCES DIRECTOR

Roles and responsibilities
- Leads the implementation of the Group's employee strategy in order to recruit, retain, motivate and develop high quality employees
- Provides guidance and support on all HR matters to the Group Chief Executive Officer, ExCo and the Group Board and Remuneration Committee
- Delivers HR services to the Group.

ANDY MOSS
CHIEF EXECUTIVE, PHOENIX LIFE

Roles and responsibilities
- Leads the development and delivery of the Phoenix Life business strategy, including the continued integration of life businesses
- Leads the Phoenix Life business to optimise outcomes for customers in terms of both value and security
- Ensures Phoenix Life deploys capital efficiently and effectively, with due regard to regulatory requirements, the risk universe and strategy.

WAYNE SNOW
GROUP CHIEF RISK OFFICER

Roles and responsibilities
- Leads the Group's risk management function, embracing changes in best practice and regulation including Solvency II
- Oversees and manages the Group's relationship with the FCA and PRA
- Supports the Group Board Risk Committee in the oversight of the Group's risk framework, in line with risk strategy and appetite.

SIMON TRUE
GROUP CHIEF ACTUARY

Roles and responsibilities
- Ensures capital is managed efficiently across the Group
- Manages the Group's solvency position
- Leads the development of the Group's investment strategy
- Identifies and delivers opportunities to enhance shareholder value across the Group.

QUENTIN ZENTNER
GENERAL COUNSEL

Roles and responsibilities
- Leads provision of legal advice to the Group Board, other Group company Boards, ExCo and senior management
- Oversees and co-ordinates maintenance of, and adherence to, appropriate corporate governance procedures across the Group
- Designs and implements a framework to manage legal risk within the Group, including compliance by Group companies and staff with relevant legal obligations.

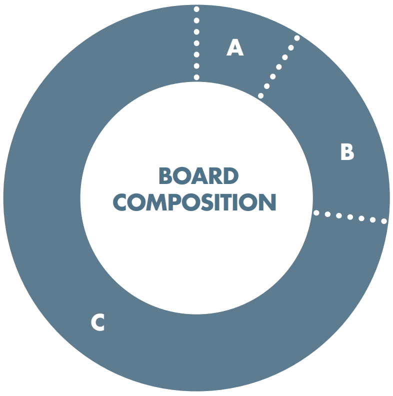
CORPORATE GOVERNANCE REPORT

INTRODUCTION

The Board is committed to high standards of corporate governance and the Group's Corporate Governance policy is aligned to compliance with the UK Corporate Governance Code ('the Code') which sets standards of good practice for UK listed companies. It is the Board's view that the Company has been fully compliant during 2016 with the provisions set down in the Code.

THE BOARD

The Board comprises the Non-Executive Chairman, the Group Chief Executive Officer, the Group Finance Director and eight independent Non-Executive Directors. Biographical details of all Directors are provided on pages 44 to 45.



A	Chairman	9%
B	Executive Directors	18%
C	Independent Non-Executive Directors	73%

The Board considers that the following Directors are independent: Alastair Barbour, Ian Cormack, Isabel Hudson, Wendy Mayall, John Pollock, Nicholas Shott, Kory Sorenson and David Woods. The Board has considered the criteria proposed by the Code in assessing the independence of the Directors.

BOARD SUCCESSION PLANNING AND CHANGES

The Board skillset must be aligned to the Group strategy of enhancing value for shareholders and policyholders and taking forward the Group's M&A agenda.

The Board responded to the skills audit undertaken in 2015 by recruiting three new Non-Executive Directors (Wendy Mayall, John Pollock and Nicholas Shott, all appointed from 1 September 2016) to replace skills and experience being lost during 2016 and 2017 on account of expected Board departures as follows: Tom Cross Brown (May 2016 AGM), Rene-Pierre Azria (November 2016), David Woods (May 2017 AGM).

The 2016 recruitment provided a strong mix of experience and skills (as outlined in the Chairman's Corporate Governance introduction on page 42) and demonstrated the effectiveness of the succession planning.

The Nomination Committee and Board are now undertaking a skills audit at two-year intervals. The latest skills audit was undertaken in February 2017 and is being utilised in respect of expected 2017 and 2018 Board changes (including Isabel Hudson who is also retiring from the Board at the May 2017 AGM).

BOARD EFFECTIVENESS

In accordance with the Code, an evaluation of the performance of the Board and that of its committees and individual Directors was undertaken in the latter part of 2016. The process was led by the Chairman and internally facilitated by the Company Secretary. The process involved completion by Directors of a questionnaire covering various aspects of Board, Committee and Director effectiveness followed by individual meetings between the Chairman and each Director, concluding in a Board report which was discussed by the Board in November 2016.

A strong theme from the previous year's 2015 Board Evaluation Review had been the desire to spend more time on strategy. This was actioned with strategy at the forefront of each Board meeting agenda and contributed to the successful Board focus on acquisitions in 2016. The Chairman has reported on the main outputs of the November 2016 Board Evaluation Review in his Corporate Governance introduction on page 42, in particular the Board's wish for continued focus on strategy and also the integration of the businesses acquired in 2016. The Board, whilst commenting favourably on the quality of Board papers, also provided helpful suggestions to improve the clarity and focus of the papers, which have been actioned.

The output from the November 2016 Board and individual Director reviews informed the review of the Board composition and succession planning undertaken by the Board Nomination Committee in February 2017, leading to the Board's recommendations to shareholders regarding re-election of Directors at the 2017 Annual General Meeting ('AGM').

All Directors receive a tailored induction on joining the Board in accordance with a process approved by the Board. The new Non-Executive Directors, Wendy Mayall, John Pollock and Nicholas Shott, undertook a comprehensive induction, including detailed strategic and operational briefings and information, before and following their appointments in September 2016.

To ensure that the Directors maintain up-to-date skills and knowledge of the Company, all Directors receive regular presentations on different aspects of the Company's business and on financial, legal and regulatory issues.

THE CHAIRMAN, GROUP CHIEF EXECUTIVE OFFICER AND SENIOR INDEPENDENT DIRECTOR

Henry Staunton is Chairman of the Board of Directors of the Company, having joined the Board as Chairman on 1 September 2015. There is a division of responsibility, approved by the Board, between the Chairman, who is responsible for the leadership and effective operation of the Board and the Group Chief Executive Officer, Clive Bannister, who is responsible to the Board for the overall management and operation of the Group. The Chairman's other commitments are set out in his biographical details on page 44. The Chairman was appointed on the basis of committing two days per week to Phoenix.

The Senior Independent Director, appointed by the Board, is Ian Cormack. His role is to be available to shareholders whose concerns are not resolved through the normal channels or when such channels are inappropriate. He is also responsible for leading the annual appraisal of the Chairman's performance by the Non-Executive Directors, which occurred in November 2016.

CORPORATE GOVERNANCE REPORT
Continued

OPERATION OF THE BOARD

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

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

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

The terms of appointment for the Directors state that they are expected to attend in person regular (at least six per year) and additional Board meetings of the Company and to devote appropriate preparation time ahead of each meeting. In February 2017, the Nomination Committee reviewed the time spent by Directors and concluded that the time required of (and given by) the Company's Directors is considered at least at the level expected in their appointment terms and is believed to be high in comparison with other FTSE 250 companies.

The remuneration of the Directors is shown in the Directors' Remuneration Report on pages 58 to 84. The terms and conditions of appointment of Non-Executive Directors are on the Group's website. In accordance with the provisions of the Articles and the Code, all Directors (except Isabel Hudson and David Woods, who are standing down from the Board) will submit themselves for election or re-election at the Company's AGM on 11 May 2017.

Alastair Barbour, on account of being on the boards of a number of public companies listed in the UK and/or Bermuda and the USA and chairing the audit committee for all, has provided an analysis of his work commitments to the Nomination Committee, which shows the relatively low level of time commitment required for certain of his other roles and the complementary nature of his roles and the time committed to Phoenix (40 days in 2016, his equal largest commitment). The Nomination Committee and Board confirmed their absolute satisfaction with the time and overall commitment given to Phoenix by Mr Barbour and all other Directors.

Wendy Mayall, John Pollock and Nicholas Shott were appointed to the Board from 1 September 2016 with pre-existing commitments which affected their Board attendance during their first few months on the Board. All attended the final Board meeting in 2016 (30 November) and it is their intention to attend all Board meetings going forward.

The Board met eight times during 2016 and is scheduled to meet seven times in 2017 including for a two-day strategy-setting meeting. Additional meetings will be held as required, and the Non-Executive Directors will hold meetings with the Chairman, without the Executive Directors being present, as they did on several occasions in 2016.

KEY FOCUS AREAS AT BOARD MEETINGS IN 2016

Subject	% of time spent (approximate)
CEO Report	25
Strategy and Planning including consideration of corporate transactions	25
CFO/Management Information Report	20
Financial Reporting	15
Reports from Chairs of Board committees and subsidiary Boards	5
Board and Board committee changes and issues	5
Other Matters	5

BOARD ATTENDANCE 2016

	Board meetings	
	Maximum	Actual
Chairman		
Henry Staunton	8	7
Executive Directors		
Clive Bannister (Group CEO)	8	8
James McConville (Group FD)	8	8
Non-Executive Directors		
René-Pierre Azria[3]	8	8
Alastair Barbour	8	8
Ian Cormack	8	7
Tom Cross Brown[1]	3	3
Isabel Hudson	8	7
Wendy Mayall[2]	3	2
John Pollock[2]	3	2
Nicholas Shott[2]	3	1
Kory Sorenson	8	8
David Woods	8	6

1 Tom Cross Brown resigned from the Board on 11 May 2016.

2 Wendy Mayall, John Pollock and Nicholas Shott were appointed to the Board on 1 September 2016.

3 Rene-Pierre Azria resigned from the Board on 30 November 2016.

BOARD COMMITTEES

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

EXPECTED MAJOR FOCUS ITEMS IN 2017

Committee	Items
Audit Committee	Oversight of embedding of controls across the enlarged Group following 2016 acquisitions
Nomination Committee	Executive and Non-Executive Director Succession Planning
Remuneration Committee	New Remuneration Policy for May 2017 AGM and continued focus on aligning remuneration with strategic performance
Risk Committee	Forward-looking risk planning

CORPORATE GOVERNANCE REPORT
Continued

Audit Committee

ALASTAIR BARBOUR
Audit Committee Chairman

"Our focus in 2017 will be ensuring the control environment remains strong across our enlarged Group following our recent acquisitions. This will be supported by strengthening the links between the Group and Phoenix Life Audit Committees."

OTHER MEMBERS
Isabel Hudson
Kory Sorenson
David Woods

	Audit Committee	
MEETING ATTENDANCE 2016	Maximum	Actual
Chairman		
Alastair Barbour	7	7
Other members		
Isabel Hudson	7	7
Kory Sorenson	7	6
David Woods	7	6

The composition of the Audit Committee is in accordance with the requirements of the Code that the Audit Committee should consist of at least three independent Non-Executive Directors of whom at least one has recent and relevant financial experience. Both Alastair Barbour and Kory Sorenson have that experience. The Audit Committee met seven times during 2016. Its meetings are attended by the Chairman of the Risk Committee (who is also a member of the Audit Committee), the Group Finance Director, the Deputy Group Finance Director, the Group Head of Internal Audit, the external auditors and usually also by the Group Chairman and the Group Chief Executive Officer. The Audit Committee holds private meetings at least annually with each of the Group Finance Director, the Group Head of Internal Audit and the external auditors.

AUDIT COMMITTEE'S ROLE

- Receiving and reviewing the Annual Report and Accounts and other related financial disclosures, although the ultimate responsibility for these matters remains with the Board.
- Monitoring the overall integrity of the financial reporting by the Company and its subsidiaries and the effectiveness of the Group's internal controls.
- Provision of advice to the Board to enable the Board to report on whether the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group's performance, business model and strategy.
- Responsible for making recommendations to the Board on the appointment of the external auditors and their terms of engagement including approval of external auditor fees and non-audit services and for reviewing the performance, objectivity and independence of the external auditors. The terms of reference of the Audit Committee state that it shall meet the external auditor at least once a year without management being present.
- Considering and approving the remit of the internal audit function and reviewing its effectiveness.
- Oversight of activities of subsidiary audit committees through receipt and review of minutes, discussions between the Chairmen of the Audit Committee and subsidiary audit committees, and the Audit Committee Chairman's attendance at the Phoenix Life Audit Committee on an occasional basis, as well as his receipt of all papers going to the Phoenix Life Audit Committee. This was enhanced in 2016 through the commencement of occasional attendance at the Audit Committee by the Phoenix Life Audit Committee Chairman.

AUDIT COMMITTEE'S PRINCIPAL ACTIVITIES DURING 2016

EXTERNAL REPORTING AND CONTROLS

- Reviewed the Company's 2015 Annual Report and Accounts and 2016 Interim Financial Statements, recommending their approval to the Board, as well as related disclosures and the financial reporting process, supported by reports from management and the external auditors.
- Considered and addressed a number of significant matters in relation to the IFRS consolidated financial statements for 2015 (annual), 2016 (interim) and 2016 (annual) as summarised in the table on page 53. These matters were considered by the Audit Committee to be areas subject to the most significant levels of judgement or estimation, and identified with regard to the significant risks assessed by the Group's external auditors as set out in their audit opinion on page 91.
- Reviewed the financial forecasts prepared by management, supported by the sensitivity analysis on the key assumptions underpinning the forecasts, in support of the assumption that the Group will continue as a going concern, the Group's ongoing viability and in support of dividend payments.
- Reviewed the Line 1 risk and controls report from management, the annual internal controls effectiveness report (and the half-year update) prior to its consideration by the Board and received reports regarding consequential actions; and received a dedicated briefing, in conjunction with the Phoenix Life Audit Committee on cyber risk and controls.
- Reviewed reports from Internal Audit on the control environment in the Group's outsource service providers and on the effectiveness of the internal audit work undertaken within the outsource service providers, noting that this was addressed in more detail at the Phoenix Life Audit Committee., whose Chairman reported further on this matter through attendance at the Audit Committee.
- Considered and noted the independence of KPMG in relation to post-acquisition audit work undertaken with regard to Abbey Life.

EXTERNAL AUDIT

- Undertook an audit tender which included a review of the effectiveness, engagement and remuneration of the current external auditors. This culminated in a recommendation to re-appoint EY, which was approved by the Board and will be recommended to shareholders at the May 2017 AGM – see 'Assessment of the effectiveness of the external audit process' and 'Auditor's Appointment' on page 52.
- Reviewed and monitored the independence of the external auditors including their provision of non-audit services and fees– see Auditor's Independence and External Auditor Policy on page 52.

INTERNAL AUDIT

- Reviewed an update from Internal Audit on the recommendations from the 2015 External Quality Assessment by Independent Audit and requested, in consequence of one of the recommendations, that the 2017 Internal Audit plan provides details of the use of data analytics.
- Assessed the effectiveness of Internal Audit, supported by the April 2016 follow-up review by Independent Audit to their 2015 External Quality Assessment, noting the positive actions taken in response to the recommendations from the 2015 assessment.
- Approved the Group Internal Audit Proposition for 2017 and a more dynamic planning approach of six months fixed and six months flexible; and a continuation of the move from a static policy approach to a plan more focused on thematic audits based on emerging risks and topical matters.
- Approved the annual update of the Group Internal Audit Charter (which was aligned to the CIIA Code for 'Effective Internal Audit in Financial Services') and the Group Internal Audit Plan (including its link to the Risk Management Framework), receiving regular reports to monitor progress against the plan.
- Reviewed the internal audit control environment opinion which included Internal Audit's view on the embedding of the risk management framework across the Group.

AUDIT COMMITTEE'S PERFORMANCE

- The Committee's performance was reviewed by the Board in November 2016 as part of its overall Board Evaluation Review. The Board concluded that the Committee undertakes a difficult role very well and that the reporting from the Committee Chairman to the Board is good. The Committee undertook a self-effectiveness review in early 2017, concluding that it contained an appropriate balance of skills and that the interaction with the Phoenix Life Audit Committee should continue to be enhanced.

GENERAL

- Reviewed arrangements for whistleblowing (and whistleblowing activity) should an employee wish to raise concerns, in confidence, about any possible improprieties; and approved an updated whistleblowing policy which complied with the FCA and PRA's new whistleblowing rules and the introduction of a prescribed responsibility of a Whistleblowing Champion under the Senior Insurance Managers Regime. The Audit Committee Chairman was appointed to this role.
- Reviewed and approved updates to the Group Tax Policy and the Group Liquidity & Funding Policy.

CORPORATE GOVERNANCE REPORT
Continued

ASSESSMENT OF THE EFFECTIVENESS OF THE EXTERNAL AUDIT PROCESS

The effectiveness of the external audit process was assessed through the completion of a questionnaire by the key divisions and Group functions within Phoenix Group covering EY's performance during the 2015 financial reporting cycle to provide a more detailed analysis and to support the imminent tender process. The review was supported by the utilisation of an online questionnaire based tool provided by a third party supplier. The output from the review demonstrated the positive action taken in respect of recommendations from the previous year's review and enabled management to identify key areas of focus to further facilitate the audit process. The Audit Committee contributed feedback to the exercise, considered the effectiveness of the process and reviewed the overall findings.

During 2016, the Financial Reporting Council undertook an Audit Quality Review of EY's audit of the PGH financial statements for the year ended 31 December 2015 and reported to the Chair of the Audit Committee. None of their findings were considered to be of sufficient significance for inclusion in the report.

AUDITOR'S APPOINTMENT

The current auditors, EY, were appointed in September 2009. However, EY have been auditors to significant parts of the Group for a longer period. In accordance with the requirements of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014, the Audit Committee undertook a competitive audit tender in 2016 to take effect for the 2017 statutory audit, which it considered to be in the best interests of its shareholders in light of the length of association with the current auditors.

The tender process was overseen by the Audit Committee and undertaken in accordance with internal procurement policies and external regulations. In accordance with the requirements of the regulations, a report on the process was undertaken and the rationale supporting the decision reached was prepared to enable the Audit Committee to validate the appropriateness of the selection procedure undertaken and reach their final conclusions. The report confirmed that there was evidence that the Audit Committee had fulfilled its responsibilities in connection with the competitive tender process as set out in the regulations and that the selection process was transparent, free from influence and was conducted in a fair manner. The Audit Committee concluded, and recommended to the Board, that the incumbent audit firm, EY, should be retained as the external auditor of the Group from 2017.

The current audit partner is Ed Jervis, who has held that role from the 2014 statutory audit and will rotate off that role after the 2018 statutory audit.

AUDITOR'S INDEPENDENCE AND EXTERNAL AUDITOR POLICY

The Company has an external auditor policy which requires the Company and the external auditors to take measures to safeguard the objectivity and independence of the external auditors. These measures include a prohibition regarding non-audit services in respect of specific areas, such as secondments to management positions, or those which could create a conflict or perceived conflict. It also includes details of the procedures for the rotation of the external engagement partner. The Charter can be found on the Group's website. The policy was updated in 2016 to reflect changes brought about by the EU Audit Directive and Regulations; in particular that non-audit fees will going forward now be capped at 70% of the average audit fee over the three preceding financial years. In 2016, total fees of £8.7 million were paid to EY. Of this amount, £4.2 million related to statutory audit fees of the parent and its subsidiaries, with a further £0.8 million incurred in relation to services provided pursuant to legal or regulatory requirements. The remaining fees of £3.7 million are classified as non-audit services as defined by the new EU Audit Directive and Regulations, and give rise to a ratio of 87 % of non-audit to audit fees in 2016.

The engagement of EY to perform any non-audit service is subject to a process of pre-approval by the Audit Committee. £1.9 million of the non-audit fees related to actuarial and finance due diligence procedures conducted in relation to the acquisitions of the AXA businesses and Abbey Life. The Audit Committee considers that the engagement of the external auditors in the performance of such diligence procedures should provide synergies with audit work post-completion of the transaction and enhanced insight as to the quality of the control environment operated in the target company by comparison to Group standards. Of the remaining balance and consistent with market practice, a further £1.7 million relates to the provision of assurance services to the Board and the sponsoring banks in support of disclosures made in the public transaction documentation relating to the two acquisitions.

The Audit Committee is satisfied that the non-audit services performed during 2016 have not impaired the independence of EY in its role as external auditor. Further information on non-audit fees is provided in Auditor's Remuneration in Notes to the IFRS Consolidated Financial Statements on page 117.

SIGNIFICANT MATTERS CONSIDERED BY THE AUDIT COMMITTEE IN RELATION TO THE FINANCIAL STATEMENTS

Significant matters in relation to the 2016 IFRS financial statements	How these issues were addressed
Review of the actuarial valuation process, to include the setting of actuarial assumptions and methodologies, and the robustness of actuarial data	— Management presented papers to the Phoenix Life Audit Committee detailing recommendations for the actuarial assumptions and methodologies to be used for the interim and year-end reporting periods with justification and benchmarking as appropriate. These assumptions and methodologies were debated and challenged by the Phoenix Life Audit Committee, focusing on longevity and persistency in relation to demographics and on credit in relation to economics, prior to their approval. Papers were also presented outlining changes to assumptions proposed to align the IFRS basis of reserving more closely with the requirements of Solvency II. — A summary of these papers was presented for oversight review by the Audit Committee, and the Phoenix Life Audit Committee's conclusions were reported to the Audit Committee through minutes of its meeting and a discussion between the Chairmen of the two committees. The Audit Committee discussed, and questioned management and EY on, the content of the summary papers and the Phoenix Life Audit Committee's conclusions. — The Audit Committee received and considered detailed written and verbal reporting from the external auditors setting out their observations and conclusions in respect of the assumptions, methodologies and actuarial models. Pension assumptions for use in the IAS 19 Employee Benefits valuations were reviewed and approved by the Audit Committee prior to the finalisation of the valuation reports.
Valuation of complex and illiquid financial assets	— Management presented papers setting out the basis of valuation of financial assets, including changes in methodology and assumptions, for the interim and year-end reporting periods to the Phoenix Life Audit Committee. The assumptions, valuations and processes, particularly for financial assets determined by valuation techniques using significant non-observable inputs (Level 3), were debated and challenged by the Phoenix Life Audit Committee prior to being approved. — The valuation information was then presented for oversight review by the Audit Committee who considered and confirmed the appropriateness of the basis of valuation.
Acquisition Accounting	— The Audit Committee has considered the impact of the acquisitions of the AXA businesses and Abbey Life on the Group consolidated IFRS financial statements. This has included consideration of the adoption of Group accounting policies and methodologies by the acquired businesses. — Management presented papers detailing the basis of fair value adjustments made to the acquisition balance sheets including the recognition of intangible assets. The key assumptions and methodologies applied in determining such adjustments were reviewed and approved by the Audit Committees.
Operating Profit	— The Audit Committee reviewed the allocation of key items to operating profit to ensure the allocations were in line with the Group's operating profit framework and consistent with previous practice.
Assessment of whether the Annual Report and Accounts are fair, balanced and understandable	— The Audit Committee considered an analysis of the processes and conclusions in support of management's conclusions that the Annual Report and Accounts are fair, balanced and understandable. In particular, the Audit Committee sought assurance as to the review processes that operated over the production of the Annual Report and Accounts.
Going concern analysis	— A comprehensive going concern assessment was undertaken by the Audit Committee for the 2016 year-end and 2016 interim reporting periods, based on an assessment by management of the Group's liquidity for the going concern review period together with forecasts and a stress and sensitivity analysis. The analysis also confirmed that all regulatory and working capital requirements would be met under the base case and adverse stress scenarios throughout the going concern review period.
Viability Statement	— The Audit Committee reviewed the process to support, and the contents of, the Viability Statement. The Committee concluded that the period covered by the Viability Statement should continue to be five years to align it to the Group's strategic plan.

Please note that references in this table to the Phoenix Life Audit Committee include Audit Committees for the acquired AXA Wealth and Abbey Life businesses in respect of post-acquisition activity.

CORPORATE GOVERNANCE REPORT
Continued

Remuneration Committee

IAN CORMACK
Remuneration Committee Chairman

"The Remuneration Committee continues to be focused on alignment of reward to execution of strategy as will be reflected in our Remuneration Policy being presented to shareholders for approval at our May 2017 AGM."

OTHER MEMBERS
Isabel Hudson
Nicholas Shott
Kory Sorenson

	Remuneration Committee	
MEETING ATTENDANCE 2016	Maximum	Actual
Chairman		
Ian Cormack	6	6
Other members		
Isabel Hudson	6	6
Nicholas Shott[1]	1	1
Kory Sorenson	6	5

1 Appointed to the Committee on 20 October 2016.

The composition of the Remuneration Committee accords with the requirements of the Code that the Remuneration Committee should consist of at least three independent Non-Executive Directors. The Remuneration Committee met six times during 2016.

The Remuneration Committee is responsible for making recommendations to the Board on the Company's remuneration and compensation plans, policies and practices and for determining, within agreed terms of reference, specific remuneration packages for the Executive Directors. These include pension rights and executive incentive schemes to encourage superior performance. In 2016, the Committee approved a Remuneration Policy Statement in accordance with the PRA's Solvency II Remuneration Guidance. Details of the remuneration structure and the Remuneration Committee's activities in 2016 are provided in the Directors' Remuneration Report on pages 58 to 84.

FIT Remuneration Consultants provided advice to the Remuneration Committee in 2016 and are independent of the Group.

Risk Committee

DAVID WOODS
Risk Committee Chairman

"I am confident that on stepping down from the Board and as Risk Committee Chairman (at our May 2017 AGM), the risk management framework and governance is on a sound and robust footing."

OTHER MEMBERS
Alastair Barbour
Wendy Mayall
John Pollock

	Risk Committee	
MEETING ATTENDANCE 2016	Maximum	Actual
Chairman		
David Woods	6	5
Other members		
René-Pierre Azria[1]	6	6
Alastair Barbour	6	6
Tom Cross Brown[2]	3	3
Wendy Mayall[3]	1	1
John Pollock[3]	1	1

1 Member of Committee up to 30 Nov 2016.
2 Member of Committee up to 11 May 2016.
3 Appointed to the Committee on 20 October 2016.

The establishment of a Risk Committee is not a requirement of the Code. However, the Board believes such a Committee is important to ensure the robust oversight of the management of risk within the Group. The composition of the Risk Committee, comprised totally of independent Non-Executive Directors, is in accordance with the final recommendations of the report by Sir David Walker titled 'A review of corporate governance in UK banks and other financial industry entities'. The Risk Committee met six times in 2016. Its meetings are attended by the Chairman of the Audit Committee (who is also a member of the Risk Committee), the Chief Risk Officer, the Group Head of Internal Audit and occasionally also by the Group Chairman and the Group Chief Executive Officer.

The Risk Committee advises the Board on risk appetite and tolerance in setting the future strategy, taking account of the Board's overall degree of risk aversion, the current financial situation of the Group and the Group's capacity to manage and control risks within the agreed strategy. It advises the Board on all high-level risk matters. Details of the Risk Management Framework, for which the Risk Committee has oversight, are provided in the Risk Management section on pages 34 to 39.

RISK COMMITTEE'S PRINCIPAL ACTIVITIES DURING 2016

- Reviewed the Group's risk appetite and recommended to the Board the Group's overall risk management strategy.
- Monitored progress against the 2016 Group Risk Function plan.
- Considered any breaches of the Group's risk appetite.
- Monitored compliance with the Group's principal risk policies, satisfying itself that action plans to address significant breaches of those policies were sufficient.
- Reviewed the Group's risk profile, monitoring it against the risk categories of Market, Insurance, Credit, Financial Soundness, Customer and Operational with particular attention to risk appetite, risk trends, risk concentrations, provisions, experience against budget and key performance indicators for risk.
- Provided oversight of, and challenge to, the design and execution of the Group's stress and scenario testing, including any changes of assumptions.
- Undertook horizon scanning to consider emerging risks that could impact the Group including more prominent badging of forward-looking work in risk papers.
- Considered risks, issues and matters that are escalated from the Phoenix Life Risk Committee.
- Informed the Remuneration Committee regarding the management of the Group's material risks to support their consideration of executive's Annual Incentive Plan rewards.
- Provided oversight and due diligence on risk issues relating to material transactions and strategic proposals.

CORPORATE GOVERNANCE REPORT
Continued

Nomination Committee

HENRY STAUNTON
Nomination Committee Chairman

"I am very pleased with the Nomination Committee's role in our three new Non-Executive Director appointments from 1 September 2016 and the effective renewal of skills on our Board."

OTHER MEMBERS
Alastair Barbour
Ian Cormack
David Woods

MEETING ATTENDANCE 2016	Nomination Committee Maximum	Nomination Committee Actual
Chairman		
Henry Staunton	6	6
Other members		
Alastair Barbour[2]	3	3
Tom Cross Brown[1]	3	3
Ian Cormack	6	6
David Woods[2]	3	3

1 Member of Committee to 11 May 2016.
2 Appointed to the Committee on 11 May 2016.

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

The Nomination Committee met six times in 2016.

The standard process used by the Committee for Board appointments involves the use of an external search consultancy to source candidates external to the Group (and in the case of executive appointments also considers internal candidates). Detailed assessments of short-listed candidates are undertaken by the search consultancy, followed by interviews with Committee members and other Directors and the sourcing of references before the Committee recommends the appointments to the Board. This process was used for the appointment of Wendy Mayall, John Pollock and Nicholas Shott in 2016. The search consultancy used in 2016 for Director appointments was Korn Ferry which has no other connection with the Company.

NOMINATION COMMITTEE'S PRINCIPAL ACTIVITIES DURING 2016

- Delivered a recommendation to the Board for the appointments of Wendy Mayall, John Pollock and Nicholas Shott as Non-Executive Directors following a comprehensive search process led by the Nomination Committee with Korn Ferry search consultancy.
- Taking account of the Board Evaluation Review, reviewed the balance of skills, diversity, experience, independence and knowledge on the Board.
- Taking account of the Board Evaluation Review, reviewed the structure, size and composition of the Board.
- Reviewed the time spent by Directors in fulfilling their duties, concluding that the time spent appeared to be high in comparison with other FTSE 250 companies.
- Reviewed the succession plan for Executive and Non-Executive Directors and recommended its approval to the Board.

The Board's policy on diversity is as follows:

- The Board supports the enhancement of diversity, including gender, as a consideration when recruiting new Directors.
- The Board's overriding aim is to appoint the right Directors to the Board to drive forward the Group's strategy within a robustly compliant framework.
- The Board will undertake regular skills audits to ensure the Board's skills remain appropriate for its strategy and providing diversity where possible.

COMMUNICATION WITH SHAREHOLDERS

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

The Company's Investor Relations department is dedicated to facilitating communication with investors and analysts and an active investor relations programme is maintained.

During 2016, the Company's Investor Relations department and management held the following activity:

- 31 days of roadshows meeting investors.
- 5 institutional conferences holding one-on-one or group meetings with investors.
- 219 face-to-face meetings with investors and analysts.

The Company also held an Investor Day on 12 May 2016, which was attended by investors and research analysts.

In 2016, there was a marked increase in roadshow activity due to the AXA and Abbey Life acquisitions which involved an equity placing and rights issue respectively.

At these meetings a wide range of relevant issues including strategy, performance, management and governance were discussed. The Chairman, Senior Independent Director and Executive Directors are available to meet investors and analysts when required. Should major shareholders wish to meet newly appointed Directors, or any of the Directors generally, they are welcome to do so.

In addition, continued engagement is undertaken with shareholders and proxy advisers on evolving governance issues.

The Directors consider it important to understand the views of the market. Board members regularly receive copies of the latest analyst reports on the Company and the insurance sector, as well as market feedback to further develop their knowledge and understanding of external views about the Company. The Chairman and the Non-Executive Directors provide feedback to the Board on topics raised with them by major shareholders. The Company also undertakes perception studies, when appropriate, designed to determine the investment community's view of the core business from both institutional fund managers and sell-side analysts.

The Company's AGM provides another opportunity to communicate with its shareholders. At the 2016 meeting, the Company complied with the Code provisions relating to voting and the separation of resolutions. Shareholders were invited to ask questions during the meeting. It is intended that the same processes will be followed at the 2017 AGM. In line with the Code, details of proxy voting by shareholders will be made available at the meeting and will be posted on the Company's website following the meeting.

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

FINANCIAL REPORTING AND GOING CONCERN

The Directors have acknowledged their responsibilities in the Statement of Directors' Responsibilities in relation to the IFRS consolidated and parent company financial statements for the year ended 31 December 2016.

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 2 to 40.

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

The Board's going concern assessment is included within the Directors' Report on page 87.

VIABILITY STATEMENT

The Viability Statement, as required by section C.2.2 of the Code, has been undertaken for a period of five years to align to the Group's business planning and is contained in the Risk Management section on page 39.

REVIEW OF SYSTEM OF INTERNAL CONTROLS

The Code requires Directors to review the effectiveness of the Company's risk management and internal control systems which includes financial, operational and compliance controls. The Board has overall responsibility for the Group's risk management and internal control systems and for reviewing their effectiveness. The Group's systems of internal controls are designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss. The Board's review of the period covered by this report, which was undertaken with the assistance of the Audit and Risk Committees, was completed on 17 March 2017. Where any significant weaknesses were identified, corrective actions have been taken, or are being taken and monitored.

The Board (and its subsidiary company boards) monitor internal controls on a continual basis, in particular through Audit and Risk Committees. There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group, which has been in place throughout the period covered by this report and up to the date of approval of the Annual Report and Accounts for 2016, in accordance with the 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting' published by the Financial Reporting Council.

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

DIRECTORS' REMUNERATION REPORT

"OUR APPROACH TO REWARD ADOPTS A PRUDENT VIEW ON EXECUTIVE PAY BALANCED WITH APPROPRIATE ALIGNMENT TO A STRATEGY WELL DELIVERED BY THE GROUP IN A COMPLEX YEAR."

IAN CORMACK
REMUNERATION COMMITTEE CHAIRMAN

DEAR SHAREHOLDER

On behalf of the Board, I am pleased to present our Directors' Remuneration Report for the year ended 31 December 2016. This report covers remuneration for Executive Directors and Non-Executive Directors of the Company.

COMPANY PERFORMANCE

2016 was a year of accomplishment for Phoenix Group as set out in more detail in the Group Chief Executive Officer's report at the beginning of this Annual Report and Accounts. Particular operational and financial highlights for the year included:

- Completion of the acquisition of AXA Wealth's pensions and protection businesses financed in part by a £194 million capital raise
- Completion of the acquisition of Abbey Life, financed in part by a £735 million rights issue
- Operating companies' cash generation of £486 million
- Agreement with the Group's lending banks on a new Revolving Credit Facility of £900 million
- Development of the Phoenix Life website in order to digitise parts of the customer journey
- Improved Financial Ombudsman Service overturn rate to 18%
- Strong customer satisfaction scores of over 90%
- The accreditation, for the fifth successive year, that Phoenix has been formally recognised as one of the 'UK's Top Employers'

The above highlights have been achieved whilst also meeting the challenges of the introduction of the new Solvency II regime at the start of 2016. In addition, the volatile macroeconomic environment experienced over the course of the year, including the sharp fall in long-term interest rates, has had a negative impact on the Group's financial position.

These factors represent an effective performance by the Company and its management team and, accordingly, the Remuneration Committee ('Committee') concluded that the out-turn of the Annual Incentive Plan ('AIP') and Long-Term Incentive Plan ('LTIP') (after increasing the targets to reflect the impact of the AXA acquisition) is appropriate, as more fully described below.

REMUNERATION POLICY FOR 2017

As I explained in my letter introducing our Directors' Remuneration Report for 2015, during the course of 2016 the Committee has undertaken a review of our current Directors' Remuneration Policy in anticipation of updating the policy at the 2017 Annual General Meeting ('AGM'). Whilst the Company is a non-UK incorporated Company, and so is not technically subject to the UK's Directors' Remuneration Report regime we have always complied with this regime voluntarily, including establishing a 3-year Directors' Remuneration Policy which we first had approved by our shareholders in 2014. As this 3-year authority is now expiring we intend to seek our shareholders' authority for a new Directors' Remuneration Policy at our 2017 AGM.

In considering any changes to the policy the Committee was mindful of the wider external environment. In particular, it noted the findings of the Executive Remuneration Working Group which endorsed replacing traditional LTIPs with smaller awards of more certain restricted stock. This could have particular attractions for the Company given the additional challenges we face in setting robust targets for a business which has as its strategy the enhancement of shareholder value and dividend income through suitable acquisitions. The proposed new policy is largely a carry-forward of the current policy with the Committee planning to undertake a fuller review during 2017.

The policy to be proposed at the 2017 AGM, therefore, contains a high degree of consistency with the Company's previous policy:

- No increases to the potential quantum of Executive Directors' remuneration are proposed.
- Within the policy, each element of remuneration contains an appropriate cap. These are in place in order to comply with regulations and do not reflect aspirations or targets. None of these caps have been increased from the previous policy. Specifically within the policy section for base salary we have clarified the target positioning of Executive Directors' base salaries as between the FTSE31-100 and FTSE250 data sets.

- Within the AIP we have retained the current maximum opportunity of 150% of base salary per annum. We have increased the element of compulsory deferral into shares to 40% (from 33%), with the deferral period remaining at three years and subject to continued employment.
- The precise metrics for the AIP will be set each year in line with strategic priorities. For 2017, we have removed the profit–based measures in favour of increasing the weighting on both cash generation (the core financial metric for the Company) and the customer experience. The simplified AIP scorecard will thus comprise a 50% weighting on cash generation, 20% on customer outcomes, and 30% on strategic/personal objectives. As now, the AIP policy includes an appropriate power for the Committee to take a holistic view of performance and, as appropriate, moderate outcomes.
- For the LTIP, we have retained the current policy of 200% of base salary annual grant levels. The performance measures for the 2017 LTIP will again be relative TSR and cash generation with an equal weighting on both. The LTIP also includes a 2-year post-vesting holding period for Executive Directors.
- Share Ownership Guidelines for Executive Directors remain at a minimum of 200% of base salary.
- The holding periods applying to the LTIP awards together with bonus deferral will continue to apply post-cessation to 'good leavers'.

Last year I highlighted the negative effects that extended and frequent 'prohibited periods' that limit Directors' and senior employees' share transactions can have on our remuneration practices. This is particularly relevant for Phoenix because acquiring additional closed funds is core to our strategy and the time spent to properly consider acquisitions can mean extended prohibited periods. This constrains the normal timetables for awarding and vesting the Company's share plans.

To address this issue we have amended the rules of the LTIP and Deferred Bonus Share Scheme ('DBSS') (the deferral vehicle for the AIP) to provide that grants will be made on the fourth dealing day following the announcement of results regardless of whether the Company is then in a prohibited period. While recognising that this is unusual it will have a significant impact internally on the ability to operate the plans effectively. While awards will vest on the respective anniversary dates the exercise of awards or the sale of shares will remain possible only in open periods.

SHAREHOLDER APPROVAL

At the AGM on 11 May 2017, shareholders will be asked to approve two resolutions related to Directors remuneration matters:

- to approve the Directors' Remuneration Policy as set out in Part A of this Directors' Remuneration Report; and
- to approve the Implementation Report sections of this Directors' Remuneration Report (excluding the Directors' Remuneration Policy).

As Phoenix is a non-UK incorporated company both of these votes will be advisory in nature.

The Committee continues to seek to reflect developments in practice as deemed appropriate for the Phoenix Group.

I hope that we can continue to rely on the support of our shareholders for the resolutions which will be proposed at the 2017 AGM.

Yours sincerely

IAN CORMACK
REMUNERATION COMMITTEE CHAIRMAN

17 MARCH 2017

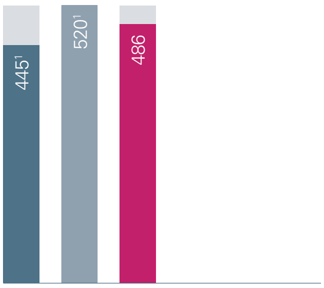
DIRECTORS' REMUNERATION REPORT Continued
At a glance

HOW WE PERFORMED IN 2016
GROUP PERFORMANCE MEASURES

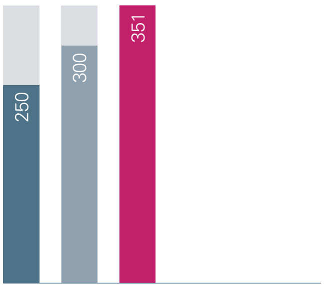
Annual Incentive Plan ('AIP'):

Below we show outturn against the metrics within the 2016 AIP. More details of the 2016 AIP can be found on page 76.

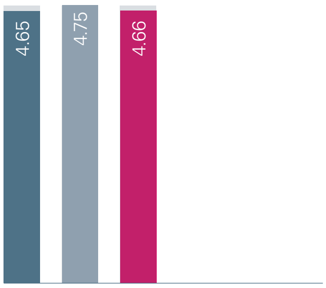
OPERATING COMPANIES' CASH GENERATION (£m)



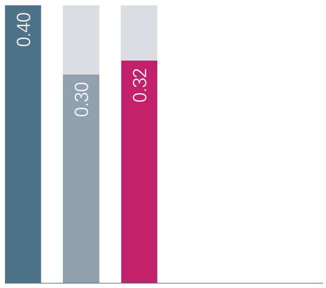
OPERATING PROFIT (£m)



CUSTOMER SATISFACTION



SERVICING COMPLAINTS AS A % OF TRANSACTIONS



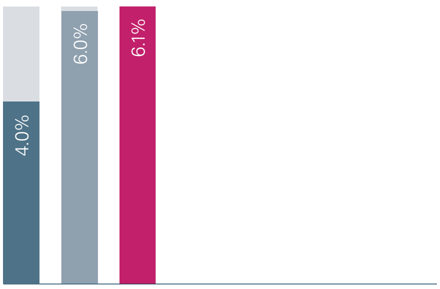
Target level for AIP
Performance
Maximum level for AIP

1 Target and maximum levels include increase of £20m (see page 76)

Long-Term Incentive Plan ('LTIP'):

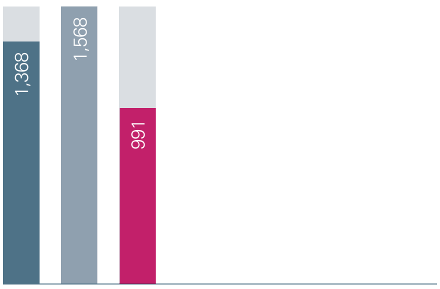
Below, we show progress against the measures which apply for the 2014 LTIP awards. Embedded value growth, cumulative cash generation and TSR performance is shown over the three-year performance period (financial years 2014, 2015 and 2016). TSR is measured against the constituents of the FTSE 250 (ex. Investment Trusts), with median being the 50th percentile and upper quintile from the 80th percentile.

GROWTH IN EMBEDDED VALUE (%)



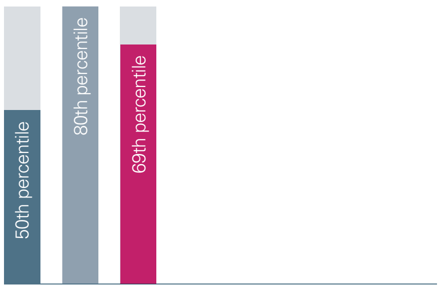
Threshold target
Maximum target
Performance (and see page 77)

CUMULATIVE CASH GENERATION (£m)



Threshold target
Maximum target
Performance

TOTAL SHAREHOLDER RETURN (%)

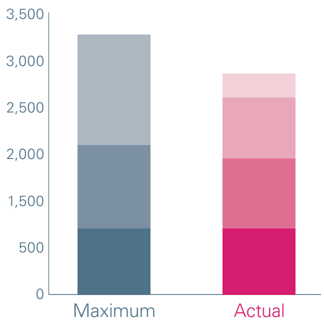


Median
Upper Quintile
Performance

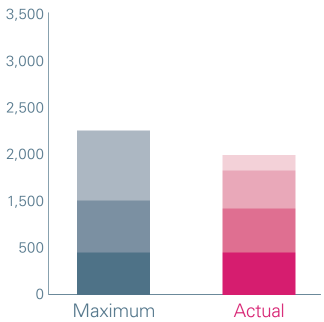
How much the Executive Directors earned in 2016 (£000)

The charts below compare the maximum levels of Total Remuneration Opportunity in the remuneration policy (see page 70) and the actual payments for 2016 detailed in the Single Figure Table. For the 2016 actual LTIP values, the share price growth and dividend element is shown separately.

CLIVE BANNISTER



JAMES MCCONVILLE



Policy maximum fixed remuneration
Policy maximum AIP
Policy maximum LTIP grant
Actual fixed remuneration
Actual AIP
Actual LTIP vesting
Share growth and dividends on vested LTIP

INTRODUCTION

This report contains the material required to be set out as the Directors' Remuneration Report ('Remuneration Report') for the purposes of Part 4 of The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013, which amended The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 ('the DRR regulations'). The Company intends to comply with the DRR regulations as a matter of good practice although as a non-UK incorporated quoted company it is not strictly required to do so and is not subject to the technical consequences of non-compliance with the DRR regulations.

Part A represents the Directors' Remuneration Policy. This policy will take effect, subject to the approval of the shareholders, immediately after the 2017 AGM.

Part B constitutes the implementation sections of the Remuneration Report ('Implementation Report').

PART A: DIRECTORS' REMUNERATION POLICY

The Directors' Remuneration Policy ('Remuneration Policy') as set out in this section of the Remuneration Report will, if approved by shareholders, take effect for all payments made to Directors from the date of the AGM on 11 May 2017.

GENERAL POLICY

The Remuneration Policy for Executive Directors is summarised in the table below along with the position of the Chairman's and the Non-Executive Directors' fees:

Overall Positioning*

The Company's overall positioning on remuneration for Executive Directors remains unchanged from prior years:

— An appropriate balance is maintained between fixed and variable components of remuneration.

— Our Remuneration Policy benchmarks the total target remuneration for the Executive Directors between FTSE 31-100 and FTSE 250 data sets, and remuneration for both Executive Directors is positioned appropriately between these data sets.

* This section does not form part of the Remuneration Policy and is for information only.

Summary of Changes from Previous Policy:

As more fully detailed in the 'Changes from Previous Policy' column in the Remuneration Policy table, the key changes to the Remuneration Policy are the following:

Element	Changes from previous policy
Base salary	— Confirmation of caps for each element of the policy, including base salary. For base salaries, we have clarified the target positioning of Executive Directors' base salaries as between the FTSE 31-100 and FTSE 250 data sets.
Annual Incentive Plan	— Increasing the level of bonus deferral to 40% of outcomes (from 33% of outcomes).
	— Confirming that at least 50% of performance measures in any year will relate to financial measures.
	— Confirming the automatic grant of deferred shares on the fourth dealing day following the announcement of annual results each year.
Long-Term Incentive Plan	— Confirming the automatic grant of LTIP awards on the fourth dealing day following the announcement of annual results each year.
	— Confirming the application of holding periods (which have applied to LTIP awards from 2015 onwards).
	— Confirming that no material changes will be made to the current performance measures or the current mix of performance measures for LTIP awards made in any year without consulting major shareholders.

DIRECTORS' REMUNERATION REPORT
Continued

Remuneration Policy table

Element and purpose

Base salary

This is the core element of pay and reflects the individual's role and position within the Group with some adjustment to reflect their capability and contribution

Policy and operation

- Base salaries are reviewed each year against companies of similar size and complexity. Both salary levels and overall remuneration are set by reference to the median data of comparators which the Remuneration Committee considers to be suitable using both the FTSE 31-100 and the FTSE 250 as a whole, and positioning the Executive Directors' salaries around the average of the median positions in these pan-sector groups. Consideration is also given to other relevant insurance company data.
- The Remuneration Committee uses this data as a key reference point in considering the appropriate level of salary. Other relevant factors including corporate and individual performance and any changes in an individual's role and responsibilities, and the level of salary increases awarded to other employees of the Group are also considered.
- Base salary is paid monthly in cash.
- Changes to base salaries normally take effect from 1 January.

Maximum

- The Remuneration Committee will apply the factors set out in the previous column in considering any salary adjustments during the duration of this policy. No increase will be made if it would take an Executive Director's salary above £780,000 (being the median level of salaries for CEOs in the FTSE 31-100), provided that this figure may be increased in line with UK RPI inflation for the duration of this policy.

Performance measures

- N/A

Changes from previous policy

- No material changes. 'Cap' for base salaries re-expressed as a monetary amount and relative positioning is confirmed.

Element and purpose

Benefits

To provide other benefits valued by recipient

Policy and operation

- The Group provides market competitive benefits in kind. Details of the benefits provided in each year will be set out in the Implementation Report. The Remuneration Committee reserves discretion to introduce new benefits where it concludes that it is in the interests of Phoenix Group to do so, having regard to the particular circumstances and to market practice.
- Where appropriate, the Company will meet certain costs relating to Executive Director relocations.

Maximum

- It is not possible to prescribe the likely change in the cost of insured benefits or the cost of some of the other reported benefits year-to-year, but the provision of benefits will normally operate within an annual limit of 10% of an Executive Director's base salary.
- The Remuneration Committee will monitor the costs in practice and ensure that the overall costs do not increase by more than the Remuneration Committee considers to be appropriate in all the circumstances.
- Relocation expenses are subject to a maximum limit of £150,000.

Performance measures

- N/A

Changes from previous policy

- No material changes.

Remuneration Policy table continued

Element and purpose

Pension

To provide retirement benefits and remain competitive within the market place

Policy and operation

- The Group provides a competitive employer sponsored defined contribution pension plan.
- All Executive Directors are eligible to participate in the Group Personal Pension ('GPP'). Executive Directors receive a contribution to GPP or they may opt to receive the contribution in cash if they are impacted by the relevant lifetime or annual limits. Any such cash payments are reduced for the effect of employers' National Insurance Contributions.
- Phoenix will honour the pensions obligations entered into under all previous policies in accordance with the terms of such obligations.

Maximum

- A contribution limit of 20% of base salary per annum per Executive Director has been set for the duration of this policy.

Performance measures

- N/A

Changes from previous policy

- No material changes.

Element and purpose

Annual Incentive Plan ('AIP') and Deferred Bonus Share Scheme ('DBSS')

To motivate employees and incentivise delivery of annual performance targets

Policy and operation

- AIP levels and the appropriateness of measures are reviewed annually to ensure they continue to support the Group's strategy.
- AIP outcomes are paid in cash in one tranche (less the deferred share award).
- At least 40% of any annual AIP award is to be deferred into shares for a period of three years although the Remuneration Committee reserves discretion to alter the current practice of deferral (whether by altering the portion deferred, the period of deferral or whether amounts are deferred into cash or shares). Such alterations may be required to ensure compliance with regulatory guidelines for pay within the insurance sector, but will not otherwise reduce the current deferral level or the period of deferral.
- Deferral of AIP outcomes into shares is currently made under the DBSS.
- Awards under DBSS will be in the form of awards to receive shares for nil-cost (with the shares either being delivered automatically at vesting or being delivered at a time following vesting at the individual's choice).
- DBSS awards are made automatically each year on the fourth dealing day following the announcement of annual results, using the average of the preceding three dealing days' share prices to calculate the number of shares in awards.
- The three-year period of deferral will run to the third anniversary of the award date.
- Dividend entitlements will accrue over the three-year deferral period and be delivered as additional vesting shares.
- Malus/clawback provisions apply to the AIP and to amounts deferred under DBSS as explained in the notes to this table.

Maximum

- The maximum annual incentive level for an Executive Director is 150% of base salary per annum.

Performance measures

- The performance measures applied to AIP will be set by the Remuneration Committee and may be financial or non-financial and corporate, divisional or individual and in such proportions as it considers appropriate. However, the weighting of financial performance measures will not be reduced below 50% of total AIP potential in any year for the duration of this policy.
- In respect of the financial performance measures, attaining the threshold performance level produces a £nil annual incentive payment and for non-financial performance measures the threshold performance level produces an annual incentive outcome that is 10% of the weighting given to these measures.
- On-target performance on all measures produces an outcome of 50% of maximum annual incentive opportunity. However, the Remuneration Committee reserves the right to adjust the threshold and target levels for future financial years in light of competitive practice.

DIRECTORS' REMUNERATION REPORT
Continued

Remuneration Policy table continued

Annual Incentive Plan ('AIP') and Deferred Bonus Share Scheme ('DBSS') continued

Performance measures (continued)

— The AIP operates subject to three levels of moderation:

i. The Remuneration Committee sets targets for relevant AIP metrics. Recognising that the business of the Company is to engage in corporate activity, the Remuneration Committee may adjust targets during the year to take account of such activity and ensure the targets continue to reflect performance as originally intended.

ii. There is a specific adjustment factor of 80%-120% of the provisional outturn whereby the Remuneration Committee may adjust the provisional figure (but subject to any over-riding cap) to take account of its broad assessment of performance both against pre-set targets and more generally, of the wider universe of stakeholders. With respect to financial performance measures, this assessment will include consideration of the quality of how particular outcomes were achieved.

iii. The AIP remains a discretionary arrangement and the Remuneration Committee reserves discretion to adjust the outturn (from zero to any cap) should it consider that to be appropriate. In particular, the Remuneration Committee may operate this discretion in respect of any risk concerns.

Changes from previous policy

— Increased the minimum level of compulsory deferral from 33% to 40%.

— Confirmed that financial performance measures will always have at least a 50% weighting for any year.

— Provides for the automatic making of DBSS awards on the fourth dealing day following the announcement of annual results.

Element and purpose

Long-Term Incentive Plan ('LTIP')

To motivate and incentivise delivery of sustained performance over the long term, and to promote alignment with shareholders' interests, the Group operates the Phoenix Group Holdings Long-Term Incentive Plan

Policy and operation

— Awards under the LTIP may be in any of the forms of awards to receive shares for nil-cost (as described for DBSS above).

— LTIP awards are made automatically each year on the fourth dealing day following the announcement of annual results, using the average of the preceding three dealing days' share prices to calculate the number of shares in awards.

— The vesting period will be at least three years and run until the third anniversary of the award date (unless a longer vesting period is introduced).

— A holding period will apply so that Executive Directors may not normally exercise vested LTIP awards until the fifth anniversary of the award date.

— Dividend entitlements will accrue until the end of the holding period in respect of performance-vested shares and be delivered as additional vesting shares.

— Malus/clawback provisions apply on a basis consistent with the equivalent provisions in the AIP and DBSS and as explained in the notes to this table.

— The Company will honour the vesting of all awards granted under previous policies in accordance with the terms of such awards.

Maximum

— The formal limit under the LTIP is 300% of base salary per annum (and 400% per annum in exceptional cases).

— The Remuneration Committee's practice is to make LTIP awards to Executive Directors each year over shares with a value (as at the award date) of 200% of the individual's annual base salary although discretion is reserved to make awards up to the maximum levels for the policy as stated above.

Remuneration Policy table continued

Long-Term Incentive Plan ('LTIP') continued

Performance measures

— The Remuneration Committee may set such performance measures for LTIP awards as it considers appropriate (whether financial or non-financial and whether corporate, divisional or individual). The Remuneration Committee would expect to consult with its major shareholders if it proposed changing materially the current performance measures applied for LTIP awards made to Executive Directors or the relative weightings between these performance measures.

— For every LTIP award, appropriate disclosures regarding the proposed performance conditions will be made in the annual Implementation Report.

— Once set, performance measures and targets will generally remain unaltered unless events occur which, in the Remuneration Committee's opinion, make it appropriate to make adjustments to the performance measures, provided that any adjusted performance measure is, in its opinion, neither materially more nor less difficult to satisfy than the original measure.

— For each part of an LTIP award subject to a specific performance condition, the threshold level of vesting is 25% of that part of the LTIP award. The Remuneration Committee reserves the discretion to make changes to these levels which it considers non-material.

— The performance period for LTIP awards will be at least three years, but the Remuneration Committee reserves discretion to lengthen the applicable performance periods for LTIP awards.

Changes from previous policy

— Provides for the automatic making of LTIP awards on the fourth dealing day following the announcement of annual results.

— Recognises the introduction of holding periods on LTIP awards since the previous policy was approved (holding periods have applied to all LTIP awards for Executive Directors since 2015).

— Confirms that material changes to either the current performance measures or the relative weightings of such measures would be subject to consultation with major shareholders.

Element and purpose

All-employee share plans

To encourage share ownership by employees, thereby allowing them to participate in the long-term success of the Group and align their interests with those of the shareholders

Policy and operation

— Executive Directors are able to participate in all-employee share plans on the same terms as other Group employees as required by HMRC legislation.

Maximum

— Sharesave – the Remuneration Committee has the facility to allow individuals to save up to a maximum of £500 each month (or such other level as permitted by HMRC legislation) for a fixed period of three or five years. At the end of the savings period, individuals may use their savings to buy ordinary shares in the Company at a discount of up to 20% of the market price set at the launch of each scheme.

— Share Incentive Plan ('SIP') – the Remuneration Committee has the facility to allow individuals to have the opportunity to purchase, out of their pre-tax salary, shares in the Company and receive up to two matching shares for every purchased share. Maximum saving is £150 each month (or up to such level as permitted by the Company in line with HMRC legislation). SIP also has the facility to allow for reinvestment of dividends in further shares, or the award of additional free shares (up to the limits as permitted by HMRC legislation).

Performance measures

— Consistent with normal practice, such awards are not subject to performance conditions.

Changes from previous policy

— No material changes.

DIRECTORS' REMUNERATION REPORT
Continued

Remuneration Policy table continued

Element and purpose

Shareholding guidelines

To encourage share ownership by the Executive Directors and ensure interests are aligned

Policy and operation

— Executive Directors are expected to retain all shares (net of tax) which vest under the DBSS and under the LTIP (or any other discretionary long-term incentive arrangement introduced in the future) until such time as they hold a minimum of 200% of their base salary in shares.

— Only beneficially owned shares and vested share awards (discounted for anticipated tax liabilities) may be counted for the purposes of the guidelines. Share awards do not count prior to vesting (including DBSS awards).

— Once shareholding guidelines have been met, individuals are expected to retain these levels as a minimum. The Remuneration Committee will review shareholdings annually in the context of this policy.

Maximum

— N/A

Performance measures

— N/A

Changes from previous policy

— No material changes.

Element and purpose

Chairman and Non-Executive Director fees

Policy and operation

— The fees paid to the Chairman and the fees of the other Non-Executive Directors are set to be competitive with other listed companies of equivalent size and complexity.

— Fee levels are periodically reviewed. The Company does not adopt a quantitative approach to pay positioning and exercises judgement as to what it considers to be reasonable in all the circumstances as regards quantum.

— Additional fees are paid to Non-Executive Directors who chair a Board committee, or sit on the board of a subsidiary company or on the Solvency II Model Governance Committee, and to the Senior Independent Director ('SID'). No separate Board committee membership fees are currently paid.

— Fees are paid monthly in cash.

— Fee levels for Non-Executive Directors are reviewed annually with any changes normally taking effect from 1 January.

Maximum

— The aggregate fees of the Chairman and Non-Executive Directors will not exceed the limit from time to time prescribed within the Company's Articles of Association for such fees (currently £2 million per annum in aggregate).

— The Company reserves the right to vary the structure of fees within this limit including, for example, introducing time-based fees or reflecting the establishment of new board committees.

Performance measures

— N/A

Changes from previous policy

— No material changes.

NOTES TO THE REMUNERATION POLICY TABLE

1. Differences between the Policy on Remuneration for Directors and the Policy on Remuneration of other employees

When determining Executive Directors' remuneration, the Committee takes into account pay throughout the Group to ensure that the arrangements in place remain appropriate.

The Group has (as required by Solvency II regulations) one consistent reward policy for all levels of employees and this policy is made available to all staff. Therefore, the same reward principles guide reward decisions for all Group employees, including Executive Directors, although remuneration packages differ to take into account appropriate factors in different areas of the business:

- **AIP** – all Group employees participate in the AIP, although the quantum and balance of corporate to individual objectives varies by level. The most senior staff are subject to the regulatory requirements of Solvency II, and these individuals also receive part of their bonus in Company shares deferred for a period of three years. A different scorecard of AIP performance measures applies for employees in 'control functions' (risk, compliance and internal audit) to exclude financial performance measures.
- **LTIP** – our most senior employees participate in the LTIP currently based on the same performance conditions as those for Executive Directors, although the Committee reserves the discretion to vary the performance conditions for awards made to employees below the Board for future awards.
- **All-employee share plans** – the Committee considers it is important for all employees to have the opportunity to become shareholders in the Company. The Company offers two HMRC tax advantaged arrangements in which all UK employees can participate and acquire shares on a discounted and tax advantaged basis (Sharesave and SIP). In recent years, the terms of both plans have been made more generous to encourage employee take-up (increasing the Sharesave discount to 20% and in 2017 increasing the SIP match from 1 for 6 to 1 for 3). In addition, selected individuals may receive ad hoc share awards contingent on continued employment.

2. Stating maximum amounts for the Remuneration Policy

The DRR regulations and related investor guidance encourages companies to disclose a cap within which each element of remuneration policy will operate. Although the Company is not subject to these provisions, the Remuneration Committee has decided to set and disclose limits in this report on a voluntary basis. Where maximum amounts for elements of remuneration have been set within the Remuneration Policy, these will operate simply as caps and are not indicative of any aspiration.

3. Malus and clawback

Malus (being the forfeiture of unvested awards) and clawback (being the ability of the Company to claim repayment of paid amounts as a debt) provisions apply to the AIP, DBSS and LTIP. These provisions may be applied where the Remuneration Committee considers it appropriate to do so following:

- a review of the conduct, capability or performance of an individual;
- a review of the performance of the Company or a Group member;
- any material misstatement of the Company's or a Group member's financial results for any period;
- any material failure of risk management by an individual, a Group member or the Company; or
- any other circumstances that have a sufficiently significant impact on the reputation of the Company.

4. Travel and hospitality

While the Remuneration Committee does not consider this to form part of benefits in the normal usage of that term, it has been advised that corporate hospitality (whether paid for by the Company or another) and certain instances of business travel (including any related tax liabilities settled by the Company or another Group company) for Directors may technically be considered as benefits and so the Remuneration Committee expressly reserves the right to authorise such activities and reimbursement of associated expenses within its agreed policies.

5. Discretions reserved in operating incentive plans

The Remuneration Committee will operate the AIP, DBSS and LTIP according to their respective rules and the above Remuneration Policy table. The Remuneration Committee retains certain discretions, consistent with market practice, in relation to the operation and administration of these plans including:

- (as described in the Remuneration Policy table) the determination of performance measures and targets and resultant vesting and pay-out levels;
- (as described in the Remuneration Policy table) the ability to adjust performance measures and targets to reflect events and/or to ensure the performance measures and targets operate as originally intended;
- (as described in the Termination Policy section below) determination of the treatment of individuals who leave employment, based on the rules of the incentive plans, and the treatment of the incentive plans on exceptional events, such as a change of control of the Company; and
- the ability to make adjustments to existing awards made under the incentive plans in certain circumstances (e.g. rights issues, corporate restructurings or special dividends).

DIRECTORS' REMUNERATION REPORT
Continued

RECRUITMENT REMUNERATION POLICY

The Company's recruitment remuneration policy aims to give the Remuneration Committee sufficient flexibility to secure the appointment and promotion of high calibre executives to strengthen the management team and secure the skill sets to deliver our strategic aims.

- In terms of the principles for setting a package for a new Executive Director, the starting point for the Remuneration Committee will be to apply the general policy for Executive Directors as set out above and structure a package in accordance with that policy. Consistent with the DRR regulations, the caps contained within the policy for fixed pay do not apply to new recruits, although the Remuneration Committee would not envisage exceeding these caps in practice.
- The AIP and LTIP will operate (including the maximum award levels) as detailed in the general policy in relation to any newly appointed Executive Director.
- For an internal appointment, any variable pay element awarded in respect of the prior role may either continue on its original terms or be adjusted to reflect the new appointment as appropriate.
- For external and internal appointments, the Remuneration Committee may agree that the Company will meet certain relocation expenses as it considers appropriate.
- For external candidates, it may be necessary to make awards in connection with the recruitment to buy-out awards forfeited by the individual on leaving a previous employer. For such buy-out awards, Phoenix Group will not pay more than is, in the view of the Remuneration Committee, necessary and will in all cases seek, in the first instance, to deliver any such awards under the terms of the existing incentive pay structure. It may, however, be necessary in some cases to make such awards on terms that are more bespoke than the existing annual and equity-based pay structures in Phoenix in order to secure a candidate. Details of any buy-out awards will be appropriately disclosed.
- All such buy-out awards, whether under the AIP, LTIP or otherwise (for example, specific arrangements made under Listing Rule 9.4.2), will take account of the service obligations and performance requirements for any remuneration relinquished by the individual when leaving a previous employer. The Remuneration Committee will seek to make buy-out awards subject to what are, in its opinion, comparable requirements in respect of service and performance. However, the Remuneration Committee may choose to relax this requirement in certain cases (such as where the service and/or performance requirements are materially completed), and where the Remuneration Committee considers it to be in the interests of shareholders and where such factors are, in the view of the Remuneration Committee, reflected in some other way, such as a significant discount to the face value of the awards forfeited. Exceptionally, where necessary, this may include a guaranteed or non pro-rated annual incentive in the year of joining.
- For the avoidance of doubt, such buy-out awards are not subject to a formal cap.
- A new Non-Executive Director would be recruited on the terms explained in the Remuneration Policy for such Directors.

DIRECTORS' SERVICE CONTRACTS

Executive Directors

Executive Director service contracts, which do not contain expiry dates, provide that compensation provisions for termination without notice will only extend to 12 months of salary, certain fixed benefits and pension (which may be payable in instalments and subject to mitigation). By excluding any entitlement to compensation for loss of the opportunity to earn variable pay, the Remuneration Committee believes the contracts to be consistent with best practice. The Remuneration Committee also has discretion to mitigate further by paying on a phased basis with unpaid instalments ceasing after the initial period of six months if the Executive Director finds alternative employment. Contracts do not contain change of control provisions. The template contract is reviewed from time-time and may be amended provided it is not overall more generous than the terms described above.

Subject to Board approval, Executive Directors are permitted to accept outside appointments on external boards as long as these are not deemed to interfere with the business of the Group.

Non-Executive Directors

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

TERMINATION POLICY SUMMARY

In practice, the facts surrounding any termination do not always fit neatly into defined categories for good or bad leavers. Therefore, it is appropriate for the Remuneration Committee to consider the suitable treatment on a termination having regard to all of the relevant facts and circumstances available at that time. This policy applies both to any negotiations linked to notice periods on a termination and any treatment which the Remuneration Committee may choose to apply under the discretions available to it under the terms of the AIP, DBSS and LTIP plans. The potential treatments on termination under these plans are summarised below.

Incentives	Good Leaver[1]	Bad Leaver	Exceptional Events
	A participant is considered a Good Leaver if leaving through redundancy, serious ill health or death or otherwise at the discretion of the Remuneration Committee	A participant would typically be considered a Bad Leaver following a voluntary resignation or leaving for disciplinary reasons	For example change in control or winding-up of the Company
AIP	Pro-rated annual incentive. Pro-rating to reflect only the period worked. Performance metrics determined by the Remuneration Committee	No awards made	Either the AIP will continue for the year or there will be a pro-rated annual incentive. Performance metrics determined by the Remuneration Committee
DBSS	Deferred awards vest at the end of the original vesting period	Deferred awards normally lapse	Deferred awards vest
LTIP	Will receive a pro-rated award subject to the application of the performance conditions at the normal measurement date and, generally, any holding period will continue to apply Remuneration Committee discretion to disapply pro-rating or to accelerate vesting to the date of leaving (subject to pro-rating and performance conditions) and/or the release of any holding period	All awards will normally lapse	Will receive a pro-rated award subject to the application of the performance conditions at the date of the event. Remuneration Committee discretion to disapply pro-rating

1 Where the reason for leaving is retirement, the individual will be required to provide confirmation of his continued retirement before any payments are released to him after the end of the vesting period.

The Company has power to enter into settlement agreements with executives and to pay compensation to settle potential legal claims. In addition, and consistent with market practice, in the event of termination of an Executive Director, the Company may pay a contribution towards the individual's legal fees and fees for outplacement services as part of a negotiated settlement. Any such fees would be disclosed as part of the detail of termination arrangements. For the avoidance of doubt, the policy does not include an explicit cap on the cost of termination payments.

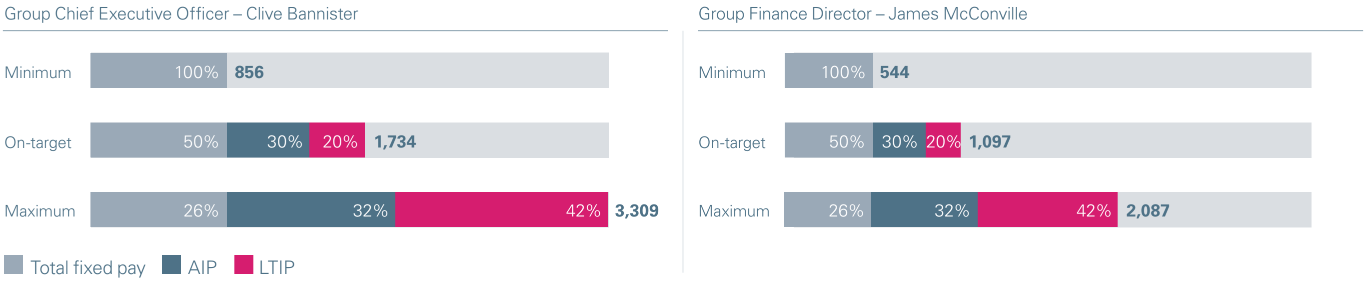
In the event of cessation of a Non-Executive Director's appointment (excluding the Chairman) they would be entitled to a one month's notice period. The Chairman, as detailed in his letter of appointment, would be entitled to a six months' notice period.

DIRECTORS' REMUNERATION REPORT
Continued

POTENTIAL REWARDS UNDER VARIOUS SCENARIOS

The potential total rewards available to the Executive Directors, ignoring any change in share price and roll-up of dividends are:

TOTAL REMUNERATION OPPORTUNITY (£000)



The above chart aims to show how the Remuneration Policy set out above for Executive Directors is applied using the following assumptions.

Minimum

Consists of base salary, benefits and pension

Base salary is the salary to be paid in 2017

Benefits measured as benefits paid in 2016 as set out in the single figure table. Pension measured as the 20% of base salary receivable either as a pension contribution or as cash, and ignoring the reduction to payments made in cash for employers' national insurance contributions

Name	Base salary £000	Benefits £000	Pension £000	**Total fixed £000**
Clive Bannister	700	16	140	**856**
James McConville	440	16	88	**544**

On-target

Based on what the Executive Director would receive if performance was on-target:

- AIP: consists of the on-target annual incentive (75% of base salary).
- LTIP: consists of the threshold level of vesting (50% of base salary). The benefit of a single year's participation in the Sharesave scheme is recognised using an expected value for the Sharesave options of 30%. The benefit of a single year's participation in the SIP is recognised using one matching share for every three shares invested on the maximum value which can be invested.

Maximum

Based on the maximum remuneration receivable:

- AIP: consists of the maximum annual incentive (150% of base salary).
- LTIP: assumes maximum vesting of awards and valued as on the date of grant (normal award 200% of base salary) Sharesave and SIP valued on the same basis as in the on-target row.

CONSIDERATION OF EMPLOYMENT CONDITIONS ELSEWHERE IN THE GROUP

As explained in the notes to the Remuneration Policy table, the Remuneration Committee takes into account Group-wide pay and employment conditions. The Remuneration Committee reviews the average Group-wide base salary increase and annual incentive costs and is responsible for all discretionary and all-employee share arrangements.

Consistent with normal practice, the Remuneration Committee did not consult with employees in preparing the Remuneration Policy.

The Remuneration Committee is cognisant of the requests from, amongst others, the Investment Association, for companies to publish ratios comparing CEO to employee pay. The Remuneration Committee has not, however, published this data in the Directors' Remuneration Report given the absence of a common methodology for these comparisons; the Company's expectation is that it will publish ratios showing comparisons in future years when, as can be expected, UK regulations or guidance develop a common methodology.

CONSIDERATION OF SHAREHOLDERS' VIEWS

Each year the Remuneration Committee takes into account the approval levels of remuneration-related matters at our AGM in determining that the current Remuneration Policy remains appropriate for the Company.

The Remuneration Committee also seeks to build an active and productive dialogue with investors on developments in the remuneration aspects of corporate governance generally and any changes to the Company's executive pay arrangements in particular. The Remuneration Committee consulted with its largest shareholders before proposing the changes reflected in this Remuneration Policy.

PART B: ANNUAL IMPLEMENTATION REPORT – UNAUDITED INFORMATION

IMPLEMENTATION OF REMUNERATION POLICY IN 2017

Element of Remuneration Policy	Detail of Implementation of Policy for 2017
Base Salary	Salaries in 2017 will remain unchanged at £700,000 for the Group Chief Executive Officer (unchanged from 2011) and £440,000 for the Group Finance Director (unchanged from 2014).
Benefits	There are no proposed changes to the benefits offered to Executive Directors in 2017.
Pension	There are no proposed changes to the pension benefits offered to Executive Directors in 2017.
Annual Incentive Plan ('AIP')	The AIP for 2017 will operate on a basis that is consistent with how the AIP operated in 2016, although there have been changes to the precise measures and weightings of the Corporate (financial and strategic) performance measures for 2017's AIP to reflect our evolving business focus. The AIP maximum potential and on-target levels remain unchanged at 150% of base salary and at 50% of maximum levels (75% of base salary) respectively. The overall weightings between Corporate and Personal performance measures for AIP in 2017 are unchanged from 2016: — Corporate (financial and strategic) performance measures – 70%. — Personal (individual objectives) – 30%. The weightings of the AIP performance measures for 2017 are summarised below:

Performance measure	% of incentive potential
Corporate measure	
Operating companies' cash generation	50%
Customer experience	20%
Personal	
Individual objectives	30%
TOTAL	100%

The changes made from 2016's Corporate performance measures for AIP can be summarised as follows:

— In 2017, the sole financial metric will be operating companies' cash generation which remains core to our business and is linked directly to Phoenix Life free surplus under Solvency II. The overall weighting for cash generation has increased from 2016 (35% of incentive potential). At the same time, the profit-based metric (operating profit) has been removed.

— Greater weighting has been given to customer experience (2016: 17.5% of incentive potential), reflecting the focus of the Board as well as the general preference of our regulators. The 2017 customer experience measures will combine a number of measures reflecting the customer experience. The measures, the specific targets and attainment levels will be disclosed in the Directors' Remuneration Report for 2017.

— Personal performance retains a 30% weighting. As for 2016, specific targets of employee engagement and expense management are included as part of the objectives for the Personal performance element.

In addition, and as previously stated in the Remuneration Policy, there are three potential levels at which the performance measures and targets and related outcomes from AIP in 2017 may be moderated (downwards or upwards) by the Committee – more details are provided in the Remuneration Policy table set out on pages 63 and 64.

Deferred Bonus Share Scheme ('DBSS')	40% of AIP outcomes for 2017 will be delivered as an award of deferred shares under the DBSS which will vest after a three-year deferral period. For DBSS awards made in 2017 (in respect of 2016's AIP outcome) and for DBSS awards to be made in subsequent years: — The DBSS award will be made automatically on the fourth dealing day following the announcement of the Company's 2016 annual results. — The number of shares for DBSS awards will be calculated using the average share price for the three dealing days before the grant of awards. — The three-year deferral period will run to the three-year anniversary of the making of the DBSS award. — Dividend entitlements for the DBSS shares will accrue over the three-year deferral period.

DIRECTORS' REMUNERATION REPORT
Continued

Element of Remuneration Policy	Detail of Implementation of Policy for 2017
Long-Term Incentive Plan ('LTIP')	From March 2017, awards under the LTIP will be made under a procedure similar to that described above for awards under the DBSS: — The LTIP award will be made automatically on the fourth dealing day following the announcement of the Company's annual results. — The number of shares for LTIP awards will be calculated using the average share price for the three dealing days before the grant of awards. — The initial three-year vesting period will run to the three-year anniversary of the making of the LTIP award. At this time, the performance conditions will be determined. — However, all annual LTIP awards made to Executive Directors under this process will also be subject to a holding period so that any LTIP awards for which the performance conditions are satisfied will not be released for a further two years from the third anniversary of the original award date. Dividend accrual for LTIP awards will continue until the end of the holding period. Award levels for Executive Directors for 2017 are unchanged at 200% of base salary. The weightings of the LTIP performance measures for 2017 are summarised below:

Performance measure	Weighting of performance measure
Cumulative cash generation	50%
TSR	50%
TOTAL	**100%**

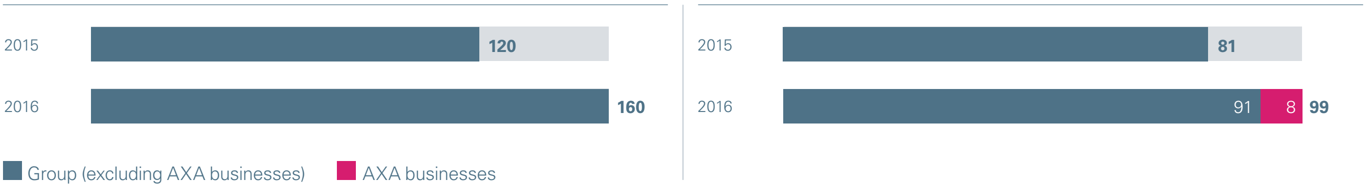
	These weightings are unchanged from the weightings for 2016 LTIP awards. The performance measures are measured over a period of three financial years, commencing with financial year 2017. Additionally, all 2017 LTIP awards are subject to a further underpin measure relating to debt and risk management within the Group, consideration of customer satisfaction and, to meet Solvency II requirements, in exceptional cases, personal performance. These measures and the relative weightings are considered to be appropriate for 2017's LTIP awards. The relative TSR measure is calculated against the constituents of the FTSE 250 (excluding Investment Trusts), with vesting commencing at median (25% of this part of the award vests) and full vesting at upper quintile levels, subject to an underpin regarding underlying financial performance. The performance targets for the Cumulative cash generation measure are £1,372 million (25% of this part of the award vests) and £1,572 million (full vesting of this part of the award).
All-Employee Share Plans	Executive Directors have the opportunity to participate in HMRC tax advantaged Sharesave and Share Incentive Plans ('SIP') on the same basis as all other UK employees. To increase the potential benefit to be available to all staff under SIP, from 2017 the matching ratio will be increased to one free matching share for every three partnership shares purchased (the previous ratio was one free matching share for every six partnership shares purchased).
Shareholding requirements	Requirement levels are 200% of base salary level for the Group Chief Executive Officer and the Group Finance Director. Where any performance vested LTIP awards are subject to a holding period requirement, the relevant LTIP award shares (discounted for anticipated tax liabilities) will count towards the shareholding requirements.
Chairman and Non-Executive Directors' fees	Fee levels for the Chairman and the Non-Executive Directors are unchanged from 2016. The fee levels for 2017 are £325,000 for the Chairman, £105,000 for the role of Non-Executive Director with additional fees of: (i) £5,000 payable for the role of Senior Independent Director; and/or (ii) £10,000 payable where an individual also chairs the Audit, Remuneration or Risk Committee; and/or (iii) £20,000 payable where a Non-Executive Director also serves on the board of a subsidiary company; and/or (iv) £10,000 payable for service on the Solvency II Model Governance Committee.

Note: All incentive plans are subject to malus/clawback. See page 67 'Notes to the Remuneration Policy' for details.

DISTRIBUTION STATEMENT

The DRR regulations require each quoted company to provide a comparison between profits distributed by way of dividend and overall expenditure on pay.

RELATIVE IMPORTANCE (£ millions)



Profit distributed by way of dividend has been taken as the dividend paid and proposed in respect of the relevant financial year. For 2016 this is the interim dividend paid (£66 million) and the recommended final dividend of 23.9p per share multiplied by the total share capital issued at the date of the Annual Report as set out in note D1 'Share capital' in the notes to the consolidated financial statements. No share buy-backs were made in either year.

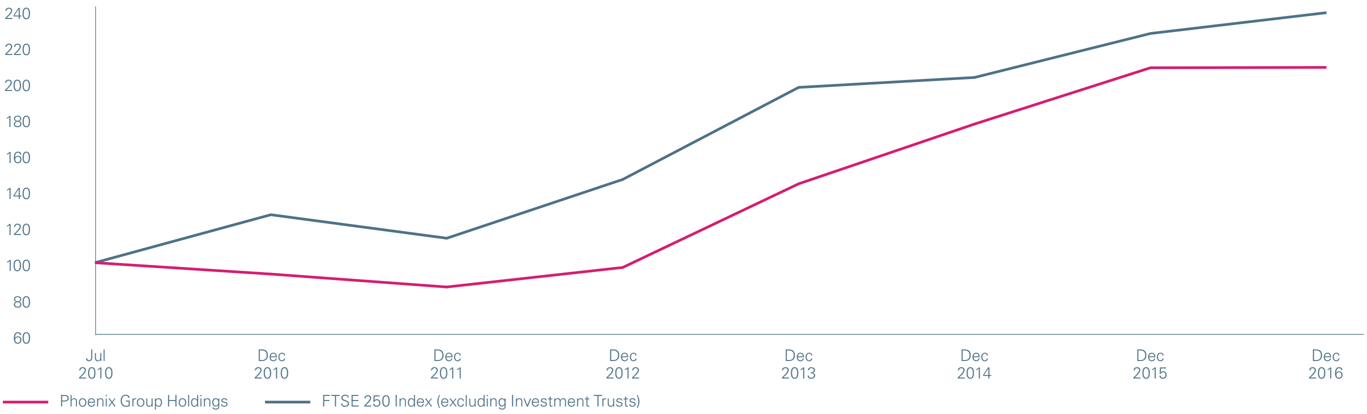
Overall expenditure on pay has been taken as the employee costs as set out in note C2 'Administrative expenses' in the notes to the consolidated financial statements. The current year figure includes £8 million in respect of the acquired AXA businesses. Expenditure on pay from existing businesses has increased by 12%, primarily due to increased staff payroll, recruitment and training costs associated with the increased project activity within the Group during the year, increased share-based payment costs (see note I2 for further details) and higher AIP costs due to higher year end accrual than compared to the prior year.

PERFORMANCE GRAPH AND TABLE

The graph below shows the value to 31 December 2016, on a TSR basis, of £100 invested in Phoenix Group Holdings on 5 July 2010 (the date of the Company's Premium Listing) compared with the value of £100 invested in the FTSE 250 Index (excluding Investment Trusts).

The FTSE 250 Index (excluding Investment Trusts) is considered to be an appropriate comparator for this purpose as it is a broad equity index of which the Company is a constituent.

TOTAL SHAREHOLDER RETURN



Source: Thomson Reuters Datastream

The DRR regulations also require that a performance graph is supported by a table summarising aspects of the Group Chief Executive Officer's remuneration for the period covered by the above graph (which will in due course be for a period of ten years).

DIRECTORS' REMUNERATION REPORT
Continued

GROUP CHIEF EXECUTIVE OFFICER REMUNERATION

		Single figure of total remuneration (£000)	Annual variable element award rates against maximum opportunity ('AIP')	Long-term incentive vesting rates against maximum opportunity ('LTIP')
2016	Clive Bannister	2,794	84%	55%
2015	Clive Bannister	2,867[1]	82%	57%
2014	Clive Bannister	3,104	68%	57%[2]
2013	Clive Bannister	2,737	69%	67%[2]
2012	Clive Bannister	1,583	69%	n/a[3]
2011	Clive Bannister[4]	1,333	73%	n/a[3]
	Jonathan Moss[5]	704	n/a	n/a
2010	Jonathan Moss	2,307	88%	100%

1 The single figure of total remuneration for 2015 has been restated and now reflects the actual price of shares on the day the 2013 LTIP vested (15 November 2016: 736.50p per share) rather than the three-month average share price to 31 December 2015 (873.4924p per share) which was required to be used last year for the single figure of total remuneration, and also reflects the actual dividends accrued on the award until the date of vesting.

2 The long-term incentive vesting rate for 2013 is shown at 67% and for 2014 is shown as 57%. In both years the Group Chief Executive Officer decided to waive voluntarily any entitlement in excess of two-thirds of the shares which would otherwise have vested.

3 Long-term incentive vesting rates against maximum opportunity values are not applicable for 2011 and 2012 due to no awards vesting in those financial years.

4 Jonathan Moss left the role of Group Chief Executive Officer on 7 February 2011 and left Phoenix Group on 29 March 2011. Clive Bannister joined Phoenix Group on 7 February 2011 and was appointed to the Board as a Director on 28 March 2011.

5 Jonathan Moss' 2011 single figure of total remuneration does not include compensation for loss of office.

PERCENTAGE CHANGE IN PAY OF THE GROUP CHIEF EXECUTIVE OFFICER 2015 TO 2016

In accordance with DRR regulations, the table below provides a comparison of the percentage change in the prescribed pay elements of the Group Chief Executive Officer (salary, taxable benefits and annual incentive outcomes) between financial years 2015 and 2016 and the equivalent percentage changes in the average of all staff (representing all permanent staff during 2015 and 2016 on a matched basis). This group was selected as being representative of the wider workforce using the same process as was used for this comparison in last year's accounts.

Year-on-year % change	Salary	Taxable Benefits	Annual incentive	Total
Group Chief Executive Officer	0.00	(0.40)	2.61	1.42
Staff	3.44	1.84	5.30	3.79

Overall the data shows minimal change in the level of remuneration for the Group Chief Executive; the small increase in annual incentive being due to a higher outcome under the personal element of the AIP. Staff more generally have experienced a small overall increase, due in part to higher outcomes under the personal element of annual incentive reflective of their personal achievements over the year. The median salary increase for staff was 2.25%; this is lower than the figures above which are based on averages.

VOTING OUTCOMES FROM THE 2016 AGM

The table below shows the votes cast to approve the Directors' Remuneration Report for the year ended 31 December 2015 at the 2016 AGM held on 11 May 2016.

	For		Against		
	Number	% of votes cast	Number	% of votes cast	Abstain Number
To approve the Directors' Remuneration Report for the year ended 31 December 2015	136,362,734	98.98[1]	1,395,487	1.01[1]	9,589,645

1 The small balance to 100% was for Chairman's discretionary votes not voted.

A vote to approve the Remuneration Policy was passed at the 2014 AGM held on 30 April 2014. Details of the votes cast in relation to this resolution were disclosed in the Company's Directors' Remuneration Report for 2014 which is available as part of the Phoenix Group Holdings Annual Report and Accounts 2014.

IMPLEMENTATION REPORT – AUDITED INFORMATION

SINGLE FIGURE TABLE

£000	Salary/fees[1] 2016	Salary/fees[1] 2015	Benefits[2] 2016	Benefits[2] 2015	Annual Incentive[3] 2016	Annual Incentive[3] 2015	Long-term incentives 2016[4]	Long-term incentives 2015[5] (restated)	Pension[6] 2016	Pension[6] 2015	Total 2016	Total 2015[5] (restated
Clive Bannister[4]	**700**	700	**16**	16	**883**	861	**1,072**	1,167[5]	**123**	123	**2,794**	2,867
James McConville	**440**	440	**16**	16	**555**	566	**674**	667[5]	**77**	77	**1,762**	1,766

1 The Executive Directors are entitled to adjust their salary/benefit combination under flexible benefits arrangements and the figures shown are before individual elections.

2 Benefits for Clive Bannister comprise car allowance and private medical insurance totalling £16,111. Benefits for James McConville comprise car allowance and private medical insurance totalling £15,889.

3 Annual incentive amounts are presented inclusive of any amounts which must be deferred into shares for three years (i.e. one-third of the AIP award). In 2016 and 2015, £294,490 and £287,000 respectively of Clive Bannister's incentive payment is subject to three-year deferral delivered in shares, and £185,108 and £188,650 of James McConville's incentive payment is subject to a similar deferral. Details of the performance measures and targets applicable to the AIP for 2016 are set out below.

4 In accordance with the requirements of the DRR regulations, the 2016 value for long-term incentives is an estimate of the vesting outcomes for LTIP awards granted in 2014 and which are due to vest on 26 March 2017 for Clive Bannister and James McConville. These estimated vesting levels are at 55% reflecting outcomes against the embedded value growth (see page 77), Cumulative cash generation and TSR performance measures to 31 December 2016 and assumptions regarding dividends for the period until vesting. This vesting outcome is then applied to the average share price between 1 October 2016 and 31 December 2016 (730.0761p) to produce the estimated long-term incentives figures shown for 2016 in the above table. These assumptions will be trued up for actual share prices and dividends on vesting in the report for 2017. Details of the performance measures and targets applicable to the 2014 LTIP are set out on page 77.

5 For 2013's LTIP awards which are reflected in the 2015 long-term incentives column above, the performance conditions were met as to 57% of maximum. The 2015 long-term incentives values in the above table reflect the value of the Company's shares on the date of vesting which was 15 November 2016 (736.5p per share) multiplied by the number of shares vesting, whereas the equivalent figure within the published 2015 single figure table was an estimate which reflected the average share price between 1 October 2015 and 31 December 2015 (873.4924p per share) and certain assumptions regarding the cumulative value of dividends on the number of shares vesting. The number of shares vesting has been increased to take into account the impact of the rights issue; this adjustment has been based on the Theoretical Ex-RightsPrice ('TERP') and approved by the Remuneration Committee.

6 Clive Bannister and James McConville are entitled to each receive a Company pension contribution of 20% of base salary, which may at their own choice, be paid to their Group Personal Pension ('GPP') or received in cash. Pension contributions paid as cash supplements are reduced for the effect of employers' National Insurance contributions. No Director participated in a defined benefit pension arrangement in the year.

The aggregate remuneration of all Executive and Non-Executive Directors under salary, fees, benefits, cash supplements in lieu of pensions and annual incentive was £4.041 million (2015: £3.937 million).

There were no payments made to former Directors and no payments for loss of office in the year.

DIRECTORS' REMUNERATION REPORT
Continued

AIP OUTCOMES FOR 2016

The Committee seeks to set suitable ranges for each measure in the context both of the Company's own internal budgets and of external projections (whether through management guidance or consensus forecasts). As an entirely closed life business, targets are significantly impacted by management actions and year-on-year growth is not an inherent objective. The ranges are considered appropriate in that context.

As set out in the Remuneration Policy, the business of the Company is to engage in corporate activity and the Remuneration Committee may adjust targets during the year to include such activity and ensure the targets continue to reflect performance as originally intended. 2016 was an exceptional year in terms of corporate activity with respect to both the AXA and Abbey Life acquisitions. As management was able to close the AXA acquisition in November 2016, the Committee approved an increase in the original cash generation target range for the AIP of £20 million to be broadly consistent with the original basis for setting the original target range. We believe that this increased target range provides a fair measure of the actual achievement for both staff and shareholders. The range disclosed below is inclusive of this £20 million addition.

Against the specific Corporate measures, outturns were as follows:

Performance measure	Threshold performance level for 2016 AIP	Target performance level for 2016 AIP	Maximum performance level for 2016 AIP	Performance level attained for 2016 AIP	% of 70% of incentive potential based on Performance Measure	% achieved
Operating companies' cash generation	£370m	£445m	£520m	£ 486m	50%	38.7%
Operating profit	£200m	£250m	£300m	£351m	25%	25.0%
Customer experience						
Customer satisfaction[1]	4.6 rating	4.65 rating	4.75 rating	4.66 rating	10%	5.5%
Servicing complaints as a percentage of transactions[2]	0.50%	0.40%	0.30%	0.32%	10%	9.0%
Customer Experience – subjective[3]	0%	2.5%	5%	4.5%	5%	4.5%
Total						82.7%

1 The rating is a score based on questions answered by customers in a satisfaction survey managed by Ipsos MORI. Customers surveyed were asked to give a satisfaction rating of between 1 and 5 to a number of questions (with a rating of 3 or above regarded as satisfied). The 4.66 rating (out of 5) in 2016 is the average score of all questions answered.

2 The measure looks at servicing (i.e. not product or advice) complaints received as a percentage of customer transactions. It is calculated in accordance with the FCA requirements for reporting the volume of complaints.

3 This element of customer experience is judged by the Committee as a broad assessment of the overall outcome for Phoenix customers throughout 2016. It allows for consideration of subjective and qualitative matters for customer experience which the Committee considers to be relevant and which may not be captured in the quantitative assessments which are otherwise considered in this part of the AIP, thereby ensuring a holistic assessment.

Personal objectives (which were agreed by the PGH Board and shared with the Remuneration Committee at the start of the year) are viewed across four quadrants:

- Customer/business
- Financial
- People
- Risk/Governance.

Whilst the Board regards a number of the personal objectives set as commercially sensitive (and accordingly, it is not appropriate for such objectives to be disclosed), achievements by the Executive Directors which were considered by the Remuneration Committee included:

- The successful acquisition of the Abbey Life and AXA businesses
- Embedding Solvency II reporting and related Pillar 3 reporting
- Ensuring that Treating Customers Fairly is embedded in our culture
- Delivery of financial KPIs, including in relation to expense management
- Maintaining staff engagement at, or more than, 78% (the outcome was 81%; the 78% objective representing an increase from our target of 72% for 2015)
- Maintaining a satisfactory risk and control environment across the Group and the extent to which the Group has operated within its risk appetite.

For the Personal (individual objectives) element of 2016 AIP, performance of both Executive Directors was discussed with the Board, and the Remuneration Committee considered individual performance in light of their objectives, on the basis of a 5-point scale, separately assessing both 'what' was achieved and 'how' it was delivered, with equal weightings given to each assessment.

Taking account of the attainment of objectives across the four quadrants, each of the Group Chief Executive Officer and the Group Finance Director received an 87.5% payout for this element, consistent with their ratings for 2016.

The table below shows the actual outturn against the annual incentive maximum. For 2016 AIP, Corporate (financial and strategic) measures applied to 70% of incentive opportunity and Personal (individual objectives) measures applied to 30% of incentive opportunity.

	Corporate		Personal		Total	Maximum
Name	As a % of maximum corporate element	As a % of salary	As a % of maximum personal element	As a % of salary	As a % of salary	As a % of salary
Clive Bannister	82.70	86.83	87.50	39.38	126.21	150.00
James McConville	82.70	86.83	87.50	39.38	126.21	150.00

In addition, whilst the performance measures for the AIP for 2017 have been disclosed (see Implementation of Remuneration Policy for 2017), the performance targets for these measures are regarded as commercially sensitive at the current time and accordingly are not disclosed. However, the Company intends to disclose the performance targets for 2017's AIP retrospectively in next year's Directors' remuneration report on a similar basis to the disclosures made above in respect of 2016's AIP.

LTIP OUTCOMES FOR 2014 AWARDS

Performance measure and weighting	Target range	Performance achieved	Vesting outcome	% achieved
Embedded Value growth[1] (40%)	Target range between Embedded value growth in excess of the risk-free rate by 4% per annum and Embedded value growth in excess of the risk-free rate by 6% per annum.	6.1%	100%	40%
Cumulative cash generation[2] (40%)	Target range between cumulative cash generation of £1.368 billion (previously £1.348 billion) and cumulative cash generation of £1.568 billion (previously £1.548 billion).	£0.991bn	0%	0%
TSR (20%)	Target range between median performance against the constituents of the FTSE 250 (excluding Investment Trusts) rising on a pro rata basis until full vesting for upper quintile performance. In addition, the Committee must consider whether the TSR performance is reflective of the underlying financial performance of the Company.	69th percentile	73%	15%
Total				55%

1 As disclosed on page 68 of the 2015 Directors' remuneration report, with the introduction of Solvency II, Phoenix no longer reports MCEV.

MCEV growth for the Company's LTIP is measured using a combination of the growth in balance sheet values plus the value of dividends paid over a three-year performance period. As MCEV is no longer reported by Phoenix from 31 December 2015, for the proportion of the 2014 LTIP awards (three-year performance period ends 31 December 2016) subject to an MCEV growth measure, the Remuneration Committee considered it appropriate to measure the balance sheet element of MCEV growth using growth in MCEV over the period of two financial years to 31 December 2015 as reported, and then deriving the growth rate for the 2016 financial year by using the percentage growth in Solvency II own funds, which has been adjusted for Solvency II specific items ('Adjusted Solvency II Own Funds). Adjusted Solvency II Own Funds is considered appropriate as it is the economic value of an entity calculated on a Solvency II basis, and therefore is more conservative than MCEV and is based on Phoenix's own funds as reported. With the addition of dividends paid over the period to 31 December 2016, the MCEV growth achieved for the 2014 LTIP awards was 6.1%.

For the only other 'inflight' LTIP award subject to an MCEV growth measure (2015's LTIP award measured over three financial years to 31 December 2017) a similar calculation will be followed, using MCEV in 2015 and then the growth in Solvency II Own Funds in 2016 and 2017 for the balance sheet growth element of MCEV growth in this three-year period.

In making these amendments for the 2014 and 2015 LTIP awards, the Remuneration Committee has acted in line with the Directors' Remuneration Policy by ensuring that the amended performance condition is not easier than the original performance condition was intended to be, with Adjusted Solvency II Own Funds being viewed as the most appropriate proxy for the balance sheet growth element within the LTIP measure of MCEV growth.

2 The Committee followed the same approach as reported above for the AIP in increasing the LTIP cash generation target ranges so the figures below are £20 million higher than previously.

The above targets were all measured over the period of three financial years 1 January 2014 to 31 December 2016.

In addition to the above targets, the Committee confirmed that the underpin performance condition relating to debt levels and associated interest costs, and management of debt, capital restructuring and risk management within the Group (as described more fully on page 80 had been achieved in the performance period.

DIRECTORS' REMUNERATION REPORT
Continued

NON-EXECUTIVE FEES

The emoluments of the Non-Executive Directors for 2016 based on the current disclosure requirements were as follows:

Name	Directors' salaries/fees 2016 £000	Directors' salaries/fees 2015 £000	Benefits[1] 2016 £000	Benefits[1] 2015 £000	Total 2016 £000	Total 2015 £000
Non-Executive Chairman						
Howard Davies[2]	**–**	217	**–**	–	**–**	217
Henry Staunton[3]	**325**	108	**–**	–	**325**	108
Non-Executive Directors						
René-Pierre Azria[4]	**96**	100	**–**	–	**96**	100
Alastair Barbour	**145**	130	**6**	7	**151**	137
Ian Cormack	**140**	125	**–**	–	**140**	125
Tom Cross Brown[5]	**46**	120	**–**	–	**46**	120
Isabel Hudson	**105**	100	**–**	–	**105**	100
Wendy Mayall[6]	**35**	–	**–**	–	**35**	–
John Pollock[7]	**35**	–	**–**	–	**35**	–
Nicholas Shott[8]	**35**	–	**–**	–	**35**	–
Kory Sorenson	**105**	90	**–**	–	**105**	90
David Woods	**145**	130	**13**	11	**158**	141
Total	**1,212**	1,120	**19**	18	**1,231**	1,138

1 The amounts within the benefits columns reflect the fact that the reimbursement of expenses to Non-Executive Directors for travel and accommodation costs incurred in attending Phoenix Life Holdings Limited Board and associated meetings represent a taxable benefit. This position has been clarified with HMRC and the amounts shown are for reimbursed travel and accommodation expenses (and the related tax liability which is settled by the Group).

2 Howard Davies retired from the Board 31 August 2015.

3 Henry Staunton joined the Board 1 September 2015.

4 Rene-Pierre Azria retired from the Board 30 November 2016.

5 Tom-Cross Brown retired from the Board 11 May 2016.

6 Wendy Mayall joined the Board 1 September 2016.

7 John Pollock joined the Board 1 September 2016.

8 Nicholas Shott joined the Board 1 September 2016.

SHARE-BASED AWARDS

As at 31 December 2016, Directors' interests under long-term share-based arrangements were as follows:

LTIP

	Date of grant	Share price on grant	No. of shares as at 1 Jan 2016	No. of shares granted in 2016	Increase in shares following rights issue[1]	No. of dividend shares acquired as at vesting[2]	No. of shares exercised[3]	No. of shares not vested[4]	No of shares as at 31 Dec 2016	Vesting date[6]
Clive Bannister										
LTIP[3]	15 Nov 2013	712.0p	**196,629**	**–**	**34,619**	**46,716**	**(158,439)**	**(119,525)**	**–**	15 Nov 2016
LTIP	26 Mar 2014	741.5p	**188,806**	**–**	**33,242**	**–**	**–**	**–**	**222,048**	26 Mar 2017
LTIP	28 Sept 2015	827.7p	**169,150**	**–**	**29,781**	**–**	**–**	**–**	**198,931**	28 Sept 2018
LTIP[5]	2 Jun 2016	877.5p	**–**	**159,544**	**28,090**	**–**	**–**	**–**	**187,634**	2 Jun 2019
			554,585	**159,544**	**125,732**	**46,716**	**(158,439)**	**(119,525)**	**608,613**	
James McConville										
LTIP	15 Nov 2013	712.0p	**112,359**	**–**	**19,782**	**26,694**	**–**	**(68,300)**	**90,535**	15 Nov 2016
LTIP	26 Mar 2014	741.5p	**118,678**	**–**	**20,895**	**–**	**–**	**–**	**139,573**	26 Mar 2017
LTIP	28 Sept 2015	827.7p	**106,322**	**–**	**18,719**	**–**	**–**	**–**	**125,041**	28 Sept 2018
LTIP[5]	2 Jun 2016	877.5p	**–**	**100,284**	**17,656**	**–**	**–**	**–**	**117,940**	2 Jun 2019
			337,359	**100,284**	**77,052**	**26,694**	**–**	**(68,300)**	**473,089**	

1 The number of shares for all outstanding LTIP awards have been increased to take into account the impact of the rights issue. This adjustment has been based on the Theoretical Ex-Rights Price ('TERP') and approved by the Remuneration Committee. The share price on grant shown is the actual price used at the date of the grant and has not been adjusted following the Rights Issue.

2 In addition to the shares awarded under the LTIP presented above, participants receive an additional number of shares (based on the number of LTIP awards which actually vest) to reflect the dividends paid during the vesting period (and which for awards made from 2015, will include dividends paid during any applicable holding period).

3 Gains of Directors from share options exercised and vesting shares under the LTIP in 2016 were £1,121,682 (Clive Bannister's gain was £1,121,682 arising from an LTIP award exercised on 1 December 2016 at a share price of £7.079588; James McConville did not exercise any share options under the LTIP in the year) (2015: £3,037,992).

4 The 2013 LTIP award vested at 57%.

5 The face value of awards granted in 2016 represents the maximum vesting of awards (but before any credit for dividends over the period to vesting) and is calculated using a share price of 877.50p being the average of the closing middle market prices of Phoenix shares for the 3 dealing days preceding the award date, being £1,399,999 for Clive Bannister and £879,992 for James McConville. The vesting percentage at threshold performance (2016 awards) for Clive Bannister and James McConville is 25%.

6 As detailed earlier, for LTIP awards made from 2015 onwards, a holding period applies so that any LTIP awards for which the performance vesting requirements are satisfied will not be released for a further two years from the third anniversary of the original award date.

DIRECTORS' REMUNERATION REPORT
Continued

The performance conditions for the 2014, 2015 and 2016 awards are set out below including the adjustment to the cash generation targets to reflect the impact of both the AXA and Abbey Life acquisitions to ensure that the acquisitions are treated consistently with the underlying assets and are not, overall, more or less challenging to achieve:

Performance measure	2014 award (40% Embedded value growth, 40% Cumulative cash generation and 20% TSR)	2015 award (40% Embedded value growth, 40% Cumulative cash generation and 20% TSR)	2016 award (50% Cumulative cash generation and 50% TSR)
Embedded value growth[1] 25% of this part vests at threshold performance rising on a pro rata basis until 100% vests. Measured over three financial years commencing with the year of award.	Target range between Embedded value growth in excess of the risk-free rate by 4% per annum and Embedded value growth in excess of the risk-free rate by 6% per annum. For this award, an additional £50 million was added to the base Embedded value figure to increase the level of challenge.	Target range between Embedded value growth in excess of the risk-free rate by 3% per annum and Embedded value growth in excess of the risk-free rate by 5% per annum.	Not applicable.
Cumulative cash generation 25% of this part vests at threshold performance rising on a pro rata basis until 100% vests. Measured over three financial years commencing with the year of award.	Target range of £1.348 billion to £1.548 billion. This was increased to £1.368 billion to £1.568 billion to reflect the AXA acquisition (£20 million increase to the range).	Target range of £841 million to £991 million. This was increased to £1.032 billion to £1.182 billion to reflect the AXA and Abbey acquisitions (£191 million increase to the range).	Target range of £949 million to £1.149 billion. This was increased to £1.311 billion to £1.511 billion to reflect the AXA and Abbey acquisitions (£362 million increase to the range).
TSR 25% of this part vests at threshold performance rising on a pro rata basis until 100% vests. In addition, the Committee must consider whether the TSR performance is reflective of the underlying financial performance of the Company. Measured over three financial years commencing with the year of award.	Target range between median performance against the constituents of the FTSE 250 (excluding Investment Trusts) rising on a pro rata basis until full vesting for upper quintile performance.	Target range as for 2014.	Target range as for 2014.

Underpin: Notwithstanding the Embedded value growth, Cumulative cash generation and TSR performance targets, if the Committee determines that the Group's debt levels and associated interest costs have not remained within parameters acceptable to the Committee over the performance period, and that the Group has not made progress considered to be reasonable by it in executing any strategy agreed by the Board on debt management, capital structuring and risk management, the level of awards vesting will either be reduced or lapse in full. For 2016's awards, the underpin has been extended to include consideration of customer satisfaction and, to meet Solvency II requirements, in exceptional cases, personal performance.

1 Please see footnote 1 on page 77 regarding the discontinuation of reporting on MCEV Growth.

As noted in the section describing the Implementation of Remuneration Policy in 2017 on page 72, LTIP awards made in 2017 will be subject to Cumulative cash generation and Relative TSR performance measures similar to those described in the table above.

DBSS

	Date of grant	Share price on grant	No. of shares as at 1 Jan 2016	No. of shares granted in 2016	Increase in shares following rights issue[1]	No. of dividend shares acquired at vesting	No. of shares exercised[2]	No. of shares lapsed/ waived	No. of shares as at 31 Dec 2016	Vesting date
Clive Bannister										
DBSS	27 Mar 2013	658.5p	**36,748**	**–**	**–**	**9,096**	**(45,844)**	**–**	**–**	27 Mar 2016
DBSS	28 Mar 2014	652.0p	**34,029**	**–**	**5,991**	**–**	**–**	**–**	**40,020**	28 Mar 2017
DBSS	28 Sept 2015	827.7p	**28,840**	**–**	**5,077**	**–**	**–**	**–**	**33,917**	19 Mar 2018
DBSS[3]	2 Jun 2016	877.5p	**–**	**32,706**	**5,758**	**–**	**–**	**–**	**38,464**	23 Mar 2019
			99,617	**32,706**	**16,826**	**9,096**	**(45,844)**	**–**	**112,401**	
James McConville										
DBSS	27 Mar 2013	658.5p	**11,999**	**–**	**–**	**2,968**	**(14,967)**	**–**	**–**	27 Mar 2016
DBSS	28 Mar 2014	652.0p	**20,417**	**–**	**3,594**	**–**	**–**	**–**	**24,011**	28 Mar 2017
DBSS	28 Sept 2015	827.7p	**19,124**	**–**	**3,367**	**–**	**–**	**–**	**22,491**	19 Mar 2018
DBSS[3]	2 Jun 2016	877.5p	**–**	**21,498**	**3,785**	**–**	**–**	**–**	**25,283**	23 Mar 2019
			51,540	**21,498**	**10,746**	**2,968**	**(14,967)**	**–**	**71,785**	

1 The number of shares for all outstanding DBSS awards have been increased to take into account the impact of the rights issue. This adjustment has been based on the Theoretical Ex-Rights Price ('TERP') and approved by the Remuneration Committee. The share price on grant shown is the actual price used at the date of the grant and has not been adjusted following the Rights Issue.

2 Gains of Directors from share options exercised and vesting shares under the DBSS in 2016 were £530,014 (Clive Bannister's gain was £399,875 arising from an award exercised on 3 June 2016 at a share price of £8.722509; James McConville's gain was £130,139 arising from an award exercised on 2 June 2016 at a share price of £8.695086.

3 The face value of awards granted in 2016 is equivalent to 50% of the cash element of the 2015 AIP and is calculated using a share price of 877.50p, being the average closing market price on the three days preceding the award date giving £286,995 for Clive Bannister and £188,645 for James McConville.

The DBSS is the share scheme used for the deferral of AIP. No performance conditions apply therefore other than being subject to continued employment. In addition to the shares awarded under the DBSS presented above, participants receive an additional number of shares to reflect the dividends paid during the vesting period (or until transfer of shares for DBSS awards made before 2014).

SHARESAVE

	As at 1 Jan 2016	Shares granted in 2016	Shares exercised	Shares lapsed	As at 31 Dec 2016	Exercise price	Exercisable from	Date of expiry
Clive Bannister	**–**	**–**	**–**	**–**	**–**	–	–	–
James McConville	**1,607**	**–**	**1,607**	**–**	**0**	£5.60	–	–

Gains of Directors from share options exercised under Sharesave during 2016 were £4,998 (2015: nil). Sharesave options are granted with an option price that is a 15% discount to the three-day average share price when invitations are made. This is permitted by HMRC regulations for such options. For options from 2016 this discount will be 20%. Sharesave options are not subject to performance conditions. The Sharesave options exercised by James McConville represented options granted for the then maximum monthly savings of £250 per calendar month for three years.

Aggregate gains of Directors from share options exercised and vesting shares under all share plans in 2016 were £1,656,694 (2015: £3,476,618).

During the year ended 31 December 2016, the highest mid-market price of the Company's shares was 809.654p and the lowest mid-market price was 610.217p. At 31 December 2016, the Company's share price was 735.00p.

DIRECTORS' REMUNERATION REPORT
Continued

DIRECTORS' INTERESTS

The number of shares held by each Director is shown below:

Name	As at 1 January 2016 or date of appointment if later	As at 31 December 2016 or retirement if earlier	Total share plan interests as at 31 December 2016 – LTIP	Total share plan interests as at 31 December 2016 – DBSS	Total share plan interests as at 31 December 2016 – Sharesave
Clive Bannister	305,964	614,521	608,613	112,401	–
James McConville[1]	95,094	123,465	473,089	71,785	–
René-Pierre Azria	34,491	54,610	–	–	–
Alastair Barbour	3,000	6,625	–	–	–
Ian Cormack	3,650	5,779	–	–	–
Tom Cross Brown	1,988	1,988	–	–	–
Isabel Hudson	3,880	6,142	–	–	–
Wendy Mayall[2]	–	–	–	–	–
John Pollock	–	–	–	–	–
Nicholas Shott	–	–	–	–	–
Kory Sorenson	1,380	2,185	–	–	–
Henry Staunton	20,000	70,000	–	–	–
David Woods	3,500	5,541	–	–	–

1 James McConville exercised an LTIP award of 90,535 shares on 5 January 2017.

2 Wendy Mayall purchased 10,000 shares on 14 February 2017.

SHAREHOLDING REQUIREMENTS

As explained in the Remuneration Policy under the Shareholding Guidelines section, the Executive Directors are subject to shareholding requirements.

The extent to which Executive Directors have achieved the requirements by 31 December 2016 (using the share price on 31 December 2016) can be summarised as follows:

Position	Shareholding Guideline (minimum % of salary)	Value of shares held at 31 December 2016 (% of salary)
Clive Bannister	200%	645%
James McConville	200%	206%

The Executive Directors are required to sign a declaration that they have not and will not at any time during their employment with Phoenix Group, enter into any hedging contract in respect of their participation in the AIP, LTIP, Sharesave, SIP or any other incentive plan of the Company, or pledge awards in such plans as collateral, and additionally that they will neither enter into a hedging contract in respect of, nor pledge as collateral, any shares which are required to be held for the purposes of the Company's Shareholding requirements or any vested LTIP award shares subject to a LTIP holding period.

ADDITIONAL UNAUDITED INFORMATION

DIRECTORS' SERVICE CONTRACTS

The dates of contracts and letters of appointment and the respective notice periods for Directors are as follows:

EXECUTIVE DIRECTORS' CONTRACTS

Name	Date of appointment	Date of contract	Notice period from either party (months)
Clive Bannister	28 March 2011	7 February 2011	12
James McConville	28 June 2012	28 May 2012	12

Subject to Board approval, Executive Directors are permitted to accept outside appointments on external boards as long as these are not deemed to interfere with the business of the Group. The Executive Directors are entitled to retain any external fees. During 2016, Clive Bannister received £45,000 from Punter Southall Group and CHF 50,000 from UniGestion in respect of two external directorships. James McConville received £112,000 from Tesco Personal Finance plc.

NON-EXECUTIVE DIRECTORS' CONTRACTS

Name	Date of letter of appointment	Date of Joining the Board	Appointment end date	Unexpired term (months)
Alastair Barbour	30 September 2016	1 October 2013	11 May 2017	2
Ian Cormack	25 May 2016	2 September 2009	11 May 2017	2
Isabel Hudson	25 May 2016	18 February 2010	11 May 2017	2
Wendy Mayall	24 August 2016	1 September 2016	1 September 2019	30
John Pollock	24 August 2016	1 September 2016	1 September 2019	30
Nicholas Shott	24 August 2016	1 September 2016	1 September 2019	30
Kory Sorenson	9 May 2014	1 July 2014	1 July 2017	4
Henry Staunton	19 August 2015	1 September 2015	1 September 2018	18
David Woods	25 May 2016	18 February 2010	11 May 2017	2

The above tables have been included to comply with UKLA Listing Rule 9.8.8. In the event of cessation of a Non-Executive Director's appointment (excluding the Chairman) they would be entitled to a one month notice period. The Chairman, as detailed in his letter of appointment, would be entitled to a six months' notice period.

REMUNERATION COMMITTEE GOVERNANCE

The Group established the Committee in 2010. The terms of reference of the Committee are available at www.thephoenixgroup.com. The main determinations of the Committee in 2016 in respect of the application of the Remuneration Policy are summarised in the Committee Chairman's letter to shareholders at the start of the Directors' remuneration report.

The table below shows the independent Non-Executive Directors who served on the Committee during 2016 and their date of appointment:

Member	From	To
Ian Cormack (Committee Chairman)	18 February 2010	To date
Isabel Hudson	18 February 2010	To date
Nicholas Shott	20 October 2016	To date
Kory Sorenson	3 July 2014	To date

Under the Committee's Terms of Reference, the Committee meets at least twice a year but more frequently if required. During 2016, six Committee meetings were held and details of attendance at meetings are set out in the Corporate Governance Report on page 54.

Consistent with the requirements of Solvency II, the Committee is responsible for establishing, implementing, overseeing and reviewing the firm-wide remuneration policy in the context of business strategy and changing risk conditions. The firm-wide remuneration policy focuses on ensuring sound and effective risk management so as not to encourage risk-taking outside of the Company's risk appetite. None of the Committee members has any personal financial interest (other than as shareholders), conflicts of interests arising from cross-directorships or day-to-day involvement in running the business.

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

DIRECTORS' REMUNERATION REPORT
Continued

ADVICE

The Committee received independent remuneration advice during the year from its appointed adviser, FIT Remuneration Consultants LLP ('FIT'). FIT is a member of the Remuneration Consultants Group (the professional body for consultants) and adheres to its code of conduct. This appointment was made by the Committee following consideration of FIT's experience in this sector. FIT provided no other services to the Group and accordingly the Committee was satisfied that the advice provided by FIT was objective and independent. FIT's fees in respect of 2016 were £239,665, all of which were attributed to work relating to the Committee. FIT's fees were charged on the basis of the firm's standard terms of business for advice provided.

The Committee also consulted with the Group Chief Executive Officer, Group HR Director and General Counsel who attended, by invitation, various Committee meetings during the year although no executive is ever permitted to participate in discussions or decisions regarding his or her own remuneration. Input is also sought from the Chief Risk Officer (without management present) and from representatives from finance, as appropriate.

APPROVAL

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

IAN CORMACK
REMUNERATION COMMITTEE CHAIRMAN

17 MARCH 2017

DIRECTORS' REPORT

The Directors of the Group present their report for the year ended 31 December 2016.

Phoenix Group Holdings is incorporated in the Cayman Islands (registered no. 202172) and has a Premium Listing on the London Stock Exchange. The Company is therefore not required to comply with the requirements of section 415 of the UK Companies Act 2006. However, the Directors support these enhanced standards for disclosure and have sought to comply voluntarily with these requirements.

SHAREHOLDERS

DIVIDENDS

Dividends for the year are as follows:

Ordinary shares	
Paid interim dividend	26.7p per share (2015: 26.7p per share)
Recommended final dividend	23.9p per share (2015: 26.7p per share)
Total ordinary dividend	50.6p per share (2015: 53.4p per share)

As explained in the Chairman's statement on page 5, the proposed dividend of 23.9p per share is an equivalent 5% increase to the 2015 level (rebased to take into account the bonus element of the rights issue completed in November 2016).

As a result of regulatory changes applicable to the Group under Solvency II, dividends declared in respect of the Company's Ordinary Shares must be capable of being cancelled and withheld or deferred at any time prior to payment. This is in order that the Company's Ordinary Shares be counted towards Group capital. Accordingly, the final dividend will be declared on a conditional basis and the Directors reserve the right to cancel or defer the recommended dividend. The Directors do not expect to exercise this right other than where they believe that it may be necessary to do so as a result of legal or regulatory requirements. The Company is also proposing to amend its Articles of Association so as to make clear that any dividend declared in respect of the Company's Ordinary Shares may be cancelled or deferred by the Directors before payment in circumstances where this is required.

SHARE CAPITAL

The issued share capital of the Company was increased by 167,430,371 ordinary shares during 2016 which related to:

- the placement of shares in relation to the acquisition of the AXA business;
- shares issued in relation to the Abbey Life acquisition; and
- shares issued under the Company's Sharesave Scheme.

At 31 December 2016, the issued ordinary share capital totalled 392,849,817. Subsequently, 2,258 ordinary shares have been issued in 2017 in connection with the Company's Sharesave Scheme to bring the total in issue to 392,852,375 at the date of this report.

Full details of the authorised, issued and fully paid share capital as at 31 December 2016 and movements in share capital during the period are presented in note D1 to the IFRS consolidated financial statements.

At the Company's AGM held on 11 May 2016, shareholders granted the Company authority to purchase up to 10% of its issued ordinary shares. Any ordinary shares purchased under the authority would, subject to the Cayman Islands Companies Law (as amended), either be cancelled by operation of law or held in treasury.

Subject to obtaining shareholder approval for the renewal of this authority at the forthcoming AGM on 11 May 2017, the Company is authorised to make purchases of its own shares under Article 20 and make payment for the redemption or purchase of its own shares in any manner permitted by the Cayman Islands Companies Law (as amended), including without limitation, out of capital, profits, share premium or the proceeds of a new issue of shares. The Company held no treasury shares during the year or up to the date of this report.

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

Where the Employee Benefit Trust ('EBT') holds shares for unvested awards, the voting rights for these shares are exercisable by the trustees of the EBT at their discretion, taking into account the recommendations of the Group.

RESTRICTIONS ON TRANSFER OF SHARES

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

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

SUBSTANTIAL SHAREHOLDINGS

Information provided to the Company pursuant to the FCA's Disclosure and Transparency Rules is published on a Regulatory Information Service and on the Company's website. As at 17 March 2017, the Company had been notified of the following significant holdings of voting rights in its shares.

	Number of voting rights in shares	Percentage of shares in issue
Artemis Investment Management LLP	30,921,652	7.87%
Aviva plc & its subsidiaries	21,217,596	5.40%
Prudential plc group of companies[1]	12,649,238	5.10%

1 Number of voting rights and percentage notified are pre-rights issue. Prudential plc have not provided an update post rights issue.

ANNUAL GENERAL MEETING ('AGM')

The AGM of the Company will be held at 1st Floor, 32 Commercial Street, St Helier, Jersey JE2 3RU on Thursday, 11 May 2017 at 12.30pm.

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

44 Read more about our Board of Directors

DIRECTORS' REPORT
Continued

BOARD

BOARD OF DIRECTORS

The membership of the Board of Directors during 2016 is given within the Corporate Governance Report on pages 44 and 45, which is incorporated by reference into this report. Details of Directors' (and persons closely associated with them) interests in the shares of the Company are shown in the Directors' remuneration report.

During 2016 and up to the date of this report, the following changes to the Board took place:

– Tom Cross-Brown resigned from the Board on 11 May 2016.
– Rene-Pierre Azria resigned from the Board on 30 November 2016
– Wendy Mayall, John Pollock and Nicholas Shott were appointed to the Board with effect from 1 September 2016.

Details of related party transactions which took place during the year with Directors of the Company and consolidated entities where Directors are deemed to have significant influence, are provided in the Directors' Remuneration Report and in note I5 to the IFRS consolidated financial statements.

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

In accordance with the UK Corporate Governance Code, Directors must stand for re-election annually. The Board of Directors will be unanimously recommending that all of the Directors, except Isabel Hudson and David Woods who are standing down from the Board, should be put forward for election/re-election at the forthcoming AGM to be held on 11 May 2017.

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

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

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

DIRECTORS' REMUNERATION AND INTERESTS

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

DIRECTORS' INDEMNITIES

Following shareholder approval on 15 March 2010, the Company entered into a deed of indemnity by way of deed poll with its Directors whereby the Company has agreed to indemnify each Director against all losses incurred by them in the exercise, execution or discharge of their powers or duties as a Director of the Company, provided that the indemnity shall not apply to the extent prohibited by any applicable law.

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

58 Read more about Directors' remuneration

DIRECTORS' CONFLICTS OF INTEREST

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

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

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

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

EMPLOYEES

EQUAL OPPORTUNITIES

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

The Group recognises the need to treat people with disabilities fairly and equally including where an employee becomes disabled during their employment. Full and fair consideration is given to internal and external applications from disabled people for employment and further career opportunities, including training and development. Internal and external applicants are asked if they have any special requirements when invited to attend an interview and reasonable provisions are made to meet the applicant's request. Applicants are considered on the basis of the job requirements and their ability and competencies, also taking into consideration any appropriate reasonable workplace adjustments.

The Group provides the opportunity for employees to participate in the Company's all-employee share schemes, Sharesave and Share Incentive Plan, to facilitate share ownership in the Company.

EMPLOYEE ENGAGEMENT

Phoenix Group continues to communicate with staff across a wide variety of channels, including regular news bulletins via the intranet, Executive Committee presentations and other face-to-face briefings. The staff briefings and Executive Committee presentations typically include updates on the Company's strategy and plans, progress against key financial and operational targets, regulatory and risk management updates and review of economic or other factors which could affect the Company's strategy and performance. Regular feedback mechanisms are also in place, ensuring communication at Phoenix is a continuous two-way dialogue.

The views and opinions of staff are sought through Phoenix's annual Engagement Survey and more regular interim surveys and employee communication and engagement forums. Phoenix undertakes meaningful consultation with staff representatives on all major organisational changes and other matters affecting employees engagement.

GOVERNANCE

GOING CONCERN

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report. The Strategic Report also provides details of any key events affecting the Company (and its consolidated subsidiaries) since the end of the financial year. The Strategic Report includes details of the Group's cash flow and solvency position, including sensitivities for both. Principal risks and their mitigation are detailed on pages 37 to 38 and the viability statement is included on page 39. In addition, the IFRS consolidated financial statements include, amongst other things, notes on the Group's borrowings (note E5), management of its financial risk including market, credit and liquidity risk (note E6), its commitments and contingent liabilities (notes I7 and I8) and its capital position and management (note I4). The Strategic Report (on pages 2 to 40) sets out the business model and how the Group creates value for shareholders and policyholders.

The Board has followed the requirements of the UK Financial Reporting Council's 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, (September 2014) when performing its going concern assessment. As part of its comprehensive assessment of whether the Group and the Company are a going concern, the Board has undertaken a review of the liquidity and solvency of the Group under both normal and stressed conditions as at the date of preparation of the statement of consolidated financial position.

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

CORPORATE GOVERNANCE STATEMENT

The disclosures required by section 7.2 of the FCA's Disclosure Guidance and Transparency Rules can be found in the Corporate Governance Report on pages 47 to 57 which is incorporated by reference into this Directors' Report and comprises the Company's Corporate Governance Statement. The UK Corporate Governance Code (the 'Code') applies to the Company and full details on the Company's compliance with the Code are included in the Corporate Governance Report. The Code is available on the website of the Financial Reporting Council – www.frc.org.uk.

GREENHOUSE GAS EMISSIONS

All disclosures concerning the Group's greenhouse emissions are contained in the Environmental Report forming part of the Strategic Report on page 40.

FINANCIAL RISK MANAGEMENT

The Group operates a Risk Management Framework ('RMF') consisting of several components, as detailed in the Risk Management section of the Strategic Report. The RMF provides a consistent approach to highlighting and controlling key risks throughout the organisation. This is achieved primarily through review and compliance, at a functional level, with the risk universe and related policies (and the risk appetites therein).

34 Read more about risk management

At its highest level the RMF considers the following risks: strategic, market, credit, insurance, financial soundness, customer and operational. As a result, in preparing the consolidated financial statements, assessment is given to a broad range of risk categories.

MEMORANDUM AND ARTICLES

Changes to the Company's Memorandum and Articles require prior shareholder approval. Changes proposed at the 11 May 2017 AGM will be set out in the notice for that meeting.

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

RE-APPOINTMENT OF THE AUDITORS

Ernst & Young LLP ('EY') has indicated its willingness to continue in office and a resolution that it is re-appointed will be proposed at the AGM on 11 May 2017.

The Audit tender exercise undertaken in 2016 is described in the Corporate Governance Report on page 52.

There is no cap on auditor liability in place in relation to audit work carried out on the IFRS consolidated financial statements and the Group's UK subsidiaries' individual financial statements.

Details of fees paid to EY during 2016 for audit and non-audit work are disclosed in note C3 to the IFRS consolidated financial statements.

DISCLOSURE OF INFORMATION TO AUDITORS

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

GROUP COMPANY SECRETARY

The Group Company Secretary throughout the 2016 financial period was Gerald Watson.

CONTRACTUAL/OTHER

SIGNIFICANT AGREEMENTS IMPACTED BY A CHANGE OF CONTROL OF THE COMPANY

There are change of control clauses contained in certain of the Group's financing agreements. The £900million revolving credit facility has a provision which would enable the lending banks to require repayment of all amounts borrowed following a change of control. In addition, certain provisions of the Articles relating to the City Code on Takeovers and Mergers apply in connection with a takeover bid.

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

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

DIRECTORS' REPORT
Continued

DISCLOSURES UNDER LISTING RULE 9.8.4R

For the purposes of Listing Rule 9.8.4C, the information required to be disclosed under Listing Rule 9.8.4R can be found within the following sections of the Report and Accounts:

Section	Requirement	Location
1	Statement of interest capitalised	Note E5 to the Consolidated Financial Statements
2	Publication of unaudited financial information	Not applicable
3	Deleted	Not applicable
4	Details of long-term incentive schemes	Directors' remuneration report
5	Waiver of emoluments by a Director	Not applicable
6	Waiver of any future emoluments by a Director	Not applicable
7	Non pre-emptive issue of equity for cash	Page 8 – Group Chief Executive Report
8	As per 7, but for major subsidiary undertakings	Not applicable
9	Parent participation in any placing of a subsidiary	Not applicable
10	Contracts of significance	Not applicable
11	Controlling shareholder provision of services	Not applicable
12	Shareholder dividend waiver	Not applicable
13	Shareholder dividend waiver – future periods	Not applicable
14	Controlling shareholder agreements	Not applicable

STRATEGIC AND DIRECTORS' REPORT APPROVAL

The Board has prepared a Strategic Report which provides an overview of the development and performance of the Group's business for the year ended 31 December 2016, covers the future developments in the business of Phoenix Group Holdings and its consolidated subsidiaries, and provides details of any important events affecting the Company and its subsidiaries after the year-end. For the purposes of compliance with DTR 4.1.5R(2) and DTR 4.1.8R, the required content of the 'Management Report' can be found in the Strategic Report and this Directors' Report, including the sections of the Annual Report and Accounts incorporated by reference.

In addition, the Directors at the date of this report consider that the Annual Report and Accounts, taken as a whole, provides users (who have a reasonable knowledge of business and economic activities) the information necessary to assess the Group's performance, business model and strategy and is fair, balanced and understandable.

The Strategic Report and the Directors' Report were approved by the Board of Directors on 17 March 2017.

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

JAMES MCCONVILLE
GROUP FINANCE DIRECTOR

ST HELIER, JERSEY
17 MARCH 2017

FINANCIALS

IN THIS SECTION

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND ACCOUNTS

The Directors of Phoenix Group Holdings are responsible for the preparation of the Annual Report and Accounts, the Strategic Report, the Directors' Report, the Directors' remuneration report, the Group consolidated financial statements and the Company financial statements in accordance with applicable law and regulations.

The Directors have prepared the Group consolidated financial statements and the Company financial statements in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'). The Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Group and the Company for that period.

In preparing these financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether IFRS, as adopted by the IASB, have been followed, subject to any material departures disclosed and explained in the Group and the Company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Company will continue in business.

The Directors are responsible for:

- keeping adequate accounting records that are sufficient to show and explain the Group's and the Company's transactions and disclose, with reasonable accuracy at any time, the financial position of the Group and the Company;
- safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities; and
- preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement in compliance with applicable laws and regulations.

The Directors as at the date of this report, whose names and functions are listed in the Board of Directors section on pages 44 and 45, confirm that, to the best of their knowledge:

- the Group's consolidated financial statements and the Company financial statements, which have been prepared in accordance with IFRS as issued by the IASB, give a true and fair view of the assets, liabilities, financial position and profit of the Group and the Company; and
- the Directors' Report and the Strategic Report include a fair review of the development and the performance of the business and the position of the Company and its consolidated subsidiaries taken as a whole, together with a description of the principal risks and uncertainties that they face.

In addition, the Directors as at the date of this report consider that the Annual Report and Accounts, taken as a whole, provides users (who have a reasonable knowledge of business and economic activities) with the information necessary for shareholders to assess the Group's performance, business model and strategy, and is fair, balanced and understandable.

The Directors have elected to comply with certain Companies Act and Listing Rules ('LR') which would otherwise only apply to companies incorporated in the UK – namely:

- the Directors' statement under LR 9.8.6R(3) (statement by the Directors that the business is a going concern);
- the Directors remuneration disclosures made under LR 9.8.4R(5) and (6); and
- the requirements of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 of the United Kingdom pertaining to Directors' remuneration that UK quoted companies are required to comply with.

CLIVE BANNISTER
GROUP CHIEF EXECUTIVE OFFICER

JAMES MCCONVILLE
GROUP FINANCE DIRECTOR

ST HELIER, JERSEY
17 MARCH 2017

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PHOENIX GROUP HOLDINGS

OUR OPINION ON THE FINANCIAL STATEMENTS

In our opinion:

– Phoenix Group Holdings' consolidated financial statements and parent company financial statements (the 'financial statements') give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2016 and of the Group's loss and of the parent company's profit for the year then ended; and

– the financial statements have been properly prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB').

WHAT WE HAVE AUDITED

We have audited the consolidated financial statements of Phoenix Group Holdings and its subsidiaries (collectively 'the Group') and the parent company for the year ended 31 December 2016, included within the Annual Report and Accounts, which comprise:

Group	Parent company
– The consolidated income statement for the year then ended	– The statement of comprehensive income for the year then ended
– The consolidated statement of comprehensive income for the year then ended	– The statement of financial position as at 31 December 2016
– The pro forma reconciliation of Group operating profit to results attributable to owners for the year then ended	– The statement of cash flows for the year then ended
– The statement of consolidated financial position as at 31 December 2016	– The statement of changes in equity for the year then ended
– The statement of consolidated cash flows for the year then ended	– Related notes 1 to 16 to the financial statements
– The statement of consolidated changes in equity for the year then ended	
– Related notes A1 to I9 to the consolidated financial statements	

Certain required disclosures have been presented elsewhere in the Annual Report and Accounts, rather than in the notes to the financial statements. These have been cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as issued by the IASB.

OVERVIEW OF OUR AUDIT APPROACH

Materiality	– Overall Group materiality of £67 million (2015: £46 million) which represents 2.0% (2015: 1.9%) of total equity attributable to owners of the parent ('Group equity').
Audit scope	– We performed an audit of the complete financial information of the Group Function, Phoenix Life Division and Abbey Life Assurance Company Limited and audit procedures on specific balances for Other Companies. These are explained further on pages 95 to 96.
	– The reporting units where we performed full or specific audit procedures accounted for more than 99% of the equity and operating profit of the Group.
Risks of material misstatement	– Valuation of insurance contract liabilities, comprising of the following risk areas: – actuarial assumptions; – actuarial modelling; and – data.
	– Valuation of complex and illiquid financial investments.
	– Acquisition of AXA Wealth Limited and Abbey Life Assurance Company Limited.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PHOENIX GROUP HOLDINGS

Continued

OUR ASSESSMENT OF RISK OF MATERIAL MISSTATEMENT

We identified the risks of material misstatement described below as those that had the greatest effect on our overall audit strategy, the allocation of resources in the audit and the direction of the efforts of the audit team. In addressing these risks, we have performed the procedures below which were designed in the context of the financial statements as a whole and, consequently, we do not express any opinion on these individual areas.

Risk

Valuation of insurance contract liabilities (£46.7 billion; 2015: £40.9 billion)

Refer to the Audit Committee Report (page 53); Critical accounting estimates (page 107); Accounting policies and notes F1, F2 and F4 of the consolidated financial statements (pages 145 to 153).

We considered the valuation of insurance contract liabilities to be a significant risk for the Group. Specifically we considered the actuarial assumptions and modelling that are applied, as these involve complex and significant judgements about future events, both internal and external to the business for which small changes can result in a material impact to the resultant valuation. Additionally, the valuation process is conditional upon the accuracy and completeness of the data.

We have split the risks relating to the valuation of insurance contract liabilities into the following component parts:

– actuarial assumptions;

– actuarial modelling; and

– data.

We consider changes in the valuation basis, following discontinuation of Solvency I, not to increase the significant risk in actuarial assumptions and modelling from the prior year as the approach has streamlined financial reporting and reduced the reliance on legacy Solvency I processes and requirements.

We assessed management's analysis of movements in insurance contract liabilities and obtained evidence to support large or unexpected movements. This provided important audit evidence over the valuation of insurance contract liabilities. Further additional audit procedures performed to respond to the specific risk areas are set out below:

Risk area	Our response to the risk	Key observations communicated to the Audit Committee
Actuarial assumptions *There has been no change in our assessment of this risk from the prior year.* Economic assumptions are set by management taking into account market conditions as at the valuation date. Non-economic assumptions such as future expenses, longevity and mortality are set based on past experience, market experience, market practice, regulations and expectations about future trends. The assumptions that we consider to have the most significant impact are the rate of interest used for discounting liabilities, the life expectancy of policyholders (including improvement rates), the lapse rates of polices and expenses. These assumptions are used as inputs into a valuation model which uses standard actuarial methodologies.	To obtain sufficient audit evidence to conclude on the appropriateness of actuarial assumptions, we: – tested the design and operating effectiveness of key controls over management's process for setting and updating actuarial assumptions; – compared the methodology and assumptions used with those we would expect based on our knowledge of the Group, industry standards and regulatory and financial reporting requirements; – assessed the results of management's experience analysis, which supports the adopted assumptions and methodology, and checked that the assumptions used are consistent with this experience analysis; – evaluated the choice of the industry standard Continuous Mortality Investigation ('CMI') model and the parameters used to ensure that it was appropriate given the demographics of policyholders; – benchmarked the demographic and economic assumptions against those of other industry participants; and – reviewed that disclosures have been made in the financial statements regarding the sensitivity of the valuation of insurance contract liabilities to changes in the key assumptions.	We determined that the actuarial assumptions used by management are reasonable based on the analysis of the experience to date, industry practice and the financial and regulatory requirements.

Risk area	Our response to the risk	Key observations communicated to the Audit Committee
Actuarial modelling *There has been no change in our assessment of this risk from the prior year.* We consider the integrity and appropriateness of models to be critical to the overall valuation of insurance contract liabilities. Over £43.1 billion of the £46.7 billion of insurance contract liabilities are modelled using the actuarial modelling systems with the residual balance modelled outside these systems to cater for ancillary business. The key risk is therefore associated with the modelling systems but risks also exist in the calculation of amounts outside these systems.	To obtain sufficient audit evidence to conclude on actuarial models, including those models outside the core system, we: – having confirmed in prior periods that the core system is appropriately valuing liabilities, tested the design, implementation and operating effectiveness of key controls over management's process for model changes during the year; – evaluated the methodology, inputs and assumptions used for a sample of model changes based on our knowledge of the Group, industry standards and regulatory and financial reporting requirements; – assessed the results of the analysis of movements in insurance contract liabilities in order to confirm the completeness of model changes; – tested the design, implementation and operating effectiveness of key controls over management's process for modelling insurance contract liabilities outside the actuarial modelling systems; and – assessed, on a sample basis, the rationale for modelling certain insurance contract liabilities outside the actuarial modelling systems, including evaluating the underlying methodology and accuracy of the calculations for valuations modelled outside the actuarial modelling systems.	We determined that the models used are appropriate and that changes to the models were implemented as intended.
Data *There has been no change in assessment of this risk from the prior year.* The actuarial data is a key input into the valuation process. The valuation of insurance contract liabilities is therefore conditional upon the accuracy and completeness of the data used.	To obtain sufficient audit evidence to assess the integrity of actuarial data we: – tested the adequacy of Outsourced Service Provider ('OSP') controls regarding the maintenance of policyholder data, and where applicable reviewed the Service Organisation Controls ('SOC1') reports produced by the OSPs; – confirmed that the actuarial model data extracts provided by the OSPs were those used as an input to the actuarial model; – tested the design and operating effectiveness of key controls including information technology general controls over management's data collection, extraction and validation process; – assessed the appropriateness of management's grouping of data for input into the actuarial model; and – tested the reconciliations of premiums and claims information from the actuarial data extract to the general ledger, where applicable.	We determined based on our audit work that the data used for the actuarial model inputs are materially complete and accurate.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PHOENIX GROUP HOLDINGS
Continued

Risk area	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of complex and illiquid financial investments ('Level 3 assets') (£1.8 billion; 2015: £1.4 billion) *There has been no change in assessment of this risk from the prior year.* *Refer to the Audit Committee Report (page 53); Critical accounting estimates (page 107); Accounting policies and notes E1 and E2 of the consolidated financial statements (pages 122 to 131).* The extent of judgement applied by management in valuing the Group's financial investments varies with the nature of securities held, the markets in which they are traded and the valuation methodology applied. We focused our audit procedures on the financial investments which require judgement to be applied and for which quoted market prices are not readily available and consequently where management use models and other inputs to estimate their value. These investments are referred to as Level 3 assets in the financial statements.	To obtain sufficient audit evidence to conclude on the valuation of complex and illiquid financial investments, we: – tested the design and operating effectiveness of key controls over management's process in respect of the valuation of investments, including those operated by OSPs via the relevant SOC1 reports; – evaluated the methodology, inputs and assumptions used for a sample of mark to model investments, by comparing yields, spreads, earnings, house prices and market rents to published market benchmarks and other demographic and economic assumptions (such as voluntary early redemption and house price inflation) against those of other industry participants, to confirm that key valuation inputs were consistent with industry norms and our understanding of the asset type; – recalculated a sample of modelled valuations to assess their reasonableness; – obtained net asset valuation ('NAV') statements provided by third party administrators in respect of private equity and fund of fund structures and compared them with management's valuations. We performed 'back-testing' of recent realisations to confirm that the NAV continues to be an appropriate proxy for fair value; – used our real estate valuation specialists to assess the reasonableness of investment property valuations; – assessed the fair value of the fixed and variable rate income securities valuations versus comparable bonds and, where applicable, broker quotes; and – reviewed that disclosures have been made in the financial statements regarding the sensitivity of the valuation of certain illiquid and complex assets to changes in the key assumptions.	Based on our procedures performed on the marked to model assets and manually priced investments we are satisfied that the valuation of these complex and illiquid assets is reasonable.

Risk area	Our response to the risk	Key observations communicated to the Audit Committee
Acquisition of AXA Wealth Limited and Abbey Life Assurance Company Limited *This is a new significant risk for the current year.* *Refer to the Audit Committee Report (page 53); Critical accounting estimates (page 107); Accounting policies and notes H1 and H2 of the consolidated financial statements (pages 175 to 177).* On 1 November 2016, the Group acquired AXA Wealth Limited, AXA Wealth Services Limited, AXA Sun Life Direct Limited, Winterthur Life UK Holdings Limited and AXA Trustee Services Limited (collectively the 'AXA entities') for £373 million. AXA Wealth Limited is material to the Group. On 30 December 2016, the Group acquired Abbey Life Assurance Company Limited, Abbey Life Trustee Services Limited and Abbey Life Trust Securities Limited (collectively the 'Abbey entities') for £933 million. Abbey Life Assurance Company Limited is material to the Group. We focused on this area as it involved significant judgements in respect of the identification of the intangible assets acquired and the valuation of the assets and liabilities acquired. The purchase price allocation exercise has been performed by management, assisted by an external expert. The primary elements of the valuation exercise assessed the fair value of the identifiable intangible assets in the form of acquired value of in-force business ('AVIF') (£218 million) and brands (£20 million).	To obtain sufficient audit evidence to assess the impact of the acquisition of AXA Wealth Limited and Abbey Life Assurance Company Limited we: – reviewed the work performed by the Phoenix Life Division component audit team on the AXA Wealth Limited statement of financial position as at the date of acquisition; – reviewed the work performed by the Abbey Life Assurance Company Limited component audit team on the statement of financial position as at the date of acquisition; – assessed the methodology and assumptions adopted by management and its appointed expert for calculating the fair values of intangible assets arising on acquisition; – ensured that the acquisition accounting and disclosure of these acquisitions are in compliance with IFRS 3 *Business Combinations;* and – read relevant contracts, agreements and board minutes which supported the final conclusions in respect of the acquisition accounting.	Based on our procedures performed on the acquisition of AXA Wealth Limited and Abbey Life Assurance Company Limited, we are satisfied that the valuation of the assets and liabilities acquired, including the identification and initial measurement of intangible assets is reasonable.

THE SCOPE OF OUR AUDIT

TAILORING THE SCOPE

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each reporting unit ('component') within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of Group-wide controls, changes in the business environment and other factors when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the consolidated financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, we selected all four reporting components of the Group. The Group reporting components consists of Phoenix Life Division, Abbey Life Assurance Company Limited, Group Function and Other Companies. In the Phoenix Life Division component the most significant insurance companies are Phoenix Life Assurance Limited, Phoenix Life Limited, and in the current year includes the acquired AXA Wealth Limited. The Group Function consists of Group entities that primarily hold external debt, PA(GI) Limited and certain pension schemes of the Group. The Other Companies are the service companies and Opal Reassurance Limited.

Details of the four components which were audited by component teams are set out below:

Component	Scope	Auditor
Phoenix Life Division	Full	EY
Abbey Life Assurance Company Limited	Full	Non-EY
Group Function	Full	EY
Other Companies	Specific	EY

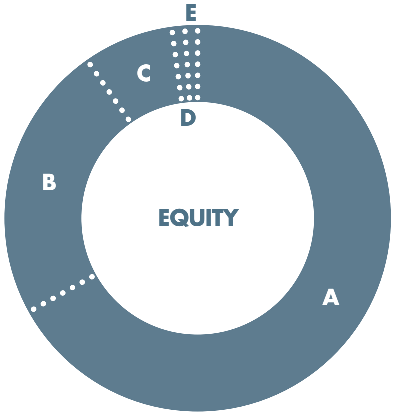
For the Other Companies component, we performed audit procedures on provisions and administrative expenses for the service companies and on financial assets for Opal Reassurance Limited. The extent of audit work in respect of Other Companies component was based on our assessment of the risks of material misstatement at a financial statement line level.

The reporting components where we performed audit procedures accounted for more than 99% of the Group equity and the Group's operating profit. For the current year, the full scope components contributed 98% (2015: 97%) of the equity and 92% (2015: 88%) of the Group's operating profit. The specific scope component contributed 1% (2015: 2%) of the Group's equity and 7% (2015: 11%) of the Group's operating profit.

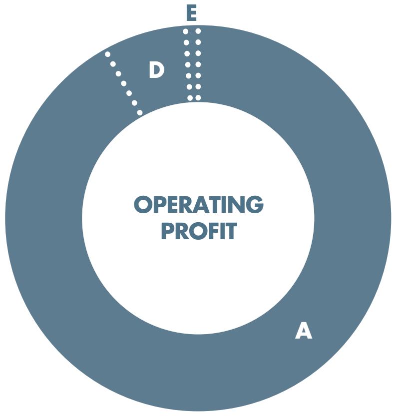
INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PHOENIX GROUP HOLDINGS

Continued

The charts below illustrate the coverage obtained from the work performed by our audit teams.



A	Phoenix Life Division – full scope	69%
B	Abbey Life – full scope	24%
C	Group function – full scope	5%
D	Other companies – specific scope	1%
E	Out of scope	less than 1%



A	Phoenix Life Division – full scope	92%
B	Abbey Life – full scope	0%
C	Group function – full scope	0%
D	Other companies – specific scope	7%
E	Out of scope	less than 1%

CHANGES FROM THE PRIOR YEAR

We have an additional component as a result of the acquisition of Abbey Life Assurance Company Limited. AXA Wealth Limited was incorporated into the Phoenix Life Division during the year.

INVOLVEMENT WITH COMPONENT TEAMS

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by the component auditors operating under our instruction.

The Group audit team provided detailed audit instructions to the component teams which included guidance on areas of focus, including the relevant risks of material misstatement detailed above, and set out the information required to be reported to the Group team.

The Group audit team is responsible for the audit of the Group Function. The Group team visited the full scope component of the Phoenix Life Division, and reviewed key work papers and participated in the planning and execution of the component team's audit of the identified risks. The Group team attended the closing meetings with the management of the Phoenix Life Division and attended key audit committee meetings. As Abbey Life Assurance Company Limited was acquired on 30 December 2016, audit planning by the non-EY component audit team was already complete at the acquisition date. The Group team then reviewed and challenged their audit plan and approach, especially with a focus on the significant risk areas for the Group. The Group team held weekly meetings with the Abbey Life Assurance Company Limited auditors and a specific meeting to discuss the actuarial assumptions. The Group team then performed a detailed review of the execution audit procedures and reporting performed by the non-EY component team. The Group team attended the closing meeting with the management of Abbey Life Assurance Company Limited.

For the specific scope component, the Group team have reviewed the audit procedures performed by the component team on the specific accounts.

The work performed on the components, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the consolidated financial statements as a whole.

OUR APPLICATION OF MATERIALITY

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

MATERIALITY

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be £67 million (2015: £46 million), which is 2.0% (2015: 1.9%) of Group equity. Our aim is that materiality should not exceed 2.0% of year-end Group equity. Whilst profit before tax or operating profit are common bases used across the life insurance industry, we believe that the use of equity as the basis for assessing materiality is more appropriate given that the Group is a closed life assurance consolidator and as such equity provides a more stable, long-term measure of value. We note also that equity more closely correlates with key Group performance metrics such as Solvency II capital requirements and Own Funds. However, as these measures are non-GAAP measures, we consider equity to be most appropriate.

During the course of our audit, we reassessed initial materiality and concluded that materiality assessed at planning stages of our audit remained appropriate.

PERFORMANCE MATERIALITY

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 50% (2015: 50%) of our planning materiality, namely £34 million (2015: £23 million).

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £7 million to £25 million (2015: £4.6 million to £18.4 million).

REPORTING THRESHOLD

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report all uncorrected audit differences in excess of £3.0 million (2015: £2.3 million), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

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 Group's and the parent 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. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Statement of Directors' Responsibilities set out on page 90, 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.

Phoenix Group Holdings is a non-UK company and as such is not required to comply with the UK Companies Act 2006. As the Group is listed on the UK Stock Exchange, the Directors have voluntarily chosen to comply with the Companies Act 2006 and listing rules that apply to UK Companies and have engaged us to provide an opinion as if they were. Accordingly, we have been engaged to:

- report as to whether the Strategic Report and Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- report as to whether the information given in the Corporate Governance Statement with respect to internal control and risk management systems in relation to financial reporting processes is consistent with the financial statements;
- report as to whether the section in the Directors' remuneration report that is described as audited has been properly prepared in accordance with the basis of preparation described therein; and
- report if we are not satisfied that:
  - adequate accounting records have been kept (including returns from those branches which have not been visited); or
  - the financial statements are in agreement with the records and returns; or
  - we have obtained all the information and explanations which we consider necessary for the purposes of the audit.

This report is made solely to the Company's members, as a body, in accordance with our engagement letter dated 10 March 2016. 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.

REPORT ON MATTERS PRESCRIBED BY OUR ENGAGEMENT LETTER

In our opinion:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the information given in the Corporate Governance Statement set out on pages 47 to 57 with respect to internal control and risk management systems in relation to financial reporting processes is consistent with the financial statements; and
- the part of the Directors' remuneration report that has been described as audited has been properly prepared in accordance with the basis of preparation as described therein.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PHOENIX GROUP HOLDINGS

Continued

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

ISAs (UK and Ireland) reporting	We are required to report to you if, in our opinion, financial and non-financial information in the Annual Report and Accounts is: – materially inconsistent with the information in the audited financial statements; or – apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or – otherwise misleading. In particular, we are required to report whether we have identified any inconsistencies between our knowledge acquired in the course of performing the audit and the Directors' statement that they consider the Annual Report and Accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the entity's performance, business model and strategy; and whether the Annual Report and Accounts appropriately addresses those matters that we communicated to the audit committee that we consider should have been disclosed.	We have no exceptions to report.
Listing rules review requirements	We are required to review: – the Directors' statement in relation to going concern, set out on page 87, and the longer-term viability, set out on page 39; and – the part of the Corporate Governance Statement relating to the Company's compliance with the provisions of the UK Corporate Governance Code specified for our review.	We have no exceptions to report.
Engagement letter reporting	We are required to report to you if, in our opinion: – adequate accounting records have not been kept (including returns from those branches which have not been visited); or – the financial statements are not in agreement with the accounting records and returns; or – we have not received all the information and explanations which we require for the audit.	We have no exceptions to report.

STATEMENT ON THE DIRECTORS' ASSESSMENT OF THE PRINCIPAL RISKS THAT WOULD THREATEN THE SOLVENCY OR LIQUIDITY OF THE ENTITY

ISAs (UK and Ireland) reporting	We are required to give a statement as to whether we have anything material to add or to draw attention to in relation to: – the Directors' confirmation in the Annual Report and Accounts that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity; – the disclosures in the Annual Report and Accounts that describe those risks and explain how they are being managed or mitigated; – the Directors' statement in the Annual Report and Accounts about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements; and – the Directors' explanation in the Annual Report and Accounts as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	We have nothing material to add or to draw attention to.

Ernst & Young LLP

ERNST & YOUNG LLP

LONDON
17 MARCH 2017

Notes:

1 The maintenance and integrity of the Phoenix Group Holdings website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

2 Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
Gross premiums written		**999**	902
Less: premiums ceded to reinsurers	F3	**(75)**	(1,376)
Net premiums written		**924**	(474)
Fees		**88**	95
Net investment income	C1	**6,361**	1,064
Total revenue, net of reinsurance payable		**7,373**	685
Gain on transfer of business	I1.1	**52**	–
Other operating income		**20**	7
Net income		**7,445**	692
Policyholder claims		**(3,726)**	(3,931)
Less: reinsurance recoveries		**456**	326
Change in insurance contract liabilities		**(1,970)**	2,959
Change in reinsurers' share of insurance contract liabilities		**(281)**	1,003
Transfer from unallocated surplus	F2	**4**	84
Net policyholder claims and benefits incurred		**(5,517)**	441
Change in investment contract liabilities		**(1,194)**	(232)
Acquisition costs		**(9)**	(7)
Change in present value of future profits	G7	**(11)**	(6)
Amortisation and impairment of acquired in-force business	G7	**(76)**	(148)
Amortisation of other intangibles	G7	**(14)**	(15)
Administrative expenses	C2	**(506)**	(430)
Net income attributable to unitholders		**(66)**	(7)
Total operating expenses		**(7,393)**	(404)
Profit before finance costs and tax		**52**	288
Finance costs	C4	**(122)**	(136)
(Loss)/profit for the year before tax		**(70)**	152
Tax (charge)/credit attributable to policyholders' returns	C5	**(58)**	33
(Loss)/profit before the tax attributable to owners		**(128)**	185
Tax (charge)/credit	C5	**(30)**	97
Add: tax attributable to policyholders' returns	C5	**58**	(33)
Tax credit attributable to owners	C5	**28**	64
(Loss)/profit for the year attributable to owners		**(100)**	249
Attributable to:			
Owners of the parent		**(101)**	201
Non-controlling interests	D3	**1**	48
		(100)	249
Earnings per ordinary share			
Basic (pence per share)	B3.1	**(34.3)p**	76.1p*
Diluted (pence per share)	B3.2	**(34.3)p**	76.0p*

* Restated following rights issue.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
(Loss)/profit for the year		**(100)**	249
Other comprehensive income:			
Items that are or may be reclassified to profit or loss:			
Reclassification adjustments relating to foreign collective investment schemes disposed of in the period		**–**	(10)
Items that will not be reclassified to profit or loss:			
Owner-occupied property revaluation gains	G8	**–**	4
Remeasurements of net defined benefit asset/liability	G6	**219**	11
Tax charge relating to other comprehensive income items	C5	**(1)**	(5)
Total other comprehensive income for the year		**218**	–
Total comprehensive income for the year		**118**	249
Attributable to:			
Owners of the parent		**117**	201
Non-controlling interests	D3	**1**	48
		118	249

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

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
Operating profit			
Phoenix Life		**357**	336
Group costs		**(6)**	(12)
Total operating profit		**351**	324
Investment return variances and economic assumption changes on long-term business	B2.2	**(207)**	13
Variance on owners' funds	B2.3	**(5)**	(12)
Amortisation of acquired in-force business		**(68)**	(75)
Amortisation of other intangibles	B1.2	**(14)**	(15)
Other non-operating items		**(95)**	49
(Loss)/profit before finance costs attributable to owners		**(38)**	284
Finance costs attributable to owners	B1.2	**(90)**	(99)
(Loss)/profit before the tax attributable to owners		**(128)**	185
Tax credit attributable to owners		**28**	64
(Loss)/profit for the year attributable to owners		**(100)**	249

STATEMENT OF CONSOLIDATED FINANCIAL POSITION

As at 31 December 2016

	Notes	2016 £m	2015 £m
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	D1	–	–
Share premium		1,643	861
Shares held by the employee benefit trust	D2	(7)	(5)
Foreign currency translation reserve		96	96
Owner-occupied property revaluation reserve		4	4
Retained earnings		1,597	1,478
Total equity attributable to owners of the parent		3,333	2,434
Non-controlling interests	D3	–	570
Total equity		3,333	3,004
Liabilities			
Pension scheme liability	G6	680	–
Insurance contract liabilities			
Liabilities under insurance contracts	F1	45,807	39,983
Unallocated surplus	F2	879	877
		46,686	40,860
Financial liabilities			
Investment contracts		27,332	7,905
Borrowings	E5	2,036	1,998
Deposits received from reinsurers		392	378
Derivatives	E3	1,567	1,360
Net asset value attributable to unitholders		1,040	5,120
Obligations for repayment of collateral received		1,623	725
	E1	33,990	17,486
Provisions	G1	109	28
Deferred tax	G2	378	354
Reinsurance payables		21	19
Payables related to direct insurance contracts	G3	484	364
Current tax	G2	12	7
Accruals and deferred income	G4	204	128
Other payables	G5	102	677
Liabilities classified as held for sale	I1	–	1,587
Total liabilities		82,666	61,510
Total equity and liabilities		85,999	64,514

STATEMENT OF CONSOLIDATED FINANCIAL POSITION

As at 31 December 2016
Continued

	Notes	2016 £m	2015 £m
ASSETS			
Pension scheme asset	G6	**225**	506
Intangible assets			
Goodwill		**57**	39
Acquired in-force business		**1,407**	1,265
Other intangibles		**214**	219
	G7	**1,678**	1,523
Property, plant and equipment	G8	**25**	19
Investment property	G9	**646**	1,942
Financial assets			
Loans and receivables		**1,232**	577
Derivatives	E3	**3,003**	1,498
Equities		**17,759**	12,351
Investment in associate		**525**	–
Fixed and variable rate income securities		**29,290**	31,814
Collective investment schemes		**18,432**	3,826
Reinsurers' share of investment contract liabilities		**6,808**	–
	E1	**77,049**	50,066
Insurance assets			
Reinsurers' share of insurance contract liabilities	F1	**3,744**	3,954
Reinsurance receivables		**37**	29
Insurance contract receivables		**11**	9
		3,792	3,992
Current tax	G2	**44**	47
Prepayments and accrued income		**361**	335
Other receivables	G10	**513**	474
Cash and cash equivalents	G11	**1,666**	3,940
Assets classified as held for sale	I1	**–**	1,670
Total assets		**85,999**	64,514

STATEMENT OF CONSOLIDATED CASH FLOWS

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
Cash flows from operating activities			
Cash utilised by operations	I3	**(1,845)**	(576)
Taxation paid		**(52)**	(110)
Net cash flows from operating activities		**(1,897)**	(686)
Cash flows from investing activities			
Acquisition of AXA subsidiaries, net of cash acquired	H2.1	**(343)**	–
Acquisition of Abbey Life subsidiaries, net of cash acquired	H2.2	**(886)**	–
Net cash flows from investing activities		**(1,229)**	–
Cash flows from financing activities			
Proceeds from issuing ordinary shares, net of associated commission and expenses	D1	**908**	2
Proceeds from issuing shares in subsidiaries to non-controlling interests	D3	**–**	35
Ordinary share dividends paid	B4	**(126)**	(120)
Coupon paid on Perpetual Reset Capital Securities		**(1)**	(20)
Cash settlement of Perpetual Reset Capital Securities	D3	**(6)**	(3)
Fees associated with the issuance of subordinated notes		**–**	(3)
Fees associated with the amendment of existing bank facility		**(3)**	–
Dividends paid to non-controlling interests	D3	**–**	(23)
Repayment of policyholder borrowings		**(38)**	(118)
Repayment of shareholder borrowings		**(882)**	(190)
Proceeds from new policyholder borrowings, net of associated expenses		**–**	99
Proceeds from new shareholder borrowings, net of associated expenses		**1,079**	–
Interest paid on policyholder borrowings		**(6)**	(15)
Interest paid on shareholder borrowings		**(73)**	(85)
Net cash flows from financing activities		**852**	(441)
Net decrease in cash and cash equivalents		**(2,274)**	(1,127)
Cash and cash equivalents at the beginning of the year		**3,940**	5,067
Cash and cash equivalents at the end of the year	G11	**1,666**	3,940

STATEMENT OF CONSOLIDATED CHANGES IN EQUITY

For the year ended 31 December 2016

	Share capital (note D1) £m	Share premium £m	Shares held by the employee benefit trust (note D2) £m	Foreign currency translation reserve £m	Owner-occupied property revaluation reserve £m	Retained earnings £m	Total £m	Non-controlling interests (note D3) £m	Total £m
At 1 January 2016	–	861	(5)	96	4	1,478	2,434	570	3,004
(Loss)/profit for the year	–	–	–		–	(101)	(101)	1	(100)
Other comprehensive income for the year	–	–	–	–	–	218	218	–	218
Total comprehensive income for the year	–	–	–	–	–	117	117	1	118
Issue of ordinary share capital, net of associated commissions and expenses	–	908	–	–	–	–	908	–	908
Dividends paid on ordinary shares	–	(126)	–	–	–	–	(126)	–	(126)
Coupon paid to non-controlling interests, net of tax relief	–	–	–	–	–	–	–	(1)	(1)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	7	7	–	7
Redemption of non-controlling interests	–	–	–	–	–	–	–	(6)	(6)
Elimination of non-controlling interest following loss of control	–	–	–	–	–	–	–	(564)	(564)
Shares distributed by the employee benefit trust	–	–	5	–	–	(5)	–	–	–
Shares acquired by the employee benefit trust	–	–	(7)	–	–	–	(7)	–	(7)
At 31 December 2016	–	1,643	(7)	96	4	1,597	3,333	–	3,333

STATEMENT OF CONSOLIDATED CHANGES IN EQUITY

For the year ended 31 December 2015

	Share capital (note D1) £m	Share premium £m	Shares held by the employee benefit trust (note D2) £m	Foreign currency translation reserve £m	Owner-occupied property revaluation reserve £m	Retained earnings £m	Total £m	Non-controlling interests (note D3) £m	Total £m
At 1 January 2015	–	979	(8)	103	–	1,291	2,365	913	3,278
Profit for the year	–	–	–	3	–	198	201	48	249
Other comprehensive (expense)/ income for the year	–	–	–	(10)	4	6	–	–	–
Total comprehensive (expense)/income for the year	–	–	–	(7)	4	204	201	48	249
Issue of ordinary share capital, net of associated commissions and expenses	–	2	–	–	–	–	2	–	2
Dividends paid on ordinary shares	–	(120)	–	–	–	–	(120)	–	(120)
Dividends paid to non-controlling interests	–	–	–	–	–	–	–	(23)	(23)
Coupon paid to non-controlling interests, net of tax relief	–	–	–	–	–	–	–	(15)	(15)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	4	4	–	4
Shares in subsidiaries subscribed for by non-controlling interests	–	–	–	–	–	–	–	35	35
Exchange of non-controlling interests for subordinated notes	–	–	–	–	–	–	–	(388)	(388)
Loss on exchange of non-controlling interests	–	–	–	–	–	(12)	(12)	–	(12)
Shares distributed by employee benefit trust	–	–	9	–	–	(9)	–	–	–
Shares acquired by employee benefit trust	–	–	(6)	–	–	–	(6)	–	(6)
At 31 December 2015	–	861	(5)	96	4	1,478	2,434	570	3,004

Phoenix Group Holdings is subject to Cayman Islands Companies Law. Under Cayman Islands Companies Law distributions can be made out of profits or share premium subject, in each case, to a solvency test. The solvency test is broadly consistent with the Group's going concern assessment criteria.

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

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

A. SIGNIFICANT ACCOUNTING POLICIES

A1. BASIS OF PREPARATION

The consolidated financial statements for the year ended 31 December 2016 comprise the financial statements of Phoenix Group Holdings ('the Company') and its subsidiaries (together referred to as 'the Group').

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

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'). The financial statements are presented in sterling (£) rounded to the nearest million except where otherwise stated.

Assets and liabilities are offset and the net amount reported in the statement of consolidated financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expenses are not offset in the consolidated income statement unless required or permitted by an IFRS or interpretation, as specifically disclosed in the accounting policies of the Group.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries, including collective investment schemes, where the Group exercises overall control. In accordance with the principles set out in IFRS 10 *Consolidated Financial Statements*, the Group controls an investee if and only if the Group has all the following:

- power over the investee;
- exposure, or rights, to variable returns from its involvement with the investee; and
- the ability to use its power over the investee to affect its returns.

The Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including relevant activities, substantive and protective rights, voting rights and purpose and design of an investee. The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Further details about the consolidation of subsidiaries, including collective investment schemes, is included in note H1.

A2. ACCOUNTING POLICIES

The principal accounting policies have been consistently applied in these consolidated financial statements. Where an accounting policy can be directly attributed to a specific note to the consolidated financial statements, the policy is presented within that note, with a view to enabling greater understanding of the results and financial position of the Group. All other significant accounting policies are disclosed below.

A2.1 Foreign currency transactions

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated financial statements are presented in sterling, which is the Group's presentation currency.

The results and financial position of all Group companies that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities are translated at the closing rate at the period end;
- income, expenses and cash flows denominated in foreign currencies are translated at average exchange rates; and
- all resulting exchange differences are recognised through the statement of consolidated comprehensive income.

Foreign currency transactions are translated into the functional currency of the transacting Group entity using exchange rates prevailing at the date of translation. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement.

Translation differences on debt securities and other monetary financial assets measured at fair value through profit or loss are included in foreign exchange gains and losses. Translation differences on non-monetary items at fair value through profit or loss are reported as part of the fair value gain or loss.

A3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Critical accounting estimates are those which involve the most complex or subjective judgements or assessments. The areas of the Group's business that typically require such estimates are the measurement of insurance and investment contract liabilities, determination of the fair value of financial assets and liabilities, impairment tests for intangible assets, income tax assets and liabilities, and pension scheme assets and liabilities. The determination of operating profit, identification and valuation of intangible assets and the deconsolidation of a property investment company all require management to make judgements, details of which are included below.

A3.1 Insurance and investment contract liabilities

Insurance and investment contract liability accounting is discussed in more detail in the accounting policies in note F1 with further detail of the key assumptions made in determining insurance and investment contract liabilities included in note F4.

A3.2 Fair value of financial assets and liabilities

Financial assets and liabilities are measured at fair value and accounted for as set out in the accounting policies in note E1. Where possible, financial assets and liabilities are valued on the basis of listed market prices by reference to quoted market bid prices for assets and offer prices for liabilities. These are categorised as Level 1 financial instruments and do not involve estimates. If prices are not readily determinable, fair value is determined using valuation techniques including pricing models, discounted cash flow techniques or broker quotes. Financial instruments valued where valuation techniques based on observable market data at the period end are categorised as Level 2 financial instruments. Financial instruments valued using valuation techniques based on non-observable inputs are categorised as Level 3 financial instruments. Level 2 and Level 3 financial instruments therefore involve the use of estimates. Further details of the estimates made are included in note E2.

A3.3 Impairment of intangible assets

Intangible assets are subject to regular impairment reviews as detailed in the accounting policy in note G7. Impairments are measured as the difference between the carrying value of a particular asset and its recoverable amount. Impairments are recognised in the consolidated income statement in the period in which they occur. Further details of judgements made in testing intangible assets for impairment are included in note G7.

A3.4 Income tax assets and liabilities

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. Forecasts of future profitability are made which by their nature involve management's judgement.

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.

The determination of tax provisions included in current tax liabilities involves the use of estimates and judgements.

The accounting policy for income taxes (both current and deferred) is discussed in more detail in the accounting policy in notes C5 and G2.

A3.5 Pension scheme assets and liabilities

The valuation of pension scheme assets and liabilities is determined using actuarial valuations that include a number of assumptions. As defined benefit pension schemes are long-term in nature, such assumptions are subject to significant uncertainty. Details of the key assumptions used are shown in note G6.

A3.6 Operating profit

Operating profit is the Group's non-GAAP measure of performance. The Group is required to make judgements as to the appropriate longer-term rates of investment return for the determination of operating profit, as detailed in note B2, and as to what constitutes an operating or non-operating item in accordance with the accounting policy detailed in note B1.2.

A3.7 Acquisitions

The identification and valuation of identifiable intangible assets, such as acquired in-force business or brand intangibles, arising from the Group's acquisitions requires the Group to make a number of judgements and estimates. Further details of the judgements made are included in notes G7 'Intangible assets' and H2 'Acquisitions and disposals'.

A3.8 Loss of control of investment in UK Commercial Property Trust Limited ('UKCPT')

UKCPT is a property investment company which the Group deconsolidated during the year. Judgement was applied in determining that the Group no longer controlled its investment in UKCPT. The Group's investment in UKCPT is now classified as an associate and held at fair value. Further details of the judgement made are included in note H3.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

A. SIGNIFICANT ACCOUNTING POLICIES continued

A4. ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS IN 2016

The consolidated financial statements for the year ended 31 December 2016, set out on pages 99 to 192, were authorised by the Board of Directors for issue on 17 March 2017.

In preparing the consolidated financial statements, the Group has adopted the following amendments effective from 1 January 2016:

- Annual Improvements to IFRS 2012 – 2014 cycle. The adoption of these amendments had no impact on the disclosures or amount recognised in the consolidated financial statements.
- Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38). The accounting policy for the amortisation of acquired in-force business arising on investment contracts without DPF has been updated as a result of the application of these amendments. This change has been applied prospectively from 1 January 2016. See note G7 for further details.
- Disclosure initiative (Amendments to IAS 1). The adoption of these amendments had no impact on the disclosures or amount recognised in the consolidated financial statements.

A5. NEW ACCOUNTING PRONOUNCEMENTS NOT YET EFFECTIVE

The IASB has issued the following new or amended standards and interpretations which apply from the dates shown. The Group has decided not to early adopt any of these standards, interpretations or amendments where this is permitted.

- Disclosure initiative (Amendments to IAS 7) (2017). The amendments require disclosures that enable users of the financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes.
- Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12) (2017).
- IFRS 9 *Financial Instruments* (2018). Under IFRS 9, all financial assets will be measured either at amortised cost or fair value and the basis of classification will depend on the business model and the contractual cash flow characteristics of the financial assets. The Group expects to continue to value the majority of its financial assets at fair value through profit or loss on initial recognition, so as to eliminate or reduce any potential accounting mismatch. The Group expects to take advantage of the temporary exemption granted to insurers in IFRS 4 *Insurance Contracts* from applying IFRS 9 until 1 January 2021 as a result of meeting the exemption criteria. A number of disclosures will be made as a result of applying this temporary exemption. The expected impact of applying IFRS 9 remains subject to completion of a detailed review.
- IFRS 15 *Revenue from Contracts with Customers* (2018). IFRS 15 establishes a single comprehensive framework for determining whether, how and when revenue is recognised. The standard does not apply to insurance contracts and the financial instruments within the scope of IAS 39. The Group anticipates that the application of IFRS 15 in 2018 will have limited impact on the measurement and presentation of amounts reported in the Group's financial statements.
- IFRS 16 *Leases* (2019). IFRS 16 will replace IAS 17 *Leases*. The new standard removes the classification of leases as either operating or finance leases for the lessee, thereby treating all leases as finance leases. This will result in the recognition of a right-to-use asset and a lease liability for all of the Group's previously classified operating leases. Short-term leases (less than 12 months) and leases of low-value assets are exempt from the requirements. The Group anticipates that the application of IFRS 16 in the future will have limited impact on amounts reported in the Group's financial statements as the Group has a limited number of operating leases (see note I6).
- Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2) (2018).

Where not specifically stated, the impact on the Group of adopting the above standards, amendments and interpretations is subject to evaluation.

B. EARNINGS PERFORMANCE

B1. SEGMENTAL ANALYSIS

The Group defines and presents operating segments based on the information which is provided to the Board, and therefore segmental information in this note is presented on a different basis from profit or loss in the consolidated financial statements.

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses relating to transactions with other components of the Group.

For management purposes, the Group is organised into business units based on their products and services and comprised of the Phoenix Life and Abbey Life operating segments during the reporting period. No segmental result has been shown for the Abbey Life segment as the subsidiary was acquired on 30 December 2016.

Segmental performance is evaluated based on profit or loss which, in certain respects, is presented differently from profit or loss in the consolidated financial statements. Revenues or expenses that are not directly attributable to a particular segment are allocated between segments where there is a reasonable basis for doing so.

Group financing (including finance costs) and owners' taxes are managed on a Group basis and are not allocated to individual operating segments.

Inter-segment transactions are set on an arm's length basis in a manner similar to transactions with third parties. Segmental results include those transfers between business segments which are then eliminated on consolidation.

Predominantly all revenues from external customers are sourced in the UK. No revenue transaction with a single customer external to the Group amounts to greater than 10% of the Group's revenue.

Predominantly all non-current assets are located in the UK. There are no differences between the measurement of the assets and liabilities reflected in the primary statements and that reported for the segments.

B1.1 Segmental result

2016

	Phoenix Life £m	Unallocated Group £m	Total £m
Net premiums written	924	–	924
Fees	88	–	88
Net investment income	6,357	4	6,361
Gain on transfer of business	52	–	52
Other operating income	20	–	20
Net income	7,441	4	7,445
Net policyholder claims and benefits incurred	(5,517)	–	(5,517)
Amortisation:			
Amortisation of acquired in-force business	(76)	–	(76)
Amortisation of other intangibles	(14)	–	(14)
	(90)	–	(90)
Other expenses	(1,680)	(106)	(1,786)
Total expenses	(7,287)	(106)	(7,393)
Profit/(loss) before finance costs and tax	154	(102)	52
Finance costs	(56)	(66)	(122)
Profit/(loss) before tax	98	(168)	(70)
Tax attributable to policyholders' returns	(58)	–	(58)
Segmental result before the tax attributable to owners	40	(168)	(128)

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

B. EARNINGS PERFORMANCE continued

B1. SEGMENTAL ANALYSIS continued

2015

	Phoenix Life £m	Unallocated Group £m	Total £m
Net premiums written	(474)	–	(474)
Fees	95	–	95
Net investment income	1,048	16	1,064
Other operating income	7	–	7
Net income	676	16	692
Net policyholder claims and benefits incurred	441	–	441
Amortisation and impairment:			
Amortisation and impairment of acquired in-force business	(148)	–	(148)
Amortisation of other intangibles	(15)	–	(15)
	(163)	–	(163)
Other expenses	(651)	(31)	(682)
Total expenses	(373)	(31)	(404)
Profit/(loss) before finance costs and tax	303	(15)	288
Finance costs	(60)	(76)	(136)
Profit/(loss) before tax	243	(91)	152
Tax attributable to policyholders' returns	33	–	33
Segmental result before the tax attributable to owners	276	(91)	185

B1.2 Reconciliation of operating profit to the segmental result

The Group has chosen to report a non-GAAP measure of performance being operating profit. Operating profit is considered to provide a more relevant measure of the underlying performance of the Group's business as it excludes the impact of short-term economic volatility and other one-off items. This measure incorporates an expected return, including a longer-term return on financial investments backing shareholder and policyholder funds over the period, with consistent allowance for the corresponding expected movements in liabilities. Operating profit includes the effect of variances in experience for non-economic items, such as mortality and expenses, and the effect of changes in non-economic assumptions. It also incorporates the impacts of significant management actions where such actions are consistent with the Group's core operating activities (for example, actuarial modelling enhancements and data reviews).

Impacts arising from the difference between the actual and expected experience for economic items (on both assets and liabilities) and the impacts of changes in economic assumptions on the valuation of liabilities are excluded from operating profit and are presented in profit before the tax attributable to owners (see note B2). Phoenix Life operating profit is net of policyholder finance charges and policyholder tax.

Operating profit also excludes the impact of the following items:

- amortisation and impairments of intangible assets;
- finance costs attributable to owners; and
- other non-operating items which include:
  - gains or losses on the disposal of subsidiaries, associates or joint ventures (net of related costs of disposal);
  - the financial impacts of mandatory regulatory change;
  - integration, restructuring or other significant one-off projects; and
  - any other items which, in the Directors' view, should be excluded by virtue of their nature or incidence to enable a full understanding of the Group's financial performance.

2016

	Phoenix Life £m	Unallocated Group £m	Total £m
Operating profit/(loss)	**357**	**(6)**	**351**
Investment return variances and economic assumption changes on long-term business	**(207)**	**–**	**(207)**
Variance on owners' funds	**11**	**(16)**	**(5)**
Amortisation of acquired in-force business	**(68)**	**–**	**(68)**
Amortisation of other intangibles	**(14)**	**–**	**(14)**
Other non-operating items	**(15)**	**(80)**	**(95)**
Financing costs attributable to owners	**(24)**	**(66)**	**(90)**
Segmental result before the tax attributable to owners	**40**	**(168)**	**(128)**

Other non-operating items include:

- a gain of £26 million on the implementation of a longevity swap reassurance contract on a portfolio of the Group's annuities;
- a gain of £14 million arising as a result of a premium adjustment on the 2015 reassurance arrangement with RGA International following completion of a data review;
- acquisition related costs of £31 million, comprising £12 million of transaction costs related to the acquisition of AXA Wealth's pensions and protection business and £19 million of transaction costs related to acquisition of Abbey Life (see note H2);
- a provision for costs of £30 million associated with the integration and restructuring of the acquired AXA businesses (see note G1);
- the costs of providing for claims and associated costs relating to creditor insurance underwritten prior to 2016 by a subsidiary of the Group, PA(GI) Limited ('PA(GI)'), of £33 million (see note G1);
- recognition of costs of £10 million associated with the introduction of regulations that cap early exit charges for pension customers aged over 55 at 1%, which will come into force from 2017;
- costs of £6 million associated with the transfer of non-profit annuities from with-profit funds to non-profit matching adjustment funds;
- the costs of £4 million on PGL Pension Scheme buy-in;
- other corporate project costs of £19 million; and
- net other one-off items totalling a cost of £2 million.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

B. EARNINGS PERFORMANCE continued

B1. SEGMENTAL ANALYSIS continued

2015

	Phoenix Life £m	Unallocated Group £m	Total £m
Operating profit/(loss)	336	(12)	324
Investment return variances and economic assumption changes on long-term business	13	–	13
Variance on owners' funds	(7)	(5)	(12)
Amortisation of acquired in-force business	(75)	–	(75)
Amortisation of other intangibles	(15)	–	(15)
Other non-operating items	47	2	49
Financing costs attributable to owners	(23)	(76)	(99)
Segmental result before the tax attributable to owners	276	(91)	185

Other non-operating items include:

- gain of £49 million (net of a £64 million impairment of associated acquired in-force business) arising as a result of the reassurance arrangement entered into with RGA International (see note F3.1);
- release of provisions associated with external regulatory changes, including the cap on workplace pension charges and the pension guidance levy, of £17 million;
- corporate project costs of £13 million; and
- net other one-off items (including Solvency II implementation and systems transformation costs) totalling a cost of £4 million.

B2. INVESTMENT RETURN VARIANCES AND ECONOMIC ASSUMPTION CHANGES

The long-term nature of much of the Group's operations means that, for internal performance management, the effects of short-term economic volatility are treated as non-operating items. The Group focuses instead on an operating profit measure that incorporates an expected return on investments supporting its long-term business. The accounting policy adopted in the calculation of operating profit is detailed in note B1.2. The methodology for the determination of the expected investment return is explained below together with an analysis of investment return variances and economic assumption changes recognised outside of operating profit.

B2.1 Calculation of the long-term investment return

The expected return on investments for both owner and policyholder funds is based on opening economic assumptions applied to the funds under management at the beginning of the reporting period. Expected investment return assumptions are derived actively, based on risk-free yields at the start of each financial year. In line with changes made to align assumptions and estimates used in the valuation of insurance contracts with the requirements of the Solvency II regime (see note F4.1), the assumptions used in the calculation of the long-term investment return have also been updated.

From 1 January 2016, the long-term risk-free rate used as a basis for deriving the long-term investment return is set by reference to the swap curve plus 10bps (2015: annualised return on the FTSE UK Gilt Index plus 10bps). A risk premium of 350bps is added to the risk-free yield for equities (2015: 300bps), 250bps for properties (2015: 200bps), 150bps for other fixed interest assets (2015: 100bps) and 50bps for gilts (2015: nil). If the current period long-term investment return had been calculated using a gilts plus 10bps reference rate adjusted for the relevant risk premium (as used in prior periods), the impact on operating profit for the period would be negligible.

The principal assumptions underlying the calculation of the long-term investment return are:

	2016 %	2015 %
Equities	**5.8**	5.3
Properties	**4.8**	4.3
Gilts	**2.8**	2.3
Other fixed interest	**3.8**	3.3

B2.2 Life assurance business

Operating profit for life assurance business is based on expected investment returns on financial investments backing owners' and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities. Operating profit includes the effect of variance in experience for non-economic items, for example mortality, persistency and expenses, and the effect of changes in non-economic assumptions. Changes due to economic items, for example market value movements and interest rate changes, which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed separately outside operating profit.

The movement in liabilities included in operating profit reflects both the change in liabilities due to the expected return on investments and the impact of experience variances and assumption changes for non-economic items.

The effect of differences between actual and expected economic experience on liabilities, and changes to economic assumptions used to value liabilities, are taken outside operating profit. For many types of long-term business, including unit-linked and with-profit funds, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. For other long-term business, the profit impact of economic volatility depends on the degree of matching of assets and liabilities, and exposure to financial options and guarantees.

The investment return variances and economic assumption changes excluded from the long-term business operating profit are as follows:

	2016 £m	2015 £m
Investment return variances and economic assumption changes on long-term business	**(207)**	13

Negative investment return variances and economic assumption changes on long-term business of £207 million (2015: positive £13 million) primarily resulted from the adverse impact of a fall in yields on the life funds, which has increased the margin held within insurance liabilities in respect of longevity risk. The investment return variances have also been adversely impacted by losses arising on equity hedging positions held by life funds following equity market gains in the period. Equity market gains have resulted in an unfavourable variance as the value of the hedging instruments fall without the corresponding benefit from expected future profits within the life funds being recognised. Included in the negative variance is the minority share of the result of the consolidated UKCPT property investment structure prior to its deconsolidation during the year of positive £1 million (2015: positive £46 million).

B2.3 Owners' funds

For non-long-term business including owners' funds, the total investment income, including fair value gains, is analysed between a calculated longer-term return and short-term fluctuations.

The variances excluded from operating profit in relation to owners' funds are as follows:

	2016 £m	2015 £m
Variances on owners' funds of subsidiary undertakings	**(5)**	(12)

The negative variance on owners' funds of subsidiary undertakings of £5 million (2015: £12 million) is principally driven by losses from equity hedging positions held in the Group holding companies offset by gains on interest rate hedging positions held in the life companies' shareholders' funds arising from falling yields.

B3. EARNINGS PER SHARE

The Group calculates its basic earnings per share based on the present shares in issue using the earnings attributable to ordinary equity holders of the parent, divided by the weighted average number of ordinary shares in issue during the year.

Diluted earnings per share are calculated based on the potential future shares in issue assuming the conversion of all potentially dilutive ordinary shares. The weighted average number of ordinary shares in issue is adjusted to assume conversion of dilutive share awards granted to employees and warrants.

Following the completion of the rights issue in November 2016 the earnings per share calculations, for all periods up to the date the rights issue shares were issued, have been adjusted for the bonus element of the rights issue. The bonus factor used was 1.18. Further details of the rights issue are included in note D1.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

B. EARNINGS PERFORMANCE continued

B3. EARNINGS PER SHARE continued

B3.1 Basic earnings per share

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

	2016 £m	2015 £m
(Loss)/profit for the period	(100)	249
Share of result attributable to non-controlling interests	(1)	(48)
(Loss)/profit attributable to owners of the parent	(101)	201

The weighted average number of ordinary shares outstanding during the period is calculated as detailed below:

	2016 Number million	2015 Number million
Issued ordinary shares at beginning of the period (restated for bonus element of rights issue)	266	266
Effect of ordinary shares issued	30	–
Own shares held by the employee benefit trust	(1)	(1)
Weighted average number of ordinary shares	**295**	265

Basic earnings per share is as follows:

	2016 pence	2015 pence
Basic earnings per share (restated for bonus element of rights issue)	(34.3)	76.1

B3.2 Diluted earnings per share

The result attributable to owners for the parent used in the calculation of diluted earnings per share is the same as that used in the basic earnings per share calculation in note B3.1 above. The diluted weighted average number of ordinary shares outstanding during the period is also the same as that used in the basic earnings per share calculation in note B3.1 above. As losses have an anti-dilutive effect, none of the share-based awards have a dilutive effect for the year ended 31 December 2016. The Group's deferred bonus share scheme and sharesave schemes increased the weighted average number of shares on a diluted basis by 490,276 shares for the year ended 31 December 2015.

Diluted earnings per share is as follows:

	2016 pence	2015 pence
Diluted earnings per share (restated for bonus element of rights issue)	(34.3)	76.0

5 million warrants issued on 2 September 2009 to certain entities providing finance to the Group could potentially dilute basic earnings per share in the future. The warrants have not been included in the diluted earnings per share figure because they did not have a dilutive effect for the periods presented due to the exercise price being significantly higher than the share price of the Company. Details of the warrants are given in note E3.3.

B4. DIVIDENDS

Final dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Group's owners. Interim dividends are deducted from equity when they are paid.

As permitted by Cayman Islands Companies Law, dividends have been charged within equity against the share premium account.

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.

	2016 £m	2015 £m
Dividends declared and paid in 2016	**126**	120

On 22 March 2016, the Board recommended a final dividend of 26.7p per share in respect of the year ended 31 December 2015. The dividend was approved at the Company's Annual General Meeting, which was held on 11 May 2016. The dividend amounted to £60 million and was paid on 13 May 2016.

On 24 August 2016, the Board declared an interim dividend of 26.7p per share for the half year ended 30 June 2016. The dividend amounted to £66 million and was paid on 3 October 2016.

C. OTHER INCOME STATEMENT NOTES

C1. NET INVESTMENT INCOME

Net investment income comprises interest, dividends, rents receivable, net interest income/(expense) on the net defined benefit asset/(liability), fair value gains and losses on financial assets, financial liabilities and investment property at fair value, and impairment losses on loans and receivables.

Interest income is recognised in the consolidated income statement as it accrues using the effective interest method.

Dividend income is recognised in the consolidated income statement on the date the right to receive payment is established, which in the case of listed securities is the ex-dividend date.

Rental income from investment property is recognised in the consolidated income statement on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

Fair value gains and losses on financial assets and financial liabilities designated at fair value through profit or loss are recognised in the consolidated income statement. Fair value gains and losses include both realised and unrealised gains and losses.

	2016 £m	2015 £m
Investment income		
Interest income on loans and receivables at amortised cost	**1**	3
Interest income on financial assets designated at fair value through profit or loss on initial recognition	**859**	1,076
Dividend income	**902**	911
Rental income	**38**	90
Net interest income on Group defined benefit pension scheme asset/liability	**21**	17
	1,821	2,097
Fair value gains/(losses)		
Financial assets and financial liabilities at fair value through profit or loss:		
Designated upon initial recognition	**3,236**	(1,178)
Held for trading – derivatives	**1,278**	5
Investment property	**26**	140
	4,540	(1,033)
Net investment income	**6,361**	1,064

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

C. OTHER INCOME STATEMENT NOTES continued

C2. ADMINISTRATIVE EXPENSES

Administrative expenses are recognised in the consolidated income statement as incurred.

	2016 £m	2015 £m
Employee costs	99	81
Outsourcer expenses	91	97
Professional fees	55	33
Office costs	25	23
Investment management expenses and transaction costs	129	150
Direct costs of life companies	6	15
Direct costs of collective investment schemes	11	17
PA(GI) provision (see note G1)	33	6
Pension past service costs	3	–
Pension administrative expenses	4	5
Advertising and sponsorship	7	–
Restructuring and integration costs (see note G1)	30	–
Other	13	3
	506	430

Employee costs comprise:

	2016 £m	2015 £m
Wages and salaries	90	73
Social security contributions	9	8
	99	81

	2016 Number	2015 Number
Average number of persons employed	837	750

C3. AUDITOR'S REMUNERATION

During the year the Group obtained the following services from its auditor at costs as detailed in the table below.

	2016 £m	2015 £m
Audit of the consolidated financial statements	**0.7**	0.5
Audit of the Company's subsidiaries	**3.5**	2.3
Audit of MCEV supplementary information	–	0.4
	4.2	3.2
Audit-related assurance services	**0.5**	0.9
Reporting accountant assurance services	**0.3**	0.1
Total fee for assurance services	**5.0**	4.2
Corporate finance services	**3.6**	0.1
Tax advisory services	–	0.1
Other non-audit services	**0.1**	0.3
Total fees for other services	**3.7**	0.5
Total auditor's remuneration	**8.7**	4.7

No services were provided by the Company's auditors to the Group's pension schemes in either 2016 or 2015.

Audit-related assurance services includes fees payable for services where the reporting is required by law or regulation to be provided by the auditor, such as reporting on regulatory returns. It also includes fees payable in respect of reviews of interim financial information and services where the work is integrated with the audit itself.

Reporting accountant assurance services relate to assurance reporting on historical information included within investment circulars. In 2016, this includes public reporting associated with the issuance of equity as part of the acquisition of Abbey Life and the issuance of a Medium-Term Note Programme.

Corporate finance services fees were £3.6 million (2015: £0.1 million). The increase in the year reflects services provided in connection with the acquisition of the AXA businesses and Abbey Life. £1.9 million of the fees relates to the engagement of the external auditors to perform actuarial and finance due diligence procedures where synergies were anticipated to arise with subsequent audit work. The remaining balance of £1.7 million relates to the provision of assurance services to the Board and the sponsoring banks in support of disclosures made in the public transaction documentation relating to the two acquisitions.

Other non-audit services of £0.1 million (2015: £0.3 million) primarily include fees payable in respect of assurance over aspects of the Group's Solvency II internal model. In 2015, the fees principally related to applications made to the regulator with regard to the Group's implementation of Solvency II.

Further information on auditor's remuneration and the assessment of the independence of the external auditor is set out in the Audit Committee report on page 52.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

C. OTHER INCOME STATEMENT NOTES continued

C4. FINANCE COSTS

Interest payable is recognised in the consolidated income statement as it accrues and is calculated using the effective interest method.

This note analyses the interest costs on the Group's borrowings which are described in note E5.

	2016 £m	2015 £m
Interest expense:		
On financial liabilities at amortised cost	**109**	122
On financial liabilities at fair value through profit or loss	**13**	14
	122	136
Attributable to:		
– policyholders	**32**	37
– owners	**90**	99
	122	136

C5. TAX CHARGE/(CREDIT)

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

Current tax is the expected tax payable on the taxable income for the year, using tax rates and laws enacted or substantively enacted at the date of the statement of consolidated financial position together with adjustments to tax payable in respect of previous years.

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.

C5.1 Current year tax charge/(credit)

	2016 £m	2015 £m
Current tax:		
UK corporation tax	**46**	11
Overseas tax	**15**	8
	61	19
Adjustment in respect of prior years	**(8)**	(99)
Total current tax charge/(credit)	**53**	(80)
Deferred tax:		
Origination and reversal of temporary differences	**(13)**	7
Change in the rate of UK corporation tax	**(10)**	(24)
Total deferred tax credit	**(23)**	(17)
Total tax charge/(credit)	**30**	(97)
Attributable to:		
– policyholders	**58**	(33)
– owners	**(28)**	(64)
Total tax charge/(credit)	**30**	(97)

The Group, as a proxy for policyholders in the UK, is required to pay taxes on investment income and gains each year. Accordingly, the tax credit or expense attributable to UK life assurance policyholder earnings is included in income tax expense. The tax charge/(credit) attributable to policyholder earnings was £58 million (2015: £(33) million).

C5.2 Tax charged to other comprehensive income

	2016 £m	2015 £m
Current tax credit on share schemes	**(1)**	(1)
Deferred tax charge on defined benefit schemes	**3**	5
Deferred tax on share schemes	**(1)**	1
	1	5

C5.3 Reconciliation of tax charge/(credit)

	2016 £m	2015 £m
(Loss)/profit before tax	**(70)**	152
Policyholder tax (charge)/credit	**(58)**	33
(Loss)/profit before the tax attributable to owners	**(128)**	185
Tax at standard UK[1] rate of 20% (2015: 20.25%)	**(26)**	37
Non-taxable income and gains[2]	**(10)**	(13)
Disallowable deductions[3]	**24**	6
Prior year tax credit for shareholders[4]	**(6)**	(41)
Movement on acquired in-force amortisation at less than 20%[5] (2015: 20.25%)	**2**	15
Profits taxed at rates other than 20%[6] (2015: 20.25%)	**–**	(36)
Recognition of previously unrecognised deferred tax assets[7]	**(5)**	(6)
Deferred tax rate change[8]	**(9)**	(24)
Temporary differences not valued	**–**	(1)
Other	**2**	(1)
Owners' tax credit	**(28)**	(64)
Policyholder tax charge/(credit)	**58**	(33)
Total tax charge/(credit) for the period	**30**	(97)

1 The Phoenix Life operating segment operates predominantly in the UK. The reconciliation of the tax charge/(credit) has, therefore, been completed by reference to the standard rate of UK tax rather than by reference to the Jersey income tax rate of 0% which is applicable to Phoenix Group Holdings.
2 Includes non-taxable dividends and gains and non-taxable pension scheme items.
3 Includes non-recurring disallowable deductions in relation to claims and other costs relating to creditor insurance underwritten by PA(GI) Limited of £7 million and a consolidation adjustment on the PGL Pension scheme 'buy-in' agreement of £12 million.
4 The 2015 prior year tax credit represents the impact of reaching agreement with HMRC in respect of the Group's uncertain tax positions for the years 2007 to 2014.
5 2015 included a non-recurring write off for the acquired in-force business relating to Opal Reassurance Limited ('Opal Re') of £13 million as a result of the reinsurance of annuity liabilities.
6 2015 included non-taxable profits arising in Opal Re of £23 million and UKCPT of £10 million. The 2016 element for both is de minimis.
7 Represents the recognition of losses in acquired businesses.
8 Represents the effect of the 1% reduction in the tax rate from April 2020 which was substantively enacted in the year (2015: 2% reduction).

D. EQUITY

D1. SHARE CAPITAL

The Group has issued ordinary shares which are classified as equity. Incremental external costs that are directly attributable to the issue of these shares are recognised in equity, net of tax.

	2016 £	2015 £
Authorised:		
410 million (2015: 410 million) ordinary shares of €0.0001 each	**31,750**	31,750
Issued and fully paid:		
392.8 million (2015: 225.4 million) ordinary shares of €0.0001 each	**33,112**	18,463

The value of the authorised share capital was translated at a historical rate. Issued and fully paid share capital transactions are translated at the rate prevailing at the date of issue.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

D. EQUITY continued

D1. SHARE CAPITAL continued

The holders of ordinary shares are entitled to one vote per share on matters to be voted on by owners and to receive such dividends, if any, as may be declared by the Board of Directors in its discretion out of legally available profits. Movements in issued share capital during the year:

2016

	Number	£
Shares in issue at 1 January	**225,419,446**	**18,463**
Placement of ordinary shares	**22,542,000**	**1,748**
Ordinary shares issued under the rights issue	**144,727,282**	**12,888**
Other ordinary shares issued in the period	**161,089**	**13**
Shares in issue at 31 December	**392,849,817**	**33,112**

On 1 June 2016, the Group completed an equity placing of 22,542,000 new ordinary shares in association with the proposed acquisition of the AXA businesses (see note H2) which raised gross proceeds of £194 million. The proceeds from the equity placing, net of deduction of commissions and expenses, were £190 million.

On 9 November 2016, the Group issued 144,727,282 shares following a rights issue undertaken in connection with the proposed acquisition of Abbey Life, where 7 rights issue shares were issued at 508 pence per share for every 12 existing Phoenix Group Holdings shares held. The rights issue raised gross proceeds of £735 million and proceeds, net of deduction of commission and expenses, were £717 million.

During the year, the Company issued 161,089 shares at a premium of £1 million in order to satisfy its obligations to employees under the Group's sharesave schemes (see note I2).

2015

	Number	£
Shares in issue at 1 January	225,090,284	18,439
Other ordinary shares issued in the period	329,162	24
Shares in issue at 31 December	225,419,446	18,463

During 2015, the Company issued 329,162 shares at a premium of £2 million in order to satisfy its obligations to employees under the Group's sharesave schemes.

D2. SHARES HELD BY THE EMPLOYEE BENEFIT TRUST

Where the Phoenix Group Holdings Employee Benefit Trust ('PGH EBT') acquires shares in the Company or obtains rights to purchase its shares, the consideration paid (including any attributable transaction costs, net of tax) is shown as a deduction from owners' equity. Gains and losses on sales of shares held by the PGH EBT are charged or credited to the own shares account in equity.

The PGH EBT holds shares to satisfy awards granted to employees under the Group's share-based payment schemes.

	2016 £m	2015 £m
At 1 January	**5**	8
Shares acquired by the PGH EBT in year	**7**	6
Shares awarded to employees by the PGH EBT in year	**(5)**	(9)
At 31 December	**7**	5

During the year 690,711 (2015: 1,398,290) shares were awarded to employees by the PGH EBT and 1,196,011 (2015: 735,068) shares were purchased. The number of shares held by the PGH EBT at 31 December 2016 was 1,092,634 (2015: 587,334).

The Company provides the PGH EBT with an interest-free facility arrangement to enable it to purchase the shares. Details of this loan are included in note 9 to the parent company financial statements.

D3. NON-CONTROLLING INTERESTS

Non-controlling interests are stated at the share of net assets attributed to the non-controlling interest holder at the time of acquisition, adjusted for the relevant share of subsequent changes in equity.

2016

	Perpetual Reset Capital Securities £m	UK Commercial Property Trust Limited £m	Total £m
At 1 January	**7**	**563**	**570**
Profit for the year	**–**	**1**	**1**
Coupon paid, net of tax relief	**(1)**	**–**	**(1)**
Redemption of Notes	**(6)**	**–**	**(6)**
Derecognition of non-controlling interest following loss of control	**–**	**(564)**	**(564)**
At 31 December	**–**	**–**	**–**

2015

	Perpetual Reset Capital Securities £m	UK Commercial Property Trust Limited £m	Total £m
At 1 January	408	505	913
Profit for the year	2	46	48
Dividends paid	–	(23)	(23)
Coupon paid, net of tax relief	(15)	–	(15)
Exchange of Notes for subordinated notes	(388)	–	(388)
Shares in subsidiaries subscribed for by non-controlling interests	–	35	35
At 31 December	7	563	570

D3.1 Perpetual Reset Capital Securities

On 1 January 2010, Pearl Group Holdings (No.1) Limited ('PGH1') had in issue £500 million of Perpetual Reset Capital Securities ('the Notes'). Following amendments made to the Notes during 2010, the aggregate amount payable on redemption of the Notes was £425 million. On 23 January 2015, the Group exchanged 99% of the Notes for £428 million of new subordinated notes, issued by PGH Capital plc, and £3 million of cash. £32 million of the new notes were held by Group companies. The exchange resulted in a loss of £12 million which was recognised in equity. On 23 January 2015, the coupon that was due on the Notes was settled with the noteholders that exchanged their Notes. On 25 April 2015, the 2015 coupon was settled in full with the remaining noteholders.

On 25 April 2016 the coupon that was due on the remaining Notes was settled and PGH1 redeemed the remaining £6 million of Notes at par.

D3.2 UK Commercial Property Trust Limited

UK Commercial Property Trust Limited ('UKCPT') is a property investment company which is domiciled in Guernsey and is admitted to the Official List of the UK Listing Authority and to trading on the London Stock Exchange. In February 2016, the Group reduced its holdings to 48.9% (2015: 50.0%) of the issued share capital of UKCPT. The Group deems that it no longer exercises control over UKCPT and as a result UKCPT has been deconsolidated from the effective date of this loss of control. The Group's remaining interest in UKCPT is recognised as an associate and held at fair value (see note H3 for further details).

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES
E1. FAIR VALUES

Financial assets

Purchases and sales of financial assets are recognised on the trade date, which is the date that the Group commits to purchase or sell the asset.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. For the majority of the Group's loans and receivables 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. The Group holds a portfolio of loans that are designated at fair value through profit or loss.

Derivative financial instruments are classified as held for trading. They are recognised initially at fair value and subsequently are remeasured to fair value. The gain or loss on remeasurement to fair value is recognised in the consolidated income statement.

Equities, fixed and variable rate income securities, collective investment schemes and certain loans and receivables are designated at fair value through profit or loss and accordingly are stated in the statement of consolidated financial position at fair value. They are designated at fair value through profit or loss because this is reflective of the manner in which the financial assets are managed and reduces a measurement inconsistency that would otherwise arise with regard to the insurance liabilities that the assets are backing.

Reinsurers share of investment contracts liabilities without DPF are valued on a basis consistent with investment contracts liabilities without DPF as detailed under Financial liabilities below.

Impairment of financial assets

The Group assesses at each period end whether a financial asset or group of financial assets held at amortised cost is impaired. The Group first assesses whether objective evidence of impairment exists. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be recognised, are not included in the collective assessment of impairment.

Fair value estimation

The fair value of financial instruments traded in active markets such as publicly traded securities and derivatives is based on quoted market prices at the period end. The quoted market price used for financial assets is the applicable bid price on the period end date. The fair value of investments that are not traded in an active market is determined using valuation techniques such as broker quotes, pricing models or discounted cash flow techniques. Where pricing models are used, inputs are based on market-related data at the period end. Where discounted cash flow techniques are used, estimated future cash flows are based on contractual cash flows using current market conditions and market-calibrated discount rates and interest rate assumptions for similar instruments.

For units in unit trusts and shares in open-ended investment companies, fair value is determined by reference to published bid-values. The fair value of receivables and floating rate and overnight deposits with credit institutions is their carrying value. The fair value of fixed interest-bearing deposits is estimated using discounted cash flow techniques.

Associates

Investments in associates that are held for investment purposes are accounted for under IAS 39 *Financial Instruments: Recognition and Measurement* as permitted by IAS 28 *Investments in Associates and Joint Ventures*. These are measured at fair value through profit or loss. There are no investment in associates which are of a strategic nature.

Joint ventures

Investments in joint ventures that are held for investment purposes are accounted for under IAS 39 *Financial Instruments: Recognition and Measurement* as permitted by IAS 28 *Investments in Associates and Joint Ventures*. These are measured at fair value through profit or loss. There are no investments in joint ventures which are of a strategic nature.

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 without DPF 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 and where doing so results in more meaningful information because either:

- it eliminates or significantly reduces accounting mismatches that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or
- a group of financial assets, financial liabilities or both is managed and its performance is evaluated and managed on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the investments is provided internally on that basis to the Group's key management personnel.

Investment contracts without DPF

Contracts under which the transfer of insurance risk to the Group from the policyholder is not significant are classified as investment contracts and accounted for as financial liabilities.

Receipts and payments on investment contracts without DPF are accounted for using deposit accounting, under which the amounts collected and paid out are recognised in the statement of consolidated financial position as an adjustment to the liability to the policyholder.

The valuation of liabilities on unit-linked contracts is held at the fair value of the related assets and liabilities. The liability is the sum of the unit-linked liabilities plus an additional amount to cover the present value of the excess of future policy costs over future charges.

Movements in the fair value of investment contracts without DPF are included in the 'change in investment contract liabilities' in the consolidated income statement.

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.

Deposits from reinsurers

It is the Group's practice to obtain collateral to cover certain reinsurance transactions, usually in the form of cash or marketable securities. Where cash collateral is available to the Group for investment purposes, it is recognised as a 'financial asset' and the collateral repayable is recognised as 'deposits received from reinsurers' in the statement of consolidated financial position.

Net asset value attributable to unitholders

The net asset value attributable to unitholders represents the non-controlling interest in collective investment schemes which are consolidated by the Group. This interest is classified at fair value through profit or loss and measured at fair value, which is equal to the bid value of the number of units of the collective investment scheme not owned by the Group.

Obligations for repayment of collateral received

It is the Group's practice to obtain collateral in stock lending and derivative transactions, usually in the form of cash or marketable securities. Where cash collateral is available to the Group for investment purposes, it is recognised as a 'financial asset' and the collateral repayable is recognised as 'obligations for repayment of collateral received' in the statement of consolidated financial position. The 'obligations for repayment of collateral received' are measured at amortised cost, which in the case of cash is equivalent to the fair value of the consideration received.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E1. FAIR VALUES continued

The table below sets out a comparison of the carrying amounts and fair values of financial instruments as at 31 December 2016:

2016

	Carrying value		
	Total £m	Amounts due for settlement after 12 months £m	Fair value £m
Financial assets measured at carrying and fair values			
Financial assets at fair value through profit or loss:			
Held for trading – derivatives	3,003	2,909	3,003
Designated upon initial recognition:			
Loans and receivables	812	789	812
Equities[1]	17,759	–	17,759
Investment in associate[1] (see note H3)	525	–	525
Fixed and variable rate income securities	29,290	26,408	29,290
Collective investment schemes[1]	18,432	–	18,432
Reinsurers' share of investment contract liabilities[1]	6,808	–	6,808
Loans and receivables at amortised cost	420	14	420
Total financial assets[2]	77,049		77,049

	Carrying value		
	Total £m	Amounts due for settlement after 12 months £m	Fair value £m
Financial liabilities measured at carrying and fair values			
Financial liabilities at fair value through profit or loss:			
Held for trading – derivatives	1,567	1,482	1,567
Designated upon initial recognition:			
Borrowings	270	270	270
Net asset value attributable to unitholders[1]	1,040	–	1,040
Investment contract liabilities[1]	27,332	–	27,332
Financial liabilities measured at amortised cost:			
Borrowings	1,766	1,735	1,879
Deposits received from reinsurers	392	363	392
Obligations for repayment of collateral received[3]	1,623	–	–
Total financial liabilities	33,990		32,480

1 These assets and liabilities have no expected settlement date.
2 Total financial assets includes £1,196 million of assets held in a collateral account pertaining to the PGL pension scheme buy-in agreement. See note G6.2 for further details.
3 These liabilities have no expected settlement date. As the obligations relate to the repayment of collateral received in the form of cash, the liability is stated at the value of the consideration received and therefore no fair value has been disclosed.

2015

	Carrying value		
	Total £m	Amounts due for settlement after 12 months £m	Fair value £m
Financial assets measured at carrying and fair values			
Financial assets at fair value through profit or loss:			
Held for trading – derivatives	1,498	1,335	1,498
Designated upon initial recognition:			
Loans and receivables	268	245	268
Equities[1]	12,351	–	12,351
Investment in joint venture[1]	149	–	149
Fixed and variable rate income securities	31,814	24,176	31,814
Collective investment schemes[1]	3,826	–	3,826
Loans and receivables at amortised cost	309	24	309
	50,215		50,215
Less amounts classified as held for sale (see note I1)	(149)	–	(149)
Total financial assets	50,066		50,066

	Carrying value		
	Total £m	Amounts due for settlement after 12 months £m	Fair value £m
Financial liabilities measured at carrying and fair values			
Financial liabilities at fair value through profit or loss:			
Held for trading – derivatives	1,360	1,255	1,360
Designated upon initial recognition:			
Borrowings	194	194	194
Net asset value attributable to unitholders[1]	5,120	–	5,120
Investment contract liabilities[1]	7,905	–	7,905
Financial liabilities measured at amortised cost:			
Borrowings	1,804	1,772	1,907
Deposits received from reinsurers	378	347	378
Obligations for repayment of collateral received[2]	725	–	–
Total financial liabilities	17,486		16,864

Fair value hierarchy information for non-financial assets measured at fair value is included in note G8 for property held at valuation and in note G9 for investment property.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E2. FAIR VALUE HIERARCHY

E2.1 Determination of fair value and fair value hierarchy of financial instruments

Level 1 financial instruments

The fair value of financial instruments traded in active markets (such as exchange traded securities and derivatives) is based on quoted market prices at the period end provided by recognised pricing services. Market depth and bid-ask spreads are used to corroborate whether an active market exists for an instrument. Greater depth and narrower bid-ask spread indicate higher liquidity in the instrument and are classed as Level 1 inputs. For collective investment schemes, fair value is by reference to published bid prices.

Level 2 financial instruments

Financial instruments traded in active markets with less depth or wider bid-ask spreads which do not meet the classification as Level 1 inputs are classified as Level 2. The fair values of financial instruments not traded in active markets are determined using broker quotes or valuation techniques with observable market inputs. Financial instruments valued using broker quotes are classified at Level 2, only where there is a sufficient range of available quotes. The fair value of unquoted equities, over the counter derivatives, loans and deposits, and collective investment schemes, where published bid prices are not available, are estimated using 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 flows are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market-related rate for a similar instrument.

Level 3 financial instruments

The Group's financial instruments determined by valuation techniques using non-observable market inputs are based on a combination of independent third party evidence and internally developed models. In relation to investments in hedge funds and private equity investments, non-observable third party evidence in the form of net asset valuation statements are used as the basis for the valuation. Adjustments may be made to the net asset valuation where other evidence, for example recent sales of the underlying investments in the fund, indicates this is required. Securities that are valued using broker quotes which could not be corroborated across a sufficient range of quotes are considered as Level 3. For a small number of investment vehicles and debt securities, standard valuation models are used, as due to their nature and complexity they have no external market. Inputs into such models are based on observable market data where applicable. The fair value of loans, derivatives and some borrowings with no external market is determined by internally developed discounted cash flow models using appropriate assumptions corroborated with external market data where possible.

For financial instruments that are recognised at fair value on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the start of each reporting period.

E2.2 Fair value hierarchy of financial instruments

The tables below separately identify financial instruments carried at fair value from those measured on another basis but for which fair value is disclosed.

2016

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial assets measured at fair value				
Derivatives	74	2,876	53	3,003
Financial assets designated at fair value through profit or loss upon initial recognition:				
Loans and receivables	–	–	812	812
Equities	17,078	10	671	17,759
Investment in associate	525	–	–	525
Fixed and variable rate income securities	17,282	11,862	146	29,290
Collective investment schemes	13,548	4,795	89	18,432
Reinsurers' share of investment contract liabilities	–	6,808	–	6,808
	48,433	23,475	1,718	73,626
Total financial assets measured at fair value	48,507	26,351	1,771	76,629
Financial assets for which fair values are disclosed				
Loans and receivables at amortised cost	–	420	–	420
	48,507	26,771	1,771	77,049

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial liabilities measured at fair value				
Derivatives	25	1,270	272	1,567
Financial liabilities designated at fair value through profit or loss upon initial recognition:				
Borrowings	–	–	270	270
Net asset value attributable to unitholders	1,040	–	–	1,040
Investment contract liabilities	–	27,332	–	27,332
	1,040	27,332	270	28,642
Total financial liabilities measured at fair value	1,065	28,602	542	30,209
Financial liabilities for which fair values are disclosed				
Borrowings at amortised cost	–	748	1,131	1,879
Deposits received from reinsurers	–	392	–	392
Total financial liabilities for which fair values are disclosed	–	1,140	1,131	2,271
	1,065	29,742	1,673	32,480

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E2. FAIR VALUE HIERARCHY continued

2015

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial assets measured at fair value				
Derivatives	14	1,484	–	1,498
Financial assets designated at fair value through profit or loss upon initial recognition:				
Loans and receivables	–	–	268	268
Equities	11,734	11	606	12,351
Investment in joint venture	–	–	149	149
Fixed and variable rate income securities	20,346	11,138	330	31,814
Collective investment schemes	3,098	646	82	3,826
	35,178	11,795	1,435	48,408
Less amounts classified as held for sale (see note I1)	–	–	(149)	(149)
Total financial assets measured at fair value	35,192	13,279	1,286	49,757
Financial assets for which fair values are disclosed				
Loans and receivables at amortised cost	–	309	–	309
	35,192	13,588	1,286	50,066

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial liabilities measured at fair value				
Derivatives	33	1,327	–	1,360
Financial liabilities designated at fair value through profit or loss upon initial recognition:				
Borrowings	–	–	194	194
Net asset value attributable to unitholders	5,120	–	–	5,120
Investment contract liabilities	–	7,905	–	7,905
	5,120	7,905	194	13,219
Total financial liabilities measured at fair value	5,153	9,232	194	14,579
Financial liabilities for which fair values are disclosed				
Borrowings at amortised cost	–	970	937	1,907
Deposits received from reinsurers	–	378	–	378
Total financial liabilities for which fair values are disclosed	–	1,348	937	2,285
	5,153	10,580	1,131	16,864

E2.3 Level 3 financial instrument sensitivities

Level 3 investments in indirect property, equities (including private equity) and collective investment schemes (including 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 investments, with the exception of a property investment structure and certain local authority loans, 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.

Level 3 investments in equities and fixed and variable rate income securities include equity and debt holdings in a property investment structure with a value of £22 million (2015: £22 million) and £22 million (2015: £14 million) respectively.

The investment included within equities is valued based on its listed market price adjusted for a discount spread to reflect reduced liquidity. The fair value of the debt in the structure is valued using a calculation model that takes a comparable overseas bond issue and applies a credit spread to reflect reduced liquidity.

The valuation of the equity investment is sensitive to changes in the equity discount spread, whereby an increase of 5% in the discount spread would decrease the value by £2 million (2015: £2 million) and a 5% reduction would increase the value by £1 million (2015: £1 million). The valuation of the debt investment is sensitive to a change in the credit spread whereby an increase of 100bps in the credit spread would decrease the value by £1 million (2015: £1 million) and a spread reduction of 100bps would increase the value by £1 million (2015: £1 million).

Also included within fixed and variable rate income securities are investments in local authority loans. These investments are valued using a calculation model that takes a comparable UK Treasury stock and applies a credit spread to reflect reduced liquidity. The credit spread is derived from a sample broker quote. The valuations are sensitive to movements in this spread, an increase of 25bps would decrease the value by £1 million (2015: £1 million) and a decrease of 25bps would increase the value by £nil (2015: £1 million).

Included within loans and receivables are investments in equity release mortgages with a value of £433 million (2015: £268 million). The loans are valued using a discounted cash flow model, the key inputs to which include demographic assumptions, economic assumptions (including house price index) and the use of a Black-Scholes model for valuation of the no-negative equity guarantee. The no-negative equity guarantee caps the loan repayment in the event of death or entry into long-term care to be no greater than the sales proceeds from the property. The significant sensitivities arise from movements in the yield curve, inflation rate and house prices.

An increase of 100bps in the yield curve would decrease the value by £42 million (2015: £22 million) and a decrease of 100bps would increase the value by £47 million (2015: £25 million). An increase of 1% in the inflation rate would increase the value by £3 million (2015: £2 million) and a decrease of 1% would decrease the value by £4 million (2015: £3 million). An increase of 10% in house prices would increase the value by £1 million (2015: £1 million) and a decrease of 10% would decrease the value by £2 million (2015: £1 million).

Included within borrowings measured at fair value and categorised as Level 3 financial liabilities are property reversion loans with a value of £183 million, measured using an internally developed model. The valuation is sensitive to key assumptions of the discount rate and the house price inflation rate. An increase in the discount rate of 1% would decrease the value by £5 million (2015: £5 million) and a decrease of 1% would increase the value by £5 million (2015: £5 million). An increase of 1% in the house price inflation rate would increase the value by £6 million (2015: £6 million) and a decrease of 1% would decrease the value by £6 million (2015: £6 million).

Included within financial assets and liabilities are related loans and receivables of £380 million, borrowings of £87 million and derivative liabilities of £255 million pertaining to a reinsurance and retrocession arrangement assumed following the acquisition of Abbey Life (see note E3.2). These assets and liabilities are valued using a discounted cash flow model that includes valuation adjustments in respect of liquidity and credit risk. At 31 December 2016, the net of these balances was an asset of £38 million (2015: £nil). The valuation is sensitive to movements in the euro interest rate swap curve.

An increase of 100bps in the swap curve would decrease the aggregate value by £4 million and a decrease of 100bps would increase the aggregate value by £4 million.

Also included within derivative assets and derivative liabilities are longevity swap contracts with corporate pension schemes assumed following the acquisition of Abbey Life with a fair value of £53 million and £17 million respectively (see note E3.2). These derivatives are valued on a discounted cash flow basis, key inputs to which are the overnight interest swap curve and RPI and CPI inflation rates.

An increase of 100bps in the swap curve would decrease the value by £10 million and a decrease of 100bps would increase the value by £10 million.

An increase of 1% in the RPI and CPI inflation rates would increase the value by £5 million and a decrease of 1% would decrease the value by £5 million.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E2. FAIR VALUE HIERARCHY continued

E2.4 Transfers of financial instruments between Level 1 and Level 2

2016

	From Level 1 to Level 2 £m	From Level 2 to Level 1 £m
Financial assets measured at fair value		
Financial assets designated at fair value through profit or loss upon initial recognition:		
Fixed and variable rate income securities	**155**	**153**

2015

	From Level 1 to Level 2 £m	From Level 2 to Level 1 £m
Financial assets measured at fair value		
Financial assets designated at fair value through profit or loss upon initial recognition:		
Fixed and variable rate income securities	173	210

Consistent with the prior year, all the Group's Level 1 and Level 2 assets have been valued using standard market pricing sources.

The application of the Group's fair value hierarchy classification methodology at an individual security level, in particular observations with regard to measures of market depth and bid-ask spreads, resulted in an overall net movement of financial assets from Level 1 to Level 2 in the current period and a net movement of financial assets from Level 2 to Level 1 in the comparative period.

E2.5 Movement in Level 3 financial instruments measured at fair value

2016

	At 1 January 2016 £m	Net gains/ (losses) in income £m	Effect of acquisitions/ purchases £m	Sales £m	Transfers from Level 1 and Level 2 £m	Transfers to Level 1 and Level 2 £m	At 31 December 2016 £m	Unrealised gains on assets held at end of period £m
Financial assets								
Derivatives	–	–	53	–	–	–	53	–
Financial assets designated at fair value through profit or loss upon initial recognition:								
Loans and receivables	268	31	536	(23)	–	–	812	31
Equities	606	89	83	(106)	1	(2)	671	91
Investment in joint venture	149	–	–	(149)	–	–	–	–
Fixed and variable rate income securities	330	(2)	20	(209)	31	(24)	146	7
Collective investment schemes	82	11	8	(12)	–	–	89	7
	1,435	129	647	(499)	32	(26)	1,718	136
Less amounts classified as held for sale (see note I1)	(149)	–	–	149	–	–	–	–
	1,286	129	700	(349)	32	(26)	1,771	136

	At 1 January 2016 £m	Net losses in income £m	Effect of acquisitions £m	Repayments £m	Transfers from Level 1 and Level 2 £m	Transfers to Level 1 and Level 2 £m	At 31 December 2016 £m	Unrealised losses on liabilities held at end of period £m
Financial liabilities								
Derivatives	**–**	**–**	**272**	**–**	**–**	**–**	**272**	**–**
Financial liabilities designated at fair value through profit or loss upon initial recognition:								
Borrowings	**194**	**15**	**87**	**(26)**	**–**	**–**	**270**	**15**
	194	**15**	**359**	**(26)**	**–**	**–**	**542**	**15**

2015

	At 1 January 2015 £m	Net (losses)/gains in income statement £m	Purchases £m	Sales £m	Transfers from Level 1 and Level 2 £m	Transfers to Level 1 and Level 2 £m	At 31 December 2015 £m	Unrealised (losses)/gains on assets held at end of period £m
Financial assets								
Financial assets designated at fair value through profit or loss upon initial recognition:								
Loans and receivables	–	(15)	298	(15)	–	–	268	(12)
Equities	704	(26)	79	(152)	4	(3)	606	(9)
Investment in joint venture	133	16	–	–	–	–	149	16
Fixed and variable rate income securities	735	(34)	378	(724)	–	(25)	330	(26)
Collective investment schemes	81	10	28	(37)	–	–	82	5
	1,653	(49)	783	(928)	4	(28)	1,435	(26)
Less amounts classified as held for sale (see note I1)	(133)	(16)	–	–	–	–	(149)	–
	1,520	(65)	783	(928)	4	(28)	1,286	(26)

	At 1 January 2015 £m	Net losses in income statement £m	Purchases £m	Repayments £m	Transfers from Level 1 and Level 2 £m	Transfers to Level 1 and Level 2 £m	At 31 December 2015 £m	Unrealised losses on liabilities held at end of period £m
Financial liabilities								
Derivatives	1	–	–	–	–	(1)	–	–
Financial liabilities designated at fair value through profit or loss upon initial recognition:								
Borrowings	184	37	–	(27)	–	–	194	37
	185	37	–	(27)	–	(1)	194	37

Updates to the Group's observations with regard to measures of market depth, bid-ask spreads and the extent to which inputs to the valuation of fixed and variable rate income securities are market observable resulted in a net transfer of financial assets from Level 1 and 2 to Level 3 for the current period and a net transfer of financial assets from Level 3 to Level 1 and 2 in the comparative period.

Gains and losses on Level 3 financial instruments are included in net investment income in the consolidated income statement. There were no gains or losses recognised in other comprehensive income in either the current or comparative periods.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E3. DERIVATIVES

The Group purchases derivative financial instruments principally 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 Group does not typically hold derivatives for the purpose of selling or repurchasing in the near term or with the objective of generating a profit from short-term fluctuations in price or margin.

Derivative financial instruments are classified as held for trading. They are recognised initially at fair value and subsequently are remeasured to fair value. The gain or loss on remeasurement to fair value is recognised in the consolidated income statement.

E3.1 Summary

The fair values of derivative financial instruments are as follows:

	Assets 2016 £m	**Liabilities 2016 £m**	Assets 2015 £m	Liabilities 2015 £m
Forward currency	**24**	**83**	35	94
Credit default options	**4**	**9**	3	8
Contract for differences	**1**	**–**	8	6
Interest rate swaps	**2,437**	**1,160**	1,046	1,197
Total return bond swaps	**21**	**–**	–	–
Swaptions	**364**	**–**	265	–
Inflation swaps	**19**	**14**	13	22
Equity options	**64**	**3**	115	–
Stock index futures	**7**	**20**	12	27
Fixed income futures	**8**	**6**	1	2
Retrocession contracts	**–**	**255**	–	–
Longevity swap contracts	**53**	**17**	–	–
Currency futures	**1**	**–**	–	4
	3,003	**1,567**	1,498	1,360

E3.2 Corporate transactions

Abbey Life, a Group entity, has in place longevity swap arrangements with corporate pension schemes which do not meet the definition of insurance contracts under the Group's accounting policies and are therefore recognised as derivative financial instruments. Under these arrangements the majority of the longevity risk has been passed to third parties. Derivative assets of £53 million and derivative liabilities of £17 million have been recognised as at 31 December 2016 (2015: both £nil).

In addition, Abbey Life has entered into a transaction under which it has accepted reinsurance on a portfolio of single and regular premium life insurance policies and retroceded the majority of the insurance risk. Taken as a whole, this transaction does not give rise to the transfer of significant insurance risk to the Group and therefore does not meet the definition of an insurance contract under the Group's accounting policies. The fair value of amounts due from the cedant are recognised within loans and receivables. The fair value of amounts due to the retrocessionaire are recognised as a derivative liability and totalled £255 million at 31 December 2016 (2015: £nil). A loan liability has been recognised in respect of financing obtained for the initial reinsurance premium (see note E5).

E3.3 Warrants over shares

Lenders' warrants

On 2 September 2009, the Company issued 5 million warrants over its shares to the Lenders. These warrants entitled the holder to purchase one 'B' ordinary share at a price of £15 per share, subject to adjustment. Following the achievement of the Company's Premium Listing on 5 July 2010, the lenders' warrants relate to ordinary shares rather than 'B' ordinary shares. At 31 December 2016 the terms of lenders' warrants entitled the holders to purchase 1.027873 (2015: 1.027873) ordinary shares per lenders' warrant for an exercise price of £14.59 (2015: £14.59).

The exercise period terminates on the first to occur of:

- 15th anniversary of the date issued;
- date fixed for the redemption of the warrants; and
- liquidation of the Company.

All outstanding lenders' warrants may be redeemed at the option of the Company at any time after they become exercisable and prior to their expiration at a price of €0.01 per warrant provided that the last closing bid price of the ordinary shares is equal to or exceeds £18.97 (2015: £18.97) on each of 20 consecutive trading days. The Company must give not less than 30 days' notice of the redemption date. Each warrant may then be exercised by the warrant holder (in whole or any part) at its option.

The holders are entitled to exercise their warrants for cash, assignment of an amount of outstanding principal/accrued interest of any Global Debt (i.e. any debt owed to the registered holder by any Group company) or on a cashless basis where the Company redeems the warrants. Any warrant either not exercised or tendered back to the Company by the redemption date shall be cancelled on the books of the Company and have no further value except for the €0.01 redemption price.

These lenders' warrants are not traded in an active market and have therefore been valued using an extended Black-Scholes valuation model to capture the embedded barrier feature. The key assumptions used to ascertain a value as at 31 December 2016 are:

- the share price as at 31 December 2016 of £7.35;
- volatility of 25%;
- the warrants are not adjusted for dividends; and
- the valuation incorporates the impact of amending some of the terms of the warrants on 8 May 2012.

The value of the warrants at the year-end was £143,000 (2015: £100,000).

E4. COLLATERAL ARRANGEMENTS

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

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

Non-cash collateral pledged where the Group retains the contractual rights to receive the cash flows generated is not derecognised from the statement of consolidated financial position, unless the Group defaults on its obligations under the relevant agreement. Cash collateral pledged, where the counterparty has contractual rights to receive the cash flows generated, is derecognised from the statement of consolidated financial position and a corresponding receivable is recognised for its return.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E4. COLLATERAL ARRANGEMENTS continued

E4.1 Financial instrument collateral arrangements

The Group has no financial assets and financial liabilities that have been offset in the statement of consolidated financial position as at 31 December 2016 (2015: none).

The table below contains disclosures related to financial assets and financial liabilities recognised in the statement of consolidated financial position that are subject to enforceable master netting arrangements or similar agreements. Such agreements do not meet the criteria for offsetting in the statement of consolidated financial position as the Group has no current legally enforceable right to offset recognised financial instruments. Furthermore, certain related assets received as collateral under the netting arrangements will not be recognised in the statement of consolidated financial position as the Group does not have permission to sell or re-pledge, except in the case of default. Details of the Group's collateral arrangements in respect of these recognised assets and liabilities are provided below.

2016

		Related amounts not offset			
Financial assets	Gross and net amounts of recognised financial assets £m	Financial instruments received £m	Cash collateral received £m	Derivative liabilities £m	Net amount £m
OTC derivatives	2,927	820	1,628	683	(204)
Exchange traded derivatives	76	–	–	4	72
Stock lending	446	474	–	–	(28)
Total	3,449	1,294	1,628	687	(160)

		Related amounts not offset			
Financial liabilities	Gross and net amounts of recognised financial liabilities £m	Financial instruments pledged £m	Cash collateral pledged £m	Derivative assets £m	Net amount £m
OTC derivatives	1,543	420	205	683	235
Exchange traded derivatives	24	–	16	4	4
Total	1,567	420	221	687	239

2015

		Related amounts not offset			
Financial assets	Gross and net amounts of recognised financial assets £m	Financial instruments received £m	Cash collateral received £m	Derivative liabilities £m	Net amount £m
OTC derivatives	1,483	259	725	447	52
Exchange traded derivatives	15	–	–	4	11
Stock lending	254	272	–	–	(18)
Total	1,752	531	725	451	45

Financial liabilities	Gross and net amounts of recognised financial liabilities £m	Related amounts not offset: Financial instruments pledged £m	Related amounts not offset: Cash collateral pledged £m	Related amounts not offset: Derivative assets £m	Net amount £m
OTC derivatives	1,325	455	283	447	140
Exchange traded derivatives	35	–	19	4	12
Total	1,360	455	302	451	152

E4.2 Derivative collateral arrangements

Assets accepted

It is the Group's practice to obtain collateral to mitigate the counterparty risk related to over-the-counter ('OTC') derivatives usually in the form of cash or marketable financial instruments.

The fair value of financial assets accepted as collateral for OTC derivatives but not recognised in the statement of consolidated financial position amounts to £820 million (2015: £259 million).

The amounts recognised as financial assets and liabilities from cash collateral received at 31 December 2016 are set out below.

	OTC derivatives 2016 £m	OTC derivatives 2015 £m
Financial assets	**1,628**	725
Financial liability	**(1,628)**	(725)

The maximum exposure to credit risk in respect of OTC derivative assets is £2,927 million (2015: £1,483 million) of which credit risk of £2,733 million (2015: £1,408 million) is mitigated by use of collateral arrangements (which are settled net after taking account of any OTC derivative liabilities owed to the counterparty).

Credit risk on exchange traded derivative assets of £76 million (2015: £15 million) is mitigated through regular margining and the protection offered by the exchange.

Assets pledged

The Group pledges collateral in respect of its OTC derivative liabilities. The value of assets pledged at 31 December 2016 in respect of OTC derivative liabilities of £1,543 million (2015: £1,325 million) amounted to £625 million (2015: £738 million).

E4.3 Stock lending collateral arrangements

Abbey Life, a Group company, and certain of the Group's consolidated collective investment schemes lend financial assets held in their investment portfolios to other institutions.

The Group conducts stock lending with only well-established, reputable institutions in accordance with established market conventions. The financial assets do not qualify for derecognition as the Group retains all the risks and rewards of the transferred assets except for the voting rights.

It is the Group's practice to obtain collateral in stock lending transactions, usually in the form of cash or marketable financial instruments.

The fair value of financial assets accepted as such collateral but not recognised in the statement of consolidated financial position amounts to £474 million (2015: £272 million).

The maximum exposure to credit risk in respect of stock lending transactions is £446 million (2015: £254 million) of which credit risk of £446 million (2015: £254 million) is mitigated through the use of collateral arrangements.

E4.4 Other collateral arrangements

Collateral has also been pledged and charges granted in respect of certain of the Group's borrowings. The details of these arrangements are set out in note E5.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E5. BORROWINGS

The Group classifies the majority of its interest-bearing borrowings as financial liabilities carried at amortised cost and these are recognised initially at fair value less any attributable transaction costs. The difference between initial cost and the redemption value is amortised through the consolidated income statement over the period of the borrowing using the effective interest method.

Certain borrowings are designated upon initial recognition at fair value through profit or loss and measured at fair value where doing so provides more meaningful information due to the reasons stated in the financial liabilities accounting policy (see note E1). Transaction costs relating to borrowings designated upon initial recognition at fair value through profit or loss are expensed as incurred.

Borrowings are classified as either policyholder or shareholder borrowings. Policyholder borrowings are those borrowings where there is either no or limited shareholder exposure, for example, borrowings attributable to the Group's with-profit operations.

	Carrying value		Fair value	
	2016 £m	2015 £m	**2016 £m**	2015 £m
Limited recourse bonds 2022 7.59% (note a)	**65**	66	**74**	74
Property Reversions loan (note b)	**183**	194	**183**	194
£150 million term facility (note c)	**–**	148	**–**	148
£100 million facility agreement (note c)	**–**	99	**–**	99
Retrocession contracts (note d)	**87**	–	**87**	–
Total policyholder borrowings	**335**	507	**344**	515
£200 million 7.25% unsecured subordinated loan (note e)	**167**	158	**207**	212
£300 million senior unsecured bond (note f)	**298**	298	**332**	324
£450 million revolving credit facility (note g)	**–**	443	**–**	450
£450 million amortising term loan (note g)	**–**	199	**–**	200
£900 million unsecured revolving credit facility (note g)	**843**	–	**850**	–
£428 million subordinated loans (note h)	**393**	393	**416**	400
Total shareholder borrowings	**1,701**	1,491	**1,805**	1,586
Total borrowings	**2,036**	1,998	**2,149**	2,101
Amount due for settlement after 12 months	**2,005**	1,966		

a. In 1998, Mutual Securitisation plc raised £260 million of capital through the securitisation of embedded value on a block of existing unit-linked and unitised with-profit life and pension policies. The bonds were split between two classes, which ranked pari passu and were listed on the Irish Stock Exchange. The £140 million 7.39% class A1 limited recourse bonds matured in 2012 with no remaining outstanding principal. The £120 million 7.59% class A2 limited recourse bonds with an outstanding principal of £72 million (2015: £83 million) have an average remaining life of 3 years and mature in 2022. Phoenix life Assurance Limited ('PLAL') has provided collateral of £29 million (2015: £34 million) to provide security to the holders of the recourse bonds in issue. During 2016, repayments totalling £11 million were made (2015: £11 million).

b. The Property Reversions loan from Santander UK plc ('Santander') was recognised in the consolidated financial statements at fair value. It relates to the sale of Extra-Income Plan policies that Santander finances to the value of the associated property reversions. As part of the arrangement Santander receives an amount calculated by reference to the movement in the Halifax House Price Index and the Group is required to indemnify Santander against profits or losses arising from mortality or surrender experience which differs from the basis used to calculate the reversion amount. Repayment will be on a policy-by-policy basis and is expected to occur over the next 10 to 20 years. During 2016, repayments totalling £27 million were made (2015: £27 million). Note G9 contains details of the assets that support this loan.

c. In February 2016 the Group assessed that it no longer controlled UKCPT and consequently deconsolidated this group of subsidiaries effective from this date (see note H3). As a result the UKCPT £150 million and £100 million policyholder borrowings are no longer included within Group borrowings.

d. In July 2012, AXIA Insurance Limited ('AXIA') provided financing to Abbey Life, a Group company, for Abbey Life to in turn provide the financing for the securitisation of the future surplus arising on a block of 1.7 million life insurance policies originating from the wholly owned Spanish and Portuguese insurance subsidiaries of Banco Santander, S.A. (the 'Cedants'). This transaction was executed in the form of a reinsurance and retrocession arrangement that, taken as a whole, does not meet the definition of an insurance contract under the Group's accounting policies (see note E3.2). Abbey Life received an upfront reinsurance commission from AXIA and makes monthly repayments based on the surplus emerging from the securitised policies as defined in the contracts. The repayments comprise a minimum guaranteed surplus amount and a share of any excess surplus, net of certain other amounts. Any excess amount serves to accelerate the repayment of the principal. Repayments are contingent on the receipt of payments due from the Cedants. Repayment of the loan principal is expected to occur by 2021. The contracts are recognised in the consolidated financial statements at fair value.

e. Scottish Mutual Assurance Limited issued £200 million 7.25% undated, unsecured subordinated loan notes on 23 July 2001 ('PLL subordinated debt'). The earliest repayment date of the notes is 25 March 2021 and thereafter on each fifth anniversary so long as the notes are outstanding. With effect from 1 January 2009, following a Part VII transfer, these loan notes were transferred into the shareholder fund of Phoenix Life Limited ('PLL'). In the event of the winding-up of PLL, the right of payment under the notes is subordinated to the rights of the higher-ranking creditors (principally policyholders). As a result of the acquisition of the Phoenix Life businesses in 2009, these subordinated loan notes were acquired at their fair value and as such, the outstanding principal of these subordinated loan notes differs from the carrying value in the statement of consolidated financial position. The fair value adjustments, which were recognised on acquisition, will unwind over the remaining life of these subordinated loan notes. With effect from 23 December 2014, minor modifications were made to the terms of the notes to enable them to qualify as Tier 2 capital for regulatory reporting purposes. Expenses incurred in effecting these modifications amounted to £10 million. Given the modifications were not substantial, the carrying amount of the liability was adjusted accordingly and the expenses are being amortised over the life of the notes.

f. On 7 July 2014, the Group's financing subsidiary, PGH Capital plc ('PGHC'), issued a £300 million 7-year senior unsecured bond at an annual coupon rate of 5.75% ('PGH Capital senior bond'). The senior bond is subject to guarantee by the Company.

g. In March 2016 the Group agreed an amendment of its £900 million 5-year unsecured bank facility ('PGH Capital facility'), which comprised a £450 million revolving credit facility and a £450 million amortising term loan, into a £650 million unsecured revolving credit facility ('PGH Capital revolving credit facility'), maturing in June 2020. On 9 November 2016, this facility was fully repaid using proceeds from the rights issue before being drawn down again on 28 December 2016. On the same date the Group drew down a futher £250 million tranche of this facility to finance part of the Abbey Life acquisition, increasing borrowing on the PGH Capital revolving credit facility to £900 million. On 29 December 2016, £50 million of the PGH Capital revolving credit facility was repaid, leaving £850 million outstanding as at 31 December 2016. There are no mandatory or target amortisation payments associated with this facility but prepayments are permissible. The facility accrues interest at LIBOR plus 1.35% p.a., which would change if there were a change in the guarantor's credit rating. A utilisation fee of 0.40% p.a. is payable in respect of the facility, which would reduce if the amount outstanding under the facility reduced to 67% or below.

h. On 23 January 2015, PGH Capital plc issued £428 million of subordinated notes ('PGH Capital subordinated notes') due 2025 at a coupon of 6.625%. Fees associated with these notes of £3 million have been deferred and amortised over the life of the notes in the statement of consolidated financial position. The notes are subject to a subordinated guarantee by the Company. Upon exchange £32 million of these notes were held by Group companies. These Group holdings have subsequently been disposed of during January 2017.

i. On 27 May 2016, the Group entered into a £220 million AXA bridge facility agreement of which £182 million was drawn down on 31 October 2016. The facility was repaid in full on 20 December 2016.

Changes to the Group's borrowings since 31 December 2016 have been detailed in note I9.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E6. RISK MANAGEMENT – FINANCIAL RISK

This note forms one part of the risk management disclosures in the consolidated financial statements. The Group's management of insurance risk is detailed in note F4.

E6.1 Financial risk and the asset liability management ('ALM') framework

The use of financial instruments naturally exposes the Group to the risks associated with them, chiefly market risk, credit risk and financial soundness risk.

Responsibility for agreeing the financial risk profile rests with the board of each life company, as advised by investment managers, internal committees and the actuarial function. In setting the risk profile, the board of each life company will receive advice from the appointed investment managers, the relevant with-profit actuary and the relevant actuarial function holder as to the potential implications of that risk profile with regard to the probability of both realistic insolvency and of failing to meet the regulatory minimum capital requirement. The actuarial function holder will also advise the extent to which the investment risk taken is consistent with the Group's commitment to treat customers fairly.

Derivatives are used in many of the Group's funds, within policy guidelines agreed by the board of each life company and overseen by investment committees of the boards of each life company supported by management oversight committees. Derivatives are primarily used for risk hedging purposes or for efficient portfolio management, including the activities of the Group's Treasury function.

More detail on the Group's exposure to financial risk is provided in note E6.2 below.

The Group is also exposed to insurance risk arising from its Phoenix Life segment. Life insurance risk in the Group arises through its exposure to longevity, persistency, mortality and to other variances between assumed and actual experience. These variances can be in factors such as persistency levels and management, administrative expenses and new business pricing. More detail on the Group's exposure to insurance risk is provided in note F4.

The Group's overall exposure to market and credit risk is monitored by appropriate committees, which agree policies for managing each type of risk on an ongoing basis, in line with the investment strategy developed to achieve investment returns in excess of amounts due in respect of insurance contracts. The effectiveness of the Group's ALM framework relies on the matching of assets and liabilities arising from insurance and investment contracts, taking into account the types of benefits payable to policyholders under each type of contract. Separate portfolios of assets are maintained for with-profit business funds (which includes all of the Group's participating business), non-linked non-profit funds and unit-linked funds.

E6.2 Financial risk analysis

Transactions in financial instruments result in the Group assuming financial risks. These include credit risk, market risk and financial soundness risk. Each of these are described below, together with a summary of how the Group manages them.

E6.2.1 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. These obligations can relate to both on and off balance sheet assets and liabilities.

There are two principal sources of credit risk for the Group:

– credit risk which results from direct investment activities, including investments in fixed and variable rate income securities, derivatives, collective investment schemes and the placing of cash deposits; and

– credit risk which results indirectly from activities undertaken in the normal course of business. Such activities include premium payments, outsourcing contracts, reinsurance, exposure from material suppliers and the lending of securities.

The amount disclosed in the statement of consolidated financial position in respect of all financial assets, together with rights secured under off balance sheet collateral arrangements, and excluding those that back unit-linked liabilities, represents the Group's maximum exposure to credit risk.

The impact of non-government fixed and variable rate income securities and, inter alia, the change in market credit spreads during the year is fully reflected in the values shown in these financial statements. Credit spreads are the excess of corporate bond yields over gilt yields to reflect the higher level of risk. Similarly, the value of derivatives that the Group holds takes into account fully the changes in swap rates.

There is an exposure to spread changes affecting the prices of corporate bonds and derivatives. This exposure applies to with-profit funds, non-profit funds (where risks and rewards fall wholly to shareholders) and shareholders' funds.

The Group holds £6,253 million (2015: £3,942 million) of corporate bonds which are used to back annuity liabilities in non-profit funds. These annuity liabilities include an aggregate credit default provision of £322 million (2015: £225 million) to fund against the risk of default.

A 100bps widening of credit spreads, with all other variables held constant and no change in assumed expected defaults, would result in a decrease in the profit after tax in respect of a full financial year, and in equity, of £41 million (2015: £55 million).

A 100bps narrowing of credit spreads, with all other variables held constant and no change in assumed expected defaults, would result in an increase in the profit after tax in respect of a full financial year, and in equity, of £29 million (2015: £62 million).

Credit risk is managed by the monitoring of aggregate Group exposures to individual counterparties and by appropriate credit risk diversification. The Group manages the level of credit risk it accepts through credit risk tolerances. In certain cases, protection against exposure to particular credit risk types may be achieved through the use of derivatives. The credit risk borne by the shareholder on with-profit policies is dependent on the extent to which the underlying insurance fund is relying on shareholder support.

Quality of credit assets

An indication of the Group's exposure to credit risk is the quality of the investments and counterparties with which it transacts. The following table provides information regarding the aggregate credit exposure split by credit rating (ratings obtained from reputable rating agencies are used in deriving the table below):

2016

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Non-rated £m	Unit-linked £m	Total £m
Loans and receivables	–	80	106	420	–	–	623	3	1,232
Derivatives	–	20	1,807	1,024	–	–	145	7	3,003
Fixed and variable rate income securities	4,343	13,283	6,358	4,230	326	119	439	192	29,290
Reinsurers' share of insurance contract liabilities	–	1,820	1,865	2	–	–	57	–	3,744
Reinsurers' share of investment contract liabilities	–	–	–	–	–	–	–	6,808	6,808
Cash and cash equivalents	–	573	918	89	4	–	–	82	1,666
	4,343	15,776	11,054	5,765	330	119	1,264	7,092	45,743

2015

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Non-rated £m	Unit-linked £m	Total £m
Loans and receivables	–	90	133	40	–	–	309	5	577
Derivatives	6	–	1,046	319	–	–	127	–	1,498
Fixed and variable rate income securities	3,976	14,774	8,469	3,548	425	229	388	5	31,814
Reinsurers' share of insurance contract liabilities	–	1,969	1,983	2	–	–	–	–	3,954
Cash and cash equivalents	–	483	3,415	7	–	–	–	35	3,940
	3,982	17,316	15,046	3,916	425	229	824	45	41,783

Non-equity based derivatives are included in the credit risk table above.

Credit ratings have not been disclosed in the above tables for holdings in unconsolidated collective investment schemes. The credit quality of the underlying debt securities within these vehicles is managed by the safeguards built into the investment mandates for these vehicles.

The Group maintains accurate and consistent risk ratings across its asset portfolio. This enables management to focus on the applicable risks and to compare credit exposures across all lines of business, geographical regions and products. The rating system is supported by a variety of financial analytics combined with market information to provide the main inputs for the measurement of counterparty risk. All risk ratings are tailored to the various categories of assets and are assessed and updated regularly.

The Group has established an Internal Credit Rating Committee to monitor and control oversight of both externally rated and internally rated assets. A variety of methods are used to validate the appropriateness of credit assessment from external institutions and fund managers. Internally rated assets are those that do not have a public rating from an external credit assessment institution. This committee reviews the policies, processes and practices to ensure the appropriateness of the internal ratings assigned to asset classes.

A further indicator of the quality of the Group's financial assets is the extent to which they are neither past due nor impaired. The following table gives information regarding the ageing of financial assets that are past due but not impaired and the carrying value of financial assets that have been impaired.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E6. RISK MANAGEMENT – FINANCIAL RISK continued

2016

	Neither past due nor impaired £m	Less than 30 days £m	30–90 days £m	Greater than 90 days £m	Impaired £m	Unit-linked £m	Carrying value £m
Loans and receivables	1,229	–	–	–	–	3	1,232
Derivatives	2,996	–	–	–	–	7	3,003
Fixed and variable rate income securities	29,098	–	–	–	–	192	29,290
Reinsurers' share of insurance contract liabilities	3,744	–	–	–	–	–	3,744
Reinsurers' share of investment contract liabilities	–	–	–	–	–	6,808	6,808
Reinsurance receivables	37	–	–	–	–	–	37
Prepayments and accrued income	358	–	–	–	–	3	361
Other receivables	493	–	–	–	–	20	513
Cash and cash equivalents	1,584	–	–	–	–	82	1,666

2015

	Neither past due nor impaired £m	Less than 30 days £m	30–90 days £m	Greater than 90 days £m	Impaired £m	Unit-linked £m	Carrying value £m
Loans and receivables	572	–	–	–	–	5	577
Derivatives	1,498	–	–	–	–	–	1,498
Fixed and variable rate income securities	31,795	–	–	2	12	5	31,814
Reinsurers' share of insurance contract liabilities	3,954	–	–	–	–	–	3,954
Reinsurance receivables	29	–	–	–	–	–	29
Prepayments and accrued income	335	–	–	–	–	–	335
Other receivables	474	–	–	–	–	–	474
Cash and cash equivalents	3,905	–	–	–	–	35	3,940

Please refer to page 203 for additional life company asset disclosures which include the life companies' exposure to peripheral Eurozone debt securities. Peripheral Eurozone is defined as Portugal, Spain, Italy, Ireland and Greece. The Group's exposure to peripheral Eurozone debt continues to be relatively small compared with total assets.

Assets held directly by the life companies backing unit-linked business have not been analysed in these tables as the credit risk on such financial assets is borne by the policyholders. However, these assets have been included as a separate column in these tables to reconcile the information to the statement of consolidated financial position. Shareholder credit exposure on unit-linked assets is limited to the level of fee income to the extent it is dependent on the underlying assets.

Concentration of credit risk

Concentration of credit risk might exist where the Group has significant exposure to an individual counterparty or a group of counterparties with similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic and other conditions. The Group has most of its counterparty risk within its life business and this is monitored by the counterparty limits contained within the investment guidelines and investment management agreements, overlaid by regulatory requirements and the monitoring of aggregate counterparty exposures across the Group against additional Group counterparty limits. Counterparty risk in respect of OTC derivative counterparties is monitored using a Value-at-Risk (VaR) exposure metric.

The Group is also exposed to concentration risk with outsource partners. This is due to the nature of the outsourced services market. The Group operates a policy to manage outsourcer service counterparty exposures and the impact from default is reviewed regularly by executive committees and measured through stress and scenario testing.

Reinsurance
The Group 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 Group manages its exposure to reinsurance credit risk through the operation of a credit policy, collateralisation where appropriate, and regular monitoring of exposures at the Reinsurance Management Committee.

During 2016 the Group increased its reinsurance counterparty exposure to RGA International after entering into a £2.0 billion longevity swap arrangement on a portfolio of in-force immediate annuities. The exposure remains within agreed limits.

The reinsurance exposure to ReAssure Life Limited was removed following successful completion of a Part VII Transfer. Further details of this can be found in note F3.1.

Collateral
The credit risk of the Group is mitigated, in certain circumstances, by entering into collateral agreements. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and the valuation parameters. Collateral is mainly in respect of stock lending, certain reinsurance arrangements and to provide security against the maturity proceeds of derivative financial instruments. Management monitors the market value of the collateral received, requests additional collateral when needed, and performs an impairment valuation when impairment indicators exist and the asset is not fully secured (and is not carried at fair value). See note E4.1 for further information on collateral arrangements.

E6.2.2 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market influences. Market risk comprises interest rate risk, currency risk and other price risk (comprising equity risk, property risk, inflation risk and alternative asset class risk).

The Group is mainly exposed to market risk as a result of:

- the mismatch between liability profiles and the related asset investment portfolios;
- the investment of surplus assets including shareholder reserves yet to be distributed, surplus assets within the with-profit funds and assets held to meet regulatory capital and solvency requirements; and
- the income flow of management charges from the invested assets of the business.

The Group manages the levels of market risk that it accepts through the operation of a market risk policy and an approach to investment management that determines:

- the constituents of market risk for the Group;
- the basis used to fair value financial assets and liabilities;
- the asset allocation and portfolio limit structure;
- diversification from and within benchmarks by type of instrument and geographical area;
- the net exposure limits by each counterparty or group of counterparties, geographical and industry segments;
- control over hedging activities;
- reporting of market risk exposures and activities; and
- monitoring of compliance with market risk policy and review of market risk policy for pertinence to the changing environment.

All operations comply with regulatory requirements relating to the taking of market risk.

Interest rate risk
Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate relative to the respective liability due to the impact of changes in market interest rates on the value of interest-bearing assets and on the value of future guarantees provided under certain contracts of insurance.

Interest rate risk is managed by matching assets and liabilities where practicable and by entering into derivative arrangements for hedging purposes where appropriate. This is particularly the case for the non-participating funds and supported participating funds. For unsupported participating business, some element of investment mismatching is permitted where it is consistent with the principles of treating customers fairly. The with-profit funds of the Group provide capital to allow such mismatching to be effected. In practice, the life companies of the Group maintain an appropriate mix of fixed and variable rate instruments according to the underlying insurance or investment contracts and will review this at regular intervals to ensure that overall exposure is kept within the risk profile agreed for each particular fund. This also requires the maturity profile of these assets to be managed in line with the liabilities to policyholders.

The sensitivity analysis for interest rate risk indicates how changes in the fair value or future cash flows of a financial instrument arising from changes in market interest rates at the reporting date result in a change in profit after tax and in equity. It takes into account the effect of such changes in market interest rates on all assets and liabilities that contribute to the Group's reported profit after tax and in equity.

With-profit business and non-participating business within the with-profit funds are exposed to interest rate risk as guaranteed liabilities are valued relative to market interest rates and investments include fixed interest securities and derivatives. For unsupported with-profit business the profit or loss arising from mismatches between such assets and liabilities is largely offset by increased or reduced discretionary policyholder benefits dependent on the existence of policyholder guarantees. The contribution of unsupported participating business to the Group result is largely limited to the shareholders' share of the declared annual bonus. The contribution of the supported participating business to the Group result is determined by the shareholders' interest in any change in value in the capital advanced to the with-profit funds.

In the non-participating funds, policy liabilities' sensitivity to interest rates are matched primarily with fixed and variable rate income securities and hedging if necessary to match duration, with the result that sensitivity to changes in interest rates is very low.

During the year and as a result of the Solvency II regime, management has reviewed the matching position of assets and liabilities resulting in changes to the hedging positions for certain asset portfolios. As a result, an increase of 1% in interest rates, with all other variables held constant, would now result in a decrease in profits after tax in respect of a full financial year, and in equity, of £146 million (2015: £89 million).

A decrease of 1% in interest rates, with all other variables held constant, would result in an increase in profits after tax in respect of a full financial year, and in equity, of £319 million (2015: £89 million).

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E6. RISK MANAGEMENT – FINANCIAL RISK continued

Equity, property and inflation risk

The Group has exposure to financial assets and liabilities whose values will fluctuate as a result of changes in market prices other than from interest rate and currency fluctuations. This is due to factors specific to individual instruments, their issuers or factors affecting all instruments traded in the market. Accordingly, the Group limits its exposure to any one counterparty in its investment portfolios and to any one foreign market.

The portfolio of marketable equity securities and property investments which is carried in the statement of consolidated financial position at fair value, has exposure to price risk. The Group's objective in holding these assets is to earn higher long-term returns by investing in a diverse portfolio of equities and properties. Portfolio characteristics are analysed regularly and price risks are actively managed in line with investment mandates. The Group's holdings are diversified across industries and concentrations in any one company or industry are limited.

Equity and property price risk is primarily borne in respect of assets held in with-profit or unit-linked funds. For unit-linked funds this risk is borne by policyholders and asset movements directly impact unit prices and hence policy values. For with-profit funds policyholders' future bonuses will be impacted by the investment returns achieved and hence the price risk, whilst the Group also has exposure to the value of guarantees provided to with-profit policyholders. In addition some equity investments are held in respect of shareholders' funds. The Group as a whole is exposed to price risk fluctuations impacting the income flow of management charges from the invested assets of all funds.

Equity and property price risk is managed through the agreement and monitoring of financial risk profiles that are appropriate for each of the Group's life funds in respect of maintaining adequate regulatory capital and treating customers fairly. This is largely achieved through asset class diversification and within the Group's ALM framework through the holding of derivatives or physical positions in relevant assets where appropriate.

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

A 10% decrease in equity prices, with all other variables held constant, would result in an increase in profits after tax in respect of a full financial year, and in equity, of £75 million (2015: £48 million).

A 10% increase in equity prices, with all other variables held constant, would result in a decrease in profits after tax in respect of a full financial year, and in equity, of £74 million (2015: £46 million).

A 10% decrease in property prices, with all other variables held constant, would result in a decrease in profits after tax in respect of a full financial year, and in equity, of £4 million (2015: £21 million).

A 10% increase in property prices, with all other variables held constant, would result in an increase in profits after tax in respect of a full financial year, and in equity, of £2 million (2015: £21 million).

The Group is exposed to inflation risk through certain contracts, such as annuities, which may provide for future benefits to be paid taking account of changes in the level of experienced and implied inflation, and also through the Group's cost base. The Group seeks to manage inflation risk within the ALM framework through the holding of derivatives, such as inflation swaps, or physical positions in relevant assets, such as index linked gilts, where appropriate.

Currency risk

The Group's principal transactions are carried out in sterling and therefore its exchange risk is limited principally to historical business that was written in the Republic of Ireland, where the assets are generally held in the same currency denomination as their liabilities, therefore, any foreign currency mismatch is largely mitigated. Consequently, the foreign currency risk relating to this business mainly arises when the assets and liabilities are translated into sterling.

The Group's financial assets are primarily denominated in the same currencies as its insurance and investment liabilities. Thus, the main foreign exchange risk arises from recognised assets and liabilities denominated in currencies other than those in which insurance and investment liabilities are expected to be settled and, indirectly, from the earnings of UK companies arising abroad.

Certain Phoenix Life with-profit funds have an exposure to overseas assets which is not driven by liability considerations. The purpose of this exposure is to reduce overall risk whilst maximising returns by diversification. This exposure is limited and managed through investment mandates which are subject to the oversight of the investment committees of the boards of each life company. Fluctuations in exchange rates from certain holdings in overseas assets are hedged against currency risks.

Sensitivity of profit after tax and equity to fluctuations in currency exchange rates is not considered significant at 31 December 2016, since unhedged exposure to foreign currency was relatively low (2015: not considered significant).

E6.2.3 Financial soundness risk

Financial soundness risk is a broad risk category encompassing capital management risk, tax risk, and liquidity and funding risk.

Capital management risk is defined as the failure of the Group, or one of its separately regulated subsidiaries, to maintain sufficient capital to provide appropriate security for policyholders and meet all regulatory capital requirements whilst not retaining unnecessary capital. The PLHL Group has exposure to capital management risk through the requirements of the Solvency II capital regime, as implemented by the PRA, to calculate regulatory capital adequacy at a Group level. The Group's UK life subsidiaries have exposure to capital management risk through the Solvency II regulatory capital requirements mandated by the PRA at the solo level. The Group's approach to managing capital management risk is described in detail in note I4.

Tax risk is defined as the risk of financial or reputational loss arising from a lack of liquidity, funding or capital due to an unforeseen tax cost, or by the inappropriate reporting and disclosure of information in relation to taxation. Tax risk is managed by maintaining an appropriately staffed tax team who have the qualifications and experience to make judgements on tax issues, augmented by advice from external specialists where required. The Group has a formal tax risk policy, which sets out its risk appetite in relation to specific aspects of tax risk, and which details the controls the Group has in place to manage those risks. These controls are subject to a regular review process. The Group's subsidiaries have exposure to tax risk through the annual statutory and regulatory reporting and through the processing of policyholder tax requirements. The UK government has confirmed restrictions on the rules relating to the loss absorbing capacity of deferred tax will be introduced in 2017. Surplus assets have been retained within the Group to mitigate any potential adverse impact of the change.

Liquidity and funding risk is defined as the failure of the Group to maintain adequate levels of financial resources to enable it to meet its obligations as they fall due. The Group has exposure to liquidity risk as a result of servicing its external debt and equity investors, and from the operating requirements of its subsidiaries. The Group's subsidiaries have exposure to liquidity risk as a result of normal business activities, specifically the risk arising from an inability to meet short-term cash flow requirements.

The Board of Phoenix Group Holdings has defined a number of governance objectives and principles and the liquidity risk frameworks of each subsidiary are designed to ensure that:

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

The Group's policy is to maintain sufficient liquid assets of suitable credit quality at all times including, where appropriate, by having access to borrowings so as to be able to meet all foreseeable current liabilities as they fall due in a cost-effective manner. Forecasts are prepared regularly to predict required liquidity levels over both the short and medium term allowing management to respond appropriately to changes in circumstances.

The vast majority of the Group's derivative contracts are traded OTC and have a two-day collateral settlement period. The Group's derivative contracts are monitored daily, via an end-of-day valuation process, to assess the need for additional funds to cover margin or collateral calls.

Some of the Group's commercial property investments are held through collective investment schemes. The collective investment schemes have the power to restrict and/or suspend withdrawals, which would, in turn, affect liquidity. As a result of the market volatility experienced following the result of the referendum on membership of the European Union, and in line with other firms across the industry, customer-driven transactions in certain unit trusts were temporarily suspended during July, August and September. All other unit trusts have continued to process investment and realisations in a normal manner and have not imposed any restrictions or delays.

Some of the Group's cash and cash equivalents are held through collective investment schemes. The collective investment schemes have the power, in extreme stress, to restrict and/or suspend withdrawals, which would, in turn, affect liquidity. To date, the collective investment schemes have continued to process both investments and realisations in a normal manner and have not imposed any restrictions or delays.

The following table provides a maturity analysis showing the remaining contractual maturities of the Group's undiscounted financial liabilities and associated interest. Liabilities under insurance contract contractual maturities are included based on the estimated timing of the amounts recognised in the statement of consolidated financial position in accordance with the requirements of IFRS 4 *Insurance Contracts*:

2016

	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	**3,406**	**11,143**	**31,258**	**–**	**45,807**
Investment contracts	**27,332**	**–**	**–**	**–**	**27,332**
Borrowings[1]	**121**	**1,733**	**552**	**183**	**2,589**
Deposits received from reinsurers[1]	**29**	**103**	**327**	**–**	**459**
Derivatives[1]	**85**	**170**	**1,384**	**254**	**1,893**
Net asset value attributable to unitholders	**1,040**	**–**	**–**	**–**	**1,040**
Obligations for repayment of collateral received	**1,623**	**–**	**–**	**–**	**1,623**
Reinsurance payables	**21**	**–**	**–**	**–**	**21**
Payables related to direct insurance contracts	**484**	**–**	**–**	**–**	**484**
Accruals and deferred income	**204**	**–**	**–**	**–**	**204**
Other payables	**102**	**–**	**–**	**–**	**102**

1 These financial liabilities are disclosed at their undiscounted value and therefore differ from the statement of consolidated financial position which discloses the discounted value.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

E. FINANCIAL ASSETS & LIABILITIES continued

E6. RISK MANAGEMENT – FINANCIAL RISK continued

2015

	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	2,646	9,611	26,961	765	39,983
Investment contracts	7,905	–	–	–	7,905
Borrowings[1]	32	1,056	1,155	194	2,437
Deposits received from reinsurers[1]	30	108	351	–	489
Derivatives[1]	104	137	1,760	–	2,001
Net asset value attributable to unitholders	5,120	–	–	–	5,120
Obligations for repayment of collateral received	725	–	–	–	725
Reinsurance payables	19	–	–	–	19
Payables related to direct insurance contracts	364	–	–	–	364
Accruals and deferred income	127	1	–	–	128
Other payables	677	–	–	–	677

1 These financial liabilities are disclosed at their undiscounted value and therefore differ from the statement of consolidated financial position which discloses the discounted value.

Investment contract policyholders have the option to terminate or transfer their contracts at any time and to receive the surrender or transfer value of their policies. Although these liabilities are payable on demand, and are therefore included in the contractual maturity analysis as due within one year, the Group does not expect all these amounts to be paid out within one year of the reporting date.

A significant proportion of the Group's financial assets are held in equities, gilts, cash, supranationals and investment grade securities which the Group considers sufficient to meet the liabilities as they fall due. The vast majority of these investments are readily realisable since most of them are quoted in an active market.

E6.3 Unit-linked contracts

For unit-linked contracts the Group matches all the liabilities with assets in the portfolio on which the unit prices are based. There is therefore no interest, price, currency or credit risk for the Group on these contracts.

In extreme circumstances, the Group could be exposed to liquidity risk in its unit-linked funds. This could occur where a high volume of surrenders coincides with a tightening of liquidity in a unit-linked fund to the point where assets of that fund have to be sold to meet those withdrawals. Where the fund affected consists of property, it can take several months to complete a sale and this would impede the proper operation of the fund. In these situations, the Group considers its risk to be low since there are steps that can be taken first within the funds themselves both to ensure the fair treatment of all investors in those funds and to protect the Group's own risk exposure.

F. INSURANCE CONTRACTS, INVESTMENT CONTRACTS WITH DPF AND REINSURANCE

F1. LIABILITIES UNDER INSURANCE CONTRACTS

Classification of contracts

Contracts are classified as insurance contracts where the Group accepts significant insurance risk from the policyholder by agreeing to compensate the policyholder if a specified uncertain event adversely affects the policyholder.

Contracts under which the transfer of insurance risk to the Group from the policyholder is not significant are classified as investment contracts or derivatives and accounted for as financial liabilities (see notes E1 and E3 respectively).

Some insurance and investment contracts contain a DPF. This feature entitles the policyholder to additional discretionary benefits as a supplement to guaranteed benefits. Investment contracts with a DPF are recognised, measured and presented as insurance contracts.

Insurance contracts and investment contracts with DPF

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

Insurance contract liabilities for non-participating business, other than unit-linked insurance contracts, are calculated on the basis of current data and assumptions, 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.

For unit-linked insurance contract liabilities the provision is based on the fund value, together with an allowance for any excess of future expenses over charges, where appropriate.

For participating business, the liabilities under insurance contracts and investment contracts with DPF are calculated in accordance with the following methodology:

- liabilities to policyholders arising from the with-profit business are stated at the amount of the realistic value of the liabilities, adjusted to exclude the owners' share of projected future bonuses;
- acquisition costs are not deferred; and
- reinsurance recoveries are measured on a basis that is consistent with the valuation of the liability to policyholders to which the reinsurance applies.

The with-profit bonus reserve for an individual contract is determined by either a retrospective calculation of 'accumulated asset share' approach or by way of a prospective 'bonus reserve valuation' method. The cost of future policy-related liabilities is determined using a market consistent approach, mainly based on a stochastic model calibrated to market conditions at the end of the reporting period. Non-market-related assumptions (for example, persistency, mortality and expenses) are based on experience adjusted to take into account of future trends.

The realistic liability for any contract is equal to the sum of the with-profit bonus reserve and the cost of future policy-related liabilities.

Where policyholders have valuable guarantees, options or promises in respect of the with-profit business, these costs are generally valued using a stochastic model.

In calculating the realistic liabilities, account is taken of the future management actions consistent with those set out in the Principles and Practices of Financial Management ('PPFM').

Present value of future profits on non-participating business in the with-profit funds

For UK with-profit life funds, an amount may be recognised for the present value of future profits ('PVFP') on non-participating business written in a with-profit fund where the determination of the realistic value of liabilities in that with-profit fund takes account, directly or indirectly, of this value.

Where the value of future profits can be shown to be due to policyholders, this amount is recognised as a reduction in the liability rather than as an intangible asset. This is then apportioned between the amounts that have been taken into account in the measurement of liabilities and other amounts which are shown as an adjustment to the unallocated surplus.

Where it is not possible to apportion the future profits on this non-participating business to policyholders, the PVFP on this business is recognised as an intangible asset and changes in its value are recorded as a separate item in the consolidated income statement (see note G7).

The value of the PVFP is determined in a manner consistent with realistic measurement of liabilities. In particular, the methodology and assumptions involve adjustments to reflect risk and uncertainty, are based on current estimates of future experience and current market yields, and allow for market consistent valuation of any guarantees or options within the contracts. The value is also adjusted to remove the value of capital backing the non-profit business if this is included in the realistic calculation of PVFP. The principal assumptions used to calculate the PVFP are the same as those used in calculating the insurance contract liabilities given in note F4.

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.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

F. INSURANCE CONTRACTS, INVESTMENT CONTRACTS WITH DPF AND REINSURANCE continued

F1. LIABILITIES UNDER INSURANCE CONTRACTS continued

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 with the carrying value of the liabilities. Any deficiency is charged to the consolidated income statement.

The Group's accounting policies for insurance contracts meet the minimum specified requirements for liability adequacy testing under IFRS 4 *Insurance Contracts*, as they allow for current estimates of all contractual cash flows and of related cash flows such as claims handling costs. Cash flows resulting from embedded options and guarantees are also allowed for, with any deficiency being recognised in the consolidated income statement.

Consolidated income statement recognition

Gross premiums
In respect of insurance contracts and investment contracts with DPF, premiums are accounted for on a receivable basis and exclude any taxes or duties based on premiums. Funds at retirement under individual pension contracts converted to annuities with the Group are, for accounting purposes, included in both claims incurred and premiums within gross premiums written.

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

The Group cedes insurance risk in the normal course of business. Reinsurance assets represent balances due from reinsurance providers. Reinsurers' share of insurance contract liabilities is dependent on expected claims and benefits arising under the related reinsured policies. Reinsurance assets are reviewed for impairment at each reporting date, or more frequently, when an indication of impairment arises during the reporting period. Impairment occurs when there is objective evidence, as a result of an event that occurred after initial recognition of the reinsurance asset, that the Group may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer. The impairment loss is recognised in the consolidated income statement. The reinsurers' share of investment contract liabilities is measured on a basis that is consistent with the valuation of the liability to policyholders to which the reinsurance applies.

Reinsurance premiums payable in respect of certain reinsured individual and group pensions annuity contracts are payable by quarterly instalments and are accounted for on a payable basis. Due to the period of time over which reinsurance premiums are payable under these arrangements, the reinsurance premiums and related payables are discounted to present values using a pre-tax risk-free rate of return. The unwinding of the discount is included as a charge within the consolidated income statement.

Reinsurance claims are recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

Gains or losses on purchasing reinsurance are recognised in the consolidated income statement at the date of purchase and are not amortised. They are the difference between the premiums ceded to reinsurers and the related change in the reinsurers' share of insurance contract liabilities.

The table below shows a summary of the liabilities under insurance contracts and the related reinsurers' share included within assets in the statement of consolidated financial position.

The table below shows a summary of the liabilities under insurance contracts and the related reinsurers' share included within assets in the statement of consolidated financial position.

	Gross liabilities 2016 £m	Reinsurers' share 2016 £m	Gross liabilities 2015 £m	Reinsurers' share 2015 £m
Life assurance business:				
Insurance contracts	**34,749**	**3,743**	31,150	5,474
Investment contracts with DPF	**11,058**	**1**	10,420	1
	45,807	**3,744**	41,570	5,475
Less amounts classified as held for sale (see note I1)	**–**	**–**	(1,587)	(1,521)
	45,807	**3,744**	39,983	3,954
Amounts due for settlement after 12 months	**42,401**	**3,478**	37,337	3,909

	Gross liabilities 2016 £m	Reinsurers' share 2016 £m	Gross liabilities 2015 £m	Reinsurers' share 2015 £m
At 1 January	**39,983**	**3,954**	42,930	2,772
Amounts classified as held for sale at 1 January	**1,587**	**1,521**	1,776	1,713
	41,570	**5,475**	44,706	4,485
Premiums	**999**	**75**	902	1,376
Claims	**(3,726)**	**(456)**	(3,931)	(326)
Foreign exchange adjustments	**44**	**32**	(19)	(13)
Acquisition of the AXA businesses and Abbey Life[1] (see note H2)	**3,875**	**100**	–	–
Annuity liabilities transfer (see note I1.1)	**(1,652)**	**(1,582)**	–	–
Disposal of SMI (see note H2.4)	**–**	**–**	(158)	–
Other changes in liabilities	**4,697**	**100**	70	(47)
	45,807	**3,744**	41,570	5,475
Less amounts classified as held for sale at 31 December (see note I1)	**–**	**–**	(1,587)	(1,521)
At 31 December	**45,807**	**3,744**	39,983	3,954

1 Gross liabilities in respect of the acquisition of the AXA businesses and Abbey Life are stated after the recognition of negative reserves of £181 million that arise on acquisition of the AXA businesses (see note H2).

F2. UNALLOCATED SURPLUS

The unallocated surplus comprises the excess of the assets over the policyholder liabilities of the with-profit business of the Group's life operations. For the Group's with-profit funds this represents amounts which have yet to be allocated to owners since the unallocated surplus attributable to policyholders has been included within liabilities under insurance contracts.

If the realistic value of liabilities to policyholders exceeds the value of the assets in the with-profit fund, the unallocated surplus is valued at £nil.

	2016 £m	2015 £m
At 1 January	**877**	981
Transfer to consolidated income statement	**(4)**	(84)
Acquisition of Abbey Life (see note H2)	**6**	–
Disposal of SMI (see note H2.4)	**–**	(20)
At 31 December	**879**	877

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

F. INSURANCE CONTRACTS, INVESTMENT CONTRACTS WITH DPF AND REINSURANCE continued

F3. REINSURANCE

This section includes disclosures in relation to reinsurance. Further disclosures and accounting policies relating to reinsurance are included in note F1.

F3.1 Premiums ceded to reinsurers

Premiums ceded to reinsurers during the period were £75 million (2015: £1,376 million).

During 2016, the Group entered into a longevity swap arrangement with RGA International in respect of a portfolio of the Group's in-force immediate annuity liabilities of £2.0 billion.

On 9 November 2015, the Group entered into an agreement with RGA International, effective from 1 November 2015, to reinsure substantively all of the PLAL annuity liabilities previously ceded to Opal Reassurance Limited ('Opal Re'), a subsidiary undertaking of the Company. The Group paid a reinsurance premium of £1,346 million to RGA International. Under the terms of the arrangement, RGA International holds assets in a collateral account over which the Group has a floating charge as disclosed in note F3.2.

On 31 July 2014, the Group entered into a business transfer agreement with ReAssure Life Limited (formerly Guardian Assurance Limited (see note I1.1). The transfer was initially effected under a reinsurance agreement effective from 1 January 2014.

In accordance with the business transfer agreement, the reinsurance agreement was replaced by a transfer of the business using a scheme under Part VII of the Financial Services and Markets Act 2000 on 30 December 2016.

Prior to the Part VII, in order to mitigate the risk of counterparty default, ReAssure Life Limited held assets in a collateral account over which the Group had a fixed charge as disclosed in note F3.2.

F3.2 Collateral arrangements

It is the Group's practice to obtain collateral to mitigate the counterparty risk related to reinsurance transactions usually in the form of cash or marketable financial instruments.

Where the Group receives collateral in the form of marketable financial instruments which it is not permitted to sell or re-pledge except in the case of default, it is not recognised in the statement of consolidated financial position. The fair value of financial assets accepted as collateral for reinsurance transactions but not recognised in the statement of consolidated financial position amounts to £3,780 million (2015: £4,909 million). The decrease is largely driven by the Part VII transfer of business previously reinsured to ReAssure Life Limited (see note F3.1).

Where the Group receives collateral on reinsurance transactions in the form of cash it is recognised in the statement of consolidated financial position along with a corresponding liability to repay the amount of collateral received, disclosed as 'Deposits received from reinsurers'. The amounts recognised as financial assets and liabilities from cash collateral received at 31 December 2016 are set out below.

	Reinsurance transactions	
	2016 £m	2015 £m
Financial assets	**392**	376
Financial liabilities	**392**	376

F4. RISK MANAGEMENT – INSURANCE RISK

This note forms one part of the risk management disclosures in the consolidated financial statements. Financial risk is included in note E6.

Insurance risk refers to the risk that the frequency or severity of insured events may be worse than expected and includes expense risk. The Phoenix Life segment contracts include the following sources of insurance risk, including the addition of new business pricing risk following the acquisition of the AXA businesses:

Mortality	higher than expected number of death claims on assurance products and occurrence of one or more large claims;
Longevity	faster than expected improvements in life expectancy on immediate and deferred annuity products;
Morbidity	higher than expected number of serious illness claims or more sickness claims which last longer on income protection policies;
Expenses	policies cost more to administer than expected;
Lapses	the numbers of policies terminating early is different to that expected in a way which increases expected claims costs or expenses or reduces future profits;
Options	unanticipated changes in policyholder option exercise rates giving rise to increased claims costs; and
Pricing	inadequate or inappropriate pricing of new business.

Objectives and policies for mitigating insurance risk

The Group uses several methods to assess and monitor insurance risk exposures both for individual types of risks insured and overall risks. These methods include internal risk measurement models, experience analyses, external data comparisons, sensitivity analyses, scenario analyses and stress testing.

The profitability of the run-off of the closed long-term insurance businesses within the Group depends, to a significant extent, on the values of claims paid in the future relative to the assets accumulated to the date of claim. Typically, over the lifetime of a contract, premiums and investment returns exceed claim costs in the early years and it is necessary to set aside these amounts to meet future obligations. The amount of such future obligations is assessed on actuarial principles by reference to assumptions about the development of financial and insurance risks.

It is therefore necessary for the Directors of each life company to make decisions, based on actuarial advice, which ensure an appropriate accumulation of assets relative to liabilities. These decisions include investment policy, bonus policy and, where discretion exists, the level of payments on early termination.

During 2016, a number of strategic initiatives significantly impacted the Group's longevity risk exposures. These included the outward longevity swap with RGA International, the Part VII Transfer to ReAssure Life Limited and the acquisition of Abbey Life.

Following the acquisition of the AXA businesses, the Group is exposed to increased mortality and new business pricing risk, although this provides a natural hedge to the annuity business.

Sensitivities

Insurance liabilities are sensitive to changes in risk variables, such as prevailing market interest rates, currency rates and equity prices, since these variations alter the value of the financial assets held to meet obligations arising from insurance contracts and changes in investment conditions also have an impact on the value of insurance liabilities themselves. Additionally, insurance liabilities are sensitive to the assumptions which have been applied in their calculation, such as mortality and lapse rates. Sometimes allowance must also be made for the effect on future assumptions of management or policyholder actions in certain economic scenarios. This could lead to changes in assumed asset mix or future bonus rates. The most significant non-economic sensitivities arise from mortality, longevity and lapse risk.

A decrease of 5% in assurance mortality, with all other variables held constant, would result in an increase in profits after tax in respect of a full year, and an increase in equity of £43 million (2015: £12 million).

An increase of 5% in assurance mortality, with all other variables held constant, would result in a decrease in profits after tax in respect of a full year, and a decrease in equity of £41 million (2015: £12 million).

A decrease of 5% in annuitant longevity, with all other variables held constant, would result in an increase in profits after tax in respect of a full year, and an increase in equity of £127 million (2015: £99 million).

An increase of 5% in annuitant longevity, with all other variables held constant, would result in a decrease in profits after tax in respect of a full year, and a decrease in equity of £128 million (2015: £99 million).

A decrease of 25% in lapse rates, with all other variables held constant, would result in a decrease in profits after tax in respect of a full year, and a decrease in equity of £38 million (2015: £76 million).

An increase of 25% in lapse rates, with all other variables held constant, would result in an increase in profits after tax in respect of a full year, and an increase in equity of £36 million (2015: £76 million).

F4.1 Assumptions

Valuation of participating insurance and investment contracts

For participating business, which is with-profit business (insurance and investment contracts), the insurance contract liability is calculated on a realistic basis, adjusted to exclude the shareholders' share of future bonuses and the associated tax liability. This is a market consistent valuation, which involves placing a value on liabilities similar to the market value of assets with similar cash flow patterns.

Valuation of non-participating insurance contracts

The non-participating insurance contract liabilities are determined using either a net premium or gross premium valuation method.

Process used to determine assumptions

Following the implementation of the Solvency II regulatory regime effective from 1 January 2016, the Group has made certain changes to the assumptions and estimates used in the valuation of insurance contracts, as follows:

- In determining the discount rate to be applied when calculating participating and non-participating insurance contract liabilities, the Group has amended the risk-free reference curve from a gilt yield curve plus a liquidity premium of 10bps to the swap curve plus 10bps.
- For non-participating insurance contract liabilities, the Group has previously used a valuation rate of interest and adjusted the liability discount rate by reference to the yield on the assets backing the liabilities to account for credit, default and reinvestment risk. The Group now makes an explicit adjustment to the risk-free rate to adjust for illiquidity in respect of assets backing illiquid liabilities. The new approach does not take any additional credit for investment margins compared to the previous methodology.
- For non-participating insurance contract liabilities, the Group previously derived demographic assumptions by adding an implicit prudent margin to best estimate assumptions. The Group has amended its approach in this regard and now sets assumptions at management's best estimates and recognises an explicit margin for demographic risks. For participating business in realistic basis companies, the assumptions about future demographic trends continue to represent 'best estimates'.

The assumption changes have been made to align the IFRS basis more closely with the requirements of Solvency II removing the volatility that would otherwise arise from the use of reference rates that differ across reporting bases and aligning the calculation of liquidity premiums with that performed under Solvency II.

The amendments to the risk-free reference rate and the approach for adjusting for illiquidity increased insurance contract liabilities by £77 million. This has been more than offset by the impact of the change in approach for determining the demographic prudence margin, which reduced insurance contract liabilities by £115 million. After allowing for other second order impacts of the changes of £7 million (including the revaluation of certain current liabilities using the swap rather than gilt curve), the overall impact of the above changes in the period is a benefit to profit before tax of £31 million.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

F. INSURANCE CONTRACTS, INVESTMENT CONTRACTS WITH DPF AND REINSURANCE continued

F4. RISK MANAGEMENT – INSURANCE RISK continued

During the year a number of changes were made to assumptions to reflect changes in expected experience or to harmonise the approach across the enlarged Group. The impact of material changes during the year was as follows:

	(Decrease)/increase in insurance liabilities 2016 £m	(Decrease)/increase in insurance liabilities 2015 £m
Change in longevity assumptions	**(83)**	(3)
Change in persistency assumptions	**142**	1
Change in mortality assumptions	**1**	3
Change in expenses assumptions	**(8)**	5

Expense inflation

Expenses are assumed to increase at the rate of increase in the Retail Price Index ('RPI') plus fixed margins in accordance with the various management service agreements ('MSAs') the Group has in place with outsource partners. For with-profit business the rate of RPI inflation is determined within each stochastic scenario. For other business it is based on the Bank of England inflation spot curve. For MSAs with contractual increases set by reference to national average earnings inflation, this is approximated as RPI inflation plus 1%. In instances in which inflation risk is not mitigated, a further margin for adverse deviations may then be added to the rate of expense inflation.

Mortality and longevity rates

Mortality rates are based on published tables, adjusted appropriately to take account of changes in the underlying population mortality since the table was published, company experience and forecast changes in future mortality. Where appropriate, a margin is added to assurance mortality rates to allow for adverse future deviations. Annuitant mortality rates are adjusted to make allowance for future improvements in pensioner longevity.

Lapse and surrender rates (persistency)

The assumed rates for surrender and voluntary premium discontinuance depend on the length of time a policy has been in-force and the relevant company. Surrender or voluntary premium discontinuances are only assumed for realistic basis companies. Withdrawal rates used in the valuation of with-profit policies are based on observed experience and adjusted when it is considered that future policyholder behaviour will be influenced by different considerations than in the past. In particular, it is assumed that withdrawal rates for unitised with-profit contracts will be higher on policy anniversaries on which Market Value Adjustments do not apply.

Discretionary participating bonus rate

For realistic basis companies, the regular bonus rates assumed in each scenario are determined in accordance with each company's PPFM. Final bonuses are assumed at a level such that maturity payments will equal asset shares subject to smoothing rules set out in the PPFM.

Policyholder options and guarantees

Some of the Group's products give potentially valuable guarantees, or give options to change policy benefits which can be exercised at the policyholders' discretion. These products are described below.

Most with-profit contracts give a guaranteed minimum payment on a specified date or range of dates or on death if before that date or dates. For pensions contracts, the specified date is the policyholder's chosen retirement date or a range of dates around that date. For endowment contracts, it is the maturity date of the contract. For with-profit bonds it is often a specified anniversary of commencement, in some cases with further dates thereafter. Annual bonuses when added to with-profit contracts usually increase the guaranteed amount.

There are guaranteed surrender values on a small number of older contracts.

Some pensions contracts include guaranteed annuity options (see deferred annuities in note F4.2 for details). The total amount provided in the with-profit and non-profit funds in respect of the future costs of guaranteed annuity options are £2,239 million (2015: £1,710 million) and £5 million (2015: £5 million) respectively.

In common with other life companies in the UK which have written pension transfer and opt-out business, the Group has set up provisions for the review and possible redress relating to personal pension policies. These provisions, which have been calculated from data derived from detailed file reviews of specific cases and using a certainty equivalent approach, which give a result very similar to a market consistent valuation, are included in liabilities arising under insurance contracts. The total amount provided in the with-profit funds and non-profit funds in respect of the review and possible redress relating to pension policies, including associated costs, are £376 million (2015: £254 million) and £13 million (2015: £14 million) respectively.

With-profit deferred annuities participate in profits only up to the date of retirement. At retirement, a guaranteed cash option allows the policyholder to commute the annuity benefit into cash on guaranteed terms.

F4.2 Managing product risk

The following sections give an assessment of the risks associated with the Group's main life assurance products, as shown below, and the ways in which the Group manages those risks.

2016

	Gross		Reinsurance	
	Insurance contracts £m	Investment contracts with DPF £m	Insurance contracts £m	Investment contracts with DPF £m
With-profit funds:				
Pensions:				
Deferred annuities – with guarantees	8,576	144	499	–
Deferred annuities – without guarantees	1,572	–	–	–
Immediate annuities	1,208	–	609	–
Unitised with-profit	1,000	9,005	8	–
Total pensions	12,356	9,149	1,116	–
Life:				
Immediate annuities	11	–	4	–
Unitised with-profit	633	751	6	–
Life with-profit	4,166	–	6	1
Total life	4,810	751	16	1
Other	2,211	–	82	–
Non-profit funds:				
Deferred annuities – with guarantees	479	–	–	–
Deferred annuities – without guarantees	571	–	2	–
Immediate annuities	11,376	–	2,247	–
Protection	274	–	89	–
Unit-linked	2,426	1,153	73	–
Other	246	5	118	–
	34,749	11,058	3,743	1

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

F. INSURANCE CONTRACTS, INVESTMENT CONTRACTS WITH DPF AND REINSURANCE continued

F4. RISK MANAGEMENT – INSURANCE RISK continued

F4.2 Managing product risk continued

2015

	Gross		Reinsurance	
	Insurance contracts £m	Investment contracts with DPF £m	Insurance contracts £m	Investment contracts with DPF £m
With-profit funds:				
Pensions:				
Deferred annuities – with guarantees	8,534	142	726	–
Deferred annuities – without guarantees	1,586	–	–	–
Immediate annuities	865	–	404	–
Unitised with-profit	1,017	8,574	38	–
Total pensions	12,002	8,716	1,168	–
Life:				
Immediate annuities	59	–	4	–
Unitised with-profit	555	640	20	–
Life with-profit	4,377	–	9	1
Total life	4,991	640	33	1
Other	1,967	–	182	–
Non-profit funds:				
Deferred annuities – with guarantees	14	–	–	–
Deferred annuities – without guarantees	489	–	2	–
Immediate annuities	7,933	–	2,383	–
Protection	508	–	99	–
Unit-linked	1,353	1,059	46	–
Other	306	5	40	–
	29,563	10,420	3,953	1

The tables above exclude insurance contract liabilities and related reinsurer's share of insurance contract liabilities classified as held for sale at 31 December 2016 and 31 December 2015.

With-profit fund (unitised and traditional)
The Group operates a number of with-profit funds in the UK in which the with-profit policyholders benefit from a discretionary annual bonus (guaranteed once added in most cases) and a discretionary final bonus. Non-participating business is also written in some of the with-profit funds and some of the funds may include immediate annuities and deferred annuities with Guaranteed Annuity Rates ('GAR').

The investment strategy of each fund differs, but is broadly to invest in a mixture of fixed interest investments and equities and/or property and other asset classes in such proportions as is appropriate to the investment risk exposure of the fund and its capital resources.

The Group has significant discretion regarding investment policy, bonus policy and early termination values. The process for exercising discretion in the management of the with-profit funds is set out in the PPFM for each with-profit fund and is overseen by With-Profit committees. Advice is also taken from the with-profit actuary of each with-profit fund. Compliance with the PPFM is reviewed annually and reported to the PRA, Financial Conduct Authority ('FCA') and policyholders.

The bonuses are designed to distribute to policyholders a fair share of the return on the assets in the with-profit funds together with other elements of the experience of the fund. The shareholders of the Group are entitled to receive one-ninth of the cost of bonuses declared for some funds and £nil for others.

Unitised and traditional with-profit policies are exposed to equivalent risks, the main difference being that unitised with-profit policies purchase notional units in a with-profit fund whereas traditional with-profit policies do not. Benefit payments for unitised policies are then dependent on unit prices at the time of a claim, although charges may be applied. A unitised with-profit fund price is typically guaranteed not to fall and increases in line with any discretionary bonus payments over the course of one year.

Deferred annuities

Deferred annuity policies are written to provide either a cash benefit at retirement, which the policyholder can use to buy an annuity on the terms then applicable, or an annuity payable from retirement. The policies contain an element of guarantee expressed in the form that the contract is written in, i.e. to provide cash or an annuity. Deferred annuity policies written to provide a cash benefit may also contain an option to convert the cash benefit to an annuity benefit on guaranteed terms; these are known as GAR policies. Deferred annuity policies written to provide an annuity benefit may also contain an option to convert the annuity benefit into cash benefits on guaranteed terms; these are known as Guaranteed Cash Option ('GCO') policies.

During the last decade, interest rates and inflation have fallen and life expectancy has increased more rapidly than originally anticipated. The guaranteed terms on GAR policies are more favourable than the annuity rates currently available in the market available for cash benefits. The guaranteed terms on GCO policies are currently not valuable. Deferred annuity policies which are written to provide annuity benefits are managed in a similar manner to immediate annuities and are exposed to the same risks.

The option provisions on GAR policies are particularly sensitive to downward movements in interest rates, increasing life expectancy and the proportion of customers exercising their option. Adverse movements in these factors could lead to a requirement to increase reserves which could adversely impact profit and potentially require additional capital. In order to address the interest rate risk (but not the risk of increasing life expectancy or changing customer behaviour with regard to exercise of the option), insurance subsidiaries within the Group have purchased derivatives that provide protection against an increase in liabilities and have thus reduced the sensitivity of profit to movements in interest rates.

The Group seeks to manage this risk in accordance with both the terms of the issued policies and the interests of customers, and has obtained external advice supporting the manner in which it operates the long-term funds in this respect.

Immediate annuities

This type of annuity is purchased with a single premium at the outset, and is paid to the policyholder for the remainder of their lifetime. Payments may also continue for the benefit of a surviving spouse or partner after the annuitant's death. Annuities may be level, or escalate at a fixed rate, or may escalate in line with a price index and may be payable for a minimum period irrespective of whether the policyholder remains alive.

The main risks associated with this product are longevity and investment risks. Longevity risk arises where the annuities are paid for the lifetime of the policyholder, and is managed through the initial pricing of the annuity and through reinsurance (appropriately collateralised) or transfer of existing liabilities. Annuities may also be a partial 'natural hedge' against losses incurred in protection business in the event of increased mortality (and vice versa) although the extent to which this occurs will depend on the similarity of the demographic profile of each book of business.

The pricing assumption for mortality risk is based on both historic internal information and externally-generated information on mortality experience, including allowances for future mortality improvements. Pricing will also include a contingency margin for adverse deviations in assumptions.

Market and credit risk is influenced by the extent to which the cash flows under the contracts have been matched by suitable assets which is managed under the ALM framework. Asset/liability modelling is used to monitor this position on a regular basis.

As noted earlier, a number of strategic initiatives were completed in 2016 that impacted the immediate annuity book.

Protection

These contracts are typically secured by the payment of a regular premium payable for a period of years providing benefits payable on certain events occurring within the period. The benefits may be a single lump sum or a series of payments and may be payable on death, serious illness or sickness.

The main risk associated with this product is the claims experience and this risk is managed through the initial pricing of the policy (based on actuarial principles), the use of reinsurance and a clear process for administering claims.

Market and credit risk is influenced by the extent to which the cash flows under the contracts have been matched by suitable assets which is managed under the ALM framework. Asset/liability modelling is used to monitor this position on a regular basis.

Following the acquisition and reinsurance of AXA Wealth's pension and protection business, the Group is exposed to increased mortality and new business pricing risk, although this provides a natural hedge to the annuity business.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES

G1. PROVISIONS

A provision is recognised when the Group has a present legal or constructive obligation, as a result of a past event, which is likely to result in an outflow of resources and where a reliable estimate of the amount of the obligation can be made. If the effect is material, the provision is 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.

A provision is recognised for onerous contracts when the expected benefits to be derived from the contracts are less than the related unavoidable costs. The unavoidable costs reflect the net cost of exiting the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

2016

	Leasehold properties £m	Staff related £m	Known incidents £m	PA(GI) provision £m	FCA thematic reviews provision £m	Restructuring provision £m	Other £m	Total £m
At 1 January	**5**	**13**	**2**	**6**	**–**	**–**	**2**	**28**
Additions in the year	–	1	–	33	–	30	–	64
Utilised during the year	–	(1)	–	(6)	–	–	–	(7)
Released during the year	–	–	–	–	–	–	(1)	(1)
Acquisition of Abbey Life during the year (see note H2.2)	–	–	–	–	25	–	–	25
At 31 December	**5**	**13**	**2**	**33**	**25**	**30**	**1**	**109**

Leasehold properties

The leasehold properties provision has been made for amounts in respect of the excess of lease rentals and other payments on properties that are currently vacant or are expected to become vacant, over the amounts to be recovered from subletting these properties. The discount rate used was 1.7% (2015: 1.7%) and it is expected that the provision will be utilised over the next 2 years (2015: 3 years).

Staff related

Staff related provisions include provisions for unfunded pensions of £6 million (2015: £6 million) and private medical insurance costs for former employees of £3 million (2015: £3 million).

Known incidents

The known incidents provision was created for historical data quality, administration systems problems and process deficiencies on the policy administration, financial reconciliations and operational finance aspects of business outsourced.

PA(GI) provision

In 2015, PA(GI), a subsidiary of the Group, was subject to a Companies Court judgement that directed that PA(GI) is liable to claimants for redress relating to creditor insurance policies within a book of insurance underwritten by PA(GI) until 2006. As a consequence, PA(GI) is liable for complaint handling and redress with regard to the complaints.

The PA(GI) provision of £33 million (2015: £6 million) represents the Group's best estimate of the likely future costs. However, this is subject to a number of risks and uncertainties including volumes of future complaints, the rates by which those complaints are upheld and the average redress value. No allowance has been made for any third party recoveries.

FCA thematic reviews provision

On 3 March 2016, the FCA published a thematic review report on the fair treatment of long-standing customers in the life insurance sector. Following completion of the review, Abbey Life is subject to additional investigations. Specifically, the FCA is exploring whether remedial and/or disciplinary action is necessary or appropriate in respect of exit or paid-up charges being applied. Additionally, Abbey Life is being investigated for potential contravention of regulatory requirements across a number of other areas assessed in the thematic review. The FCA has confirmed that these investigations have been commenced in order to enable the FCA to establish the reasons for the practices within firms and determine whether customers have suffered detriment as a result. No conclusion has been reached as to whether there have been any breaches of regulatory requirements. The commencement of investigations itself therefore cannot be taken to indicate that disciplinary action against Abbey Life will result nor does it indicate that a penalty will inevitably be imposed or that redress will be payable.

In addition, on 14 October 2016, the FCA published its thematic review of non-advised annuity sales. In its findings, the FCA identified concerns in a small number of firms relating to significant communications that took place orally, usually on the telephone. The FCA also identified other areas of possible concern, including in relation to the recording and maintenance of records of calls. The FCA encouraged all firms to consider its feedback and take appropriate action to address the points raised.

On acquisition of Abbey Life on 30 December 2016, obligations arising as a result of past practices in the areas covered by the two thematic reviews described above were assessed. As a result, it was determined appropriate to recognise a provision of £25 million on a fair value basis in this regard. Any resultant outflow of economic benefits is subject to uncertainty given the absence of final findings from the FCA review procedures, which would determine the extent to which the FCA may require Abbey Life to carry out remediation activities or impose financial penalties.

Under the terms of the acquisition, Deutsche Bank has provided PLHL with an indemnity, with a duration of up to eight years, in respect of exposures that may arise in Abbey Life as a result of the FCA's final thematic review findings in respect of annuity sales and enforcement in respect of long-standing customers. The maximum amount that can be claimed under the indemnity is £175 million and it applies to all regulatory fines and 80% to 90% of the costs of customer remediation. The indemnity would be expected to mitigate the Group's costs in the event of a crystallisation of exposures deemed not to trigger the recognition of a provision based on current information, or deterioration in management's estimate of the liabilities associated with present obligations.

Restructuring provision

Following the acquisition of the AXA businesses in the period, the Group is committed to the restructuring of these businesses to align their operating model with that of the other Group companies. These activities will involve separation and integration activities associated with the exiting of interim services agreements entered into with the vendor, and costs involved with implementing the Group's preferred outsourcer model. A provision of £30 million has been recognised in respect of management's best estimate of these costs as at 31 December 2016. The provision is expected to be utilised within 18 months.

Included in other provisions are litigation and onerous contract provisions.

G2. TAX ASSETS AND LIABILITIES

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.

	2016 £m	2015 £m
Current tax:		
Current tax receivable	**44**	47
Current tax payable	**(12)**	(7)
Deferred tax:		
Deferred tax liabilities	**(378)**	(354)

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G2. TAX ASSETS AND LIABILITIES continued

Movement in deferred tax assets/(liabilities)

2016

	1 January £m	Recognised in consolidated income statement £m	Recognised in other comprehensive income £m	Acquisition of AXA and Abbey Life (see note H2)	31 December £m
Trading losses	14	(5)	–	14	23
Expenses and deferred acquisition costs carried forward	16	(13)	–	–	3
Provisions and other temporary differences	8	13	1	1	23
Non-refundable pension scheme surplus	(7)	(3)	(3)	–	(13)
Committed future pension contributions	42	(8)	–	–	34
Pension scheme deficit	–	–	–	15	15
Accelerated capital allowances	6	1	–	–	7
Unpaid interest	21	(5)	–	–	16
Acquired in-force business	(359)	29	–	(34)	(364)
Customer relationships	(37)	4	–	(4)	(37)
Unrealised gains	–	(2)	–	(35)	(37)
IFRS transitional adjustments	(54)	8	–	(2)	(48)
Adjustment for insurance policies held with related parties in respect of the PGL Pension Scheme	(4)	4	–	–	–
	(354)	23	(2)	(45)	(378)

2015

	1 January £m	Recognised in consolidated income statement £m	Recognised in other comprehensive income £m	Disposals in year £m	31 December £m
Trading losses	37	(22)	–	(1)	14
Expenses and deferred acquisition costs carried forward	2	14	–	–	16
Provisions and other temporary differences	11	(2)	(1)	–	8
Non-refundable pension scheme surplus	(8)	1	–	–	(7)
Committed future pension contributions	57	(10)	(5)	–	42
Accelerated capital allowances	8	(2)	–	–	6
Unpaid interest	42	(21)	–	–	21
Acquired in-force business	(401)	42	–	–	(359)
Customer relationships	(43)	6	–	–	(37)
IFRS transitional adjustments	(64)	10		–	(54)
Adjustment for insurance policies held with related parties in respect of the PGL Pension Scheme	(5)	1	–	–	(4)
	(364)	17	(6)	(1)	(354)

The Finance Act 2014 set the rate of corporation tax at 20% from 1 April 2015. Finance (No. 2) Act 2015 reduced the rate of corporation tax to 19% in April 2017 and 18% from 1 April 2020. Finance Act 2016 reduced the corporation rate further to 17% from 1 April 2020. Consequently a blended rate of tax has been used for the purposes of providing for deferred tax in these financial statements.

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

	2016 £m	2015 £m
Deferred tax assets have not been recognised in respect of:		
Tax losses carried forward	**25**	16
Excess expenses and deferred acquisition costs	**33**	–
Provisions and other temporary differences	**3**	4
Deferred tax assets not recognised on capital losses[1]	**18**	89

1 These can only be recognised against future capital gains and have no expiry date.

G3. PAYABLES RELATED TO DIRECT INSURANCE CONTRACTS

Payables related to direct insurance contracts are recognised when due and are measured on initial recognition at the fair value of the consideration payable. Subsequent to initial recognition, these payables are measured at amortised cost using the effective interest rate method.

	2016 £m	2015 £m
Payables related to direct insurance contracts	**484**	364
Amount due for settlement after 12 months	**–**	–

G4. ACCRUALS AND DEFERRED INCOME

This note analyses the Group's accruals and deferred income at the end of the year.

	2016 £m	2015 £m
Accruals and deferred income	**204**	128
Amount due for settlement after 12 months	**–**	1

G5. OTHER PAYABLES

Other payables are recognised when due and are measured on initial recognition at the fair value of the consideration payable. Subsequent to initial recognition, these payables are measured at amortised cost using the effective interest rate method.

	2016 £m	2015 £m
Investment broker balances	**37**	581
Other payables	**65**	96
	102	677
Amount due for settlement after 12 months	**–**	–

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES

Defined contribution pension schemes

Obligations for contributions to defined contribution pension schemes are recognised as an expense in the consolidated income statement as incurred.

Defined benefit pension schemes

The net surplus or deficit (the economic surplus or deficit) in respect of the defined benefit pension schemes is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior years; that benefit is discounted to determine its present value and the fair value of any scheme assets is deducted.

The economic surplus or deficit is subsequently adjusted to eliminate on consolidation the carrying value of insurance policies issued by Group entities to the defined benefit pension schemes (the reported surplus or deficit). A corresponding adjustment is made to the carrying values of insurance contract liabilities and investment contract liabilities.

As required by IFRIC 14, IAS 19 – *'The limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'*, to the extent that the economic surplus will be available as a refund, the economic surplus is stated after a provision for tax that would be borne by the scheme administrators when the refund is made. The Group recognises a pension surplus on the basis that it is entitled to the surplus of each scheme in the event of a gradual settlement of the liabilities, due to its ability to order a winding-up of the Trust.

Additionally under IFRIC 14 pension funding contributions are considered to be a minimum funding requirement and, to the extent that the contributions payable will not be available to the Group after they are paid into the scheme, a liability is recognised when the obligation arises. The net defined benefit asset/liability represents the economic surplus net of all adjustments noted above.

The Group determines the net interest expense or income on the net defined benefit asset/liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the opening net defined benefit asset/liability. The discount rate is the yield at the period end on AA credit rated bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

The movement in the net defined benefit asset/liability is analysed between the service cost, past service cost, curtailments and settlements (all recognised within administrative expenses in the consolidated income statement), the net interest cost on the net defined benefit asset/liability, including any reimbursement assets (recognised within net investment income in the consolidated income statement), remeasurements of the net defined asset/liability (recognised in other comprehensive income) and employer contributions.

This note describes the Group's three main staff pension schemes for its employees, the Pearl Group Staff Pension Scheme, the PGL Pension Scheme, and the Abbey Life Staff Pension Scheme and explains how the pension asset/liability is calculated.

An analysis of the defined benefit asset for each pension scheme is set out below:

	2016 £m	2015 £m
Pearl Group Staff Pension Scheme (see G6.1)		
Economic surplus	448	276
Minimum funding requirement obligation	(66)	(74)
Provision for tax on that part of the economic surplus available as a refund on a winding-up of the Scheme	(157)	(97)
Net defined benefit asset	225	105
PGL Pension Scheme (see G6.2)		
Economic surplus (including £387 million (2015: £570 million) available as a refund on a winding-up of the Scheme)	465	631
Adjustment for insurance policies eliminated on consolidation	(913)	(22)
Adjustment for amounts due from subsidiary eliminated on consolidation	(6)	–
Net economic (deficit)/surplus	(454)	609
Minimum funding requirement obligation	(4)	(9)
Provision for tax on that part of the economic surplus available as a refund on a winding-up of the Scheme	(135)	(199)
Net defined benefit (liability)/asset	(593)	401
Abbey Life Staff Pension Scheme (see G6.3)		
Net defined benefit liability	(87)	–

In December 2016, the PGL Pension Scheme entered into a buy-in transaction with PLL which converted the existing longevity swap contract into a bulk annuity contract. Plan assets transferred as a result of this transaction are no longer recognised in the pension scheme asset/liability, but are instead recognised within financial assets in the consolidated statement of financial position. Further details are included in section G6.2.

The Group's defined benefit schemes typically expose the Group to a number of risks, the most significant of which are:

- Asset volatility – the value of the schemes' assets will vary as market conditions change and as such is subject to considerable volatility. The volatility in the schemes' assets can be caused by both volatility within the markets or variations in the return achieved by the schemes' investment managers relative to market performance. In particular there is the risk that the variation in asset values will not be in line with the variation in pension liability values, and as such differences in the nature and duration of the assets and liabilities can cause difference in the way that the assets and liabilities vary.
- Inflation risk – a significant proportion of the schemes' benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities (although in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). Assets in both schemes are invested so as to hedge a significant proportion of the inflation risks, further details of which are included in this note.
- Life expectancy – the majority of the schemes' obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

Information on each of these schemes is set out below.

G6.1 Pearl Group Staff Pension Scheme

Scheme details

The Pearl Group Staff Pension Scheme ('the Pearl Scheme') comprises a final salary section, a money purchase section and a hybrid section (a mix of final salary and money purchase). The final salary and hybrid sections of the Pearl Scheme are closed to new members, and since 1 July 2011 are also closed to future accrual by active members.

Defined contribution scheme

Contributions in the year amounted to £1 million (2015: £1 million).

Defined benefit scheme

The Pearl Scheme is established under, and governed by, the trust deeds and rules and is funded by payment of contributions to a separately administered trust fund. A Group company, Pearl Group Holdings No.2 Limited ('PGH2'), is the principal employer of the Pearl Scheme. The principal employer meets the administration expenses of the Scheme. The Pearl Scheme is administered by a separate Trustee company, P.A.T. (Pensions) Limited, which is separate from the company. The Trustee company is comprised of two representatives from the Group, three member nominated representatives and one independent trustee in accordance with the Trustee company's articles of association. The Trustee is required by law to act in the interest of all relevant beneficiaries and is responsible for the investment policy with regard to the assets.

To the extent that an economic surplus will be available as a refund, the economic surplus is stated after a provision for tax that would be borne by the scheme administrators when the refund is made. Additionally, pension funding contributions are considered to be a minimum funding requirement and, to the extent that the contributions payable will not be available to the Group after they are paid into the scheme, a liability is recognised when the obligation arises.

The valuation has been based on an assessment of the liabilities of the Pearl Scheme as at 31 December 2016, undertaken by independent qualified actuaries. The present values of the defined benefit obligation and the related interest costs have been measured using the projected unit credit method.

Funding

A triennial funding valuation of the Pearl Scheme as at 30 June 2015 was completed in September 2016. This showed a deficit as at 30 June 2015 of £300 million, on the agreed technical provisions basis.

On 27 November 2012, the principal employer and the Trustee of the Pearl Scheme entered into a revised pensions funding agreement (the 'Pensions Agreement'), the principal terms of which have not been altered following the 30 June 2015 triennial valuation. The principal terms of the Pensions Agreement are:

- annual cash payments into the scheme of £70 million in 2013 and 2014 payable on 30 September, followed by payments of £40 million each year from 2015 to 2021. It is expected that the timing of payment of contributions will change during 2017 so that the contributions will be paid on a monthly basis. The Pensions Agreement includes a sharing mechanism, related to the level of dividends paid out of PGH2, that in certain circumstances allows for an acceleration of the contributions to be paid to the Pearl Scheme;
- additional contributions may become payable if the scheme is not anticipated to meet the two agreed funding targets:
    (i) to reach full funding on the technical provisions basis by 30 June 2022; and
    (ii) to reach full funding on a gilts flat basis by 30 June 2031;
- the Trustee continues to benefit from a first charge over shares in Phoenix Life Assurance Limited, Pearl Group Services Limited and PGS2 Limited. The security claim granted under the share charges is capped at the lower of £600 million and 100% of the Pearl Scheme deficit (calculated on a basis linked to UK government securities) revalued every three years thereafter; and
- covenant tests relating to the embedded value of certain companies with the Group.

It should be noted that the terms of the £900 million facility agreement (see note E5) restrict the Group's ability, with certain exceptions, to transfer assets into the companies over which the Trustee holds a charge over shares.

An additional liability of £66 million (2015: £74 million) has been recognised, reflecting a charge on any refund of the resultant IAS 19 surplus that arises after adjustment for discounted future contributions of £189 million (2015: £213 million) in accordance with the minimum funding requirement. A deferred tax asset of £32 million (2015: £38 million) has also been recognised to reflect tax relief at a rate of 17% (2015: 18%) that is expected to be available on the contributions, once paid into the scheme.

Contributions totalling £40 million were paid into the scheme on 30 September 2016 (2015: £40 million), and contributions totalling £50 million are expected to be paid into the scheme in 2017, £10 million in relation to the last quarter of 2016 and £40 million by monthly instalments.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES continued

Summary of amounts recognised in the consolidated financial statements

The amounts recognised in the consolidated financial statements are as follows:

2016

	Fair value of scheme assets £m	Defined benefit obligation £m	Provision for tax on the economic surplus available as a refund £m	Minimum funding requirement obligation £m	Total £m
At 1 January	2,213	(1,937)	(97)	(74)	105
Interest income/(expense)	84	(73)	(3)	(3)	5
Included in profit or loss	84	(73)	(3)	(3)	5
Remeasurements:					
Return on plan assets excluding amounts included in interest income	453	–	–	–	453
Loss from changes in demographic assumptions	–	(15)	–	–	(15)
Loss from changes in financial assumptions		(367)			(367)
Experience gains	–	50	–	–	50
Change in provision for tax on economic surplus available as a refund	–	–	(57)	–	(57)
Change in minimum funding requirement obligation	–	–	–	11	11
Included in other comprehensive income	453	(332)	(57)	11	75
Employer's contributions	40	–	–	–	40
Benefit payments	(105)	105	–	–	–
At 31 December	2,685	(2,237)	(157)	(66)	225

2015

	Fair value of scheme assets £m	Defined benefit obligation £m	Provision for tax on the economic surplus available as a refund £m	Minimum funding requirement obligation £m	Total £m
At 1 January	2,279	(2,061)	(76)	(86)	56
Interest income/(expense)	82	(73)	(3)	(3)	3
Included in profit or loss	82	(73)	(3)	(3)	3
Remeasurements:					
Return on plan assets excluding amounts included in interest income	(85)	–	–	–	(85)
Gain from changes in demographic assumptions	–	55	–	–	55
Experience gains	–	39	–	–	39
Change in provision for tax on economic surplus available as a refund	–	–	(18)	–	(18)
Change in minimum funding requirement obligation	–	–	–	15	15
Included in other comprehensive income	(85)	94	(18)	15	6
Employer's contributions	40	–	–	–	40
Benefit payments	(103)	103	–	–	–
At 31 December	2,213	(1,937)	(97)	(74)	105

Scheme assets

The distribution of the scheme assets at the end of the year was as follows:

	2016		2015	
	Total £m	**Of which not quoted in an active market £m**	Total £m	Of which not quoted in an active market £m
Hedging portfolio	**2,327**	**(38)**	1,891	(24)
Equities	**134**	**–**	122	–
Fixed interest gilts	**129**	**–**	130	–
Other debt securities	**958**	**–**	941	–
Properties	**206**	**206**	191	191
Private equities	**38**	**38**	34	34
Hedge funds	**30**	**30**	32	32
Cash and other	**84**	**–**	99	–
Obligations for repayment of stock lending collateral received	**(1,221)**	**–**	(1,227)	–
	2,685	**236**	2,213	233

The actual return on plan assets was a gain of £537 million (2015: £3 million loss).

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES continued

The Group ensures that the investment positions are managed within an asset liability matching ('ALM') framework that has been developed to achieve long-term investments that are in line with the obligations under the Pearl Scheme. Within this framework an allocation of 25% of the scheme assets is invested in collateral for interest rate and inflation rate hedging where the intention is to hedge greater than 90% of the interest rate and inflation rate risk measured on the technical provisions basis.

The Pearl Scheme uses swaps, UK Government bonds and UK Government stock lending to hedge the interest rate and inflation exposure arising from the liabilities which are disclosed in the table above as 'Hedging Portfolio' assets. Under the Scheme's stock lending programme, the Scheme lends a Government bond to an approved counterparty and receives a similar value in the form of cash in return which is typically reinvested into other Government bonds. The Scheme retains economic exposure to the Government bond, hence the bonds continue to be recognised as scheme assets with a corresponding liability to repay the cash received as disclosed in the table above.

Defined benefit obligation

The calculation of the defined benefit obligation can be allocated to the scheme's members as follows:

– Deferred scheme members: 38% (2015: 40%)

– Pensioners: 62% (2015: 60%)

The weighted average duration of the defined benefit obligation at 31 December 2016 is 17 years (2015: 17 years).

Principal assumptions

The principal financial assumptions of the Pearl Scheme are set out in the table below:

	2016 %	2015 %
Rate of increase for pensions in payment (5% per annum or RPI if lower)	**3.05**	2.95
Rate of increase for deferred pensions ('CPI')	**2.20**	2.05
Discount rate	**2.65**	3.85
Inflation – RPI	**3.20**	3.05
Inflation – CPI	**2.20**	2.05

The discount rate and inflation rate assumptions have been determined by considering the shape of the appropriate yield curves and the duration of the Pearl Scheme's liabilities. This method determines an equivalent single rate for each of the discount and inflation rates, which is derived from the profile of projected benefit payments.

It has been assumed that post-retirement mortality is in line with a scheme-specific table which was derived from the actual mortality experience in recent years based on the SAPS standard tables for males and for females based on year of use. Future longevity improvements are based on CMI 2014 Core Projections and a long-term rate of improvement of 2% p.a. up to and including age 75 then decreasing linearly to 0% p.a. at age 110. Under these assumptions, the average life expectancy from retirement for a member currently aged 40 retiring at age 60 is 31.0 years and 33.1 years for male and female members respectively.

A quantitative sensitivity analysis for significant actuarial assumptions as at 31 December 2016 is shown below:

2016

Assumptions	**Base**	**Discount rate**		**RPI**		**Life expectancy**	
Sensitivity level		**25bps increase**	**25bps decrease**	**25bps increase**	**25bps decrease**	**1 year increase**	**1 year decrease**
Impact on the defined benefit obligation (£m)	**2,237**	**(86)**	**91**	**60**	**(56)**	**63**	**(62)**

2015

Assumptions	Base	Discount rate		RPI		Life expectancy	
Sensitivity level		25bps increase	25bps decrease	25bps increase	25bps decrease	1 year increase	1 year decrease
Impact on the defined benefit obligation (£m)	1,937	(71)	75	54	(52)	54	(54)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method has been applied as when calculating the pension asset recognised within the statement of financial position.

The UK Government currently intends to equalise benefits between males and females arising from the accrual of Guaranteed Minimum Pensions ('GMP') requirements. Legislation will be implemented following completion of the ongoing consultation on this matter. Once this consultation process has reached a conclusion, the Group will be able to quantify the impact of this change.

G6.2 PGL Pension Scheme

The PGL Pension Scheme comprises a final salary section and a defined contribution section.

Scheme details

Defined contribution scheme

Contributions in the year amounted to £6 million (2015: £6 million).

Defined benefit scheme

The defined benefit section of the PGL Pension Scheme is a final salary arrangement which is closed to new entrants and has been closed to future accrual by active members since 1 July 2011.

The PGL Scheme is administered by a separate trustee company, PGL Pension Trustee Ltd. The trustee company is comprised of two representatives from the Group, three member nominated representatives and one independent trustee in accordance with the trustee company's articles of association. The Trustee is required by law to act in the interest of all relevant beneficiaries and is responsible for the investment policy with regard to the assets plus the day to day administration of the benefits.

The valuation has been based on an assessment of the liabilities of the PGL Pension Scheme as at 31 December 2016, undertaken by independent qualified actuaries.

To the extent that an economic surplus will be available as a refund, the economic surplus is stated after a provision for tax that would be borne by the scheme administrators when the refund is made. Additionally pension funding contributions are considered to be a minimum funding requirement and, to the extent that the contributions payable will not be available to the Group after they are paid into the scheme, a liability is recognised when the obligation arises.

Funding

A triennial funding valuation of the PGL Pension Scheme as at 30 June 2015 was completed in June 2016. This showed a surplus as at 30 June 2015 of £164 million. Following discussions with the Trustee of the PGL Pension Scheme it was agreed that the existing schedule of cash contributions to the scheme amounting to £59 million in total over the period from October 2013 to August 2017 would remain unchanged. Contributions totalling £15 million were paid into the scheme in 2016 (2015: £15 million) and the remaining outstanding contributions totalling £10 million are expected to be paid into the scheme in 2017.

An additional liability has been recognised of £4 million (2015: £9 million) reflecting a charge on any refund of the resultant economic surplus (prior to the elimination of insurance policies) that arises after adjustment for discounted future contributions of £10 million (2015: £24 million) in accordance with the minimum funding requirement. A deferred tax asset of £2 million (2015: £4 million) has also been recognised to reflect tax relief at a rate of 17% (2015: 18%) that is expected to be available on the contributions, once paid into the scheme.

Liability management exercises

In January 2016, the Group carried out a pension increase exchange ('PIE') exercise in respect of the PGL Pension Scheme. Existing in-scope pensioners were offered the option to exchange future non-statutory pension increases for a one-off uplift to their current pension, thereby reducing longevity and inflation risk for the Group. The financial effect of all acceptances received in the period has been recognised in the consolidated financial statements as a reduction in scheme liabilities of £3 million shown as a past service credit in the condensed consolidated income statement.

In February 2016, the Group commenced a flexible retirement option ('FRO') exercise whereby defined members who are eligible to retire within the PGL Pension Scheme were offered a transfer value on standard terms or a pension in the scheme. The financial effect of all acceptances received have been recognised in the consolidated financial statements and an experience gain of £2 million on liabilities arose as a result of this exercise.

Insurance policies with Group entities

In June 2014, the PLL non-profit fund entered into a longevity swap with the PGL Pension Scheme with effect from 1 January 2014, under which the Scheme transferred the risk of longevity improvements to PLL. The financial effect of this contract was eliminated on consolidation.

In December 2016, the PGL Pension Scheme entered into a 'buy-in' agreement with PLL, which converted the longevity swap contract into a bulk annuity contract, covering both longevity and investment risk. The Scheme transferred £1,164 million of plan assets to a collateral account over which PLL has a fixed charge. The assets transferred to PLL are recognised in the relevant line within financial assets in the consolidated statement of financial position (see note E1). The transfer of the assets constituted the payment of the premium to PLL and a simultaneous deposit of collateral by PLL, and was net of a £23 million prepayment by PLL to the scheme in respect of benefits up to 31 May 2017. An adjustment of £6 million to the value of the premium is due to be paid by PLL to the PGL Scheme in 2017. The economic effect of the 'buy-in' transaction in the Scheme is to replace the plan assets transferred with a single line insurance policy reimbursement asset which is eliminated on consolidation. The value of this insurance policy at 31 December 2016 was £892 million.

Included within insurance policies with Group entities of £913 million is a further insurance policy reimbursement asset of £21 million (2015: £22 million) which was also eliminated on consolidation.

At the same time as the buy-in transaction, there was a rule change made with respect to pre-1997 excess benefits for members of the Phoenix section of the PGL Scheme. Pensions increases will now be increased in line with CPI inflation subject to a maximum of 5% p.a. Prior to this, members received discretionary increases in payment on these benefits with the discretionary increases not allowed for in the defined benefit obligation. The financial impact of this change has been to recognise an increase in the defined benefit obligation of £6 million, and a past service cost in the consolidated income statement.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES continued

Summary of amounts recognised in the consolidated financial statements

The amounts recognised in the consolidated financial statements are as follows:

2016

	Fair value of scheme assets £m	Defined benefit obligation £m	Provision for tax on the economic surplus available as a refund £m	Minimum funding requirement obligation £m	Total £m
At 1 January	2,006	(1,397)	(199)	(9)	401
Interest income/(expense)	76	(52)	(8)	–	16
Administrative expenses	(2)	–	–	–	(2)
Past service cost	–	(3)	–	–	(3)
Included in profit or loss	74	(55)	(8)	–	11
Remeasurements:					
Return on plan assets excluding amounts included in interest income	349	–	–	–	349
Experience gains	–	15	–	–	15
Loss from changes in financial assumptions	–	(289)	–	–	(289)
Loss from changes in demographic assumptions		(8)			(8)
Change in provision for tax on economic surplus available as a refund	–	–	72	–	72
Change in minimum funding requirement obligation	–	–	–	5	5
Included in other comprehensive income	349	(282)	72	5	144
Scheme assets transferred as premium for buy-in transaction	(1,164)	–	–	–	(1,164)
Employer's contributions	15	–	–	–	15
Benefit payments	(85)	85	–	–	–
At 31 December	1,195	(1,649)	(135)	(4)	(593)

2015

	Fair value of scheme assets £m	Defined benefit obligation £m	Provision for tax on the economic surplus available as a refund £m	Minimum funding requirement obligation £m	Total £m
At 1 January	2,024	(1,457)	(184)	(13)	370
Interest income/(expense)	73	(52)	(6)	(1)	14
Administrative expenses	(3)	–	–	–	(3)
Included in profit or loss	70	(52)	(6)	(1)	11
Remeasurements:					
Return on plan assets excluding amounts included in interest income	(40)	–	–	–	(40)
Experience gains	–	13	–	–	13
Gain from changes in financial assumptions	–	36	–	–	36
Change in provision for tax on economic surplus available as a refund	–	–	(9)	–	(9)
Change in minimum funding requirement obligation	–	–	–	5	5
Included in other comprehensive income	(40)	49	(9)	5	5
Employer's contributions	15	–	–	–	15
Benefit payments	(63)	63	–	–	–
At 31 December	2,006	(1,397)	(199)	(9)	401

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES continued

Scheme assets

The distribution of the scheme assets at the end of the year was as follows:

	2016		2015	
	Total £m	Of which not quoted in an active market £m	Total £m	Of which not quoted in an active market £m
Fixed interest gilts	320	–	930	–
Index-linked bonds	732	–	984	–
Swaps	7	7	3	3
Properties	104	104	98	98
Hedge funds	85	85	83	83
Corporate bonds	13	–		
Cash and other	29	–	21	–
Obligations for repayment of stock lending collateral received	(95)	–	(113)	–
Reported scheme assets	1,195	196	2,006	184
Add back:				
Insurance policies eliminated on consolidation	913	–	22	–
Amounts due from subsidiary eliminated on consolidation	6	–	–	–
Economic value of assets	2,114	196	2,028	184

The actual return on plan assets was £425 million (2015: £33 million).

The Group ensures that the investment positions are managed within an asset liability matching (ALM) framework that has been developed to achieve long-term investments that are in line with the obligations under the pension scheme. Within this framework an allocation of 85% of the scheme assets is invested in a combination of supranational debt and a liability hedging portfolio. The Liability Driven Investment ('LDI') portfolio is passively managed against a liability benchmark in order to hedge the duration and inflation risks.

The PGL Scheme uses swaps, UK Government bonds and UK Government stock lending to hedge the interest rate and inflation exposure arising from the liabilities. Under the Scheme's stock lending programme, the Scheme lends a Government bond to an approved counterparty and receives a similar value of cash in return which it typically reinvested into other Government bonds. The Scheme retains economic exposure to the Government bonds, hence the value of the gilts continues to be recognised as a scheme asset with a corresponding liability to repay the cash received as disclosed in the table above.

Defined benefit obligation

The calculation of the defined benefit obligation can be allocated to the scheme's members as follows:

– Deferred scheme members: 39% (2015: 39%)

– Pensioners: 61% (2015: 61%)

The weighted average duration of the defined benefit obligation at 31 December 2016 is 19 years (2015: 17 years).

Principal assumptions

The principal financial assumptions of the PGL Pension Scheme are set out in the table below:

	2016 %	2015 %
Rate of increase for pensions in payment (7.5% per annum or RPI if lower)	3.25	3.10
Rate of increase for deferred pensions ('CPI')	2.20	2.05
Discount rate	2.65	3.85
Inflation – RPI	3.20	3.05
Inflation – CPI	2.20	2.05

The discount rate and inflation assumptions have been determined by considering the shape of the appropriate yield curves and the duration of the PGL Scheme liabilities. This method determines an equivalent single rate for each of the discount and inflation rates, which is derived from the profile of projected benefit payments.

It has been assumed that post-retirement mortality is in line with 86%/94% of S1PA base tables with future longevity improvements in line with CMI 2014 Core Projections and a long-term rate of improvement of 2% p.a. up to and including age 75 then decreasing linearly to 0% at age 110. Under these assumptions, the average life expectancy from retirement for a member currently aged 40 retiring at age 62 is 27.7 years and 29.5 years for male and female members respectively.

A quantitative sensitivity analysis for significant actuarial assumptions as at 31 December 2016 is shown below:

2016

Assumptions	Base	Discount rate		RPI		Life expectancy	
Sensitivity level		25bps increase	25bps decrease	25bps increase	25bps decrease	1 year increase	1 year decrease
Impact on the defined benefit obligation (£m)	1,649	(70)	75	47	(51)	55	(55)

2015

Assumptions	Base	Discount rate		RPI		Life expectancy	
Sensitivity level		25bps increase	25bps decrease	25bps increase	25bps decrease	1 year increase	1 year decrease
Impact on the defined benefit obligation (£m)	1,397	(54)	57	37	(39)	46	(46)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method has been applied as when calculating the pension liability recognised within the statement of financial position.

The UK Government currently intends to equalise benefits between males and females arising from the accrual of Guaranteed Minimum Pension ('GMP') requirements. Legislation will be implemented following completion of the ongoing consultation on this matter. Once this consultation process has reached a conclusion, the Group will be able to quantify the impact of this change.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G6. PENSION SCHEMES continued

G6.3 Abbey Life Staff Pension Scheme

Scheme details

The Abbey Life Staff Pension Scheme ('the Abbey Life Scheme') was consolidated into the Group statement of financial position following the acquisition of Abbey Life Assurance Company Limited ('Abbey Life') (see note H2.2). The scheme is a defined benefit scheme which is currently open to future accrual. The Abbey Life Scheme is a registered occupational pension scheme, set up under Trust, and legally separate from the employer Abbey Life. The scheme is administered by Abbey Life Trust Securities Limited ('The Trustee'), a corporate trustee. There are four Trustee Directors, two of whom are nominated by the scheme members and two of whom are appointed by Abbey Life. The Trustee is responsible for administering the scheme in accordance with the trust deed and rules and pensions laws and regulations.

The trust deed under which the Abbey Life Scheme is established provides for the gradual settlement of the plan liabilities over time until all members have left the scheme. Where appropriate, any excess value of the assets over the liabilities is recognised in the consolidated statement of financial position in accordance with IFRIC 14.

The valuation has been based on an assessment of the liabilities of the Abbey Life Scheme as at 31 December 2016 undertaken by independent qualified actuaries. The present values of the defined benefit obligation and the related interest costs have been measured using the projected unit credit method.

Funding

The last funding valuation of the Scheme was carried out by a qualified actuary as at 31 March 2015 and showed a deficit of £107 million. A new schedule of contributions was introduced with effect from 1 July 2016 following completion of the 31 March 2015 funding valuation. In respect of future accrual of benefits, Abbey Life will pay 39.5% of gross pensionable earnings from 1 July 2016. In relation to deficit contributions, Abbey Life will pay the following:

- a lump sum of £15 million into the Scheme by 30 June 2016 (paid on 24 June 2016);
- monthly contributions of £246,000 into the Scheme between 1 July 2016 and 30 June 2026. These amounts are to be paid to the Scheme on or before the 19th of the calendar month following that to which the payment relates;
- annual payments of £2.92 million into the 2016 Charged Account by 31 July each year, with the first payment being due by 31 July 2016, and the last payment due by 31 July 2025.

The Charged Accounts are escrow accounts which were created to provide the Trustees with additional security in light of the funding deficit. The amounts held in the Charged Accounts do not form part of Scheme assets.

Under the terms of the 2013 Funding Agreement dated 28 June 2013, the funding position of the Scheme will be assessed as at 31 March 2021. A payment will be made from the 2013 Charged Account to the Scheme if the results of the assessment reveal a shortfall calculated in accordance with the terms of the 2013 Funding Agreement. The amount of the payment will be the lower of the amount of the shortfall and the amount held in the 2013 Charged Account.

Under the terms of the 2016 Funding Agreement dated 23 June 2016, the funding position of the Scheme will be assessed as at 31 March 2027. A payment will be made from the 2016 Charged Account to the Scheme if the results of the assessment reveal a shortfall calculated in accordance with the terms of the 2016 Funding Agreement. The amount of the payment will be the lower of the amount of the shortfall and the amount held in the 2016 Charged Account.

Summary of amounts recognised in the consolidated financial statements

The amounts recognised in the consolidated financial statements are as follows:

2016

	Fair value of scheme assets £m	Defined benefit obligation £m	Total £m
At 1 January	–	–	–
Acquisition of Abbey Life	**237**	**(324)**	**(87)**
At 31 December	**237**	**(324)**	**(87)**

As the acquisition of Abbey Life took place on 30 December 2016, no amounts are recognised in the consolidated income statement or in the statement of comprehensive income in relation to the Abbey Life Scheme.

Scheme assets

The distribution of the scheme assets at the end of the year was as follows:

	2016 Total £m	2016 Of which not quoted in an active market £m
Equities – UK	**25**	**–**
Fixed interest government bonds	**115**	**–**
Corporate bonds	**123**	**–**
Derivatives	**(35)**	**(35)**
Cash and cash equivalents	**9**	**–**
Pension scheme assets	**237**	**(35)**

Derivative values above include interest rate and inflation rate swaps and foreign exchange forward contracts. The Abbey Life Scheme has hedged its inflation risk through an inflation swap. It is currently exposed to interest rate risk to the extent that the holdings in bonds are mismatched to the scheme liabilities. The long-term intention is to fully hedge this risk through an interest rate swap. Further key risks that will remain are longevity and credit spread exposures.

Defined benefit obligation

The calculation of the defined benefit obligation can be allocated to the scheme's members as follows:

- Active scheme members: 5%
- Deferred scheme members: 59%
- Pensioners: 36%

The weighted average duration of the defined benefit obligation at 31 December 2016 is 18 years.

Principal assumptions

The principal financial assumptions of the Abbey Life Scheme are set out in the table below:

	2016 %
Rate of increase for pensions in payment	**3.05**
Rate of increase for deferred pensions ('CPI' subject to caps)	**2.20**
Discount rate	**2.70**
Inflation – RPI	**3.20**
Inflation – CPI	**2.20**
Rate of salary increases	**4.20**
Commutation of benefits to lump sums on retirement	**15.00**

The discount rate and inflation assumptions have been determined by considering the shape of the appropriate yield curves and the duration of the Abbey Life Scheme liabilities. This method determines an equivalent single rate for each of the discount and inflation rates, which is derived from the profile of projected benefit payments.

It has been assumed that post-retirement mortality is in line with a scheme-specific table which was derived from the actual mortality experience in recent years, performed as part of the actuarial funding valuation as at 31 March 2015, using the SAPS S2 'Light' tables for males and for females based on year of use. Future longevity improvements are based on CMI 2015 Core Projections with long-term improvements of 1.25% p.a. Under these assumptions the average life expectancy from retirement for a member currently aged 45 retiring at age 65 is 25.0 years and 27.2 years for male and female members respectively.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

A quantitative sensitivity analysis for significant actuarial assumptions as at 31 December 2016 is shown below:

2016

Assumptions	Base	Discount rate		RPI		Life expectancy	
Sensitivity level		25bps increase	25bps decrease	25bps increase	25bps decrease	1 year increase	1 year decrease
Impact on the defined benefit obligation (£m)	324	(14)	15	11	(11)	10	(10)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method has been applied as when calculating the pension liability recognised within the statement of financial position.

The UK Government currently intends to equalise benefits between males and females arising from the accrual of Guaranteed Minimum Pension ('GMP') requirements. Legislation will be implemented following completion of the ongoing consultation on this matter. Once this consultation process has reached a conclusion, the Group will be able to quantify the impact of this change.

G7. INTANGIBLE ASSETS

Goodwill

Business combinations are accounted for by applying the purchase method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill is measured on initial recognition at cost. Following initial recognition, goodwill is stated at cost less any accumulated impairment losses. It is tested for impairment annually or when there is evidence of possible impairment. Goodwill is not amortised. For impairment testing, goodwill is allocated to relevant cash generating units and is impaired when the recoverable amount is less than the carrying value.

Acquired in-force business

Insurance and investment contracts with DPF acquired in business combinations and portfolio transfers are measured at fair value at the time of acquisition. The difference between the fair value of the contractual rights acquired and obligations assumed and the liability measured in accordance with the Group's accounting policies for such contracts is recognised as acquired in-force business. This acquired in-force business is amortised over the estimated life of the contracts on a basis which recognises the emergence of the economic benefits.

The value of acquired in-force business related to investment contracts without DPF is recognised at its fair value and is amortised on a diminishing balance basis.

An impairment review is performed whenever there is an indication of impairment. When the recoverable amount is less than the carrying value, an impairment loss is recognised in the consolidated income statement. Acquired in-force business is also considered in the liability adequacy test for each reporting period.

The acquired in-force business is allocated to relevant cash generating units for the purposes of impairment testing.

Customer relationships

The customer relationship intangible asset includes vesting pension premiums and is measured on initial recognition at cost. The cost of this intangible asset acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, the customer relationship intangible asset is carried at cost less any accumulated amortisation and any accumulated impairment losses.

The intangible asset is amortised on a straight-line basis over its useful economic life and assessed for impairment whenever there is an indication that the recoverable amount of the intangible asset is less than its carrying value. The customer relationship intangible asset is allocated to relevant cash generating units for the purposes of impairment testing.

Internally generated intangible assets are not capitalised and expenditure is reflected in the consolidated income statement in the year in which the expenditure is incurred.

Present value of future profits on non-participating business in the with-profit fund

The present value of future profits is determined on a realistic basis.

Brands

Brands acquired in a business combination are recognised at fair value at the acquisition date, and measured on initial recognition at cost. Brands have finite lives and are carried at cost less amortisation. Amortisation is calculated using the straight-line method to allocate the cost of brands over their estimated useful lives. They are tested for impairment annually or when there is evidence of possible impairment. For impairment testing, they are allocated to the relevant cash generating unit. Brands are impaired when the recoverable amount is less than the carrying value.

2016

	Goodwill £m	Acquired in-force business £m	Other intangibles: Customer relationships £m	Other intangibles: Present value of future profits £m	Other intangibles: Brands £m	Other intangibles: Total other intangibles £m	Total £m
Cost or valuation							
At 1 January	**39**	**2,048**	**297**	**17**	**–**	**314**	**2,401**
On acquisition of AXA businesses (see note H2.1)	**10**	**38**	**–**	**–**	**20**	**20**	**68**
On acquisition of Abbey Life (see note H2.2)	**8**	**180**	**–**	**–**	**–**	**–**	**188**
Revaluation	**–**	**–**	**–**	**(11)**	**–**	**(11)**	**(11)**
At 31 December	**57**	**2,266**	**297**	**6**	**20**	**323**	**2,646**
Amortisation and impairment							
At 1 January	**–**	**(783)**	**(95)**	**–**	**–**	**(95)**	**(878)**
Amortisation charge for the year	**–**	**(76)**	**(14)**	**–**	**–**	**(14)**	**(90)**
At 31 December	**–**	**(859)**	**(109)**	**–**	**–**	**(109)**	**(968)**
Carrying amount at 31 December	**57**	**1,407**	**188**	**6**	**20**	**214**	**1,678**
Amount recoverable after 12 months	**57**	**1,302**	**174**	**6**	**18**	**198**	**1,557**

2015

	Goodwill £m	Acquired in-force business £m	Other intangibles: Customer relationships £m	Other intangibles: Present value of future profits £m	Other intangibles: Total other intangibles	Total £m
Cost or valuation						
At 1 January	39	2,048	297	23	320	2,407
Revaluation	–	–	–	(6)	(6)	(6)
At 31 December	39	2,048	297	17	314	2,401
Amortisation						
At 1 January	–	(635)	(80)	–	(80)	(715)
Amortisation charge for the year	–	(84)	(15)	–	(15)	(99)
Impairment charge for the year	–	(64)	–	–	–	(64)
At 31 December	–	(783)	(95)	–	(95)	(878)
Carrying amount at 31 December	39	1,265	202	17	219	1,523
Amount recoverable after 12 months	39	1,191	187	17	204	1,434

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G7. INTANGIBLE ASSETS continued

G7.1 Goodwill

The carrying value of goodwill has been tested for impairment at the year-end. No impairment has resulted as the value in use of this intangible continues to exceed its carrying value.

£39 million of the goodwill is attributable to the management services business of the Phoenix Life segment. Value in use has been determined as the present value of certain future cash flows associated with this business. The cash flows used in this calculation have been valued using a discount rate of 7.7% (2015: 9.0%) and are consistent with those adopted by management in the Group's operating plan and, for the period 2021 and beyond, reflect the anticipated run-off of the Phoenix Life insurance business. The underlying assumptions of these projections include management's best estimates with regards to longevity, persistency, mortality and morbidity.

Impairment tests have been performed using assumptions which management consider reasonable. Given the magnitude of the excess of the value in use over carrying value, management does not believe that a reasonably foreseeable change in key assumptions would cause the carrying value to exceed value in use.

During the year, goodwill of £10 million was recognised on the acquisition of the AXA businesses and £8 million was recognised on the acquisition of Abbey Life. These businesses are considered to be separate cash generating units for the purpose of impairment testing.

G7.2 Acquired in-force business

Acquired in-force business on insurance contracts and investment contracts with DPF represents the difference between the fair value of the contractual rights under these contracts and the liability measured in accordance with the Group's accounting policies for such contracts. This intangible is being amortised in accordance with the run-off of the book of business.

Acquired in-force business on investment contracts without DPF is being amortised on a 15% diminishing balance basis. This basis of amortisation has been updated following the application of the amendment to IAS 38 *Intangible Assets*, effective from 1 January 2016. This change has had no impact on the amounts recognised in the consolidated financial statements.

Acquired in-force business of £38 million and £180 million was recognised upon the acquisitions of the AXA businesses and Abbey Life respectively (see note H2). The £38 million arising upon the acquisition of the AXA businesses is analysed as £116 million in respect of the value in-force of acquired unit-linked business and negative AVIF of £78 million arising in respect of the acquired protection business. Further detail is provided in note H2.

G7.3 Customer relationships

The customer relationships intangible at 31 December 2016 relates to vesting pension premiums which captures the new business arising from policies in-force at the acquisition date in September 2009, specifically top-ups made to existing policies and annuities vested from matured pension policies. The total value of this customer relationship intangible at acquisition was £297 million and has been allocated to the Phoenix Life segment. This intangible is being amortised over a 20 year period.

The amortisation charge for customer relationships is presented separately in the consolidated income statement.

No indicators of impairment were identified during the period and consequently no impairment test on this intangible has been carried out.

G7.4 Present value of future profits on non-participating business in the with-profit fund

The principal assumptions used to calculate the present value of future profits are the same as those used in calculating the insurance contract liabilities given in note F4.1. Revaluation of the present value of future profits is charged or credited to the consolidated income statement as appropriate.

G7.5 Brands

The brand intangible of £20 million was recognised on acquisition of the AXA businesses and represents the value attributable to the SunLife brand as at 1 November 2016. The intangible asset was valued on a 'multi-period excess earnings' basis.

The brand intangible is being amortised over a 10 year period.

G8. PROPERTY, PLANT AND EQUIPMENT

Owner-occupied property is stated at its revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and impairment. Owner-occupied property is depreciated over its estimated useful life, which is taken as 50 years. Land is not depreciated. Gains and losses on owner-occupied property are recognised in the statement of consolidated comprehensive income.

	2016 £m	2015 £m
Owner-occupied properties	**25**	19

Owner-occupied properties have been valued by accredited independent valuers at 31 December 2016 on an open market basis in accordance with the Royal Institution of Chartered Surveyors' requirements, which is deemed to equate to fair value. The fair value measurements for the properties of £25 million have been categorised as Level 3 fair values based on the non-observable inputs to the valuation technique used.

The following table shows a reconciliation from the opening to the closing fair value for the Level 3 owner-occupied properties at valuation:

	2016 £m
At 1 January	**19**
On acquisition of AXA businesses (see note H2.1)	**6**
Depreciation recognised in consolidated income statement	**–**
Remeasurement recognised in other comprehensive income	**–**
At 31 December	**25**
Unrealised gains for the year	**–**

The fair value of the owner-occupied properties at valuation was derived using the investment method supported by comparable evidence. The significant non-observable inputs used in the valuations are the expected rental values per square foot and the capitalisation rates.

The fair value of the owner-occupied properties valuation would increase (decrease) if the expected rental values per square foot were to be higher (lower) and the capitalisation rates were to be lower (higher).

G9. INVESTMENT PROPERTY

Investment property is stated at fair value. Fair value is the price that would be received to sell a property in an orderly transaction between market participants at the measurement date. Gains and losses arising from the change in fair value are recognised in the consolidated income statement.

Leases, where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Where investment property is leased out by the Group, rental income from these operating leases is recognised as income in the consolidated income statement on a straight-line basis over the period of the lease.

	2016 £m	2015 £m
At 1 January	**1,942**	1,858
On acquisition of Abbey Life (see note H2.2)	**7**	–
Additions	**–**	152
Improvements	**23**	19
Disposals	**(44)**	(227)
On loss of control of UKCPT (see note H3)	**(1,308)**	–
Gains on adjustments to fair value (recognised in consolidated income statement)	**26**	140
At 31 December	**646**	1,942
Unrealised gains on properties held at end of period	**27**	120

As at 31 December 2016, the property portfolio of £444 million is held by the life companies and is held in a mix of commercial sectors. As at 31 December 2015, the portfolio consisted of a mix of commercial sectors, held by the life companies, of £420 million, and by the UK Commercial Property Trust, of £1,312 million. The portfolio is spread geographically throughout the UK.

In February 2016, the Group assessed that it no longer controlled UKCPT and consequently deconsolidated this group of subsidiaries effective from this date. As a result, the UKCPT property portfolio is no longer included within the Group investment property portfolio as at 31 December 2016.

Investment properties also include £202 million (2015: £210 million) of property reversions arising from sales of the NPI Extra Income Plan (see note E5 for further details).

Commercial investment property is measured at fair value by independent property valuers having appropriate recognised professional qualifications and recent experiences in the location and category of the property being valued. The valuations are carried out in accordance with the Royal Institute of Chartered Surveyors ('RICS') guidelines with expected income and capitalisation rate as the key non-observable inputs.

The residential property reversions, an interest in customers' properties which the Group will realise upon their death, are valued using a DCF model based on the Group's proportion of the current open market value, and discounted for the expected lifetime of the policyholder. The open market value is measured by independent local property surveyors having appropriate recognised professional qualifications with reference to the condition of the property and local market conditions. The individual properties are valued triennially and indexed using regional house price indices to the 31 December 2016. The discount rate is a risk-free rate appropriate for the duration of the asset, adjusted for liquidity and mortality risk. Assumptions are also made in the valuation for future movements in property prices. The residential property reversions have been substantially refinanced under the arrangements with Santander as described in note E5.

The fair value measurement of the investment properties has been categorised as a Level 3 fair value based on the inputs to the valuation techniques used. The following table shows the valuation techniques used in measuring the fair value of the investment properties, the significant non-observable inputs used, the inter-relationship between the key non-observable inputs and the fair value measurement of the investment properties:

Description	Valuation techniques	Significant non-observable inputs	Range (weighted average)
Commercial Investment Property (held by life companies)	RICS valuation	Expected income per sq. ft.	£4.91 – £99.97 (£22.62)
		Capitalisation rate	4.72% – 9.96% (6.12%)
Residential Property Reversions (held by life companies)	DCF Model and RICS valuation	Mortality	130% IFL92C15 – Female
			130% IML92C15 – Male
		Future growth in house prices	5 year RPI estimate + 1% margin
		Discount rates	5 year Gilt Spot Rate + 1.7% margin

The estimated fair value of the commercial properties held by life companies would increase (decrease) if:

- the expected income were to be higher (lower); or
- the capitalisation rate were to be lower (higher).

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

G. OTHER STATEMENT OF CONSOLIDATED FINANCIAL POSITION NOTES continued

G9. INVESTMENT PROPERTY continued

The fair value of the residential property reversions (held by life companies) would increase (decrease) if the market value of the property were to be higher (lower) or the life expectancy of the policyholders were to increase (decrease). The fair value is also sensitive to discount rate and house prices as follows:

- an increase of 1% in house price inflation would increase the fair value by £11 million (2015: £11 million);
- a decrease of 1% in house price inflation would decrease the fair value by £10 million (2015: £11 million);
- an increase of 1% in the discount rate would decrease the fair value by £10 million (2015: £10 million);
- a decrease of 1% in the discount rate would increase the fair value by £10 million (2015: £11 million).

Direct operating expenses (offset against rental income in the consolidated income statement) in respect of investment properties that generated rental income during the year amounted to £1 million (2015: £5 million). The direct operating expenses arising from investment property that did not generate rental income during the year amounted to £2 million (2015: £3 million).

Future minimum lease rental receivables in respect of non-cancellable operating leases on investment properties were as follows:

	2016 £m	2015 (restated)* £m
Not later than 1 year	**21**	21
Later than 1 year and not later than 5 years	**57**	56
Later than 5 years	**48**	50

* 2015 balances have been restated following a methodology change in valuation.

G10. OTHER RECEIVABLES

Other receivables are recognised when due and measured on initial recognition at the fair value of the amount receivable. Subsequent to initial recognition, these receivables are measured at amortised cost using the effective interest rate method.

	2016 £m	2015 £m
Investment broker balances	**71**	73
Cash collateral pledged	**295**	327
Other debtors	**147**	74
	513	474
Amount recoverable after 12 months	**–**	–

G11. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash balances and short-term deposits with an original maturity term of three months or less at the date of placement. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are deducted from cash and cash equivalents for the purpose of the statement of consolidated cash flows.

	2016 £m	2015 £m
Bank and cash balances	**1,073**	773
Short-term deposits (including demand and time deposits)	**593**	3,167
	1,666	3,940

All deposits are subject to fixed interest rates. The carrying amounts approximate to fair value at the period end. Cash and cash equivalents in long-term business operations and collective investment schemes of £1,517 million (2015: £3,836 million) are primarily held for the benefit of policyholders and so are not generally available for use by the owners.

H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES

H1. SUBSIDIARIES

Subsidiaries are consolidated from the date that effective control is obtained by the Group (see basis of consolidation in note A1) and are excluded from consolidation from the date they cease to be subsidiary undertakings. For subsidiaries disposed of during the year, any difference between the net proceeds, plus the fair value of any retained interest, and the carrying amount of the subsidiary including non-controlling interests, is recognised in the consolidated income statement.

The Group uses the acquisition method to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the consideration. Any excess of the cost of acquisition over the fair value of the net assets acquired is recognised as goodwill. Any excess of the fair value of the net assets acquired over the cost of acquisition is recognised in the consolidated income statement. Directly attributable acquisition costs are included within administrative expenses, except for acquisitions undertaken prior to 2010 when they are included within the cost of the acquisition. Costs directly related to the issuing of debt or equity securities are included within the initial carrying amount of debt or equity securities where these are not carried at fair value. Intra-group balances and income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

The Group has invested in a number of collective investment schemes such as Open-ended Investments Companies ('OEICs'), unit trusts, Société d'Investissement à Capital Variable ('SICAVs') and private equity funds. These invest mainly in equities, bonds, property and cash and cash equivalents. The Group's percentage ownership in these collective investment schemes can fluctuate according to the level of Group and third party participation in structures.

For such collective investment schemes, the following circumstances may indicate, in substance that the Group has power over the investee:

- where the investee is managed by fund managers outside the Group, the Group has existing substantive rights (such as power of veto and liquidation rights) that give it the ability to direct the current activities of the investee. In assessing the Group's ability to direct an investee the Group considers its ability relative to other investors.
- the investee is managed by the Group's fund manager, and the Group holds a significant investment in the investee. It is generally presumed that the Group has rights to variable returns and has the ability to use its power to affect its returns where the Group's holding is greater than 50%. For holdings between 25% and 50% the Group performs an assessment of power and associated control on a case-by-case basis. This assessment includes establishing the nature of the decision-making rights that the fund manager has over the investee and whether these rights give it the power to control the investee.

Where Group companies are deemed to control such collective investment schemes they are consolidated in the Group financial statements, with the interests of external third parties recognised as a liability, see the accounting policy for 'Net asset value attributable to unitholders' in note E1.

Certain of the collective investment schemes have non-coterminous period ends and are consolidated on the basis of additional financial statements prepared to the period end.

H1.1 Significant restrictions

The ability of subsidiaries to transfer funds to the Group in the form of cash dividends or to repay loans and advances is subject to local laws, regulations and solvency requirements.

Each UK Life company and the Group must retain sufficient capital at all times to meet the regulatory capital requirements mandated by or otherwise agreed with the PRA. Further information on the capital requirements applicable to Group entities are set out in the Capital Management note (I4). Under UK company law, dividends can only be paid if a UK company has distributable reserves sufficient to cover the dividend.

In addition, contractual requirements may place restrictions on the transfer of funds as follows:

- the Pearl Pension Scheme funding agreement includes certain covenants which restrict the transfer of funds within the Group. Details are provided in note G6.
- Abbey Life is required to make payments of contributions into charged accounts on behalf of the Abbey Life Staff Pension Scheme. These amounts do not form part of the pension scheme assets and at 31 December 2016, Abbey Life held £37 million within fixed and variable rate income securities in respect of these charged accounts. Further details of when these amounts may become payable to the pensions scheme are included in note G6.

H2. ACQUISITIONS AND DISPOSALS

H2.1 Acquisition of AXA businesses

On 1 November 2016, the Group acquired 100% of the issued share capital of AXA Wealth Limited ('AWL'), AXA Wealth Services Limited, AXA Sun Life Direct Limited, Winterthur Life UK Holdings Limited and AXA Trustee Services Limited from AXA UK plc for a total cash consideration of £373 million.

The AXA businesses comprise a pensions and investments business ('Embassy'), offering a range of propositions catering to both individual and corporate requirements and SunLife, a leader in the over 50's protection sector. The Group has acquired this group of companies to realise capital and cost synergies to be generated by leveraging the Group's existing operating platform and outsourcing model.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
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H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES continued

H2. ACQUISITIONS AND DISPOSALS continued

The table below summarises the fair value of the identifiable assets acquired and liabilities assumed as at the date of acquisition:

	Notes	Fair value £m
Assets		
Property, plant and equipment	G8	**6**
Intangible assets:		
Acquired in-force business	G7	**38**
Brand name	G7	**20**
Reinsurers' share of investment contracts without DPF		**6,850**
Other financial assets		**5,945**
Deferred tax assets		**1**
Cash		**40**
Prepayments and accrued income		**5**
Other receivables		**15**
Total assets		**12,920**
Liabilities		
Liabilities under insurance contracts	F1	**(181)**
Investment contracts without DPF		**12,715**
Payables related to direct insurance contracts		**9**
Accruals and deferred income		**7**
Other payables		**7**
Total liabilities		**12,557**
Fair value of net assets acquired		**363**
Goodwill arising on acquisition	G7	**10**
Purchase consideration transferred		**373**
Analysis of cash flows on acquisition:		
Net cash acquired with the subsidiaries (included in cash flow from investing activities)		**40**
Cash paid including transaction costs		**(383)**
Net cash flow on acquisition		**(343)**

Liabilities under insurance contracts
The Group's accounting policy permits the recognition of negative policy values within insurance liabilities where guaranteed surrender values do not apply. On acquisition, this results in the recognition of a negative reserve of £181 million in respect of the acquired protection business that is offset against liabilities under insurance contracts in the consolidated statement of financial position.

AVIF and other intangibles
An asset of £38 million arises reflecting the present value of future profits associated with the acquired in-force business. The £38 million asset comprises AVIF of £116 million in respect of acquired investment contracts without DPF and negative AVIF of £78 million relating to the acquired insurance business.

Under the Group's accounting policy (see note G7), AVIF arising on acquired insurance contracts is measured as the difference between the fair value of contracted rights acquired and obligations assumed and the liability measured in accordance with the Group's accounting policies for such contracts.

The fair value of the acquired insurance contracts has been assessed as £103 million, which is lower than the value of the negative reserves recognised in accordance with the Group's accounting policies of £181 million. This results in the recognition of a negative AVIF of £78 million in the consolidated statement of financial position.

The fair value of contractual rights acquired in respect of investment contracts without DPF has been assessed as £116 million and is recognised within AVIF.

Deferred acquisition and origination costs of £237 million and deferred front end fees of £(69) million are derecognised on acquisition, and are replaced by the recognised AVIF balance.

A separately identifiable intangible asset of £20 million relating to the SunLife brand has been recognised in the acquisition balance sheet. The brand has been valued using a multi-period excess earnings basis. The useful economic life of the brand has been assessed as 10 years. Further details on this intangible asset are outlined in note G7.

Tax
The tax impact of the fair value adjustments recognised on acquisition has been reflected in the acquisition balance sheet.

Goodwill
The residual goodwill of £10 million is not considered to be tax deductible and is considered to represent the value of the workforce assumed and the potential for future value creation.

Transaction costs
Transaction costs of £12 million have been expensed and are included in administrative expenses in the consolidated income statement. £10 million of these costs were paid during the period.

H2.2 Acquisition of Abbey Life
On 30 December 2016, the Group acquired 100% of the issued share capital of Abbey Life Assurance Company Limited, Abbey Life Trustee Services Limited and Abbey Life Trust Securities Limited from Deutsche Holdings No.4 Ltd (a wholly owned subsidiary of Deutsche Bank AG) for total cash consideration of £933 million. Abbey Life carries on long-term insurance business and has been closed to new retail business since 2000. The acquisition of Abbey Life will benefit the Group by increasing long-term cash generation and strengthening Group solvency.

The table below summarises the fair value of the identifiable assets acquired and liabilities assured as at the date of acquisition:

	Notes	Fair value £m
Assets		
Investment property	G9	**7**
Intangible assets: Acquired in-force business	G7	**180**
Reinsurers' share of insurance contract provisions		**100**
Other financial assets		**11,462**
Cash		**51**
Prepayments and accrued income		**52**
Other receivables		**22**
Total assets		**11,874**
Liabilities		
Pension scheme liabilities		**87**
Liabilities under insurance contracts	F1	**4,056**
Unallocated surplus		**6**
Investment contracts without DPF		**6,191**
Other financial liabilities		**392**
Provisions	G1	**25**
Deferred tax liabilities		**46**
Reinsurance payables		**2**
Payables related to direct insurance contracts		**103**
Current tax payable		**8**
Accruals and deferred income		**25**
Other payables		**8**
Total liabilities		**10,949**
Fair value of net assets acquired		**925**
Goodwill arising on acquisition	G7	**8**
Purchase consideration transferred		**933**
Analysis of cash flows on acquisition:		
Net cash acquired with the subsidiaries (included in cash flows from investing activities)		**51**
Cash paid including transaction costs		**(937)**
Net cash flow on acquisition		**(886)**

AVIF and other intangibles
The AVIF of £180 million has been determined by reference to the fair value of the insurance contract liabilities and contractual rights acquired in respect of investment contracts, and calculated in accordance with the Group's accounting policy. Deferred acquisition costs of £74 million and deferred front end fees of £(71) million have been derecognised on acquisition and replaced with the AVIF.

Tax
The tax impact of the fair value adjustments recognised on acquisition has been reflected in the acquisition balance sheet.

Goodwill
The residual goodwill of £8 million is not considered to be tax deductible and is primarily attributed to synergies arising from combining the operations with the rest of the Group.

Transaction costs
Transaction costs of £19 million have been expensed and are included in administrative expenses in the consolidated income statement. £4 million of these costs were paid during the period.

H2.3 Impact of acquisitions on results

From the date of acquisition, the AXA group of companies contributed £209 million of total revenue, net of reinsurance payable, and £8 million to profit before tax attributable to owners. Abbey Life did not contribute to either total revenue or profit before tax attributable to owners. If the acquisition of the AXA businesses and Abbey Life had taken place at the beginning of the year, total revenue, net of reinsurance payable, would have been £10,519 million and the loss before tax attributable to owners would have been £110 million.

H2.4 Disposal of Scottish Mutual International ('SMI')

On 2 December 2015, the Group completed the sale of its entire interest in SMI for gross cash consideration of £14 million following a pre-completion return of capital by SMI. The carrying value of the net assets transferred was £1 million which excludes £11 million of recoverables under an intercompany reinsurance agreement that is eliminated on consolidation.

	2015 £m
Cash consideration received (net of transaction costs)	12
Less: Carrying value of net assets sold	
Financial assets	(181)
Cash and cash equivalents	(12)
Other receivables	(1)
Liabilities under insurance contracts	169
Unallocated surplus	20
Other liabilities	4
	(1)
Intercompany liabilities under insurance contracts assumed on disposal	(11)
Loss on sale (net of tax)	–

H2.5 Castle Hill Credit Opportunities Holding Limited ('CHCOHL')

During the second half of 2015, the Group completed the disposal of its entire investment in the Sterling (Class A) loan notes of CHCOHL. No gain or loss arose on the disposal of the investment as the net assets of the structure were carried at fair value in the consolidated financial statements.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

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H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES continued

H3. ASSOCIATES: LOSS OF CONTROL OF INVESTMENT IN UK COMMERCIAL PROPERTY TRUST LIMITED ('UKCPT')

UKCPT is a property investment company which is domiciled in Guernsey and is admitted to the official list of the UK Listing Authority and to trading on the London Stock Exchange.

In February 2016, the Group reduced its holding in the issued share capital of UKCPT to 48.9%. The Group deems that it no longer controls its investment in UKCPT as it no longer has a unilateral power of veto in general meetings and also because the Group is restricted by the terms of the existing relationship agreement it has with UKCPT. Consequently, UKCPT has been deconsolidated from the date of this loss of control. No gain or loss arose on this effective disposal. The Group's investment in UKCPT is now treated as an associate and held at fair value.

The Group's remaining interest in UKCPT continues to be held in the with-profit funds of the Group's life companies. Therefore, the shareholder exposure to fair value movements in the Group's investment in UKCPT continues to be limited to the impact of those movements on the shareholder share of distributed profits of the relevant fund.

Net assets disposed of were as follows:

	Carrying amount on the date of loss of control £m
Cash received	2
Fair value of associate retained	498
Change in insurance contract liabilities	64
Less: Group's share of net assets on the date of loss of control	
Investment property	(1,308)
Collective investment schemes	(51)
Other receivables	(15)
Cash and cash equivalents	(30)
Borrowings	248
Derivative liabilities	3
Other payables	25
Non-controlling interest	564
Profit recognised on loss of control	–

As at 31 December 2016 the Group held 47.9% (2015: 50.0%) of the issued share capital of UKCPT and the value of this investment, measured at fair value, was £525 million. Summary financial information for UKCPT, showing the Group's share, is shown below:

	2016 £m	2015 £m
Non-current assets	608	683
Current assets	61	17
Non-current liabilities	(120)	(124)
Current liabilities	(14)	(13)
	535	563
Revenue	30	58
Profit before tax	19	46
Taxation	3	–
Profit for the year after tax	22	46

H4. STRUCTURED ENTITIES

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only, and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: (a) restricted activities; (b) a narrow and well-defined objective, such as to provide investment opportunities for investors by passing on risks and rewards associated with the assets of the structured entity to investors; (c) insufficient equity to permit the structured entity to finance its activities without subordinated financial support; and (d) financing in the form of multiple contractually linked instruments to investors that create concentrations of credit or other risks (tranches).

The Group has determined that all of its investments in collective investment schemes are structured entities. In addition, the PGH EBT, a number of debt security structures, private equity funds and the Group's joint venture have been identified as structured entities. The Group has assessed that it has interests in both consolidated and unconsolidated structured entities as shown below:

- Unit trusts
- OEICs
- SICAVs
- Private Equity Funds ('PEFs')
- Asset backed securities
- Collateralised Debt Obligation ('CDOs')
- Other debt structures

The Group's holdings in the above investments are subject to the terms and conditions of the respective fund's prospectus and are susceptible to market price risk arising from uncertainties about future values. The Group holds redeemable shares or units in each of the funds. The funds are managed by internal and external fund managers who apply various investment strategies to accomplish their respective investment objectives. All of the funds are managed by fund managers who are compensated by the respective funds for their services. Such compensation generally consists of an asset-based fee and a performance-based incentive fee and is reflected in the valuation of each fund.

H4.1 Interests in consolidated structured entities

The Group has determined that where it has control over funds, these investments are consolidated structured entities.

At 31 December 2016, the Group has granted further loans to the PGH EBT of £7 million (2015: £6 million). Further loans are expected to be granted in 2017. Details of this loan are included in note 9 to the parent company financial statements.

As at the reporting date the Group has no intention to provide financial or other support in relation to any consolidated structured entity.

H4.2 Interests in unconsolidated structured entities

The Group has interests in unconsolidated structured entities. These investments are held as financial assets in the Group's consolidated statement of financial position held at fair value through profit or loss. Any change in fair value is included in the consolidated income statement in 'net investment income'. Dividend and interest income is received from these investments.

A summary of the Group's interest in unconsolidated structured entities is included below. These are shown according to the financial asset categorisation in the consolidated statement of financial position and further analysed by type of fund in which the entity is invested.

	2016 Carrying value of financial assets £m	2015 Carrying value of financial assets £m
Equities	**288**	217
Collective investment schemes:		
Directly held collective investment schemes[1]:		
Equities	**4,690**	728
Bonds	**3,436**	286
Property	**502**	117
Diversified	**364**	3
Short-term liquidity	**8,052**	1,932
Indirectly held collective investment schemes[2]	**1,388**	760
Fixed and variable rate income securities:		
CDOs	**3**	221
Asset backed securities	**617**	669
	19,340	4,933

1 Directly held collective investment schemes refer to those structured entities directly invested in by Group companies. Such investments have been analysed by reference to the predominant asset class the structure is investing in.

2 Indirectly held collective investment schemes are those interests in structured entities that are held by collective investment schemes over which it has been assessed that the Group exercises overall control and have been consolidated into the financial statements.

The Group's interest in unconsolidated structured entities has increased during the year as a result of the acquisitions undertaken (see note H2) and the deconsolidation of the Ignis Liquidity Fund plc – Sterling Liquidity Fund due to loss of effective control.

The Group's maximum exposure to loss with regard to the interests presented above is the carrying amount of the Group's investments. Once the Group has disposed of its shares or units in a fund, it ceases to be exposed to any risk from that fund. The Group's holdings in the above unconsolidated structured entities are largely less than 50% and as such the size of these structured entities are likely to be significantly higher than their carrying value.

Details of commitments to subscribe to private equity funds and other unlisted assets are included in note I7.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
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H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES continued

H5. GROUP ENTITIES

The table below sets out the Group's subsidiaries (including collective investment schemes that have been consolidated within the Group's financial statements), joint ventures, associates and significant holdings in undertakings (including undertakings where holding amounts to 20% or more of the nominal value of the shares or units and they are not classified as a subsidiary, joint venture or associate).

	Registered address of incorporated entities	If unincorporated, address of principal place of business	Type of investment (including class of shares held)	% of shares/ units held
Subsidiaries:				
Phoenix Life Assurance Limited (life assurance company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Life Limited (life assurance company)	Wythall[1]		Ordinary shares	100.00%
AXA Wealth Limited (life assurance company)	Wythall[1]		Ordinary shares	100.00%
Abbey Life Assurance Company Limited (life assurance company)	Wythall[1]		Ordinary shares	100.00%
AXA Wealth Services Limited (management services company)	Wythall[1]		Ordinary shares	100.00%
AXA Sun Life Direct Limited (management services company)	Wythall[1]		Ordinary shares	100.00%
AXA Trustee Services Limited (management services company)	Wythall[1]		Ordinary shares	100.00%
Winterthur Life UK Holdings Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
Abbey Life Trustee Services Limited (life assurance company)	Wythall[1]		Ordinary shares	100.00%
Abbey Life Trust Securities Limited (pension trustee company)	Wythall[1]		Ordinary shares	100.00%
Impala Holdings Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
Mutual Securitisation plc (finance company)	Republic of Ireland[2]		N/A	N/A[3]
NP Life Holdings Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
Opal Reassurance Limited (reassurance company)[4]	Bermuda[5]		Ordinary shares	100.00%
PGH Capital plc (finance company)[4]	Republic of Ireland[6]		Ordinary shares	100.00%
PGH (LCA) Limited (finance company)[4]	Wythall[1]		Ordinary shares	100.00%
PGH (LCB) Limited (finance company)[4]	Wythall[1]		Ordinary shares	100.00%
PGH (LC1) Limited (finance company)	Wythall[1]		Ordinary shares	100.00%
PGH (LC2) Limited (finance company)	Wythall[1]		Ordinary shares	100.00%
PGH (MC1) Limited (finance company)	Wythall[1]		Ordinary shares	100.00%
PGH (MC2) Limited (finance company)	Wythall[1]		Ordinary shares	100.00%
PGH (TC1) Limited (holding company)[4]	Wythall[1]		Ordinary shares	100.00%
PGH (TC2) Limited (holding company)[4]	Wythall[1]		Ordinary shares	100.00%
Pearl Group Holdings (No. 1) Limited (finance company)	London[7]		Ordinary shares	100.00%
Pearl Group Holdings (No. 2) Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
Pearl Life Holdings Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
Pearl Group Services Limited (management services company)	Wythall[1]		Ordinary shares	100.00%
Pearl Group Management Services Limited (management services company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Life Holdings Limited (holding company)	Wythall[1]		Ordinary shares	100.00%
PGMS (Ireland) Limited (management services company)	Republic of Ireland[8]		Ordinary shares	100.00%
PA (GI) Limited (non-trading company)	Wythall[1]		Ordinary shares	100.00%
National Provident Life Limited (non-trading company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Customer Care Limited (financial services company)	Wythall[1]		Ordinary shares	100.00%
Britannic Finance Limited (finance and insurance services company)	Wythall[1]		Ordinary shares	100.00%
Britannic Money Investment Services Limited (investment advice company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Unit Trust Managers Limited (unit trust manager)	Wythall[1]		Ordinary shares	100.00%
Pearl Customer Care Limited (financial services company)	Wythall[1]		Ordinary shares	100.00%

	Registered address of incorporated entities	If unincorporated, address of principal place of business	Type of investment (including class of shares held)	% of shares/ units held
Pearl Life Services Limited (property landlord)	Wythall[1]		Ordinary shares	100.00%
Pearl (WP) Investments LLC (investment company)	USA[9]		Ordinary shares	100.00%
Phoenix SCP Limited (investment company)	Wythall[1]		Ordinary shares	100.00%
Scottish Mutual Assurance Limited (investment company)	Glasgow[10]		Ordinary shares	100.00%
Impala Loan Company 1 Limited (investment company)	Glasgow[10]		Ordinary shares	100.00%
SMA (Jersey) Limited (investment company)	Jersey[11]		Ordinary shares	100.00%
ILC1 (Jersey) Limited (investment company)	Jersey[11]		Ordinary shares	100.00%
PGH1 (Jersey) Limited (investment company)	Jersey[11]		Ordinary shares	100.00%
IH (Jersey) Limited (investment company)	Jersey[11]		Ordinary shares	100.00%
Pearl Assurance Group Holdings Limited (investment company)	Wythall[1]		Ordinary shares	100.00%
PGMS (Ireland) Holdings (holding company)	Republic of Ireland[8]		Ordinary shares	100.00%
PGMS (Glasgow) Limited (investment company)	Glasgow[10]		Ordinary shares	100.00%
Phoenix SCP Pensions Trustees Limited (trustee company)	Wythall[1]		Ordinary shares	100.00%
Phoenix SCP Trustees Limited (trustee company)	Wythall[1]		Ordinary shares	100.00%
PGS 2 Limited (investment company)	Wythall[1]		Ordinary shares	100.00%
Century Group Limited (investment company)	Wythall[1]		Ordinary shares	100.00%
Pearl RLH Limited (investment holding company)	Glasgow[10]		Ordinary shares	100.00%
SPL (Holdings) Limited (investment holding company)	Glasgow[10]		Ordinary shares	100.00%
Alcobendas Entrust Limited (investment company)	Wythall[1]		Ordinary shares	100.00%
Scottish Mutual Pension Funds Investment Limited (trustee company)	Glasgow[10]		Ordinary shares	100.00%
Britannic Group Services Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Pensions Trustee Services Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Covent Garden) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
NPI Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
NPI (Westgate) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
NPI (Printworks) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Barwell 2) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Chiswick House) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Printworks) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Stockley Park) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
London Life Trustees Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl Trustees Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl Group Secretariat Services Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Life Pension Trust Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Century Trustee Services Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl AL Limited (dormant company)	Glasgow[10]		Ordinary shares	100.00%
Phoenix Pensions Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Bradford Insurance Company Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Clearfol Investment Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl PLP Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
SL Liverpool plc (dormant company)	Wythall[1]		Ordinary shares	100.00%
SPL (Holdings 1) Limited (non-trading company)	Glasgow[10]		Ordinary shares	100.00%
Zilmer Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Alba Life Trustees Limited (non-trading company)	Glasgow[10]		Ordinary shares	100.00%

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
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H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES continued

H5. GROUP ENTITIES continued

	Registered address of incorporated entities	If unincorporated, address of principal place of business	Type of investment (including class of shares held)	% of shares/ units held
Scottish Mutual Customer Care Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
BA (FURBS) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
PG Dormant No. 1 Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Annuities Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Pension Scheme (Trustees) Limited	Wythall[1]		Ordinary shares	100.00%
Evergreen Trustee Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Corunna Limited (dormant company)	Glasgow[12]		Ordinary shares	100.00%
Pearl ULA Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Scottish Mutual Nominees Limited (dormant company)	Glasgow[12]		Ordinary shares	100.00%
National Provident Institution (dormant company)	Wythall[1]		Unlimited without shares	N/A
Phoenix & London Assurance Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Cityfourinc (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix Life Insurance Services Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
PG Dormant No 2 Holdings (holding company)	Republic of Ireland[8]		Ordinary shares	100.00%
London Life Limited (non-trading company)	Wythall[1]		Ordinary shares	100.00%
Pearl RLG Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
The London Life Association Limited (dormant company)	Wythall[1]		Limited by guarantee	N/A
Pearl BULA Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
The Scottish Mutual Assurance Society (dormant company)	Glasgow[10]		Limited by guarantee	N/A
The Phoenix Life SCP Institution (dormant company)	Glasgow[10]		Limited by guarantee	N/A
Alba LAS Pensions Management Limited (dormant company)	Glasgow[10]		Ordinary shares	100.00%
Pearl (Martineau Phase 2) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl MG Birmingham Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
The Pearl Martineau Galleries Limited Partnership (dormant company)	Wythall[1]		Limited Partnership	100.00%
Pearl (Martineau Phase 1) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl MP Birmingham Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
The Pearl Martineau Limited Partnership (dormant company)	Wythall[1]		Limited Partnership	100.00%
Pearl (Moor House 1) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Moor House 2) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Pearl (Moor House) Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
Phoenix ER1 Limited (finance company)	Wythall[1]		Ordinary shares	100.00%
Phoenix ER2 Limited (dormant company)	Wythall[1]		Ordinary shares	100.00%
CH Management Limited (investment company)	Bushey[13]		Ordinary shares	100.00%
Henderson Multi-Manager Investment Fund – Henderson Diversified Growth UK Fund		London[14]	OEIC, sub fund	79.85%
Henderson Institutional Credit Fund		London[14]	Authorised unit trust	99.96%
Henderson Global Funds – Henderson Institutional Overseas Bond Fund		London[14]	OEIC, sub fund	98.40%
Henderson Institutional Mainstream UK Equity Trust		London[14]	Authorised unit trust	100.00%
Henderson Strategic Investment Funds – Henderson Institutional European Index Opportunities Fund		London[14]	OEIC, sub fund	77.93%

	Registered address of incorporated entities	If unincorporated, address of principal place of business	Type of investment (including class of shares held)	% of shares/ units held
Henderson Strategic Investment Funds – Henderson Institutional Japan Index Opportunities Fund		London[14]	OEIC, sub fund	66.21%
Henderson Strategic Investment Funds – Henderson Institutional North American Index Opportunities Fund		London[14]	OEIC, sub fund	85.20%
Henderson Strategic Investment Funds – Henderson Institutional Asia Pacific Ex Japan Index Opportunities Fund		London[14]	OEIC, sub fund	72.32%
Henderson Institutional UK Equity Tracker Trust		London[14]	Authorised unit trust	100.00%
Henderson Institutional Short Duration Bond Fund		London[14]	Authorised unit trust	80.20%
PUTM Bothwell Floating Rate ABS Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Global Credit Fund		Wythall[1]	Authorised unit trust	99.99%
PUTM Bothwell Fixed ABS Sterling Hedged Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Asia Pacific (Excluding Japan) Fund		Wythall[1]	Authorised unit trust	99.27%
PUTM Bothwell Emerging Market Debt Unconstrained Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Emerging Markets Equity Fund		Wythall[1]	Authorised unit trust	99.88%
PUTM Bothwell European Credit Fund		Wythall[1]	Authorised unit trust	85.51%
PUTM Bothwell Europe Fund		Wythall[1]	Authorised unit trust	98.23%
PUTM Bothwell Credit Financial Sterling Hedged Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Global Bond Fund		Wythall[1]	Authorised unit trust	99.73%
PUTM Bothwell Global Equity Fund		Wythall[1]	Authorised unit trust	97.46%
PUTM Bothwell Index-Linked Sterling Hedged Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Japan Tracker Fund		Wythall[1]	Authorised unit trust	99.45%
PUTM Bothwell Long Gilt Sterling Hedged Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell North America Fund		Wythall[1]	Authorised unit trust	99.27%
PUTM Bothwell Credit Non Financial Sterling Hedged Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell UK Equity Smaller Companies Fund		Wythall[1]	Authorised unit trust	99.65%
PUTM Bothwell Sterling Government Bond Fund		Wythall[1]	Authorised unit trust	98.88%
PUTM Bothwell Euro Sovereign Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Sterling Credit Fund		Wythall[1]	Authorised unit trust	97.66%
PUTM Bothwell Tactical Asset Allocation Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell UK Equity 350 Fund		Wythall[1]	Authorised unit trust	99.52%
PUTM Bothwell UK Equity Income Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM Bothwell Sub-Sovereign Bond Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM UK All-Share Index Unit Trust		Wythall[1]	Authorised unit trust	99.97%
PUTM Cautious Unit Trust		Wythall[1]	Authorised unit trust	99.04%
PUTM European Unit Trust		Wythall[1]	Authorised unit trust	99.49%
PUTM Far Eastern Unit Trust		Wythall[1]	Authorised unit trust	99.74%
PUTM International Growth Unit Trust		Wythall[1]	Authorised unit trust	99.47%
PUTM North American Unit Trust		Wythall[1]	Authorised unit trust	99.07%
PUTM Opportunity Unit Trust		Wythall[1]	Authorised unit trust	100.00%
PUTM UK Stock Market Fund (Series 3)		Wythall[1]	Authorised unit trust	100.00%
PUTM UK Stock Market Fund		Wythall[1]	Authorised unit trust	100.00%
PUTM UK Equity Unit Trust		Wythall[1]	Authorised unit trust	99.85%
PUTM Growth Unit Trust		Wythall[1]	Authorised unit trust	100.00%
Ignis Liquidity Fund plc – Sterling Short Duration Cash Fund		Republic of Ireland[8]	OEIC, sub fund	94.74%
Ignis Strategic Solutions Funds plc – Fundamental Strategies Fund		Republic of Ireland[8]	OEIC, sub fund	100.00%

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

H. INTERESTS IN SUBSIDIARIES AND ASSOCIATES continued

H5. GROUP ENTITIES continued

	Registered address of incorporated entities	If unincorporated, address of principal place of business	Type of investment (including class of shares held)	% of shares/ units held
Ignis Strategic Solutions Funds plc – Systematic Strategies Fund		Republic of Ireland[8]	OEIC, sub fund	100.00%
Ignis Private Equity Fund LP		Cayman Islands[15]	Limited Partnership	100.00%
Ignis Strategic Credit Fund LP		Cayman Islands[15]	Limited Partnership	100.00%
BlackRock LBG DC 'A' Fund		London[16]	Authorised unit trust	96.30%
AB SICAV I – Global Factor Portfolio (SF1)		Luxembourg[17]	OEIC, sub fund	52.90%
AXA Fixed Interest Investment ICVC – Sterling Strategic Bond Fund		London[18]	OEIC, sub fund	57.80%
Aberdeen Financial Equity Fund A Inc		London[19]	OEIC, sub fund	85.61%
Aberdeen Capital Trust		London[19]	Authorised unit trust	99.48%
Associates:				
UK Commercial Property Trust Limited (property investment company)	Guernsey[20]		Ordinary shares	47.87%
UK Commercial Property Estates Holdings Limited (property investment company)	Guernsey[20]		Ordinary shares	47.87%
UK Commercial Property Holdings Limited (property investment company)	Guernsey[20]		Ordinary shares	47.87%
UK Commercial Property Estates Limited (property investment company)	Guernsey[20]		Ordinary shares	47.87%
UK Commercial Property Nominee Limited (property investment company)	Guernsey[20]		Ordinary shares	47.87%
UK Commercial Property GP Limited	Guernsey[20]		Ordinary shares	47.87%
UKCPT Limited Partnership	Guernsey[20]		Limited Partnership	47.87%
UK Commercial Property Finance Holdings Limited	Guernsey[20]		Limited Partnership	47.87%
Brixton Radlett Property Limited	UK[21]		Limited Partnership	47.87%
Castle Hill Asset Management LLC	USA[9]		Ordinary shares	40.00%
Significant holdings:				
Henderson Global Funds – World Select Fund		London[14]	OEIC, sub fund	29.66%
Henderson Global Care Funds – Henderson Institutional Global Care Managed Fund		London[14]	OEIC, sub fund	62.79%
Henderson Institutional High Alpha UK Equity Fund		London[14]	Authorised unit trust	34.72%
Henderson UK & Europe Funds – Henderson Institutional UK Gilt Fund		London[14]	OEIC, sub fund	69.89%
Henderson Institutional UK Index Opportunities Fund		London[14]	Authorised unit trust	73.19%
Ignis Liquidity Fund plc – Sterling Liquidity Fund		Dublin[8]	OEIC, sub fund	45.59%
Standard Life UK Real Estate Income Feeder Fund		Edinburgh[22]	OEIC, sub fund	37.57%

1 Wythall Green Way, Wythall, Birmingham, B47 6WG
2 Marsh Management Services (Dublin) Limited, DS-28 Adelaide Road, Dublin 2, Republic of Ireland
3 The shares of this subsidiary undertaking are held by a trust. The Group has assessed that it exercises overall control in respect of this subsidiary undertaking
4 These subsidiary undertakings are directly owned by Phoenix Group Holdings
5 The Argus Building, 12 Wesley Street, Hamilton, Bermuda
6 Arthur Cox Building, Earlsfort Terrace, Dublin 2, Dublin, Republic of Ireland
7 Juxon House, 100 St Paul's Churchyard, London, EC4M 8BU
8 25–28 North Wall Quay, IFSC, Dublin 1, Republic of Ireland
9 c/o Corporation Service Company, 2711 Centerville Road, Suite 400, Wilmington, USA
10 301 St Vincent Street, Glasgow, Strathclyde, G2 5HN
11 32 Commercial Street, St Helier, Jersey, JE2 3RU
12 50 Bothwell Street, Glasgow, G2 6HR
13 19 Middle Furlong, Bushey, England, WD23 3SZ
14 201 Bishopsgate, London, EC2M 3AE
15 Ugland House, Grand Cayman, Cayman Islands, KY1-1104
16 12 Throgmorton Avenue, London, EC2N 2DL
17 2–4, Rue Eugène Ruppert, Luxembourg, L-2453
18 7 Newgate Street, London, EC1A 7NX
19 1 Bread Street, London, EC4M 9HH
20 Trafalgar Court, Les Banques, St Peter Port, Guernsey, GY1 3QL
21 100 Barbirolli Square, Manchester, M2 3AB
22 1 George Street, Edinburgh, EH2 2LL

The following joint venture and subsidiary were fully disposed of during the period. The subsidiary was deconsolidated from the date of disposal:

- Pearl Breakfast Unit Trust (Jersey Property Unit Trust) (Joint Venture).
- Castle Hill Enhanced Floating Rate Opportunities Limited.

The following subsidiaries were reclassified as significant holdings due to the loss of effective control by the Group during the period:

- Henderson Institutional UK Enhanced Equity Trust.
- Ignis Liquidity Fund plc – Sterling Liquidity Fund.

The deconsolidation of the Ignis Liquidity Fund plc – Sterling Liquidity Fund has had a significant impact on the following line items in the statement of consolidated financial position:

- increase in the value of collective investment schemes;
- decrease in the value of net asset value attributable to unitholders; and
- decrease in value of fixed and variable rate income securities.

The following UKCPT companies were reclassified as associates due to a loss of effective control (see note H3) in the period:

- UK Commercial Property Trust Limited.
- UK Commercial Property Estates Holdings Limited.
- UK Commercial Property Holdings Limited.
- UK Commercial Property Estates Limited.
- UK Commercial Property Nominee Limited.
- UK Commercial Property GP Limited.
- UKCPT Limited Partnership.
- UK Commercial Property Finance Holdings Limited.
- Brixton Radlett Property Limited.

The Group no longer has significant holdings in the following undertakings:

- Ignis Liquidity Fund plc – Euro Liquidity Fund.
- Henderson Global Funds – Institutional Emerging Markets Fund.

Details of subsidiaries acquired during the period are included in note H2.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

I. OTHER NOTES

I1. ASSETS AND LIABILITIES HELD FOR SALE

The balances as at 31 December 2015 relate to the Part VII transfer of a portfolio of annuity liabilities to ReAssure Limited and the agreement to sell the Group's interest in an investment property joint venture held by Pearl Breakfast Unit Trust.

	2016 £m	2015 £m
Assets classified as held for sale:		
Reinsurers' share of insurance contract liabilities	–	1,521
Investment in joint venture	–	149
	–	1,670
Liabilities classified as held for sale:		
Liabilities under insurance contracts	–	1,587
	–	1,587

I1.1 Annuity liabilities transfer

On 31 July 2014, the Group entered into a reinsurance agreement, effective from 1 January 2014 to reinsure certain portfolios of the Group's annuity liabilities to ReAssure Life Limited (formerly Guardian Assurance Limited) in exchange for the transfer of financial assets of £1.7 billion. The annuity in-payment liabilities were held in the Group's with-profit funds. On 30 December 2016, the reinsurance agreement was replaced by a formal scheme under Part VII of the Financial Services and Market Act 2000 to transfer the annuity liabilities to ReAssure Limited, a fellow subsidiary of ReAssure Life Limited. Assets and liabilities classified as held for sale in 2015 were extinguished at the time of transfer. The carrying value of liabilities and assets transferred and the resulting gain are set out below:

	£m
Liabilities	
Liabilities under insurance contracts	1,652
Assets	
Reinsurers' share of insurance contract liabilities	1,582
Net liabilities transferred	70
Consideration	(18)
Gain on transfer of business	52

As the portfolio of annuities was previously held in unsupported with-profit funds, the gain is offset by an equivalent increase in policyholder liabilities and there is no net impact on the Group's result for the period.

At 31 December 2015, under the terms of this reinsurance agreement, ReAssure Life Limited held assets in a collateral account over which the Group had a fixed charge as disclosed in note F3.2.

I1.2 Sale of Pearl Breakfast Unit Trust

At 31 December 2015 the Group invested in an investment property joint venture which was held by the Pearl Breakfast Unit Trust. In 2015 the Group committed to selling the Pearl Breakfast Unit Trust (and consequently its investment in the joint venture) and on 25 February 2016 the units in the Pearl Breakfast Unit Trust were sold at their fair value to Tesco Property Holdings (No.2) Limited and Tesco Property Holdings Limited. As part of the sale agreement Tesco plc also purchased the Group's investment in Tesco Property Partner (GP) Limited. No gain or loss arose on this disposal.

I2. SHARE-BASED PAYMENT

Equity-settled share-based payments to employees and others providing services are measured at the fair value of the equity instruments at the grant date. The fair value excludes the effect of non-market-based vesting conditions. Further details regarding the determination of the fair value of equity-settled share-based transactions are set below.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest. At each period end, the Group revises its estimate of the number of equity instruments expected to vest as a result of the effect of non-market-based vesting conditions. The impact of the revision of the original estimates, if any, is recognised in the consolidated income statement such that the cumulative expense reflects the revised estimate with a corresponding adjustment to equity.

I2.1 Share-based payment expense

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

	2016 £m	2015 £m
Expense arising from equity-settled share-based payment transactions	7	4

I2.2 Share-based payment schemes in issue

Long-Term Incentive Plan ('LTIP')

The Group implemented a long-term incentive plan to retain and motivate its senior management group. The awards under this plan are in the form of nil-cost options to acquire an allocated number of ordinary shares. Assuming no good leavers or other events which would trigger early vesting rights, the 2013, 2014 and 2015 LTIP awards are subject to performance conditions tied to the Company's financial performance over a three-year period in respect of growth in MCEV (up to 31 December 2015), growth in Own Funds (from 1 January 2016), cumulative cash generation and total shareholder return ('TSR'). The 2016 LTIP award is subject to performance conditions tied to the Company's performance in respect of cumulative cash generation and TSR.

For all LTIP awards made from 2015 onwards, a holding period applies so that any LTIP awards for which the performance vesting requirements are satisfied will not be released for a further two years from the third anniversary of the original award date. Dividends will accrue on LTIP awards until the end of the holding period. There are no cash settlement alternatives.

2016 LTIP awards were granted on 30 March 2016 and 2 June 2016. The number of shares for all outstanding LTIP awards has been increased to take into account the impact of the Group's rights issue (see note D1). This adjustment has been based on the Theoretical Ex-Rights Price. The 2013 LTIP awards vested during the year. The 2014 award will vest on 26 March 2017, the 2015 award will vest on 28 September 2018 and the 2016 awards will vest on 30 March 2019 and 2 June 2019.

The fair value of these awards is estimated at the share price at the grant date, taking into account the terms and conditions upon which the instruments were granted. The fair value is adjusted in respect of the TSR performance condition which is deemed to be a 'market condition'.

Sharesave scheme

The sharesave scheme allows participating employees to save up to £250 each month over a period of either three or five years. This amount was increased to £500 each month with respect to the sharesave schemes from 2014 onwards.

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

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

The 2011 and 2012 sharesave awards were increased during 2013, and the exercise prices updated, as a result of the equity raising on 21 February 2013. All sharesave awards were increased in November 2016 following the Group's rights issue (see note D1). The exercise price of these awards was also amended as a result of this issue. The 2016 sharesave awards were granted on 25 April 2016.

The following information was relevant in the determination of the fair value of the 2012 to 2016 sharesave awards in the year:

	2016 sharesave	2015 sharesave	2014 sharesave	2013 sharesave	2012 sharesave
Share price (p)	**889.0**	843.0	674.0	630.0	524.5
Exercise price (£) (revised)	**6.39**	6.29	5.13	4.76	3.96
Expected life (years)	**3.25 and 5.25**	3.25 and 5.25	3.25 and 5.25	3.25 and 5.25	3.25 and 5.25
Risk-free rate (%) – based on UK government gilts commensurate with the expected term of the award	**0.6 (for 3.25 year scheme) and 1.0 (for 5.25 year scheme)**	0.8 (for 3.25 year scheme) and 1.2 (for 5.25 year scheme)	1.3 (for 3.25 year scheme) and 1.9 (for 5.25 year scheme)	0.4 (for 3.25 year scheme) and 0.8 (for 5.25 year scheme)	0.6 (for 3.25 year scheme) and 1.1 (for 5.25 year scheme)
Expected volatility (%) based on the Company's share price volatility to date	**30.0**	30.0	30.0	30.0	30.0
Dividend yield (%)	**6.0**	6.3	7.9	8.5	8.0

Deferred bonus share scheme ('DBSS')

Each year, part of the annual incentive for certain executives is deferred into Phoenix Group Holdings' shares. This grant of shares is conditional on the employee remaining in employment with the Group for a period of three years. For DBSS awards made in 2015 and for those to be made in subsequent years, the three-year deferral period will run to the dealing day following the three-year anniversary of the announcement of the annual results. Dividends will accrue for DBSS awards over the three-year deferral period. The 2016 DBSS was granted on 30 March 2016 and 2 June 2016 and is expected to vest on 24 March 2019. The number of shares for all outstanding DBSS awards has been increased to take into account the impact of the Group's rights issue (see note D1). This adjustment has been based on the Theoretical Ex-Rights Price. The 2013 DBSS awards vested during the year. The 2014 awards are expected to vest on 28 March 2017 and the 2015 awards are expected to vest on 19 March 2018.

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

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS
Continued

I. OTHER NOTES continued

I2. SHARE-BASED PAYMENT continued

I2.3 Movements in the year

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

	Number of share options 2016		
	LTIP	**Sharesave**	**DBSS**
Outstanding at the beginning of the year	**2,694,173**	**832,680**	**529,084**
Granted during the year[1]	**1,438,958**	**388,143**	**279,239**
Forfeited during the year	**–**	**(8,533)**	**–**
Cancelled during the year	**–**	**(15,456)**	**–**
Exercised during the year	**(663,710)**	**(159,678)**	**(175,205)**
Outstanding at the end of the year	**3,469,421**	**1,037,156**	**633,118**

1 Includes 861,845 share options granted following the Group's rights issue

	Number of share options 2015		
	LTIP	Sharesave	DBSS
Outstanding at the beginning of the year	3,153,621	987,518	482,249
Granted during the year	867,817	253,757	171,441
Forfeited during the year	(248,865)	(43,738)	(28,732)
Cancelled during the year	–	(21,585)	–
Exercised during the year	(993,902)	(343,272)	(95,874)
Waived during the year	(84,498)	–	–
Outstanding at the end of the year	2,694,173	832,680	529,084

The weighted average fair value of options granted during the year was £6.11 (2015: £6.93).

The weighted average share price at the date of exercise for the rewards exercised is £7.69 (2015: £8.36).

The weighted average remaining contractual life for the rewards outstanding as at 31 December 2016 is 1.3 years (2015: 1.6 years).

I3. CASH FLOWS FROM OPERATING ACTIVITIES

The following analysis gives further detail behind the ‘cash utilised by operations’ figure in the statement of consolidated cash flows.

	2016 £m	2015 £m
(Loss)/profit for the period before tax	**(70)**	152
Non-cash movements in profit for the year before tax		
Fair value (gains)/losses on:		
Investment property	**(26)**	(140)
Financial assets	**(4,548)**	1,125
Change in fair value of borrowings	**34**	48
Amortisation and impairment of intangible assets	**90**	163
Change in present value of future profits	**11**	6
Change in unallocated surplus	**(4)**	(84)
Share-based payment charge	**7**	4
Interest expense on borrowings	**122**	136
Net interest (income) on Group defined benefit pension scheme asset/liability	**(21)**	(17)
Other costs of pension schemes	**5**	3
(Increase)/decrease in investment assets	**(650)**	2,468
Decrease/(increase) in reinsurance assets	**345**	(1,134)
Increase/(decrease) in insurance contract and investment contract liabilities	**2,489**	(3,487)
Increase/(decrease) in deposits received from reinsurers	**14**	(30)
Increase/(decrease) in obligation for repayment of collateral received	**898**	(229)
Net (increase)/decrease in working capital	**(541)**	440
Cash utilised by operations	**(1,845)**	(576)

I4. CAPITAL MANAGEMENT

This note sets out the Group's approach to managing capital, provides a description of what the Group manages as capital and explains the regulatory requirements and capital policies of the Group and its life companies.

Risk and capital management objectives

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

In pursuing these objectives, the Group deploys financial and other assets and incurs insurance contract liabilities and financial and other liabilities. Financial and other 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 principally comprise investment contracts, borrowings for financing purposes, derivative liabilities and net asset value attributable to unit-holders.

The risk management disclosures in the IFRS consolidated financial statements set out the major risks that the Group businesses are exposed to and describe the Group’s approach to managing these. The section on financial risk is included in note E6, the section on insurance risk is included in note F4 and the sections on risk and capital management objectives and other risks are included below. The Group’s risk management framework is described in the Risk Management section on pages 34 to 39 of the Annual Report and Accounts.

Other risks

Customer risk

Customer risk is the risk of reductions in earnings and/or value, through inappropriate or poor customer treatment (including poor advice).

Operational risk

Operational risk is the risk of reductions in earnings and/or value, through financial or reputational loss, from inadequate or failed internal processes and systems, or from people-related or external events.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

I. OTHER NOTES continued

I4. CAPITAL MANAGEMENT continued

Capital management framework

The Group's capital management framework is designed to achieve the following objectives:

- to provide appropriate security for policyholders and meet all regulatory capital requirements under the Solvency II regime while not retaining unnecessary excess capital;
- to ensure sufficient liquidity to meet obligations to policyholders and other creditors;
- to optimise the Fitch Rating's financial leverage ratio to maintain an investment grade credit rating; and
- to maintain a stable and sustainable dividend policy.

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

Group capital

Following the implementation of the Solvency II Directive effective from 1 January 2016, Group capital is managed on a Solvency II basis.

Under the Solvency II framework, the primary sources of capital managed by the Group comprise of the Group's Own Funds as measured under the Solvency II principles, adjusted so as to exclude surplus funds attributable to the Group's unsupported with-profit funds and unsupported pension schemes. The Group also considers its senior bond and revolving credit facility to represent sources of capital, measured at their market value.

Prior to 1 January 2016 the primary sources of capital used by the Group comprised of equity shareholder funds as measured on an MCEV basis, the Perpetual Reset Capital Securities and shareholder borrowings. Following the implementation of Solvency II, the Group no longer reports financial information on an MCEV basis, and such an approach is no longer considered relevant to the management of the Group's capital. In addition, the Perpetual Reset Capital Securities were redeemed in April 2016 and therefore no longer represent a source of capital.

A Solvency II capital assessment involves a valuation in line with Solvency II principles of the Group's Own Funds and a risk-based assessment of the Group's Solvency Capital Requirement ('SCR'). Solvency II surplus is the excess of Own Funds over the SCR.

Each UK life company and the Group will hold an amount of Own Funds that is greater than the SCR 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, the Minimum Capital Requirement ('MCR').

The Group aims to maintain a Solvency II surplus at least equal to its Board-approved capital policy, which reflects board risk appetite for meeting prevailing solvency requirements.

The capital policy of each life company is set and monitored by each life company board. These policies ensure there is sufficient capital within each life company to meet regulatory capital requirements under a range of stress conditions. The capital policy of each life company varies according to the risk profile and financial strength of the company.

The capital policy of each Group holding company is designed to ensure that there is sufficient liquidity to meet creditor obligations through the combination of cash buffers and cash flows from the Group's operating companies.

Own Funds and SCR

Basic Own Funds represents the excess of assets over liabilities from the Solvency II balance sheet adjusted to add back any relevant subordinated liabilities that meet the criteria to be treated as capital items.

The Basic Own Funds are classified into three Tiers based on permanency and loss absorbency (Tier 1 being the highest quality and Tier 3 the lowest). The Group's Own Funds are assessed for their eligibility to cover the Group SCR with reference to both the quality of capital and its availability and transferability. Surplus funds in with-profit funds of the life companies and in the pension schemes are restricted and can only be included in Eligible Own Funds up to the value of the SCR they are used to support.

Eligible Own Funds to cover the SCR are obtained after applying the prescribed Tiering limits and transferability restrictions to the Basic Own Funds.

The SCR is calibrated so that the likelihood of a loss exceeding the SCR is less than 0.5% over one year. This ensures that capital is sufficient to withstand a broadly '1 in 200 year event'.

Group capital resources – unaudited

The Group capital resources is based on the Group's pro forma Own Funds adjusted for shareholder borrowings as analysed below:

Unaudited	2016 Pro forma £bn
PGH pro forma Own Funds[1,2]	**6.0**
Remove Own Funds pertaining to unsupported with-profit funds and the PGL pension scheme	**(2.0)**
PGH pro forma Own Funds attributable to shareholders	**4.0**
Senior borrowings[3]:	
Revolving credit facility	**0.5**
Senior unsecured bond	**0.3**
Group capital resources	**4.8**

1 Further information on the PGH pro forma Own Funds and SCR is included on page 31.
2 Further details on the pro forma basis are provided on page 23.
3 The senior borrowings are treated as liabilities within the PGH pro forma Own Funds as they do not qualify as Own Funds under Solvency II principles. Other shareholder borrowings comprising the £200 million unsecured subordinated loan, the £428 million subordinated loan and the £300 million Tier 3 bond issued in January 2017, qualify as capital under Solvency II principles, and are included within Own Funds.

PLHL Solvency II surplus

The Group's Solvency II assessment and Group supervision is performed at the PLHL level as this is the highest EEA insurance holding company. A waiver is currently in place which permits Group supervision to take place at the level of the ultimate parent, PGH, via other methods as opposed to full Group supervision. This waiver is due to expire on 30 June 2017. As part of the ongoing simplification of the Group structure, Phoenix intends to put in place a new UK-registered holding company which will be the ultimate holding company and the highest EEA insurance Group holding company at which Group supervision will be performed. From 1 July 2017 and pending completion of the simplification of the Group structure, Group supervision and the Solvency II capital adequacy assessment are expected to be performed at the PLHL and PGH level.

An analysis of the PLHL Solvency II surplus as at 31 December 2016 is provided in the Business Review section on page 29 of the Annual Report and Accounts.

Further information on the PLHL's pro forma Own Funds, SCR and MCR is included in the additional capital disclosures on pages 211 to 213 of the Annual Report and Accounts.

I5. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Group and its subsidiaries carry out transactions with related parties as defined by IAS 24 *Related party disclosures*.

I5.1 Transactions with pension scheme and associate

During the year, the Group entered into the following transactions with one of its pension schemes and associate:

	Transactions 2016 £m	**Balances outstanding 2016 £m**	Transactions 2015 £m	Balances outstanding 2015 £m
Pearl Group Staff Pension Scheme				
Payment of administrative expenses	**(2)**	**–**	(2)	–
UK Commercial Property Trust Limited				
Dividend income	**17**	**–**	–	–
Reduction in investment	**12**	**–**	–	–

I5.2 Transactions with key management personnel

The total compensation of key management personnel, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the Executive and Non-Executive Directors, are as follows:

	2016 £m	2015 £m
Salary and other short-term benefits	**4**	4
Equity compensation plans	**2**	2

Details of the shareholdings and emoluments of individual Directors are provided in the Remuneration report on pages 58 to 84.

I6. OPERATING LEASES

Leases, where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Where the Group is the lessee, payments made under operating leases, net of any incentives received from the lessor are charged to the consolidated income statement on a straight-line basis over the period of the lease.

Operating lease rentals charged within administrative expenses amounted to £6 million (2015: £8 million).

The Group has commitments under non-cancellable operating leases as set out below:

	2016 £m	2015 £m
Not later than 1 year	**7**	7
Later than 1 year and not later than 5 years	**16**	22

The principal operating lease commitments for 2016 concern office space located at St Vincent Street, Glasgow and Juxon House, London (2015: St Vincent Street, Glasgow and Juxon House, London).

Disclosures of future minimum lease rental receivables in respect of non-cancellable operating leases on investment properties are included in note G9.

NOTES TO THE IFRS CONSOLIDATED FINANCIAL STATEMENTS

Continued

I. OTHER NOTES continued

I7. COMMITMENTS

This note analyses the Group's other commitments.

	2016 £m	2015 £m
To subscribe to private equity funds and other unlisted assets	**646**	443
To purchase, construct or develop investment property	**7**	6
For repairs, maintenance or enhancements of investment property	**3**	5

I8. CONTINGENT LIABILITIES

Where the Group has a possible future obligation as a result of a past event, or 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.

During 2016, the FCA published the findings of its thematic reviews into the fair treatment of long-standing customers and into the practices of non-advised annuity sales. Following the acquisition of Abbey Life, a provision has been recognised in respect of obligations identified as a result of past practices adopted by the entity in the areas covered by the two reviews. As part of this exercise, other potential exposures were identified where it is not yet possible to conclude that the Group has a present obligation that will require an outflow of economic benefits. The determination of any liability arising remains dependent on the occurrence of uncertain future events, including finalisation of the FCA's enforcement investigation into Abbey Life that commenced in response to the findings of the review into the fair treatment of long-standing customers. Further detailed information on these exposures is included in note G1.

I9. EVENTS AFTER THE REPORTING PERIOD

The financial statements are adjusted to reflect significant events that have a material effect on the financial results and that have occurred between the period end and the date when the financial statements are authorised for issue, provided they give evidence of conditions that existed at the period end. Events that are indicative of conditions that arise after the period end that do not result in an adjustment to the financial statements are disclosed.

On 20 January 2017, PGH Capital plc ('PGHC') issued £300 million of subordinated notes ('PGH Capital Tier 3 subordinated') due 2022 at a coupon of 4.125%. The net proceeds from the bond issuance were used to repay the PGH Capital revolving credit facility.

On 17 March 2017, documentation was entered into which will substitute PGH in place of PGHC as issuer of the PGH Capital senior bond, PGH Capital subordinated notes and PGH Capital Tier 3 subordinated notes ('Substitutions'). The Substitutions will become effective on 20 March 2017.

On 28 February 2017, PGH became an additional borrower under the PGH Capital revolving credit facility. On 17 March 2017, PGH irrevocably committed to drawing down under this facility on 20 March 2017 and PGHC is due to repay its borrowings under the PGH Capital revolving credit facility.

On 17 March 2017, the Board recommended a final dividend of 23.9p per share (2015: 26.7p per share) for the year ended 31 December 2016. Payment of the final dividend is subject to shareholder approval at the AGM. The cost of this dividend has not been recognised as a liability in the financial statements for 2016 and will be charged to the statement of consolidated changes in equity in 2017.

H Staunton
C Bannister
J McConville
A Barbour
I Cormack
I Hudson
W Mayall
J Pollock
N Shott
K Sorenson
D Woods

ST HELIER, JERSEY
17 MARCH 2017

PARENT COMPANY FINANCIAL STATEMENTS

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
Net investment income	4	**92**	620
Net income		**92**	620
Administrative expenses	5	**(54)**	(19)
Impairment of investment in subsidiaries	7	**–**	(437)
Total operating expenses		**(54)**	(456)
Total comprehensive income for the year attributable to owners		**38**	164

The Company is exempt from tax in the Cayman Islands on any profits, income, gains or appreciations for a period of 30 years from 11 May 2010.

There are no other comprehensive income items for 2016 and 2015.

STATEMENT OF FINANCIAL POSITION

As at 31 December 2016

	Notes	2016 £m	2015 £m
EQUITY AND LIABILITIES			
Equity attributable to owners			
Share capital	D1	**–**	–
Share premium		**1,640**	858
Foreign currency translation reserve		**89**	89
Retained earnings		**602**	557
Total equity		**2,331**	1,504
Liabilities			
Financial liabilities			
Borrowings	6	**–**	3
Other amounts due to Group entities	14	**98**	123
Accruals and deferred income		**1**	–
Total equity and liabilities		**2,430**	1,630
ASSETS			
Investments in Group entities	7	**1,664**	800
Financial assets			
Collective investment schemes	8	**25**	11
Loans and receivables	9	**737**	819
Other amounts due from Group entities	14	**4**	–
Total assets		**2,430**	1,630

The notes identified numerically on pages 197 to 202 are an integral part of these Company financial statements. Where items also appear in the consolidated financial statements, reference is made to the notes (identified alphanumerically) on pages 106 to 192.

PARENT COMPANY FINANCIAL STATEMENTS

STATEMENT OF CASH FLOWS

For the year ended 31 December 2016

	Note	2016 £m	2015 £m
Cash flows from operating activities			
Cash utilised by operations	10	**(78)**	(28)
Net cash flows from operating activities		**(78)**	(28)
Cash flows from investing activities			
Dividends received from Group entities		**8**	40
Loan advance to Group entities		**(657)**	(6)
Capital contributions to Group entities		**(929)**	–
Repayment of loans from Group entities		**775**	–
Interest received from Group entities		**25**	19
Return of share capital from Opal ReAssurance Limited ('Opal Re')		**77**	90
Net cash flows from investing activities		**(701)**	143
Cash flows from financing activities			
Proceeds from issuing ordinary shares		**908**	2
Ordinary share dividends paid		**(126)**	(120)
Repayment of loan to Impala Holdings Limited		**(3)**	–
Net cash flows from financing activities		**779**	(118)
Net decrease in cash and cash equivalents		**–**	(3)
Cash and cash equivalents at the beginning of the year		**–**	3
Cash and cash equivalents at the end of the year		**–**	–

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2016

	Share capital (note D1) £m	Share premium £m	Foreign currency translation reserve £m	Retained earnings £m	Total £m
At 1 January 2016	**–**	**858**	**89**	**557**	**1,504**
Total comprehensive income for the year attributable to owners	**–**	**–**	**–**	**38**	**38**
Issue of ordinary share capital (note D1)	**–**	**908**	**–**	**–**	**908**
Dividends paid on ordinary shares (note B4)	**–**	**(126)**	**–**	**–**	**(126)**
Credit to equity for equity-settled share-based payments (note I2.1)	**–**	**–**	**–**	**7**	**7**
At 31 December 2016	**–**	**1,640**	**89**	**602**	**2,331**

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2015

	Share capital (note D1) £m	Share premium £m	Foreign currency translation reserve £m	Retained earnings £m	Total £m
At 1 January 2015	–	976	89	389	1,454
Total comprehensive income for the year attributable to owners	–	–	–	164	164
Issue of ordinary share capital (note D1)	–	2	–	–	2
Dividends paid on ordinary shares (note B4)	–	(120)	–	–	(120)
Credit to equity for equity-settled share-based payments (note I2.1)	–	–	–	4	4
At 31 December 2015	–	858	89	557	1,504

Phoenix Group Holdings is subject to Cayman Islands Companies Law. Under Cayman Islands Companies Law distributions can be made out of profits or share premium subject, in each, to a solvency test. The solvency test is broadly consistent with the Group's going concern assessment criteria.

The notes identified numerically on pages 197 to 202 are an integral part of these Company financial statements. Where items also appear in the consolidated financial statements, reference is made to the notes (identified alphanumerically) on pages 106 to 192.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

1. ACCOUNTING POLICIES

(A) BASIS OF PREPARATION

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

STATEMENT OF COMPLIANCE

The financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'). The financial statements are presented in sterling (£) rounded to the nearest million unless otherwise stated.

Assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously. Income and expenses are not offset in the statement of comprehensive income unless required or permitted by an IFRS or interpretation, as specifically disclosed in the accounting policies of the Company.

(B) ACCOUNTING POLICIES

The accounting policies in the separate financial statements are the same as those presented in the consolidated financial statements on pages 106 to 108, except for the policy noted below. Where an accounting policy can be directly attributed to a specific note to the consolidated financial statements, the policy is presented within that note. Each note within the Company financial statements makes reference to the note to the consolidated financial statements containing the applicable accounting policy. The accounting policy in relation to foreign currency transactions is included within note A2.1 to the consolidated financial statements.

INVESTMENTS IN GROUP ENTITIES

Investments in Group entities are carried in the statement of financial position at cost less impairment.

The Company assesses at each reporting date whether an investment is impaired. The Company first assesses whether objective evidence of impairment exists. Evidence of impairment needs to be significant or prolonged to determine that objective evidence of impairment exists. If objective evidence of impairment exists, the Company calculates the amount of impairment as the difference between the recoverable amount of the Group entity and its carrying value and recognises the amount as an expense in the statement of comprehensive income.

The recoverable amount is determined based on the cash flow projections of the underlying entities.

The assessment of whether an investment in a Group entity is impaired is considered to be a critical accounting judgement for the Company.

2. FINANCIAL INFORMATION

In preparing the financial statements the Company has adopted the standards, interpretations and amendments effective 1 January 2016 which have been issued by the IASB as detailed in note A4 to the consolidated financial statements, none of which have had a significant impact on the Company's financial statements. Details of standards, interpretations and amendments to be adopted in future periods are also detailed in note A5 to the consolidated financial statements.

3. SEGMENTAL ANALYSIS

The Company has one reportable segment, comprising its investment in and loans to/from its subsidiaries. Its revenue principally comprises the dividend and interest income derived from these investments and loans. Information relating to this segment is included in the Company's primary financial statements on pages 194 to 196. The accounting policy for segmental analysis is included in note B1 to the consolidated financial statements.

Predominantly, all revenues from external customers are sourced in the UK.

Predominantly, all assets are located in the UK.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

Continued

4. NET INVESTMENT INCOME

The accounting policy for net investment income is included in note C1 to the consolidated financial statements.

	2016 £m	2015 £m
Investment income		
Dividend income from other Group entities	8	487
Interest income from other Group entities	72	58
	80	545
Reversal of impairment losses on loans and receivables	–	75
Gain on return of capital from Opal Re	12	–
Net investment income	**92**	**620**

5. ADMINISTRATIVE EXPENSES

The accounting policy for administrative expenses is included in note C2 to the consolidated financial statements.

	2016 £m	2015 £m
Employee costs[1]	1	1
Professional fees	25	1
Write down of loans due from other Group entities	11	8
Staff costs recharged from other Group entities	10	4
Other	7	5
Administrative expenses	**54**	**19**

1 In addition to the Non-Executive Directors, one employee was employed by Phoenix Group Holdings during the period (2015: one). Other Group employees are employed by other Group entities.

6. BORROWINGS

The accounting policy for borrowings is included in note E5 to the consolidated financial statements.

	Carrying value		Fair value	
	2016 £m	2015 £m	2016 £m	2015 £m
Loan due to Impala Holdings Limited	–	3	–	3

All borrowings are due to Group entities and are measured at amortised cost using the effective interest method.

On 16 July 2010, the Company was granted a loan from Impala Holdings Limited of £3 million which matured on 31 December 2016. The loan accrued interest at six month LIBOR plus a margin of 3.25% which was capitalised semi-annually on 7 April and 7 October. Interest of £0.2 million (2015: £0.1 million) was accrued during the year. The balance outstanding at the maturity date was £3 million (2015: £3 million) and has been repaid.

All borrowings are categorised as Level 3 financial instruments. The fair value of borrowings with no external market is determined by internally developed discounted cash flow models using a risk-adjusted discount rate corroborated with external market data where possible.

Changes to the Company's borrowings since 31 December 2016 are detailed in note I9 to the consolidated financial statements.

7. INVESTMENTS IN GROUP ENTITIES

	2016 £m	2015 £m
Cost		
At 1 January	**1,237**	1,317
Additions	**929**	10
Return of share capital from Opal Re	**(65)**	(90)
At 31 December	**2,101**	1,237
Impairment		
At 1 January	**(437)**	–
Charge for the year	**–**	(437)
At 31 December	**(437)**	(437)
Carrying amount at 31 December	**1,664**	800

During 2016, the Company made capital contributions totalling £929 million in an equal share to PGH (LCA) Limited and PGH (LCB) Limited.

On 24 March 2016, the Company received £77 million (2015: £90 million) as a result of a return of share capital from Opal Re. As the cost of the Company's investment in Opal Re was £65 million, a gain of £12 million was recognised on return of the capital.

On 27 April 2015, the Company received a £10 million dividend from Opal Re in the form of preference shares.

During 2015, following a restructure of the Company's holdings in PGH (LCA) Limited, PGH (LCB) Limited, PGH (TC1) Limited and PGH (TC2) Limited, the Company received dividends of £205 million and £232 million from PGH (TC1) Limited and PGH (TC2) Limited respectively. The Company impaired its investments in PGH (TC1) Limited and PGH (TC2) Limited to the extent of dividends received.

For a list of principal Group entities, refer to note H5 of the consolidated financial statements. The entities directly held by Phoenix Group Holdings are separately identified.

8. COLLECTIVE INVESTMENT SCHEMES

The accounting policy for collective investment schemes is included in note E1 to the consolidated financial statements.

	Carrying value		Fair value	
	2016 £m	2015 £m	2016 £m	2015 £m
Investment in collective investment schemes	**25**	11	**25**	11
Amount due for settlement after 12 months	**–**	–		

All investments are categorised as Level 1 financial instruments. Details of the factors considered in determination of the fair value are included in note E2 to the consolidated financial statements.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

Continued

9. LOANS AND RECEIVABLES

	Carrying value		Fair value	
	2016 £m	2015 £m	**2016 £m**	2015 £m
Loans due from PGH (LCA) Limited and PGH (LCB) Limited	**603**	626	**718**	791
Loans due from PGH (MC1) Limited and PGH (MC2) Limited	**128**	113	**235**	262
Loans due from Employee Benefit Trust	**6**	5	**6**	5
Notes due from Phoenix Life Holdings Limited	**–**	75	**–**	74
	737	819	**959**	1,132
Amounts due after 12 months	**731**	814		

The accounting policy for loans and receivables is included in note E1 to the consolidated financial statements.

All loans and receivables balances are due from Group entities and are measured at amortised cost using the effective interest method. The fair value of these loans and receivables are also disclosed.

On 22 March 2010, the Company subscribed for £325 million of Eurobonds which were issued equally by PGH (LCA) Limited and PGH (LCB) Limited. On 23 March 2010, the Eurobonds were listed on the Channel Islands Stock Exchange. Interest accrues on these Eurobonds at a rate of LIBOR plus a margin of 2.5% and the final maturity date is 30 June 2025. The Eurobonds were initially recognised at fair value and are accreted to par over the period to 2025. At 31 December 2016 £191 million was due (2015: £175 million).

On 12 December 2011, the Company, PGH (LCA) Limited and PGH (LCB) Limited, became party to a joint £77 million loan agreement to formalise an inter-company balance which had arisen in 2009 relating to fees payable to a syndicate of external banks. The loan accrued interest at a rate of LIBOR plus a margin of 1.25% and matured on 30 June 2016. No interest was capitalised during the year (2015: £0.1 million). On 22 March 2016, the outstanding balance of £5 million was written off.

In June 2015, the Company was assigned loans of £436 million issued equally by PGH (LCA) Limited and PGH (LCB) Limited. These loans accrue interest at a rate of LIBOR plus a margin of 2.9% and mature on 5 June 2020. During the year, interest of £16 million was capitalised (2015: £10 million) and £50 million of repayments were received (2015: £nil). At 31 December 2016 £412 million was due (2015: £446 million).

On 22 March 2010, the Company subscribed for £250 million of Eurobonds which were issued equally by PGH (MC1) Limited and PGH (MC2) Limited. On 23 March 2010, the Eurobonds were listed on the Channel Islands Stock Exchange. Interest accrues on these Eurobonds at a rate of LIBOR plus a margin of 2.5% and the final maturity date is 30 June 2025. The Eurobonds were initially recognised at fair value and are accreted to par over the period to 2025. At 31 December 2016 £128 million was due (2015: £113 million).

On 16 July 2010, the Company entered into an interest free facility arrangement with Phoenix Group Holdings' Employee Benefit Trust ('EBT'). In 2016, an additional £7 million was drawn down against this facility (2015: £6 million). The loan is recoverable until the point the awards held by the EBT vest to the participants, at which point the loan is reviewed for impairment. Any impairments are determined by comparing the carrying value to the estimated recoverable amount of the loan. Following the vesting of awards in 2016 £6 million of the loan (2015: £8 million) has been written off. At 31 December 2016 £6 million was due (2015: £5 million).

On 22 April 2010, Pearl Group Holdings (No.1) Limited ('PGH1') issued a balancing instrument under which notes with a principal of £75 million were issued to Phoenix Group Holdings. During January 2015 the notes were transferred from PGH1 to Phoenix Life Holdings Limited ('PLHL'). The notes have no fixed maturity. Phoenix Group Holdings paid no consideration for the notes and has waived its right to receive a coupon on the notes. At 31 December 2015, £75 million was due. On 25 April 2016, having obtained the necessary approvals PLHL repaid the notes in full.

On 9 November 2016, the Company entered into a joint loan agreement with PGH (LCA) Limited and PGH (LCB) Limited and advanced payment of £650 million. The loan accrued interest at LIBOR plus a margin of 0.85% and was fully repaid on 28 December 2016.

No other loans are considered to be past due or impaired.

For the purposes of the additional fair value disclosures for assets recognised at amortised cost, all loans and receivables are categorised as Level 3 financial instruments. The fair value of loans and receivables with no external market is determined by internally developed discounted cash flow models using a risk-adjusted discount rate corroborated with external market data where possible.

Details of the factors considered in determination of fair value are included in note E2 to the consolidated financial statements.

10. CASH FLOWS FROM OPERATING ACTIVITIES

	2016 £m	2015 £m
Profit for the year before tax	38	164
Adjustments to reconcile profit for the year to cash flows from operating activities:		
Interest income from other Group entities	(72)	(58)
Reversal of impairment losses on loans and receivables	–	(75)
Gain on return of capital from subsidiary	(12)	–
Dividends received	(8)	(487)
Write down of loans to Group entities	11	8
Impairment of investment in subsidiaries	–	437
Share-based payment charge	7	4
Net increase in investment assets	(14)	(29)
Net (increase)/decrease in working capital	(28)	8
Cash utilised by operations	**(78)**	(28)

11. CAPITAL AND RISK MANAGEMENT

The Company's capital comprises share capital and all reserves. At 31 December 2016 total capital was £2,331 million (2015: £1,504 million). The movement in capital in the year comprises the total comprehensive income for the year attributable to owners of £38 million (2015: £164 million), proceeds from the issue of ordinary share capital of £908 million (2015: £2 million) and a credit to equity for equity-settled share-based payments of £7 million (2015: £4 million), partly offset by payment of dividends of £126 million (2015: £120 million).

There are no externally imposed capital requirements on the Company. The Company's capital is monitored by the Directors and managed on an ongoing basis via a monthly close process to ensure that it remains positive at all times.

Details of the Group risk management policies are outlined in notes E6 and F4 to the consolidated financial statements.

The primary operation of the Company is to manage its investment in subsidiaries. The Company's other assets and liabilities mainly consist of receivables due from and borrowings owed to other Group entities.

The principal risks and uncertainties facing the Company are:

- interest rate risk, since the movement in interest rates will impact the value of interest receivable and payable by the Company;
- liquidity risk, exposure to liquidity risk as a result of normal business activities, specifically the risk arising from an inability to meet short-term cash flow requirements; and
- credit risk, arising from the default of the counterparty to a particular financial asset and is significantly reduced as assets are primarily intercompany receivables from other Group entities.

The Company's exposure to all these risks is monitored by the Directors, who agree policies for managing each of these risks on an ongoing basis.

12. SHARE-BASED PAYMENTS

For detailed information on the long-term incentive plans, sharesave schemes and deferred bonus share schemes refer to note I2 to the consolidated financial statements.

13. DIRECTORS' REMUNERATION

Details of the remuneration of the Directors' of Phoenix Group Holdings are included in the Directors' remuneration report on pages 58 to 84 of the Annual Report and Accounts.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS
Continued

14. RELATED PARTY TRANSACTIONS

The Company has related party transactions with Group entities and its key management personnel. Details of the total compensation of key management personnel, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the Executive and Non-Executive Directors, are included in note I5 to the consolidated financial statements.

During the year ended 31 December 2016 the Company entered into the following transactions with Group entities:

	2016 £m	2015 £m
Dividends received	**8**	487
Interest received on loans and receivables due from Group entities	**72**	58
	80	545
Amounts due from related parties at the end of the year:		
Loans due from Group entities	**737**	819
Other amounts due from Group entities	**4**	–
	741	819
Amount due for settlement after 12 months	**731**	814
Amounts due to related parties at the end of the year:		
Loans due to Group entities	**–**	3
Other amounts due to Group entities	**98**	123
	98	126
Amount due for settlement after 12 months	**–**	–

The Company guarantees certain borrowings of PGH Capital plc as detailed in note E5 to the consolidated financial statements. These guarantees applied up to the date of the Substitutions of debt to PGH from PGH Capital plc as detailed in note I9 to the consolidated financial statements.

15. AUDITOR'S REMUNERATION

Details of auditor's remuneration, for Phoenix Group Holdings subsidiaries, is included in note C3 to the consolidated financial statements.

16. EVENTS AFTER THE REPORTING PERIOD

Details of events after the reporting date are included in note I9 to the consolidated financial statements.

H Staunton
C Bannister
J McConville
A Barbour
I Cormack
I Hudson
W Mayall
J Pollock
N Shott
K Sorenson
D Woods

ST HELIER, JERSEY
17 MARCH 2017

ASSET DISCLOSURES

ADDITIONAL LIFE COMPANY ASSET DISCLOSURES

The analysis of the asset portfolio provided below comprises the assets held by the Group's life companies, and is stated net of derivative liabilities. It excludes other Group assets such as cash held in the holding and service companies and the assets held by the non-controlling interests in consolidated collective investment schemes.

The following table provides an overview of the exposure by asset category of the Group's life companies' shareholder and policyholder funds:

31 December 2016

Carrying value	Shareholder and non-profit funds[1] £m	Participating supported[1] £m	Participating non-supported[2] £m	Unit-linked[2] £m	Total[3] £m
Cash and cash equivalents	1,239	2,457	4,342	1,858	9,896
Debt securities – gilts	3,121	425	6,724	2,163	12,433
Debt securities – bonds	8,645	1,878	6,427	2,926	19,876
Equity securities	182	53	5,699	15,747	21,681
Property investments	144	74	802	619	1,639
Other investments[4]	833	188	1,849	7,449	10,319
At 31 December 2016	**14,164**	**5,075**	**25,843**	**30,762**	**75,844**
Cash and cash equivalents in Group holding companies					570
Cash and financial assets in other Group companies					449
Financial assets held by the non-controlling interest in consolidated collective investment schemes					931
Total Group consolidated assets					**77,794**
Comprised of:					
Investment property					646
Financial assets					77,049
Cash and cash equivalents					1,666
Derivative liabilities					(1,567)
					77,794

1 Includes assets where shareholders of the life companies bear the investment risk.
2 Includes assets where policyholders bear most of the investment risk.
3 This information is presented on a look through basis to underlying funds where available.
4 Includes equity release mortgages of £433 million, policy loans of £10 million, other loans of £308 million, net derivative assets of £1,468 million, reinsurers' share of investment contracts of £6,808 million, and other investments of £1,292 million.

31 December 2015

Carrying value	Shareholder and non-profit funds[1] £m	Participating supported[1] £m	Participating non-supported[2] £m	Unit-linked[2] £m	Total[3] £m
Cash and cash equivalents	1,236	2,498	3,921	1,065	8,720
Debt securities – gilts	1,262	818	7,275	602	9,957
Debt securities – bonds	5,203	1,380	6,263	724	13,570
Equity securities	186	62	5,231	7,294	12,773
Property investments	140	74	821	336	1,371
Other investments[5]	266	(31)	767	(1)	1,001
At 31 December 2015	8,293	4,801	24,278	10,020	47,392
Cash and cash equivalents in Group holding companies					706
Cash and financial assets in other Group companies					328
Financial assets held by the non-controlling interest in the consolidated UKCPT					838
Financial assets held by the non-controlling interest in consolidated collective investment schemes					5,473
Total Group consolidated assets					54,737
Comprised of:					
Investment property					1,942
Financial assets					50,066
Cash and cash equivalents					3,940
Assets held for sale					149
Derivative liabilities					(1,360)
					54,737

5 Includes equity release mortgages of £268 million, policy loans of £11 million, other loans of £15 million, net derivative assets of £139 million and other investments of £568 million.

The following table analyses by type the debt securities of the life companies:

31 December 2016

Analysis by type of debt securities	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
Gilts	**3,121**	**425**	**6,724**	**2,163**	**12,433**
Other government and supranational[6]	**1,195**	**474**	**2,103**	**328**	**4,100**
Corporate – financial institutions	**3,375**	**531**	**1,983**	**2,081**	**7,970**
Corporate – other	**3,219**	**184**	**1,700**	**401**	**5,504**
Asset backed securities ('ABS')	**856**	**689**	**641**	**116**	**2,302**
At 31 December 2016	**11,766**	**2,303**	**13,151**	**5,089**	**32,309**

6 Includes debt issued by governments; public and statutory bodies; government backed institutions and supranationals.

ASSET DISCLOSURES

ADDITIONAL LIFE COMPANY ASSET DISCLOSURES

Continued

31 December 2015

Analysis by type of debt securities	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
Gilts	1,262	818	7,275	602	9,957
Other government and supranational[1]	713	673	2,058	88	3,532
Corporate – financial institutions	1,859	367	1,588	153	3,967
Corporate – other	2,079	164	2,121	441	4,805
Asset backed securities ('ABS')	552	176	496	42	1,266
At 31 December 2015	6,465	2,198	13,538	1,326	23,527

1 Includes debt issued by governments; public and statutory bodies; government backed institutions and supranationals.

The life companies' debt portfolio was £32.3 billion at 31 December 2016. Shareholders had direct exposure to £14.1 billion of these assets (including supported participating funds), of which 99% of rated securities were investment grade. The shareholders' credit risk exposure to the non-supported participating funds is primarily limited to the shareholders' share of future bonuses. Shareholders' credit risk exposure to the unit-linked funds is limited to the level of asset management fee, which is dependent on the underlying assets.

Sovereign and supranational debt represented 37% of the debt portfolio in respect of shareholder exposure, or £5.2 billion, at 31 December 2016. The vast majority of the life companies' exposure to sovereign and supranational debt holdings is to UK gilts.

The following table sets out a breakdown of the life companies' sovereign and supranational debt security holdings by country:

31 December 2016

Analysis of sovereign and supranational debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	**3,369**	**494**	**7,051**	**2,173**	**13,087**
Supranationals	**673**	**144**	**446**	**20**	**1,283**
USA	**16**	**5**	**25**	**107**	**153**
Germany	**143**	**103**	**526**	**45**	**817**
France	**40**	**25**	**90**	**11**	**166**
Netherlands	**16**	**12**	**112**	**6**	**146**
Italy	**–**	**–**	**–**	**26**	**26**
Spain	**–**	**–**	**–**	**10**	**10**
Other – non-Eurozone	**45**	**114**	**542**	**87**	**788**
Other – Eurozone	**14**	**2**	**35**	**6**	**57**
At 31 December 2016	**4,316**	**899**	**8,827**	**2,491**	**16,533**

31 December 2015

Analysis of sovereign and supranational debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	1,400	905	7,560	609	10,474
Supranationals	310	195	553	17	1,075
USA	1	12	15	24	52
Germany	211	232	593	14	1,050
France	31	50	64	4	149
Netherlands	–	–	1	1	2
Italy	–	–	–	5	5
Spain	–	–	–	3	3
Other – non-Eurozone	22	87	511	13	633
Other – Eurozone	–	10	36	–	46
At 31 December 2015	1,975	1,491	9,333	690	13,489

All of the life companies' debt securities are held at fair value through profit or loss under IAS 39, and therefore already reflect any reduction in value between the date of purchase and the reporting date.

The life companies have in place a comprehensive database that consolidates credit exposures across counterparties, geographies and business lines. This database is used for credit monitoring, stress testing and scenario planning. The life companies continue to manage their balance sheets prudently and have taken extra measures to ensure their market exposures remain within risk appetite.

The following table sets out a breakdown of the life companies' financial institution corporate debt security holdings by country:

31 December 2016

Analysis of financial institution corporate debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	**1,607**	**65**	**736**	**924**	**3,332**
USA	**602**	**56**	**403**	**271**	**1,332**
Germany	**75**	**1**	**27**	**34**	**137**
France	**165**	**6**	**73**	**121**	**365**
Netherlands	**249**	**58**	**190**	**112**	**609**
Italy	**15**	**–**	**7**	**11**	**33**
Ireland	**30**	**–**	**–**	**29**	**59**
Spain	**1**	**–**	**15**	**10**	**26**
Other – non-Eurozone	**550**	**328**	**499**	**516**	**1,893**
Other – Eurozone	**81**	**17**	**33**	**53**	**184**
At 31 December 2016	**3,375**	**531**	**1,983**	**2,081**	**7,970**

31 December 2015

Analysis of financial institution corporate debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	845	151	566	71	1,633
USA	449	39	298	16	802
Germany	16	18	86	3	123
France	58	–	43	3	104
Netherlands	189	52	238	30	509
Italy	7	–	7	–	14
Ireland	28	1	12	–	41
Spain	3	–	12	–	15
Other – non-Eurozone	208	94	272	29	603
Other – Eurozone	56	12	54	1	123
At 31 December 2015	1,859	367	1,588	153	3,967

ASSET DISCLOSURES

ADDITIONAL LIFE COMPANY ASSET DISCLOSURES

Continued

The life companies had £46 million (2015: £39 million) shareholder exposure to financial institution corporate debt of the Peripheral Eurozone, defined as Portugal, Italy, Ireland, Greece, and Spain, at 31 December 2016. The £3,906 million (2015: £2,226 million) total shareholder exposure to financial institution corporate debt comprised £2,125 million (2015: £1,742 million) senior debt, £2 million (2015: £4 million) Tier 1 debt and £1,779 million (2015: £480 million) Tier 2 debt.

The £3,906 million shareholder exposure to financial institution corporate debt comprised £2,170 million (2015: £1,281 million) bank debt and £1,736 million (2015: £945 million) non-bank debt.

For each of the life companies' significant financial institution counterparties, industry and other data has been used to assess the exposure of the individual counterparties. As part of the Group's risk appetite framework and analysis of shareholder exposure to a potential worsening of the economic situation, this assessment has been used to identify counterparties considered to be most at risk from defaults. The financial impact on these counterparties, and the contagion impact on the rest of the shareholder portfolio, is assessed under various scenarios and assumptions. This analysis is regularly reviewed to reflect the latest economic outlook, economic data and changes to asset portfolios. The results are used to inform the Group's views on whether any management actions are required.

The following table sets out a breakdown of the life companies' corporate – other debt security holdings by country:

31 December 2016

Analysis of corporate – other debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	**1,517**	**74**	**830**	**211**	**2,632**
USA	**567**	**33**	**303**	**83**	**986**
Germany	**256**	**38**	**128**	**25**	**447**
France	**276**	**17**	**127**	**28**	**448**
Netherlands	**69**	**–**	**17**	**4**	**90**
Italy	**62**	**1**	**35**	**5**	**103**
Ireland	**4**	**–**	**1**	**6**	**11**
Spain	**48**	**–**	**23**	**5**	**76**
Other – non-Eurozone	**381**	**7**	**217**	**31**	**636**
Other – Eurozone	**39**	**14**	**19**	**3**	**75**
At 31 December 2016	**3,219**	**184**	**1,700**	**401**	**5,504**

31 December 2015

Analysis of corporate – other debt security holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	1,073	76	1,607	363	3,119
USA	288	33	115	15	451
Germany	142	24	93	15	274
France	173	15	113	20	321
Netherlands	39	–	19	3	61
Italy	56	2	27	3	88
Ireland	1	–	2	2	5
Spain	45	–	24	2	71
Other – non-Eurozone	190	13	77	11	291
Other – Eurozone	72	1	44	7	124
At 31 December 2015	2,079	164	2,121	441	4,805

The following table sets out a breakdown of the life companies' ABS holdings by country:

31 December 2016

Analysis of ABS holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total[1] £m
UK	**729**	**488**	**551**	**108**	**1,876**
USA	**10**	**8**	**4**	**1**	**23**
Germany	**–**	**74**	**29**	**–**	**103**
France	**–**	**29**	**–**	**–**	**29**
Netherlands	**9**	**84**	**32**	**1**	**126**
Ireland	**30**	**1**	**18**	**–**	**49**
Other – non-Eurozone	**78**	**2**	**7**	**3**	**90**
Other – Eurozone	**–**	**3**	**–**	**3**	**6**
At 31 December 2016	**856**	**689**	**641**	**116**	**2,302**

1 Improved look-through data received in respect of certain collective investment schemes has identified additional holdings in ABS as at 31 December 2016.

31 December 2015

Analysis of ABS holdings by country	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
UK	499	172	399	41	1,111
USA	3	–	4	–	7
Germany	–	–	28	–	28
France	–	1	–	–	1
Netherlands	10	–	20	1	31
Italy	–	–	12	–	12
Spain	–	–	1	–	1
Other – non-Eurozone	40	–	10	–	50
Other – Eurozone	–	3	22	–	25
At 31 December 2015	552	176	496	42	1,266

ASSET DISCLOSURES

ADDITIONAL LIFE COMPANY ASSET DISCLOSURES

Continued

The following table sets out the credit rating analysis of the debt portfolio:

31 December 2016

Credit rating analysis of debt portfolio	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
AAA	1,333	935	1,626	519	4,413
AA	4,578	943	7,962	1,415	14,898
A	3,358	287	1,312	550	5,507
BBB	2,274	54	1,624	360	4,312
BB	132	4	167	47	350
B and below	16	2	117	11	146
Non-rated	75	78	343	2,187	2,683
At 31 December 2016	11,766	2,303	13,151	5,089	32,309

98% of rated securities were investment grade at 31 December 2016 (2015: 97%). The percentage of rated securities that were investment grade in relation to the shareholder and policyholders' funds were 99% and 98% respectively (2015: 99% and 96% respectively).

31 December 2015

Credit rating analysis of debt portfolio	Shareholder and non-profit funds £m	Participating supported £m	Participating non-supported £m	Unit-linked £m	Total £m
AAA	746	625	1,740	72	3,183
AA	2,336	1,272	8,443	487	12,538
A	1,618	189	902	84	2,793
BBB	1,635	92	1,751	179	3,657
BB	100	11	205	21	337
B and below	1	–	327	–	328
Non-rated	29	9	170	483	691
At 31 December 2015	6,465	2,198	13,538	1,326	23,527

CAPITAL DISCLOSURES

ADDITIONAL CAPITAL DISCLOSURES

The Group's capital management framework is described in the Business Review section on pages 28 to 31 of the Annual Report and Accounts. The Group's capital policies and capital resources are set out on note I4 of the IFRS financial statements.

The Solvency II capital assessment and the Group's regulatory supervision is performed at the PLHL level as this is the highest EEA insurance group holding company. This section provides additional analysis of PLHL's Solvency II Own Funds, SCR and MCR.

PLHL SOLVENCY II SURPLUS

The pro forma PLHL's surplus at 31 December 2016 is £1.9 billion (2015: £1.3 billion, actual). The rationale for the use of the pro forma metric is set out on page 23.

	31 December 2016 Pro forma £bn	31 December 2015 Actual £bn
Own Funds	**6.8**	5.7
SCR	**(4.9)**	(4.4)
Surplus	**1.9**	1.3

COMPOSITION OF OWN FUNDS

Own funds items are classified into different Tiers based on the features of the specific items and the extent to which they possess the following characteristics:

– availability to be called up on demand to fully absorb losses on a going-concern basis, as well as in the case of winding-up ('permanent availability');

– in the case of winding-up, the total amount that is available to absorb loses before repayment to the holder until all obligations to policyholders and other beneficiaries have been met ('subordination').

PLHL's pro forma Own Funds are analysed by Tier as follows:

	31 December 2016 Pro forma £bn	31 December 2015 Actual £bn
Tier 1	**5.8**	5.0
Tier 2	**0.6**	0.6
Tier 3	**0.4**	0.1
Total Own Funds	**6.8**	5.7

PLHL's Tier 1 capital accounts for 83% (2015: 86%) of total Own Funds and comprise of ordinary share capital, surplus funds of the unsupported with-profit funds which are recognised only to a maximum of the SCR, and the accumulated profits of the remaining business.

Tier 2 capital comprise of subordinated notes whose terms enable them to qualify as Tier 2 capital for regulatory reporting purposes.

Tier 3 items include the new Tier 3 bond issued in January 2017 of £0.3 billion on a pro forma basis (2015: nil) and deferred tax asset of £0.1 billion (2015: £0.1 billion).

BREAKDOWN OF SCR

An analysis of the undiversified SCR of PLHL is presented below:

	31 December 2016 Pro forma %	31 December 2015 Actual %
Longevity	**33**	**30**
Credit	**16**	**21**
Persistency	**13**	**11**
Interest rates	**9**	**5**
Operational	**7**	**8**
Swap spreads	**4**	**6**
Other market risks	**10**	**13**
Other non-market risks	**8**	**6**
	100%	**100%**

The principal risks are described in detail in note E6 and F4 in the IFRS financial statements.

MINIMUM CAPITAL REQUIREMENTS

Minimum Capital Requirement ('MCR') is the minimum amount of capital an insurer is required to hold below which policyholders and beneficiaries would become exposed to an unacceptable level of risk if an insurer was allowed to continue its operations.

The MCR is calculated according to a formula prescribed by the Solvency II regulations and is subject to a floor of 25% of the SCR or EUR 3.7 million, whichever is higher, and a cap of 45% of the SCR. The MCR formula is based on factors applied to technical provisions and capital at risk.

PLHL's MCR at 31 December 2016 is £1.2 billion (2015: £1.1 billion) which is a sum of the underlying insurance companies' MCRs.

PLHL's eligible Own Funds to cover MCR is £6.0 billion (2015: £5.2 billion) leaving an excess of eligible own funds over MCR of £4.8 billion (2015: £4.1 billion), which translates to an MCR coverage ratio of 496% (2015: 482%).

The eligible Own Funds to cover the MCR is subject to quantitative limits as shown below:

– the eligible amounts of Tier 1 items should be at least 80% of the MCR; and

– the eligible amounts of Tier 2 items shall not exceed 20% of the MCR.

	31 December 2016 Pro forma £bn	31 December 2015 Actual £bn
Eligible own funds to cover MCR		
Tier 1	**5.8**	**4.9**
Tier 2	**0.2**	**0.3**
Total eligible own funds to cover MCR	**6.0**	**5.2**

ADDITIONAL INFORMATION

IN THIS SECTION

SHAREHOLDER INFORMATION

ANNUAL GENERAL MEETING

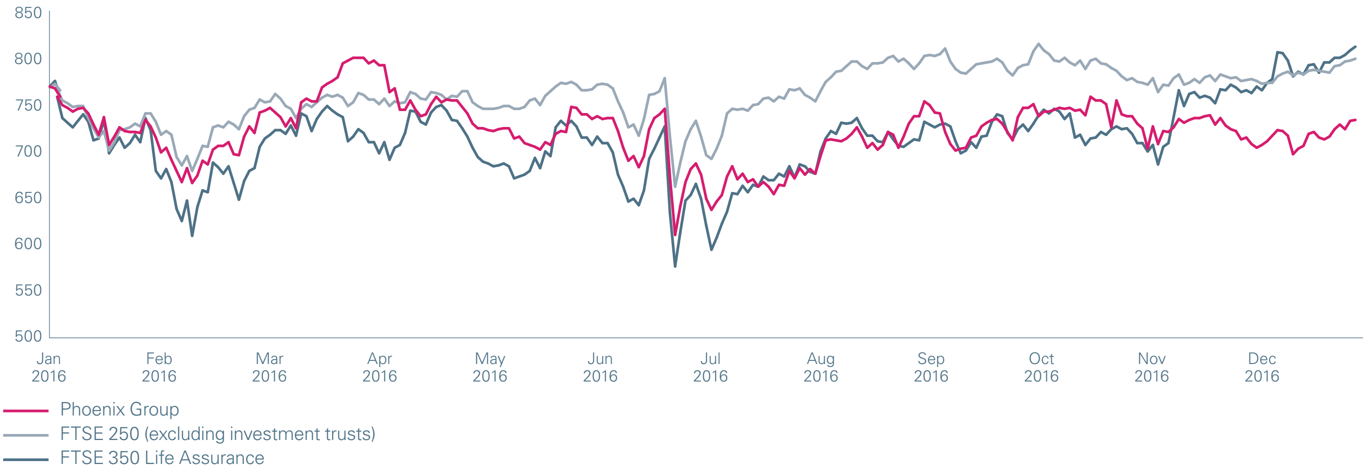
Our Annual General Meeting ('AGM') will be held on 11 May 2017 at 12:30pm.

The voting results for our 2017 AGM, including proxy votes and votes withheld, will be available on the Group's website shortly after the meeting.

SHARE PRICE PERFORMANCE

PHOENIX GROUP HOLDINGS SHARE PRICE PERFORMANCE

Price (rebased to PHNX) pence



SHAREHOLDER PROFILE AS AT 31 DECEMBER 2016

Range of shareholdings	No. of shareholders	%	No. of shares	%
1–1,000	487	29.3	229,682	0.1
1,001–5,000	559	33.7	1,287,888	0.3
5,001–10,000	129	7.8	934,583	0.2
10,001–250,000	319	19.2	21,857,365	5.6
250,001–500,000	55	3.3	18,715,782	4.8
500,001 and above	112	6.7	349,824,517	89.0
Total	**1,661**	**100**	**392,849,817**	**100**

SHAREHOLDER INFORMATION

Continued

SHAREHOLDER SERVICES

MANAGING YOUR SHAREHOLDING

Our registrar, Computershare, maintains the Company's register of members. Shareholders may request a hard copy of this Annual Report from our registrar and if you have any further queries in respect of your shareholding, please contact directly using the contact details set out below.

REGISTRAR DETAILS

Computershare Investor Services (Cayman) Limited
Queensway House
Hilgrove Street
St Helier
Jersey, JE1 1ES

Shareholder helpline number +44 (0) 370 702 0000
Fax number +44 (0) 370 703 6101
Shareholder helpline email address info@computershare.co.je

DIVIDEND MANDATES

Shareholders may find it convenient to have their dividends paid directly to their bank or building society account. If you wish to take advantage of this facility please call Computershare and request a 'Dividend Mandate' form.

SCRIP DIVIDEND ALTERNATIVE

The Company does not currently offer a scrip dividend alternative.

WARNING TO SHAREHOLDERS

Over recent years, many companies have become aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters. These are typically from overseas-based 'brokers' who target UK shareholders, offering to sell them what often turn out to be worthless or high-risk shares in US or UK investments. These operations are commonly known as 'boiler rooms'.

Shareholders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free reports about the Company.

If you receive any unsolicited investment advice:

- make sure you get the correct name of the person and organisation;
- check that they are properly authorised by the Financial Conduct Authority ('FCA') before getting involved by visiting www.fca.org.uk/firms/systems-reporting/register;
- report the matter to the FCA by calling the FCA Consumer Helpline on 0800 111 6768; and
- if the calls persist, hang up.

If you deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme ('FSCS'). The FCA can also be contacted by completing an online form available at www.fca.org.uk/consumers/scams/investment-scams/share-fraud-and-boiler-room-scams/reporting-form.

Details of any share dealing facilities that the Company endorses will be included in Company mailings.

More detailed information on this or similar activity can be found on the FCA website available at www.fca.org.uk/consumers.

SHARE PRICE

You can access the current share price of Phoenix Group Holdings on the Group's website together with electronic copies of the Group's financial reports and presentations at www.thephoenixgroup.com/investor-relations.aspx.

ORDINARY SHARES – 2016 FINAL DIVIDEND

Ex-dividend date	**30 March 2017**
Record date	**31 March 2017**
Payment date for the recommended final dividend	**15 May 2017**

GROUP FINANCIAL CALENDAR FOR 2017

Annual General Meeting	**11 May 2017**
Announcement of unaudited six months' Interim Results	**24 August 2017**

FORWARD-LOOKING STATEMENTS

The 2016 Annual Report and Accounts contains, and the Group may make other statements (verbal or otherwise) containing, forward-looking statements and other financial and/or statistical data about the Group's current plans, goals and expectations relating to future financial conditions, performance, results, strategy and/or objectives.

Statements containing the words: 'believes', 'intends', 'will', 'may', 'should', 'expects', 'plans', 'aims', 'seeks', 'targets', 'continues' and 'anticipates' or other words of similar meaning are forward-looking. Such forward-looking statements and other financial and/or statistical data involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group's control. For example, certain insurance risk disclosures are dependent on the Group's choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that we have estimated. Other factors which could cause actual results to differ materially from those estimated by forward-looking statements include but are not limited to:

- domestic and global economic and business conditions;
- asset prices;
- market-related risks such as fluctuations in interest rates and exchange rates, the potential for a sustained low-interest rate environment, and the performance of financial markets generally;
- the policies and actions of governmental and/or regulatory authorities, including, for example, new government initiatives related to the financial crisis and the effect of the European Union's 'Solvency II' requirements on the Group's capital maintenance requirements;
- the political, legal and economic effects of the UK's vote to leave the European Union;
- the impact of inflation and deflation;
- market competition;
- changes in assumptions in pricing and reserving for insurance business (particularly with regard to mortality and morbidity trends, gender pricing and lapse rates);
- the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries;
- risks associated with arrangements with third parties;
- inability of reinsurers to meet obligations or unavailability of reinsurance coverage; and
- the impact of changes in capital, solvency or accounting standards, and tax and other legislation and regulations in the jurisdictions in which members of the Group operate.

As a result, the Group's actual future financial condition, performance and results may differ materially from the plans, goals and expectations set out in the forward-looking statements and other financial and/or statistical data within the 2016 Annual Report and Accounts.

The Group undertakes no obligation to update any of the forward-looking statements contained within the 2016 Annual Report and Accounts or any other forward-looking statements it may make or publish.

The 2016 Annual Report and Accounts has been prepared for the members of the Company and no one else. The Company, its Directors or agents do not accept or assume responsibility to any other person in connection with this document and any such responsibility or liability is expressly disclaimed.

Nothing in the 2016 Annual Report and Accounts is or should be construed as a profit forecast or estimate.

GLOSSARY

ABBEY LIFE	The companies comprising of Abbey Life Assurance Company Limited, Abbey Life Trustee Services Limited and Abbey Life Trust Securities Limited
ABS	Asset Backed Securities – A collateralised security whose value and income payments are derived from a specified pool of underlying assets
ALM	Asset Liability Management – Management of mismatches between assets and liabilities within risk appetite
ALTERNATIVE PERFORMANCE MEASURE	An Alternative Performance Measure ('APM') is a financial measure of historic or future financial performance, financial position,or cash flows, other than a financial measure defined under IFRS or under Solvency II regulations. The Group uses a range of these metrics to provide a better understanding of the underlying performance of the Group. Where appropriate, reconciliations of APMs to IFRS or Solvency II measures are provided in the Annual Report and Accounts. All APMs are defined within this glossary.
ANNUITY POLICY	A policy that pays out regular benefit amounts, either immediately and for the remainder of a policyholder's lifetime (immediate annuity), or deferred to commence at some future date (deferred annuity)
ASSET MANAGEMENT	The management of assets using a structured approach to guide the act of acquiring and disposing of assets, with the objective of meeting defined investment goals and maximising value for investors,including policyholders
AVIF	Acquired Value of In-Force business
BLACK-SCHOLES	A mathematical model used to calculate the value of an option
BREXIT	The vote by the people of the United Kingdom to leave the EU in the referendum held on 23 June 2016
CLOSED LIFE FUND	A fund that no longer accepts new business. The fund continues to be managed for the existing policyholders
DPF	Discretionary Participation Feature – A contractual right under an insurance contract to receive, as a supplement to guaranteed benefits, additional benefits whose amount or timing is contractually at the discretion of the issuer
EBT	Employee Benefit Trust – A trust set up to enable its Trustee to purchase and hold shares to satisfy employee share-based incentive plan awards. The Company's EBT is the Phoenix Group Holdings Employee Benefit Trust
ECONOMIC ASSUMPTIONS	Assumptions related to future interest rates, inflation, market value movements and tax
EEA	European Economic Area – Established on 1 January 1994 and is an agreement between Norway, Iceland, Liechtenstein and the European Union. It allows these countries to participate in the EU's single market without joining the EU
EXPERIENCE VARIANCES	Current period differences between the actual experience incurred and the assumptions used in the calculation of IFRS insurance liabilities
FINANCIAL REPORTING COUNCIL	The UK's independent regulator responsible for promoting high-quality corporate governance and reporting to foster investment
FREE SURPLUS	The amount of capital held in life companies in excess of that needed to support their minimum regulatory capital requirement, plus the capital required under the Group's capital management policy
FCA	Financial Conduct Authority – The body responsible for supervising the conduct of all financial services firms and for the prudential regulation of those financial services firms not supervised by the Prudential Regulation Authority ('PRA'), such as asset managers and independent financial advisers
FOS	Financial Ombudsman Service – An ombudsman established in 2000, and given statutory powers in 2001 by the Financial Services and Markets Act 2000, to help settle disputes between consumers and UK-based businesses providing financial services
GAR	Guaranteed Annuity Rate – A rate available to certain pension policyholders to acquire an annuity at a contractually guaranteed conversion rate
HMRC	HM Revenue and Customs
HOLDING COMPANIES	Refers to Phoenix Group Holdings, PGH Capital plc, Phoenix Life Holdings Limited, Pearl Group Holdings (No. 2) Limited, Impala Holdings Limited, Pearl Group Holdings (No. 1) Limited, PGH (TC1) Limited, PGH (TC2) Limited, PGH (MC1) Limited, PGH (MC2) Limited, PGH (LCA) Limited, PGH (LCB) Limited, PGH (LC1) Limited, PGH (LC2) Limited and Pearl Life Holdings Limited
IFRS	International Financial Reporting Standards – Accounting standards, interpretations and the framework adopted by the International Accounting Standards Board
IMC	Investment Management Contract – A contract between an investor and an investment manager
IN-FORCE	Long-term business written before the period end and which has not terminated before the period end

INHERITED ESTATE	The assets of the long-term with-profit funds less the realistic reserves for non-profit policies written into the non-profit fund, less asset shares aggregated across the with-profit policies and any additional amounts expected at the valuation date to be paid to in-force policyholders in the future in respect of smoothing costs and guarantees
INTERNAL MODEL	The agreed methodology and model, approved by the PRA, to calculate the Group Solvency Capital Requirement pursuant to Solvency II
LIBOR	London Interbank Offer Rate – The average interbank interest rate at which a selection of banks on the London money market are prepared to lend to one another
LSE	London Stock Exchange
LTIP	Long-Term Incentive Plan – The part of an executive's remuneration designed to incentivise long-term value for shareholders through an award of shares with vesting contingent on employment and the satisfaction of stretching performance conditions linked to Group strategy
MSA	Management Services Agreement – Contracts that exist between Phoenix Life and management services companies or between management services companies and their outsource partners
NON-ECONOMIC ASSUMPTIONS	Assumptions related to future levels of mortality, morbidity, persistency and expenses
NON-PROFIT FUND	A fund which is not a with-profit fund, where risks and rewards of the fund fall wholly to shareholders
OPEN ENDED INVESTMENT COMPANIES	A type of company or a fund in the UK that is structured to invest in other companies with the ability to adjust its investment criteria and fund size
OPERATING COMPANIES	Refers to the trading companies within Phoenix Life
OPERATING COMPANIES' CASH GENERATION	Operating companies' cash generation represents cash remitted by the Group's operating companies to the holding companies
OPERATING PROFIT	Operating profit is a non-GAAP measure that is considered a more representative measure of performance than IFRS profit or loss after tax as it provides long-term performance information unaffected by short-term economic volatility
ORIGO	An electronic pensions transfer system
OWN FUNDS	Basic Own Funds comprise the excess of assets over liabilities valued in accordance with the Solvency II principles and subordinated liabilities which qualify to be included in Own Funds under the Solvency II rules. Eligible Own Funds are the amount of Own Funds that are available to cover the Solvency Capital Requirements after applying prescribed tiering limits and transferability restrictions to Basic Own Funds.
PART VII TRANSFER	The transfer of insurance policies under Part VII of FSMA 2000. The insurers involved can be in the same corporate group or in different groups. Transfers require the consent of the High Court, which will consider the views of the PRA and FCA and of an Independent Expert
PARTICIPATING BUSINESS	See with-profit fund
PERIPHERAL EUROZONE	Refers to Portugal, Ireland, Italy, Greece and Spain
PPFM	Principles and Practices of Financial Management – A publicly available document which explains how a company's with-profit business is run. As part of demonstrating that customers are treated fairly, the Board certifies that the PPFM has been complied with
PRA	Prudential Regulation Authority – The body responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. The PRA and FCA use a Memorandum of Understanding to co-ordinate and carry out their respective responsibilities
PROTECTION POLICY	A policy which provides benefits payable on certain events. The benefits may be a single lump sum or a series of payments and may be payable on death, serious illness or sickness
SHAREHOLDER CAPITAL COVERAGE RATIO	The Shareholder Capital Coverage Ratio represents the shareholder view of the Group solvency position and is calculated as the ratio of Eligible Own Funds to SCR adjusted to exclude amounts relating to those unsupported with-profit funds and Group pension schemes whose Own Funds exceed their SCR
SOLVENCY II	A new regime for the prudential regulation of European insurance companies that came into force on 1 January 2016
SOLVENCY II SURPLUS	The excess of Eligible Own Funds over the Solvency Capital Requirement

GLOSSARY
Continued

SOLVENCY CAPITAL REQUIREMENTS ('SCR')	SCR relates to the risks and obligations to which the Group is exposed, and is calibrated so that the likelihood of a loss exceeding the SCR is less than 0.5% over one year. This ensures that capital is sufficient to withstand a broadly '1 in 200 year event'
STANDARD FORMULA	A set of calculations prescribed by the Solvency II regulations for generating the SCR
TRANSITIONAL MEASURES ON TECHNICAL PROVISIONS	Transitional Measures to Technical Provisions ('TMTP') is an allowance, subject to the PRA's approval, to apply a transitional deduction to technical provisions. The transitional deduction corresponds to the difference between net technical provisions calculated in accordance with Solvency II principals and net technical provisions calculated in accordance with the previous regime is expected to decrease linearly over a period of 16 years starting from 1 January 2016 to 1 January 2032
TSR	Total Shareholder Return – The total return, over a fixed period, to an investor in terms of share price growth and dividends (assuming that dividends paid are re-invested, on the ex-dividend date, in acquiring further shares)
UK CORPORATE GOVERNANCE CODE	Standards of good corporate governance practice in the UK relating to issues such as board composition and development, remuneration, accountability, audit and relations with shareholders
UKCPT	UK Commercial Property Trust Limited – A property subsidiary of the Group which is domiciled in Guernsey and listed on the London Stock Exchange
UK GAAP	Generally Accepted Accounting Principles adopted within the UK
UNIT-LINKED POLICY	A policy where the benefits are determined by the investment performance of the underlying assets in the unit-linked fund
WITH-PROFIT FUND	A fund where policyholders are entitled to a share of the profits of the fund. Normally, policyholders receive their share of the profits through bonuses. Also known as a participating fund as policyholders have a participating interest in the with-profit funds and any declared bonuses. Generally, policyholder and shareholder participation in the with-profit funds in the UK is split 90:10

ONLINE RESOURCES

REDUCING OUR ENVIRONMENTAL IMPACT

In line with our Corporate Responsibility programme, and as part of our desire to reduce our environmental impact, you can view key information on our website.

Go online
www.thephoenixgroup.com

INVESTOR RELATIONS

Our Investor Relations section includes information such as our most recent news and announcements, results presentations, annual and interim reports, share-price performance, AGM and EGM information, UK Regulatory Returns and contact information.

Go online
www.thephoenixgroup.com/investor-relations

NEWS AND UPDATES

To stay up-to-date with Phoenix Group news and other changes to our site's content, you can sign up for e-mail alerts, which will notify you when content is added.

To sign up visit
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