A. Accountants' Report

KPMG Audit Plc
Chartered Accountants
8 Salisbury Square
London
EC4Y 8BB
United Kingdom

KPMG
Certified Public Accountants
Prince's Building
10 Chater Road
Central
Hong Kong

The Directors
Prudential plc
Laurence Pountney Hill
London, EC4R 0HH

Credit Suisse (Hong Kong) Limited
45th Floor, Two Exchange Square
8 Connaught Place
Central
Hong Kong

17 May 2010

Dear Sirs

Prudential plc

INTRODUCTION

We report on the financial information relating to Prudential plc (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group" or "Prudential Group") comprising the consolidated income statements, consolidated statements of comprehensive income, the consolidated statements of changes in equity and the consolidated cash flow statements of the Group, for each of the years ended 31 December 2007, 31 December 2008 and 31 December 2009 (the "Relevant Period"), and the consolidated statements of financial position of the Group and the statements of financial position of the Company as at 31 December 2007, 31 December 2008 and 31 December 2009, together with the notes thereto (the "Financial Information"), set out in section B of this Appendix I of this listing document of the Company dated 17 May 2010 (the "Listing Document").

The directors of the Company have prepared the consolidated financial information of the Group for the Relevant Period in accordance with IFRSs issued by the International Accounting Standards Board (the "IASB") (the "Underlying Financial Information"). The Underlying Financial Statements for each of the years ended 31 December 2007, 31 December 2008 and 31 December 2009 were audited by KPMG Audit Plc in accordance with International Standards on Auditing (UK and Ireland) issued by the Audit Practices Board.

The Financial Information has been prepared by the directors of the Company based on the Underlying Financial Statements, with no adjustments made thereon, except for adjustments to comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules").

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND REPORTING ACCOUNTANTS

The directors of the Company are responsible for the preparation and true and fair presentation of the Financial Information in accordance with IFRSs issued by the IASB, the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Listing Rules. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the Financial Information that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Our responsibility is to form an opinion on the Financial Information based on our procedures.

Save for any responsibility arising under the Hong Kong Listing Rules to any person as and to the extent there provided, to the fullest extent permitted by law we do not assume any responsibility and will not accept any liability to any other person for any loss suffered by any such other person as a result of, arising out of, or in connection with this opinion or our statement, required by and given solely for the purposes of complying with the Hong Kong Listing Rules, consenting to its inclusion in the Listing Document.

BASIS OF OPINION

As a basis for forming an opinion on the Financial Information, for the purpose of this report, we have examined the Underlying Financial Statements and have carried out such appropriate procedures as we considered necessary in accordance with Auditing Guideline "Prospectuses and the Reporting Accountant" (Statement 3.340) issued by the HKICPA.

We have not audited any financial statements of the Company, its subsidiaries or the Group in respect of any period subsequent to 31 December 2009.

OPINION

In our opinion, for the purpose of this report, the Financial Information, in accordance with the accounting policies set out in Note A of the Financial Information (in section B of this Appendix I), gives a true and fair view of the Group's consolidated results, cash flows, comprehensive income and changes in equity for the Relevant Period, and the state of affairs of the Group and the Company as at 31 December 2007, 31 December 2008 and 31 December 2009.

Yours faithfully

KPMG Audit Plc
Chartered Accountants
London, United Kingdom

KPMG
Certified Public Accountants
Hong Kong

B. Consolidated financial information for the years ended 31 December 2007, 31 December 2008 and 31 December 2009

CONSOLIDATED INCOME STATEMENT

	Note	Year ended 31 December 2007	2008	2009
		£m	£m	£m
Gross premiums earned		18,359	18,993	20,299
Outward reinsurance premiums		(171)	(204)	(323)
Earned premiums, net of reinsurance	F2	18,188	18,789	19,976
Investment return	F2	12,225	(30,202)	26,889
Other income	F2	2,457	1,146	1,234
Total revenue, net of reinsurance	F1,F2	32,870	(10,267)	48,099
Benefits and claims		(26,224)	4,620	(39,901)
Outward reinsurers' share of benefits and claims		(20)	389	265
Movement in unallocated surplus of with-profits funds	H12	(541)	5,815	(1,559)
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance		(26,785)	10,824	(41,195)
Acquisition costs and other operating expenditure	F3	(4,859)	(2,459)	(4,572)
Finance costs: interest on core structural borrowings of shareholder-financed operations	F4	(168)	(172)	(209)
Loss on sale of Taiwan agency business	I1	—	—	(559)
Total charges, net of reinsurance	F1	(31,812)	8,193	(46,535)
Profit (loss) before tax (*being tax attributable to shareholders' and policyholders' returns*)*		1,058	(2,074)	1,564
Tax credit attributable to policyholders' returns		5	1,624	(818)
Profit (loss) before tax attributable to shareholders	B1	1,063	(450)	746
Tax credit (charge)	F5	(349)	1,683	(873)
Less: tax credit attributable to policyholders' returns		(5)	(1,624)	818
Tax credit (charge) attributable to shareholders' returns	F5	(354)	59	(55)
Profit (loss) from continuing operations after tax		709	(391)	691
Discontinued operations (net of tax)	I9	241	—	(14)
Profit (loss) for the year		950	(391)	677
Attributable to:				
Equity holders of Prudential		947	(396)	676
Minority interests		3	5	1
Profit (loss) for the year		950	(391)	677
Earnings per share (in pence)				
Basic:				
Based on profit (loss) from continuing operations attributable to the equity holders of Prudential	B2	28.8p	(16.0)p	27.6p
Based on profit (loss) from discontinued operations attributable to the equity holders of Prudential	B2	9.9p	—	(0.6)p
		38.7p	(16.0)p	27.0p
Diluted:				
Based on profit (loss) from continuing operations attributable to the equity holders of Prudential	B2	28.8p	(16.0)p	27.6p
Based on profit (loss) from discontinued operations attributable to the equity holders of Prudential	B2	9.8p	—	(0.6)p
		38.6p	(16.0)p	27.0p

* This measure is the formal profit (loss) before tax measure under IFRS but is not the result attributable to shareholders.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December 2007	2008	2009
		£m	£m	£m
Profit (loss) for the year		950	(391)	677
Other comprehensive income (loss):				
Exchange movements on foreign operations and net investment hedges:				
Exchange movements arising during the year	B4	11	391	(206)
Related tax		2	119	11
		13	510	(195)
Movement in cash flow hedges		(3)	—	—
Related tax		1	—	—
		(2)	—	—
Available-for-sale securities:				
Unrealised valuation movements on securities classified as available-for-sale of banking operations		(2)	—	—
Unrealised valuation movements on securities of US insurance operations classified as available-for-sale:	D3(a)			
Unrealised holding gains (losses) arising during the year		(231)	(2,482)	2,249
Add back net losses included in the income statement on disposal and impairment		(13)	378	420
Total		(246)	(2,104)	2,669
Related change in amortisation of deferred income and acquisition costs	H1	88	831	(1,069)
Related tax		53	442	(557)
		(105)	(831)	1,043
Other comprehensive income (loss) for the year, net of related tax		(94)	(321)	848
Total comprehensive income (loss) for the year		856	(712)	1,525
Attributable to:				
Equity holders of Prudential Group		853	(717)	1,524
Minority interests		3	5	1
Total comprehensive income (loss) for the year		856	(712)	1,525

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

		Year ended 31 December 2007								
	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Hedging reserve	Share-holders' equity	Minority interests	Total equity
						£m				
Reserves										
Profit for the year		—	—	947	—	—	—	947	3	950
Other comprehensive income (loss):										
Exchange movements on foreign operations and net investment hedges, net of related tax		—	—	—	13	—	—	13	—	13
Movement on cash flow hedges, net of related tax		—	—	—	—	—	(2)	(2)	—	(2)
Unrealised valuation movements, net of related change in amortisation of deferred income and acquisition costs and related tax		—	—	—	—	(105)	—	(105)	—	(105)
Total other comprehensive income (loss)		—	—	—	13	(105)	(2)	(94)	—	(94)
Total comprehensive income (loss) for the year		—	—	947	13	(105)	(2)	853	3	856
Dividends	B3	—	—	(426)	—	—	—	(426)	(5)	(431)
Reserve movements in respect of share-based payments		—	—	18	—	—	—	18	—	18
Change in minority interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and of other consolidated investment funds		—	—	—	—	—	—	—	(28)	(28)
Share capital and share premium										
New share capital subscribed	H11	1	181	—	—	—	—	182	—	182
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	H11	—	(175)	175	—	—	—	—	—	—
Treasury shares										
Movement in the value of own shares held in respect of share-based payment plans		—	—	7	—	—	—	7	—	7
Movement in the value of Prudential plc shares purchased by unit trusts consolidated under IFRS		—	—	4	—	—	—	4	—	4
Net increase (decrease) in equity		1	6	725	13	(105)	(2)	638	(30)	608
At beginning of year		122	1,822	3,576	(125)	27	2	5,424	132	5,556
At end of year	H11	123	1,828	4,301	(112)	(78)	—	6,062	102	6,164

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (continued)

	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Hedging reserve	Share-holders' equity	Minority interests	Total equity
		Year ended 31 December 2008								
						£m				
Reserves										
Loss for the year		—	—	(396)	—	—	—	(396)	5	(391)
Other comprehensive income (loss):										
Exchange movements on foreign operations and net investment hedges, net of related tax		—	—	—	510	—	—	510	—	510
Unrealised valuation movements, net of related change in amortisation of deferred income and acquisition costs and related tax		—	—	—	—	(831)	—	(831)	—	(831)
Total other comprehensive income (loss)		—	—	—	510	(831)	—	(321)	—	(321)
Total comprehensive income (loss) for the year		—	—	(396)	510	(831)	—	(717)	5	(712)
Dividends	B3	—	—	(453)	—	—	—	(453)	(2)	(455)
Reserve movements in respect of share-based payments		—	—	18	—	—	—	18	—	18
Change in minority interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and of other consolidated investment funds		—	—	—	—	—	—	—	(50)	(50)
Share capital and share premium										
New share capital subscribed	H11	2	168	—	—	—	—	170	—	170
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	H11	—	(156)	156	—	—	—	—	—	—
Treasury shares										
Movement in own shares held in respect of share-based payment plans		—	—	3	—	—	—	3	—	3
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS		—	—	(25)	—	—	—	(25)	—	(25)
Net increase (decrease) in equity		2	12	(697)	510	(831)	—	(1,004)	(47)	(1,051)
At beginning of year		123	1,828	4,301	(112)	(78)	—	6,062	102	6,164
At end of year	H11	125	1,840	3,604	398	(909)	—	5,058	55	5,113

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (continued)

	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Hedging reserve	Share-holders' equity	Minority interests	Total equity
		Year ended 31 December 2009								
						£m				
Reserves										
Profit for the year		—	—	676	—	—	—	676	1	677
Other comprehensive income (loss):										
Exchange movements on foreign operations and net investment hedges, net of related tax		—	—	—	(195)	—	—	(195)	—	(195)
Unrealised valuation movements, net of related change in amortisation of deferred income and acquisition costs and related tax		—	—	—	—	1,043	—	1,043	—	1,043
Total other comprehensive income (loss)		—	—	—	(195)	1,043	—	848	—	848
Total comprehensive income (loss) for the year		—	—	676	(195)	1,043	—	1,524	1	1,525
Dividends	B3	—	—	(481)	—	—	—	(481)	—	(481)
Reserve movements in respect of share-based payments		—	—	29	—	—	—	29	—	29
Change in minority interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and of other consolidated investment funds		—	—	—	—	—	—	—	(24)	(24)
Share capital and share premium										
New share capital subscribed	H11	2	139	—	—	—	—	141	—	141
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	H11	—	(136)	136	—	—	—	—	—	—
Treasury shares										
Movement in own shares held in respect of share-based payment plans		—	—	3	—	—	—	3	—	3
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS		—	—	(3)	—	—	—	(3)	—	(3)
Net increase (decrease) in equity		2	3	360	(195)	1,043	—	1,213	(23)	1,190
At beginning of year		125	1,840	3,604	398	(909)	—	5,058	55	5,113
At end of year	H11	127	1,843	3,964	203	134	—	6,271	32	6,303

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	31 December 2007	31 December 2008	31 December 2009
		£m	£m	£m
ASSETS				
Intangible assets attributable to shareholders:				
Goodwill	H1(a)	1,341	1,341	1,310
Deferred acquisition costs and other intangible assets	H1(b)	2,836	5,349	4,049
Total		4,177	6,690	5,359
Intangible assets attributable to with-profits funds:				
In respect of acquired subsidiaries for venture fund and other investment purposes	H2(a)	192	174	124
Deferred acquisition costs and other intangible assets	H2(b)	19	126	106
Total		211	300	230
Total		4,388	6,990	5,589
Other non-investment and non-cash assets:				
Property, plant and equipment	H6	1,012	635	367
Reinsurers' share of insurance contract liabilities	H3	783	1,240	1,187
Deferred tax assets	H4	951	2,886	2,708
Current tax recoverable	H4	285	657	636
Accrued investment income	G1,H5	2,023	2,513	2,473
Other debtors	G1,H5	909	1,232	762
Total		5,963	9,163	8,133
Investments of long-term business and other operations:				
Investment properties	H7	13,688	11,992	10,905
Investments accounted for using the equity method	H8	12	10	6
Financial investments:	G1			
Loans		7,924	10,491	8,754
Equity securities and portfolio holdings in unit trusts		86,157	62,122	69,354
Debt securities		83,984	95,224	101,751
Other investments		4,396	6,301	5,132
Deposits		7,889	7,294	12,820
Total		204,050	193,434	208,722
Properties held for sale	H9	30	—	3
Cash and cash equivalents	G1,H10	4,951	5,955	5,307
Total assets	B6	219,382	215,542	227,754

CONSOLIDATED STATEMENT OF FINANCIAL POSITION (continued)

	Note	31 December 2007	2008	2009
		£m	£m	£m
EQUITY AND LIABILITIES				
Equity				
Shareholders' equity	H11	6,062	5,058	6,271
Minority interests		102	55	32
Total equity		6,164	5,113	6,303
Liabilities				
Policyholder liabilities and unallocated surplus of with-profits funds:				
Insurance contract liabilities	H12	132,776	136,030	145,713
Investment contract liabilities with discretionary participation features	G1	29,550	23,446	24,880
Investment contract liabilities without discretionary participation features	G1	14,032	14,501	15,805
Unallocated surplus of with-profits funds	H12	13,959	8,414	10,019
Total		190,317	182,391	196,417
Core structural borrowings of shareholder-financed operations:				
Subordinated debt	H13	1,570	1,987	2,691
Other	H13	922	971	703
Total	G1,H13	2,492	2,958	3,394
Other borrowings:				
Operational borrowings attributable to shareholder-financed operations	G1,H13	3,081	1,977	2,751
Borrowings attributable to with-profits funds	G1,H13	987	1,308	1,284
Other non-insurance liabilities:				
Obligations under funding, securities lending and sale and repurchase agreements	G1	4,081	5,572	3,482
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	G1	3,556	3,843	3,809
Deferred tax liabilities	H4	3,402	3,229	3,872
Current tax liabilities	H4	1,237	842	1,215
Accruals and deferred income		599	630	594
Other creditors	G1	1,020	1,496	1,612
Provisions	H14	575	461	643
Derivative liabilities	G1,G3	1,080	4,832	1,501
Other liabilities	G1,H15	791	890	877
Total		16,341	21,795	17,605
Total liabilities	B6	213,218	210,429	221,451
Total equity and liabilities		219,382	215,542	227,754

CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	Year ended 31 December 2007	2008	2009
		£m	£m	£m
Cash flows from operating activities				
Profit (loss) before tax from continuing operations (*being tax attributable to shareholders' and policyholders' returns*)[†]		1,058	(2,074)	1,564
Profit (loss) before tax from discontinued operations	I9	222	—	(14)
Total profit (loss) before tax		1,280	(2,074)	1,550
Changes in operating assets and liabilities:				
Investments		(11,818)	32,424	(26,388)
Other non-investment and non-cash assets		(378)	(828)	(384)
Policyholder liabilities (including unallocated surplus)		11,845	(26,987)	24,932
Other liabilities (including operational borrowings)		902	(631)	(299)
Interest income and expense and dividend income included in profit before tax		(8,301)	(7,927)	(7,267)
Other non-cash items (including £559 million in 2009 for the loss on disposal of Taiwan agency business)		(141)	(74)	650
Operating cash items:				
Interest receipts		5,641	5,875	5,734
Dividend receipts		2,732	2,019	1,780
Tax paid		(624)	(653)	(200)
Net cash flows from operating activities		1,138	1,144	108
Cash flows from investing activities				
Purchases of property, plant and equipment	H6	(231)	(240)	(91)
Proceeds from disposal of property, plant and equipment		61	11	54
Disposal of Taiwan agency business	I1	—	—	(497)
Completion adjustment for previously disposed business	I9	—	—	(20)
Acquisition of subsidiaries, net of cash balances	I7(iii)	(77)	—	—
Disposal of Egg, net of cash balances	I9	(538)	—	—
Disposal of other subsidiaries, net of cash balances	I7(iii)	157	—	—
Deconsolidation of investment subsidiaries	I7(iii)	(91)	—	—
Net cash flows from investing activities		(719)	(229)	(554)
Cash flows from financing activities				
Structural borrowings of the Group:	I10			
Shareholder-financed operations:				
Issue of subordinated debt, net of costs		—	—	822
Redemption of senior debt		(150)	—	(249)
Interest paid		(171)	(167)	(207)
With-profits operations:				
Interest paid		(9)	(9)	(9)
Equity capital:*				
Issues of ordinary share capital	H11	6	12	3
Dividends paid	B3	(255)	(297)	(344)
Net cash flows from financing activities		(579)	(461)	16
Net increase (decrease) in cash and cash equivalents		(160)	454	(430)
Cash and cash equivalents at beginning of year		5,071	4,951	5,955
Effect of exchange rate changes on cash and cash equivalents		40	550	(218)
Cash and cash equivalents at end of year	H10	4,951	5,955	5,307

† This measure is the formal (loss) profit before tax measure under IFRS but it is not the result attributable to shareholders.

* Cash movements in respect of equity capital exclude scrip dividends.

Statement of financial position of the parent company

	31 December		
	2007	2008	2009
	£m	£m	£m
ASSETS			
Non-current assets			
Investments:			
Shares in subsidiary undertakings	7,170	7,193	10,071
Loans to subsidiary undertakings	2,809	3,212	899
	9,979	10,405	10,970
Current assets			
Debtors:			
Amounts owed by subsidiary undertakings	3,291	1,986	2,760
Deferred tax	9	117	186
Other debtors	25	11	7
Derivative assets	10	267	151
Cash and cash equivalents	178	102	360
	3,513	2,483	3,464
Total assets	13,492	12,888	14,434
LIABILITIES AND EQUITY			
Liabilities			
Non-current liabilities			
Subordinated liabilities	1,566	1,983	2,687
Debenture loans	797	549	549
Other borrowings	7	9	—
Amounts owed to subsidiary undertakings	2,643	1,464	3,326
Pension liabilities	31	20	22
	5,044	4,025	6,584
Current liabilities			
Debenture loans	—	249	—
Commercial paper	2,422	1,269	2,031
Other borrowings	48	200	207
Derivative liabilities	144	235	136
Amounts owed to subsidiary undertakings	2,455	3,341	1,279
Tax payable	332	311	379
Sundry creditors	6	19	4
Accruals and deferred income	44	44	41
	5,451	5,668	4,077
Total liabilities	10,495	9,693	10,661
Equity			
Share capital	123	125	127
Share premium	1,828	1,840	1,843
Retained earnings	1,046	1,230	1,803
Total equity	2,997	3,195	3,773
Total equity and liabilities	13,492	12,888	14,434

NOTES ON THE PRUDENTIAL GROUP FINANCIAL STATEMENTS

A: BACKGROUND AND ACCOUNTING POLICIES

A1: Nature of operations

Prudential plc (the Company) together with its subsidiaries (collectively, the Prudential Group) is an international financial services group with its principal operations in the UK, the US and Asia. The Prudential Group operates in the UK through its subsidiaries, primarily The Prudential Assurance Company Limited ("PAC"), Prudential Annuities Limited (PAL), Prudential Retirement Income Limited ("PRIL") and M&G Investment Management Limited.

In the US, the Prudential Group's principal subsidiary is Jackson National Life Insurance Company (Jackson). The Prudential Group also has operations in Hong Kong, Malaysia, Singapore, Indonesia and other Asian countries.

Prudential Group offers a wide range of retail financial products and services and asset management services throughout these territories. The retail financial products and services principally include life insurance, pensions and annuities as well as collective investment schemes.

Long-term business products written in the UK and Asia are principally with-profits deposit administration, other conventional and unitised with-profits policies and non-participating pension annuities in the course of payment. Long-term business also includes linked business written in the UK and Asia. The principal products written by Jackson are interest-sensitive deferred annuities and whole-life policies, variable annuities, guaranteed investment contracts, fixed index deferred annuities and term life insurance.

The Company was incorporated in England on 30 May 1848 as The Prudential Mutual Assurance Investment and Loan Association under relevant UK legislation. At the current time Prudential is a limited liability company subject to the Companies' Act. Prudential has been the holding company of the companies comprising the Prudential Group, details of which are set out in note I7, throughout the Relevant Period.

Substantially all companies comprising the Prudential Group have adopted 31 December as their financial year end date. Details of the principal companies comprising the Prudential Group that are subject to audit during the Relevant Period and the names of the respective auditors are set out in note I7. The statutory financial information of these companies was converted in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union (EU) for the purposes of the group accounts. Prudential is a public limited company incorporated and registered in England and Wales. The registered office is:

Laurence Pountney Hill
London
EC4R 0HH
Registered number: 1397169

A2: Basis of preparation

The consolidated financial information consolidates the Prudential Group and the Prudential Group's interest in associates and jointly-controlled entities.

The consolidated financial information of Prudential and the parent company financial information has been prepared and approved by the directors in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and as endorsed by the EU. EU-endorsed IFRS may differ from IFRS as issued by the IASB if, at any point in time, new or amended IFRS have not been endorsed by the EU. At 31 December 2009, there were no unendorsed standards effective for the three years ended 31 December 2009 affecting the consolidated or the parent company financial information, and there was no difference between IFRS endorsed by the EU and IFRS issued by the IASB in terms of their application to Prudential. Accordingly, Prudential's financial information for the three years ended 31 December 2009 is prepared in accordance with IFRS as issued by the IASB.

The Prudential Group has applied IFRS standards and interpretations adopted by the EU that are effective for financial years commencing on or before 1 January 2009. All accounting pronouncements adopted at 31 December 2009 have been applied consistently across the three year track record period unless the relevant standard permits an alternative approach upon transition. The only such transitional arrangements which the Prudential Group has taken advantage of during the track record period are as follows:

i) Amendments to IFRS 7 'Improving Disclosures about financial instruments' — this standard enhances the disclosures around financial instruments. Comparatives are not required for these disclosures and the Prudential Group has taken advantage of this exemption. As a disclosure standard this has no impact on the primary financial statements of the Prudential Group.

ii) Amendments to IAS 40 — 'Investment Property' — although full retrospective application is permitted, the Prudential Group has taken advantage of the ability to apply this prospectively from 1 January 2009 on the basis that full retrospective application would not have had a significant impact on the Prudential Group's financial results and position in 2007 and 2008. Further details on the application of new accounting pronouncements are provided in note A5.

For the purposes of the Prudential Group's annual report and accounts, the parent company prepares its own financial statements in accordance with applicable accounting standards under UK Generally Accepted Accounting Practice (UK GAAP). For the purpose of this document, the parent company financial information has been prepared in accordance with IFRS, applying accounting policies which are consistent with those applied for the Prudential Group consolidated financial information. In addition, investments in subsidiary undertakings are shown at cost, net of impairments.

A3: Critical accounting policies, estimates and judgements

a Critical accounting policies

Prudential's discussion and analysis of its financial condition and results of operations are based upon Prudential's consolidated financial information, which have been prepared in accordance with IFRS adopted for use in the EU. Were the Prudential Group to apply IFRS as published by the IASB, as opposed to the EU-adopted IFRS, no additional measurement adjustments or disclosures would be required. It is the Prudential Group's policy to adopt mandatory requirements of new or altered EU-adopted IFRS standards where required, with earlier adoption applied where permitted and appropriate in the circumstances.

The preparation of this financial information requires Prudential to make estimates and judgements that affect the reported amounts of assets, liabilities, and revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, Prudential evaluates its estimates, including those related to long-term business provisioning, the fair value of assets and the declaration of bonus rates. Prudential bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgements and uncertainties, and potentially give rise to different results under different assumptions and conditions. Prudential believes that its critical accounting policies are limited to those described below.

The critical accounting policies in respect of the items discussed below are critical for the Prudential Group's results insofar as they relate to the Prudential Group's shareholder-financed business. In particular this applies for Jackson which is the largest shareholder-backed business in the Prudential Group. The policies are not critical in respect of the Prudential Group's with-profits business. This distinction reflects the basis of recognition of profits and accounting treatment of unallocated surplus of with-profits funds. Additional explanation is provided later in this note and cross-referenced notes as to why the distinction between with-profits business and shareholder-backed business is relevant.

The items discussed below and in cross-referenced notes explain the effect of changes in estimates and the effect of reasonably likely changes in the key assumptions underlying these estimates as of the latest statements of financial position date so as to provide analysis that recognises the different accounting effects on profit and loss or equity. In order to provide relevant analysis that is appropriate to the circumstances applicable to the Prudential Group's businesses, the explanations refer to types of business, fund structure, the relationship between asset and policyholder liability measurement, and the differences in the method of accounting permitted under IFRS 4 for accounting for insurance contract assets, policyholder liabilities and unallocated surplus of the Group's with-profits funds.

Insurance contract accounting

With the exception of certain contracts described in note D1, the contracts issued by the Prudential Group's life assurance business are classified as insurance contracts and investment contracts with discretionary participating features. As permitted by IFRS 4, 4, assets and liabilities of these contracts are accounted for under previously applied GAAP. In limited circumstances the Prudential Group has chosen to apply a more relevant or reliable measure. The following paragraphs explain how the current Prudential Group applies this policy. Except as described below, in respect of UK regulated with-profits funds where the basis applied has been improved to a more relevant or reliable measure (also as permitted under IFRS 4), the modified statutory basis (MSB) of reporting as set out in the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers (ABI) has been applied to the Prudential Group's UK and overseas operations.

In 2005 the Group chose to improve its IFRS accounting for UK regulated with-profits funds by the voluntary application of the UK accounting standard FRS 27, 'Life Assurance'. Under this standard, the main accounting changes that were required for UK with-profits funds were:

- Derecognition of deferred acquisition costs and related deferred tax; and
- replacement of MSB liabilities with adjusted realistic basis liabilities.

The results included in the IFRS financial information reflect this basis.

Unallocated surplus represents the excess of assets over policyholder liabilities for the Prudential Group's with-profits funds that have yet to be appropriated between policyholders and shareholders. The Prudential Group has opted to account for unallocated surplus wholly as a liability with no allocation to equity. This treatment reflects the fact that shareholders' participation in the cost of bonuses arises only on distribution. Shareholder profits on with-profits business reflect one-ninth of the cost of declared bonus.

For the Prudential Group's current overseas operations, the application of the MSB (which permits the use of local GAAP in some circumstances) varies depending upon the basis of accounting applied prior to IFRS adoption or acquisition by the Prudential Group, and whether adjustments to the basis or a more appropriate method should be applied. For Jackson, applying the MSB as applicable to overseas operations, which permits the application of local GAAP in some circumstances, the assets and liabilities of insurance contracts are accounted for under insurance accounting prescribed by US GAAP. For the assets and liabilities of insurance contracts of the Prudential Group's current Asian operations, the local GAAP is applied with adjustments, where necessary, to comply with UK GAAP. For the operations in Taiwan, Vietnam and Japan, countries where local GAAP is not appropriate in the context of the previously applied MSB, accounting for insurance contracts is based on US GAAP. For participating business the liabilities include provisions for the policyholders' interest in realised investment gains and other surpluses that, where appropriate, and in particular for Vietnam, have yet to be declared as bonuses.

The usage of these bases of accounting has varying effects on the way in which product options and guarantees are measured. For UK regulated with-profits funds, options and guarantees are valued on a market consistent basis. The basis is described in note D2(f)(ii). For other operations a market consistent basis is not applied under the accounting basis described in note A4. Details of the guarantees, basis of setting assumptions, and sensitivity to altered assumptions are described in notes D3 and D4.

Valuation and accounting presentation of fair value movements of derivatives and debt securities of Jackson

Under IAS 39, derivatives are required to be carried at fair value. Unless net investment hedge accounting is applied, value movements on derivatives are recognised in the income statement. With the exception of value movements on derivatives held for variable annuities and other equity related hedging activities, the value movements on derivatives held by Jackson are separately identified within the short-term fluctuations in investment returns identified as part of the Prudential Group's segment results described below and in note B1. Derivative value movements in respect of equity risk within variable annuity business and other equity related hedging activities are included within the operating profit based on longer-term investment returns.

For derivative instruments of Jackson, the Prudential Group has considered whether it is appropriate to undertake the necessary operational changes to qualify for hedge accounting so as to achieve matching of value movements in hedging instruments and hedged items in the performance statements. In reaching the decision a number of factors were particularly relevant. These were:

- IAS 39 hedging criteria have been designed primarily in the context of hedging and hedging instruments that are assessable as financial instruments that are either stand-alone or separable from host contracts, rather than, for example, duration characteristics of insurance contracts;
- the high hurdle levels under IAS 39 of ensuring hedge effectiveness at the level of individual hedge transactions;
- the difficulties in applying the macro hedge provisions under IAS 39 (which are more suited to banking arrangements) to Jackson's derivative book;
- the complexity of asset and liability matching of US life insurers such as those with Jackson's product range; and finally
- whether it is possible or desirable, without an unacceptable level of costs and constraint on commercial activity, to achieve the accounting hedge effectiveness required under IAS 39.

Taking account of these considerations the Prudential Group has decided that, except for certain minor categories of derivatives, it is not appropriate to seek to achieve hedge accounting under IAS 39. As a result of this decision the total income statement results are more volatile as the movements in the value of Jackson's derivatives are reflected within it.

Under IAS 39, unless carried at amortised cost (subject to impairment provisions where appropriate) under the held-to-maturity category, debt securities are also carried at fair value. The Prudential Group has chosen not to classify any financial assets as held-to-maturity. Debt securities of Jackson are designated as available-for-sale with value movements, unless impaired, being recorded as movements within other comprehensive income. Impairments are recorded in the income statement.

Presentation of results before tax

The total tax charge for the Prudential Group reflects tax that in addition to relating to shareholders' profits is also attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. This is explained in more detail in note F5. However, pre-tax profits are determined after transfers to or from unallocated surplus of with-profits funds. These transfers are in turn determined after taking account of tax borne by with-profits funds. Consequently reported profit before the total tax charge is not representative of pre-tax profits attributable to shareholders. In order to provide a measure of pre-tax profits attributable to shareholders the Prudential Group has chosen to adopt an income statement presentation of the tax charge and pre-tax results that distinguishes between policyholder and shareholder components.

Segmental analysis of results and earnings attributable to shareholders

The Group uses operating profit based on longer-term investment returns as the segmental measure of its results. The basis of calculation is disclosed in note A4(d).

For shareholder-backed business, with the exception of debt securities held by Jackson and assets classified as loans and receivables, all financial investments and investment property are designated as assets at fair value through profit and loss. Short-term fluctuations in investment returns on such assets held by with-profits funds, do not affect directly reported shareholder results. This is because (i) the unallocated surplus of with-profits funds is accounted for as liabilities and (ii) excess or deficits of income and expenditure of the funds over the required surplus for distribution are transferred to or from unallocated surplus. However, for shareholder-backed businesses the short-term fluctuations affect the result for the year and the Prudential Group provides additional analysis of results to provide information on results before and after short-term fluctuations in investment returns.

b Critical accounting estimates and judgements

Investments

Determining the fair value of financial investments when the markets are not active

The Prudential Group holds certain financial investments for which the markets are not active. These can include financial investments which are not quoted on active markets and financial investments for which markets are no longer active as a result of market conditions e.g. market illiquidity. When the markets are not active, there is generally no or limited observable market data to account for financial investments at fair value. The determination of whether an active market exists for a financial investment requires management's judgement.

If the market for a financial investment of the Prudential Group is not active, the fair value is determined by using valuation techniques. The Prudential Group establishes fair value for these financial investments by using quotations from independent third-parties, such as brokers or pricing services or by using internally developed pricing models. Priority is given to publicly available prices from independent sources, when available but overall, the source of pricing and/or the valuation technique is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The valuation techniques include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these financial investments.

The financial investments measured at fair value are classified (from 1 January 2009) into the following three level hierarchy on the basis of the lowest level of inputs that is significant to the fair value measurement of the financial investment concerned:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Level 2: Inputs other than quoted prices included within level 1 that are observable either directly or indirectly (i.e. derived from prices).

Level 3: Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At 31 December 2009, £5,557 million of the financial investments (net of derivative liabilities) valued at fair value were classified as level 3. Of these £1,684 million are held to back shareholder non-linked business and so changes to these valuations will directly impact shareholders' equity. Prudential has applied the amendments to IFRS 7 described in note A5 for periods beginning on 1 January 2009. Additional supplementary 2008 disclosures have been prepared in certain instances. Further details of the classification of financial instruments are given in note G1.

Determining impairments relating to financial assets

Available-for-sale securities

Under IAS 39, the Prudential Group has the option on purchase to account for individual financial instruments as available-for-sale. Currently, the only financial investments carried on an available-for-sale basis by the Prudential

Group are represented by Jackson's debt securities portfolio. The consideration of evidence of impairment requires management's judgement. In making this determination the factors considered include, for example,

- Whether the decline of the financial investment's fair value is substantial

A substantial decline in fair value might be indicative of a credit loss event that would lead to a measurable decrease in the estimated future cash flows.

- The impact of the duration of the security on the calculation of the revised estimated cash flows

The duration of a security for maturity helps to inform whether assessments of estimated future cash flows that are higher than market value are reasonable.

- The duration and extent to which the amortised cost exceeds fair value

This factor provides an indication of how the contractual cash flows and effective interest rate of a financial asset compares with the implicit market estimate of cash flows and the risk attaching to a 'fair value' measurement. The length of time for which that level of difference has been in place may also provide further evidence as to whether the market assessment implies an impairment loss has arisen.

- The financial condition and prospects of the issuer or other observable conditions that indicate the investment may be impaired.

If a loss event that will have a detrimental effect on cash flows is identified an impairment loss in the income statement is recognised. The loss recognised is determined as the difference between the book cost and the fair value of the relevant impaired securities. This loss comprises the effect of the expected loss of contractual cash flows and any additional market price driven temporary reductions in values.

For Jackson's residential mortgage-backed and other asset-backed securities, all of which are classified as available-for-sale, the model used to analyse cash flows, begins with the current delinquency experience of the underlying collateral pool for the structure, by applying assumptions about how much of the currently delinquent loans will eventually default, and multiplying this by an assumed loss severity. Additional factors are applied to anticipate ageing effect. After applying a cash flow simulation an indication is obtained as to whether or not the security has suffered, or is anticipated to suffer, contractual principal or interest payment shortfall. If a shortfall applies an impairment charge is recorded.

The difference between the fair value and book cost for unimpaired securities accounted for as available-for-sale falls to be accounted for as unrealised gains or losses, with the movements in the accounting period being accounted for in other comprehensive income.

The Prudential Group's review of fair value involves several criteria, including economic conditions, credit loss experience, other issuer-specific developments and future cash flows. These assessments are based on the best available information at the time. Factors such as market liquidity, the widening of bid/ask spreads and a change in cash flow assumptions can contribute to future price volatility. If actual experience differs negatively from the assumptions and other considerations used in the consolidated financial information, unrealised losses currently in equity may be recognised in the income statement in future periods. The preceding note in this section provides explanation on how fair value is determined when the markets for the financial investments are not active. Further, additional details on the impairments of the available-for-sale securities of Jackson are described in notes D3 and G5.

Assets held at amortised cost

Financial assets classified as loans and receivables under IAS 39 are initially recognised at fair value plus transaction costs. Subsequently they are carried at amortised cost using the effective interest rate method. The loans and receivables include loans collateralised by mortgages, deposits and loans to policyholders. In estimating future cash flows, the Prudential Group looks at the expected cash flows of the assets and applies historical loss experience of assets with similar credit risks that has been adjusted for conditions in the historical loss experience which no longer exist or for conditions that are expected to arise. The estimated future cash flows are discounted using the financial asset's original or variable effective interest rate and exclude credit losses that have not yet been incurred.

The risks inherent in reviewing the impairment of any investment include the risk that market results may differ from expectations; facts and circumstances may change in the future and differ from estimates and assumptions; or the Prudential Group may later decide to sell the asset as a result of changed circumstances.

Insurance contracts

Product classification

IFRS 4 requires contracts written by insurers to be classified as either 'insurance contracts' or 'investment contracts' depending on the level of insurance risk transferred. Insurance risk is a pre-existing risk, other than financial risk, transferred from the contract holder to the contract issuer. If significant insurance risk is transferred by the contract then it is classified as an insurance contract. Contracts that transfer financial risk but not significant insurance risk are termed investment contracts. Furthermore, some contracts, both insurance and investment, contain discretionary participating features representing the contractual right to receive additional benefits as a supplement to guaranteed benefits:

a that are likely to be a significant portion of the total contract benefits;

b whose amount or timing is contractually at the discretion of the insurer; and

c that are contractually based on asset or fund performance, as discussed in IFRS 4.

Accordingly, insurers must perform a product classification exercise across their portfolio of contracts issued to determine the allocation to these various categories. IFRS 4 permits the continued usage of previously applied GAAP for insurance contracts and investment contracts with discretionary participating features. Except for UK regulated with-profits funds, as described subsequently, this basis has been applied by the Prudential Group.

For investment contracts that do not contain discretionary participating features, IAS 39 and, where the contract includes an investment management element, IAS 18, apply measurement principles to assets and liabilities attaching to the contract.

Valuation assumptions

i Contracts of with-profits funds

The Prudential Group's insurance contracts and investment contracts with discretionary participating features are primarily with-profits and other protection type policies. For UK regulated with-profits funds, the contract liabilities are valued by reference to the UK Financial Services Authority's (FSA) realistic basis. In aggregate, this basis has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances.

The basis of determining liabilities for the Prudential Group's with-profits business has little or no effect on the results attributable to shareholders. This is because movements on liabilities of the with-profits funds are absorbed by the unallocated surplus. Except through indirect effects, or in remote circumstances as described below, changes to liability assumptions are therefore reflected in the carrying value of the unallocated surplus, which is accounted for as a liability rather than shareholders' equity.

A detailed explanation of the basis of liability measurement is contained in note D2(f)(ii).

The Prudential Group's other with-profits contracts are written in with-profits funds that operate in some of the Prudential Group's Asian operations. The liabilities for these contracts and those of Prudential Annuities Limited, which is a subsidiary company of the PAC with-profits funds, are determined differently. For these other with-profits contracts applicable to the Prudential Group's activities in 2007, 2008 and 2009 the liabilities are estimated using actuarial methods based on assumptions relating to premiums, interest rates, investment returns, expenses, mortality and surrenders. The assumptions to which the estimation of these reserves is particularly sensitive are the interest rate used to discount the provision and the assumed future mortality experience of policyholders.

For liabilities determined using the basis described above for UK regulated with-profits funds, and the other liabilities described in the preceding paragraph, changes in estimates arising from the likely range of possible changes in underlying key assumptions have no direct impact on the reported profit.

This lack of sensitivity reflects the with-profits fund structure, basis of distribution, and the application of previous GAAP to the unallocated surplus of with-profits funds as permitted by IFRS 4. Changes in liabilities of these contracts that are caused by altered estimates are absorbed by the unallocated surplus of the with-profits funds with no direct effect on shareholders' equity. The Prudential Group's obligations and more detail on such circumstances are described in note H14.

ii Other contracts

Contracts, other than those of with-profits funds, are written in shareholder-backed operations of the Prudential Group. The significant shareholder-backed product groupings and the factors that may significantly affect IFRS results due to experience against assumptions or changes of assumptions vary significantly between business units. For some types of business the effect of changes in assumptions may be significant, whilst for others, due to the nature of the product, assumption setting may be of less significance. The nature of the products and the significance of assumptions are discussed in notes D2, D3 and D4. From the perspective of shareholder results the key sensitivity relates to the assumption for allowance for credit risk for UK annuity business. Prior to its disposal of the Taiwan agency business in the first half of 2009, the Prudential Group's financial results were also sensitive to the assumed future investment returns for that business.

Jackson

Jackson offers individual fixed annuities, fixed index annuities, immediate annuities, variable annuities, individual and variable life insurance and institutional products. With the exception of institutional products and an incidental amount of business for annuity, certain contracts which are accounted for as investment contracts under IAS 39, all of Jackson's contracts are accounted for under IFRS 4 as insurance contracts by applying US GAAP, the previous GAAP used before IFRS adoption. Under US GAAP the requirements of SFAS 60 'Accounting and Reporting for Insurance Enterprises' and SFAS 97 'Accounting and Reporting by Insurance Enterprises for certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments' apply to these contracts. The accounting requirements under these standards and the effect of changes in valuation assumptions are considered below for fixed annuity, variable annuity and traditional life insurance contracts.

Fixed annuity contracts, which are investment contracts under US GAAP terminology, are accounted for by applying in the first instance a retrospective deposit method to determine the liability for policyholder benefits. This is then augmented by potentially three additional amounts, namely deferred income, any amounts previously assessed against policyholders that are refundable on termination of the contract, and any premium deficiency, i.e., any probable future loss on the contract. These types of contract contain considerable interest rate guarantee features. Notwithstanding the accompanying market risk exposure, except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of Jackson's fixed annuity products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement.

Variable annuity contracts written by Jackson may provide for guaranteed minimum death, income, or withdrawal benefit features. In general terms, liabilities for these benefits are accounted for under US GAAP by using estimates of future benefits and fees under best estimate assumptions. For variable annuity business the key assumption is the expected long-term level of equity market returns, which for 2007, 2008 and 2009 was 8.4 % per annum (gross of fund management fees) determined using a mean reversion methodology. Under the mean reversion methodology, projected returns over the next five years are flexed (subject to capping) so that, combined with the actual rates of return for the current and the previous two years the 8.4 % rate is maintained. The projected rates of return are capped at no more than 15 % for each of the next five years. Further details are explained in note D3(h).

These returns affect the level of future expected profits through their effects on the fee income with consequential impact on the amortisation of deferred acquisition costs as described below and the required level of provision for guaranteed minimum death benefit claims.

For traditional life insurance contracts, provisions for future policy benefits are determined using the net level premium method and assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviation.

Except to the extent of mortality experience, which primarily affects profits through variations in claim payments and the guaranteed minimum death benefit reserves, the profits of Jackson are relatively insensitive to changes in insurance risk. This reflects the principally spread and fee-based nature of Jackson's business.

Asian operations

The insurance products written in the Prudential Group's Asian operations principally cover with-profits business, unit-linked business, and other non-participating business. The results of with-profits business are relatively insensitive to changes in estimates and assumptions that affect the measurement of policyholder liabilities. As for the UK business, this feature arises because unallocated surplus is accounted for by the Prudential Group as a liability. The results of Asian unit-linked business are also relatively insensitive to changes in estimates or assumptions.

Prior to its disposal in the first half of 2009, the principal non-participating business in the Prudential Group's Asian operations, for which changes in estimates and assumptions was important from year to year, was the traditional whole-life business written in Taiwan. Premium rates were set to give a guaranteed minimum sum assured on death and a guaranteed surrender value on early surrender based on prevailing interest rates at the time of policy issue. Premium rates also included an allowance for mortality and expenses. This business was therefore especially sensitive to falling interest rates. This exposure has been removed following the disposal of the Taiwan agency business. The remaining non-participating business in Asia remains sensitive to interest rates but this sensitivity is of a much lower order. Further details are provided in note D4(i).

Deferred acquisition costs

Significant costs are incurred in connection with acquiring new insurance business. Except for acquisition costs of with-profits contracts of the UK regulated with-profits funds, which are accounted for under the realistic FSA regime as described in note A4, these costs, which vary with, and are primarily related to, the production of new business, are capitalised and amortised against margins in future revenues on the related insurance policies. The recoverability of the asset is measured and the asset is deemed impaired if the projected future margins are less than the carrying value of the asset. To the extent that the future margins differ from those anticipated, then an adjustment to the carrying value of the deferred acquisition cost asset will be necessary.

The deferral and amortisation of acquisition costs is of most relevance to the Prudential Group's results for shareholder-financed long-term business of Jackson and Asian operations. The majority of the UK shareholder-backed business is for individual and group annuity business where the incidence of acquisition costs is negligible.

Jackson

For term business, acquisition costs are deferred and amortised in line with expected premiums. For annuity business, acquisition costs are deferred and amortised in line with expected gross profits on the relevant contracts. For interest-sensitive business, the key assumption is the long-term spread between the earned rate and the rate credited to policyholders, which is based on the annual spread analysis. In addition, expected gross profits depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges), all of which are based on a combination of Jackson's actual industry experience and future expectations. A detailed analysis of actual experience is measured by internally developed mortality studies.

For variable annuity business, the key assumption is the expected long-term level of equity market returns as described above.

The level of acquisition costs carried in the statement of financial position is also sensitive to unrealised valuation movements on debt securities held to back the liabilities and solvency capital. Further details are explained in notes D3(h) and H1.

Asian operations

In 2008, a number of changes were made to the basis of estimating the level of deferred acquisition costs, as described in note D4(h)(c).

Pensions

The Prudential Group applies the requirements of IAS 19, 'Employee benefits' and associated interpretations including IFRIC 14 IAS 19 — The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction', to its defined benefit pension schemes. The principal defined benefit pension scheme is the Prudential Staff Pension Scheme ("PSPS"). For PSPS the terms of the trust deed restrict shareholders' access to any underlying surplus. Accordingly, applying the interpretation of IFRIC 14, any underlying IAS 19 basis surplus is not recognised for IFRS reporting. The financial position for PSPS recorded in the IFRS financial statements reflects the higher of any underlying IAS 19 deficit and any obligation for deficit funding.

The economic participation in the surplus or deficits attaching to PSPS and the smaller Scottish Amicable Pensions Scheme (SAPS) are shared between the PAC with-profits sub-fund ("WPSF") and shareholder operations. The economic interest reflects the source of contributions over the scheme life, which in turn reflects the activity of the members during their employment.

In the case of PSPS, movements in the apportionment of the financial position for PSPS between the WPSF and shareholders' funds in 2009 reflect the 70/30 ratio applied to the base deficit position as at 31 December 2005 but with service cost and contributions for ongoing service apportioned by reference to the cost allocation for activity of current employees. For SAPS the ratio is estimated to be 50/50 between the WPSF and shareholders' funds.

Due to the inclusion of actuarial gains and losses in the income statement rather than being recognised in other comprehensive income, the results of the Prudential Group are affected by changes in interest rates for corporate bonds that affect the rate applied to discount projected pension payments, changes in mortality assumptions and changes in inflation assumptions.

Deferred tax

Deferred tax assets are recognised to the extent that they are regarded as recoverable, that is to the extent that, on the basis of all the available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which the losses can be relieved. The taxation regimes applicable across the Prudential Group apply 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 judgements made, and uncertainties considered, in arriving at deferred tax balances in the financial information are discussed in note H4.

Goodwill

Goodwill impairment testing requires the exercise of judgement by management as to prospective future cash flows. Further information is disclosed in note H1.

A4: Significant accounting policies

a Financial instruments other than financial instruments classified as long-term business contracts

Investment classification

Under IAS 39, subject to specific criteria, financial instruments should be accounted for under one of the following categories; financial investments at fair value through profit and loss, financial investments held on an available-for-sale basis, financial investments held-to-maturity or loans and receivables. Upon initial recognition, financial investments are measured at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. These IAS 39 classifications have been changed by IFRS 9 "Financial Investments: Classification and Measurement" which is not required to be adopted until 2013 and is still subject to EU endorsement. This standard has not been adopted by the Prudential Group in 2009. The Prudential Group holds financial investments on the following bases:

i Financial assets and liabilities at fair value through profit and loss — this comprises assets and liabilities designated by management as fair value through profit and loss on inception and derivatives that are held for trading. These investments are measured at fair value with all changes thereon being recognised in investment income.

ii Financial investments on an available-for-sale basis — this comprises assets that are designated by management and/or do not fall into any of the other categories. Available-for-sale financial assets are initially recognised at fair value plus attributable transaction costs. For available-for-sale debt securities, the difference between their cost and par value is amortised to the income statement using the effective interest rate. Available-for-sale financial assets are subsequently measured at fair value. Interest income is recognised on an effective interest basis in the income statement. Except for foreign exchange gains and losses on debt securities, not in functional currency, which are included in the income statement, unrealised gains and losses are recognised in other comprehensive income (i.e. outside of the income statement). Upon disposal or impairment, accumulated unrealised gains and losses are transferred from other comprehensive income to the income statement as realised gains or losses.

iii Loans and receivables — this comprises non-quoted investments that have fixed or determinable payments and are not designated as fair value through profit and loss or available-for-sale. These investments include loans collateralised by mortgages, deposits, loans to policyholders and other unsecured loans and receivables. These investments are initially recognised at fair value plus transaction costs. Subsequently they are carried at amortised cost using the effective interest method.

As permitted under IAS 39, the Prudential Group has designated certain financial assets as fair value through profit and loss as these assets are managed and their performance is evaluated on a fair value basis. Currently, these assets represent all of the Prudential Group's financial assets except all loans and receivables and debt securities held by Jackson. Debt securities held by Jackson are accounted for on an available-for-sale basis. The use of the fair value option is consistent with the Prudential Group's risk management and investment strategies.

The Prudential Group uses the trade date method to account for regular purchases and sales of financial assets.

Use of fair values

The Prudential Group uses current bid prices to value its investments with quoted prices. Actively traded investments without quoted prices are valued using prices provided by third parties. If there is no active established market for an investment, the Prudential Group applies an appropriate valuation technique such as a discounted cash flow technique. Additional details are provided in note G1.

Impairments

The Prudential Group assesses at each statement of financial position date whether there is objective evidence that a financial asset or group of financial assets not held at fair value through profit and loss is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (a loss event) and that a loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of financial assets is impaired includes observable data that comes to the attention of the Prudential Group. For assets designated as available-for-sale, the initial impairment is the cumulative loss which is removed from the available-for-sale reserve within equity and recognised in the income statement. Any subsequent impairment loss is measured as the cumulative loss, less any impairment loss previously recognised.

For loans and receivables carried at amortised cost, the impairment amount is the difference between carrying value and the present value of the expected cash flows discounted at the original effective interest rate.

If, in subsequent periods, an impaired debt security held on an available-for-sale basis or an impaired loan or receivable recovers in value (in part or in full), and this recovery can be objectively related to an event occurring after the impairment, then the previously recognised impairment loss is reversed through the income statement (in part or in full).

Derivatives and hedge accounting

Derivative financial instruments are used to reduce or manage investment, interest rate and currency exposures, to facilitate efficient portfolio management and for investment purposes.

The Prudential Group may designate certain derivatives as hedges. This includes fair value hedges, cash flow hedges and hedges of net investments in foreign operations. If the criteria for hedge accounting are met then the following accounting treatments are applied from the date at which the designation is made and the accompanying requisite documentation is in place:

i Hedges of net investments in foreign operations — the effective portion of any change in fair value of derivatives or other financial instruments designated as net investment hedges are recognised in other comprehensive income (i.e. outside of the income statement). The ineffective portion of changes in the fair value of the hedging instrument is recorded in the income statement. The gain or loss on the hedging instrument recognised directly in the Statement of comprehensive income is recognised in the income statement on disposal of the foreign operation.

ii Fair value hedges — movements in the fair value of the hedged item attributable to the hedged risk are recognised in the income statement.

iii Cash flow hedges — the effective portion of changes in the fair value of derivatives designated as cash flow hedges is recognised in other comprehensive income (i.e. outside of the income statement). Movements in fair value relating to the ineffective portion are booked in the income statement. Amounts recognised in other comprehensive income are recorded in the income statement in the periods in which the hedged item affects profit or loss.

All derivatives that do not meet the relevant hedging criteria are carried at fair value with movements in fair value being recorded in the income statement.

The primary areas of the Prudential Group's continuing operations where derivative instruments are held are the UK with-profits funds and annuity business, and Jackson.

For the Prudential Group's continuing operations, hedge accounting under IAS 39 is not usually applied. The exceptions, where hedge accounting has been applied in 2007, 2008 and 2009, are summarised in note G3.

For UK with-profits funds the derivative programme is undertaken as part of the efficient management of the portfolio as a whole. As noted in section D2 value movements on the with-profits funds investments are reflected in changes in asset-share liabilities to policyholders or the liability for unallocated surplus. Shareholders' profit and equity are not affected directly by value movements on the derivatives held.

For UK annuity business the derivatives are held to contribute to the matching, as far as practical, of asset returns and duration with those of liabilities to policyholders. The carrying value of these liabilities is sensitive to the return on the matching financial assets including derivatives held. Except for the extent of minor mismatching, value movements on derivatives held for this purpose do not affect shareholders' profit or equity.

For Jackson an extensive derivative programme is maintained. Value movements on the derivatives held can be very significant in their effect on shareholder results. The Prudential Group has chosen generally not to seek to construct the Jackson derivative programme so as to facilitate hedge accounting where theoretically possible, under IAS 39. Further details on this aspect of the Prudential Group's financial reporting are described in note A3.

Embedded derivatives

Embedded derivatives are present in host contracts issued by various Prudential Group companies, in particular for Jackson. They are embedded within other non-derivative host financial instruments and insurance contracts to create hybrid instruments. Where economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value with the changes in fair value recognised in the income statement, the embedded derivative is bifurcated and carried at fair value as a derivative in accordance with IAS 39. In addition, the Prudential Group applies the requirement of IFRS 4 to not separate and fair value surrender options embedded in host contracts and with-profit investment contracts whose strike price is either a fixed amount or a fixed amount plus interest.

Further details on the valuation basis for embedded derivatives attaching to Jackson's life assurance contracts are provided in note D3(f).

Securities lending including repurchase agreements

The Prudential Group is party to various securities lending agreements under which securities are loaned to third-parties on a short-term basis. The loaned securities are not derecognised; rather, they continue to be recognised within the appropriate investment classification. An operational policy of the Prudential Group is that collateral in excess of 100% of the fair value of securities loaned is required from all securities' borrowers and typically consists of cash, debt securities, equity securities or letters of credit.

In cases where the Prudential Group takes possession of the collateral under its securities lending programme, the collateral, and corresponding obligation to return such collateral, are recognised in the consolidated statement of financial position.

Derecognition of financial assets and liabilities

The Prudential Group's policy is to derecognise financial assets when it is deemed that substantially all the risks and rewards of ownership have been transferred. The Prudential Group also derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire. Where the Prudential Group neither transfers nor retains substantially all the risks and rewards of ownership, the Prudential Group will derecognise the financial asset where it is deemed that the Prudential Group has not retained control of the financial asset.

Where the transfer does not result in the Prudential Group transferring the right to receive the cash flows of the financial assets, but does result in the Prudential Group assuming a corresponding obligation to pay the cash flows to another recipient, the financial assets are also accordingly derecognised providing all of the following conditions are met:

- the Prudential Group has no obligation to pay amounts to the eventual recipients unless it collects the equivalent amounts from the original asset;
- the Prudential Group is prohibited by the terms of the transfer contract from selling or pledging the original asset; and
- the Prudential Group has an obligation to remit any cash flows it collects on behalf of the eventual recipients without material delay.

The Prudential Group derecognises financial liabilities only when the obligation specified in the contract is discharged, cancelled or has expired.

Borrowings

Although initially recognised at fair value, net of transaction costs, borrowings, excluding liabilities of consolidated collateralised debt obligations, are subsequently accounted for on an amortised cost basis using the effective interest method. Under the effective interest method, the difference between the redemption value of the borrowing and the initial proceeds (net of related issue costs) is amortised through the income statement to the date of maturity or, for hybrid debt, over the expected life of the instrument.

Financial liabilities designated at fair value through profit and loss

Consistent with the Prudential Group's risk management and investment strategy and the nature of the products concerned, the Group has designated under IAS 39 classification certain financial liabilities at fair value through profit and loss as these instruments are managed and their performance evaluated on a fair value basis. These instruments include liabilities related to consolidated collateralised debt obligations and net assets attributable to unit holders of consolidated unit trusts and similar funds.

b Long-term business contracts

Income statement treatment

Premiums and claims

As noted previously, subject to certain conditions, IFRS 4 permits the continued usage of previously applied GAAP for measurements of assets and liabilities of insurance contracts and investment contracts with discretionary participating features. This permission also applies to the basis of presentation of premiums and benefits and claims. It is therefore possible under this "grandfathering" for diverse treatments of these items to apply in the income statement. This diversity can include a treatment whereby all premiums, benefits and claims are recorded in the income statement. Alternatively, for life assurance products with investment features, but with sufficient risk to be accounted for as insurance contracts under IFRS 4, premiums and claims may be accounted for as movements on deposits within the liability to policyholders in the statement of financial position. Prudential's current policy is to "grandfather" the treatment previously applied before conversion to IFRS or acquisition of an operation.

Premium and annuity considerations for conventional with-profits policies and other protection type insurance policies are recognised as revenue when due. Premiums and annuity considerations for linked policies, unitised with-profits and other investment type policies are recognised as revenue when received or, in the case of unitised or unit-linked policies, when units are issued. These amounts exclude UK premium taxes and similar duties where the company collects and settles taxes borne by the customer.

Policy fees charged on linked and unitised with-profits policies for mortality, asset management and policy administration are recognised as revenue when related services are provided.

Claims paid include maturities, annuities, surrenders and deaths. Maturity claims are recorded as charges on the policy maturity date. Annuity claims are recorded as charges when each annuity instalment becomes due for payment. Surrenders are charged to the income statement when paid and death claims are recorded when notified.

For investment contracts which do not contain discretionary participating features, the accounting is done under IAS 39 to reflect the deposit nature of the arrangement, with premiums and claims reflected as deposits and withdrawals and taken directly to the statement of financial position as movements in the financial liability balance.

Acquisition costs

With the exception of costs incurred in respect of with-profit contracts valued on a realistic basis, costs of acquiring new insurance business, principally commissions, marketing and advertising costs and certain other costs associated with policy issuance and underwriting that are not reimbursed by policy charges, are specifically identified and capitalised as part of deferred acquisition costs (DAC), which are included as an asset in the statement of financial position. The DAC asset in respect of insurance contracts is amortised against margins in future revenues on the related insurance policies, to the extent that the amounts are recoverable out of the margins. Recoverability of the unamortised DAC asset is assessed at the time of policy issue and reviewed if profit margins have declined.

Under IFRS, investment contracts (excluding those with discretionary participation features) accounted for as financial liabilities in accordance with IAS 39 which also offers investment management services, require the application of IAS 18 for the revenue attached to these services. The Prudential Group's investment contracts primarily comprise certain unit-linked savings contracts in the UK and Asia and contracts with fixed and guaranteed terms in the US (such as guaranteed investment contracts and annuity-certain) all of which offer an investment service.

Incremental, directly attributable acquisition costs relating to the investment management element of these contracts are capitalised and amortised in line with the related revenue. If the contracts involve up-front charges, this income is also deferred and amortised through the income statement in line with contractual service provision.

UK regulated with-profits funds

Prudential's long-term business written in the UK comprises predominantly life insurance policies with discretionary participating features under which the policyholders are entitled to participate in the returns of the funds supporting these policies. Business similar to this type is also written in certain of the Prudential Group's Asian operations subject to local market and regulatory conditions. Such policies are called with-profits policies. Prudential maintains with-profits funds within the Prudential Group's long-term business funds, which segregate the assets and liabilities and accumulate the returns related to that with-profits business. The amounts accumulated in these with-profits funds are available to provide for future policyholder benefit provisions and for bonuses to be distributed to with-profits policyholders. The bonuses, both annual and final, reflect the right of the with-profits policyholders to participate in the financial performance of the with-profits funds. Shareholders' profits with respect to bonuses declared on with-profits business correspond to the shareholders' share of the cost of bonuses as declared by the board of directors. The shareholders' share currently represents one-ninth of the cost of bonuses declared for with-profits policies.

Annual bonuses are declared and credited each year to with-profits policies. The annual bonuses increase policy benefits and, once credited, become guaranteed. Annual bonuses are charged to the profit and loss account in the year declared. Final bonuses are declared each year and accrued for all policies scheduled to mature and for death benefits expected to be paid during the next financial year. Final bonuses are not guaranteed and are only paid on policies that result from claims through the death of the policyholder or maturity of the policy within the period of declaration or by concession on surrender. No policyholder benefit provisions are recorded for future annual or final bonus declarations.

The policyholders' liabilities of the UK regulated with-profits funds are accounted for under FRS 27.

Under FRS 27 for the UK regulated with-profits funds:

- no deferred acquisition costs and related deferred tax are recognised; and
- adjusted realistic basis liabilities instead of MSB liabilities are recognised.

FRS 27 realistic liabilities are underpinned by the FSA's Peak 2 basis of reporting. This Peak 2 basis requires the value of liabilities to be calculated as:

- a with-profits benefits reserve (WPBR); plus
- future policy related liabilities (FPRL); plus
- the realistic current liabilities of the fund.

The WPBR is primarily based on the retrospective calculation of accumulated asset shares but is adjusted to reflect future policyholder benefits and other outgoings.

The FPRL must include a market consistent valuation of costs of guarantees, options and smoothing, less any related charges, and this amount is determined using either a stochastic approach, hedging costs or a series of deterministic projections with attributed probabilities.

The assumptions used in the stochastic models are calibrated to produce risk-free returns on each asset class. Volatilities of, and correlations between, investment returns from different asset classes are as determined by the Prudential Group's Portfolio Management Group on a market consistent basis.

The cost of guarantees, options and smoothing is very sensitive to the bonus, market value reduction ("MVR") and investment policies the Prudential Group employs and therefore the stochastic modelling incorporates a range of management actions that would help to protect the fund in adverse scenarios. Substantial flexibility has been included in the modelled management actions in order to reflect the discretion that the Prudential Group retains in adverse investment conditions, thereby avoiding the creation of unreasonable minimum capital requirements. The management actions assumed are consistent with management's policy for with-profits funds and the disclosures made in the publicly available Principles and Practices of Financial Management.

The realistic basis liabilities representing the Peak 2 basis realistic liabilities for with-profits business included in Form 19 of the FSA regulatory returns, exclude the element for the shareholders' share of the future bonuses. For accounting under FRS 27, this latter item is reversed because, consistent with the current basis of financial reporting, shareholder transfers are recognised only on declaration.

Unallocated surplus

The unallocated surplus represents the excess of assets over policyholder liabilities for the Prudential Group's with-profits funds. As allowed under IFRS 4, the Prudential Group has opted to continue to record unallocated surplus of with-profits funds wholly as a liability. The annual excess (shortfall) of income over expenditure of the with-profits funds, after declaration and attribution of the cost of bonuses to policyholders and shareholders, is transferred to (from) the unallocated surplus each year through a charge (credit) to the income statement. The balance retained in the unallocated surplus represents cumulative income arising on the with-profits business that has not been allocated to policyholders or shareholders. The balance of the unallocated surplus is determined after full provision for deferred tax on unrealised appreciation on investments.

Other insurance contracts (i.e. contracts which contain significant insurance risk as defined under IFRS 4)

For these contracts UK GAAP has been applied, which reflects the MSB. Under this basis the following approach applies:

Other UK insurance contracts

Other UK insurance contracts that contain significant insurance risk include unit-linked, annuity and other non-profit business. For the purposes of local regulations, segregated accounts are established for linked business for which policyholder benefits are wholly or partly determined by reference to specific investments or to an investment-related index. The interest rates used in establishing policyholder benefit provisions for pension annuities in the course of payment are adjusted each year. Mortality rates used in establishing policyholder benefit provisions were based on published mortality tables adjusted to reflect actual experience.

Overseas subsidiaries

For the Prudential Group's overseas operations, the application of the MSB (which permits the application of local GAAP in some circumstances) varies depending upon the basis of accounting applied prior to IFRS adoption or acquisition by the Prudential Group, and whether adjustments to the basis or a more appropriate method should be applied.

Jackson

The future policyholder benefit provisions for Jackson's conventional protection-type policies are determined using the net level premium method under US GAAP principles and assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviations. For non-conventional protection-type policies, the policyholder benefit provision included within policyholder liabilities in the consolidated statement of financial position is the policyholder account balance.

For the business of Jackson, the determination of the expected emergence of margins, against which the amortisation profile of the DAC asset is established, is dependent on certain key assumptions. For single premium deferred annuity business, the key assumption is the expected long-term spread between the earned rate and the rate credited to policyholders. For variable annuity business, the key assumption is the expected long-term level of equity market returns which, for 2007, 2008 and 2009, was 8.4% per annum implemented using a mean reversion methodology. These returns affect the level of future expected profits through their effects on fee income and the required level of provision for guaranteed minimum death benefit claims.

Jackson accounts for the majority of its investment portfolio on an available-for-sale basis (see investment policies above) whereby unrealised gains and losses are recognised in other comprehensive income. As permitted by IFRS 4, Jackson has used shadow accounting. Under shadow accounting, to the extent that recognition of unrealised gains or losses on available-for-sale securities causes adjustments to the carrying value and amortisation patterns of DAC and deferred income, these adjustments are recognised in other comprehensive income to be consistent with the treatment of the gains or losses on the securities.

Asian operations

Consistent with the overarching provisions of IFRS 4 which, as described in note A3(a), permits the accounting for assets and liabilities of insurance contracts and investment contracts with discretionary participating features under previously applied GAAP except for the Prudential Group's current operations in Taiwan, Vietnam and Japan, the future policyholder benefit provisions for the Prudential Group's current Asian businesses in 2007, 2008 and 2009 are determined in accordance with methods prescribed by local GAAP adjusted to comply, where necessary, with UK GAAP. For the Hong Kong business, which is a branch of the PAC, and the Singapore and Malaysian operations the valuation principles and sensitivities to changes of assumptions of conventional with-profits and other protection-type policies are similar to those described above for equivalent products written by the UK operations. Refinements to the local reserving methodology are generally treated as change in estimates, dependent on the nature of the change. Such a refinement arose in 2009 in respect of Malaysia as explained in note D4(h)

For the operations in Taiwan, Vietnam and Japan, countries where local GAAP is not appropriate in the context of the previously applied MSB, accounting for insurance contracts is based on US GAAP. For these three operations the business written is primarily non-participating and linked business. The future policyholder benefit provisions for non-linked business are determined using the net level premium method, with an allowance for surrenders, maintenance and claim expenses. Rates of interest used in establishing the policyholder benefit provisions vary by operation depending on the circumstances attaching to each block of business. Where appropriate, liabilities for participating business for these three operations include provisions for the policyholders' interest in realised investment gains and other surpluses that have yet to be declared as bonuses.

Although the basis of valuation of the Prudential Group's overseas operations is in accordance with the requirements of the Companies Act 2006 and ABI SORP, the valuation of policyholder benefit provisions for these businesses may differ from that determined on a UK MSB for UK operations with the same features. These differences are permitted under IFRS 4.

Liability adequacy

The Prudential Group performs liability adequacy testing on its insurance provisions to ensure that the carrying amounts of provisions (less related DAC and present value of in-force business — see policy on business acquisitions and disposals) is sufficient to cover current estimates of future cash flows. When performing the liability adequacy test, the Group discounts all contractual cash flows and compares this amount to the carrying value of the liability. Any deficiency is immediately charged to the income statement.

Reinsurance

In the normal course of business, the Prudential Group seeks to reduce loss exposure by reinsuring certain levels of risk in various areas of exposure with other insurance companies or reinsurers. An asset or liability is recognised in the consolidated statement of financial position representing premiums due to or payments due from reinsurers and the share of benefits and claims recoverable from reinsurers. The measurement of reinsurance assets is consistent with the measurement of the underlying direct insurance contracts.

The only material purchases of reinsurance contracts in the periods of the results in the financial information arise in Jackson. Gains arising on the purchase of reinsurance contracts by Jackson are deferred and amortised over the contract duration.

Any loss is recognised in the income statement immediately.

Investment contracts (contracts which do not contain significant insurance risk as defined under IFRS 4)

For investment contracts with discretionary participation features, the accounting basis is consistent with the accounting for similar with-profits insurance contracts. Other investment contracts are accounted for on a basis that reflects the hybrid nature of the arrangements whereby part is accounted for as a financial instrument under IAS 39 and the investment management service component is accounted for under IAS 18. The method used to measure the liability for these investment contracts depends upon the terms of the contracts and will therefore vary by the type of product.

For certain investment contracts with fixed and guaranteed terms, the Prudential Group uses the amortised cost model to measure the liability. On contract inception, the liability is measured at fair value less incremental, directly attributable acquisition costs. Remeasurement at future reporting dates is on an amortised cost basis utilising an effective interest rate methodology whereby the interest rate utilised discounts to the net carrying amount of the financial liability.

Those investment contracts without fixed and guaranteed terms are designated at fair value through profit and loss. because the resulting liabilities are managed and their performance is evaluated on a fair value basis. Fair value is based upon the fair value of the underlying assets of the fund. Where the contract includes a surrender option its carrying value is subject to a minimum carrying value equal to its surrender value.

c Other assets, liabilities, income and expenditure

Basis of consolidation

The Prudential Group consolidates those entities it is deemed to control. The degree of control is determined by the ability of the Prudential Group to govern the financial and operating policies of an entity in order to obtain benefits. Consideration is given to other factors such as potential voting rights.

The Prudential Group has consolidated special purpose entities (SPEs), such as funds holding collateralised debt obligations (CDOs), where; evaluation of the substance of the relationship between the SPE and the Prudential Group indicates that the Prudential Group is deemed to control the SPE under IFRS.

The Prudential Group holds investments in internally and externally managed open-ended investment companies (OEICs) and unit trusts. These are consolidated where the Group's ownership level is 50% or greater. The Prudential Group's percentage ownership levels in these entities can fluctuate from day to day according to changes in the Prudential Group's and third-party participation in the funds. In instances where the Prudential Group's ownership of internally managed funds declines marginally below 50% and, based on historical analysis and future expectations the decline in ownership is expected to be temporary, the funds continue to be consolidated as subsidiaries under IAS 27.

Where the Prudential Group exercises significant influence or has the power to exercise significant influence over an entity, generally through ownership of 20% or more of the entity's voting rights, but does not control the entity, then this is considered to be an investment in an associate. With the exception of those referred to below, the Prudential Group's investments in associates are recorded at the Prudential Group's share of the associates' net assets. The carrying value of investments in associates is adjusted each year for the Prudential Group's share of the entities' profit or loss. This does not apply to investments in associates held by the Prudential Group's insurance or investment funds including the venture capital business or mutual funds and unit trusts, which, as permitted by IAS 28, are carried at fair value through profit and loss.

The Prudential Group's investments in joint ventures are recognised using proportional consolidation whereby the Prudential Group's share of an entity's individual balances are combined line-by-line with similar items into the Prudential Group financial information.

Other interests in entities, where significant influence is not exercised, are carried as investments at fair value through profit and loss.

The consolidated financial information of the Prudential Group includes the assets, liabilities and results of Prudential and subsidiary undertakings in which Prudential has a controlling interest, using accounts drawn up to 31 December 2007, 31 December 2008 and 31 December 2009 respectively, except where entities have non-coterminous year ends. In such cases, the information consolidated is based on the accounting period of these entities and is adjusted for material changes up to 31 December. Accordingly, the information consolidated is deemed to cover the same period for all entities throughout the Prudential Group. The results of subsidiaries are included in the financial information from the date control commences to the date control ceases. All inter-company transactions are eliminated on consolidation. Results of asset management activities include those for managing internal funds.

Investment properties

Investments in leasehold and freehold properties not for occupation by the Prudential Group including from 2009 (See note A5 for further details) properties under development for future use as investment properties, are carried at fair value, with changes in fair value included in the income statement. Properties are valued annually either by the

Prudential Group's qualified surveyors or by taking into consideration the advice of professional external valuers. In the UK the valuations are undertaken using the guidelines of the Royal Institution of Chartered Surveyors (RICS). The RICS guidelines apply separate assumptions to the value of the land, buildings and tenancy associated with each property. Each property is externally valued at least once every three years. For overseas operations investment property valuations are obtained from qualified valuers. The cost of additions and renovations is capitalised and considered when estimating fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific property. If this information is not available, the Prudential Group uses alternative valuation methods such as discounted cash flow projections or recent prices in less active markets.

Leases of investment property where the Prudential Group has substantially all the risks and rewards of ownership are classified as finance leases (leasehold property). Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. Where a lease has a contingent rent element, the rent is calculated in accordance with individual lease terms and charged as an expense as incurred.

Pension schemes

The Prudential Group operates a number of pension schemes around the world. The largest of these schemes is the PSPS, a defined benefit scheme. The Prudential Group also operates defined contribution schemes. Defined contribution schemes are schemes where the Prudential Group pays contributions into a fund and the Prudential Group has no legal or constructive obligation to pay further contributions should the assets of that fund be insufficient to pay the employee benefits relating to employee service in both current and prior periods. Defined benefit schemes are post-employment benefit plans that are not defined contribution schemes.

For the Prudential Group's defined benefit schemes, if the present value of the defined benefit obligation exceeds the fair value of the scheme assets, then a liability is recorded in the Prudential Group's statement of financial position. By contrast, if the fair value of the assets exceeds the present value of the defined benefit obligation then the surplus will only be recognised if the nature of the arrangements under the Trust deed, and funding arrangements between the Trustee and Prudential support the availability of refunds or recoverability through agreed reductions in future contributions. In addition, if there is a constructive obligation for the Prudential Group to pay deficit funding, this is also recognised.

The Prudential Group utilises the projected unit credit method to calculate the defined benefit obligation. Estimated future cash flows are then discounted at a high-quality corporate bond rate, adjusted to allow for the difference in duration between the bond index and the pension liabilities where appropriate, to determine its present value. These calculations are performed by independent actuaries.

The plan assets of the Prudential Group's pension schemes exclude several insurance contracts that have been issued by the Prudential Group. These assets are excluded from plan assets in determining the pension obligation recognised in the consolidated statement of financial position.

The aggregate of the actuarially determined service costs of the currently employed personnel and the unwind of discount on liabilities at the start of the period, less the expected investment return on scheme assets at the start of the period, is charged to the income statement. Actuarial gains and losses as a result of changes in assumptions or experience variances are also charged or credited to the income statement.

Contributions to the Prudential Group's defined contribution schemes are expensed when due. Once paid, the Prudential Group has no further payment obligations. Any prepayments are reflected as an asset on the statement of financial position.

Share-based payments

The Prudential Group offers share award and option plans for certain key employees and a Save As You Earn (SAYE) plan for all UK and certain overseas employees. The arrangements for distribution to employees of shares held in trust relating to share award plans and for entitlement to dividends depend upon the particular terms of each plan. Shares held in trust relating to these plans are conditionally gifted to employees.

The compensation expense charged to the income statement is primarily based upon the fair value of the options granted, the vesting period and the vesting conditions. Vesting conditions exclude the ability of an employee to voluntarily exit a scheme and such exits are treated as an acceleration of vesting and hence a shortening of the period over which the expense is charged. The Prudential Group revises its estimate of the number of options likely to be exercised at each statement of financial position date and adjusts the charge to the income statement accordingly. Where the share-based payment depends upon vesting outcomes attaching to market-based performance conditions, additional modelling is performed to estimate the fair value of the awards. No subsequent adjustment is then made to the fair value charge for awards that do not vest on account of these performance conditions not being met.

Prudential has established trusts to facilitate the delivery of Prudential Shares under employee incentive plans and savings-related share option schemes. None of the trusts that hold shares for employee incentive and savings plans continue to hold these shares once they are issued to employees. The cost to Prudential of acquiring these treasury shares held in trusts is shown as a deduction from shareholders' equity.

Tax

The Prudential Group's UK subsidiaries each file separate tax returns. Jackson and other foreign subsidiaries, where permitted, file consolidated income tax returns. In accordance with UK tax legislation, where one domestic UK company is a 75% owned subsidiary of another UK company or both are 75% owned subsidiaries of a common parent, the companies are considered to be within the same UK tax group. For companies within the same tax group, trading profits and losses arising in the same accounting period may be offset for purposes of determining current and deferred taxes.

Current tax expense is charged or credited to operations based upon amounts estimated to be payable or recoverable as a result of taxable operations for the current year. To the extent that losses of an individual UK company are not offset in any one year, they can be carried back for one year or carried forward indefinitely to be offset against profits arising from the same company.

Deferred taxes are provided under the liability method for all relevant temporary differences, being the difference between the carrying amount of an asset or liability in the statement of financial position and its value for tax purposes. IAS 12, 'Income Taxes' does not require all temporary differences to be provided for, in particular, the Group does not provide for deferred tax on undistributed earnings of subsidiaries where the Prudential Group is able to control the timing of the distribution and the temporary difference created is not expected to reverse in the foreseeable future. The tax effects of losses available for carry forward are recognised as an asset. Deferred tax assets are only recognised when it is more likely than not, that future taxable profits will be available against which these losses can be utilised. Deferred tax related to charges or credits taken directly to equity is also credited or charged directly to equity and is subsequently recognised in the income statement together with the deferred gain or loss.

The tax charge for long-term business includes tax expense on with-profits funds attributable to both the policyholders and the shareholders. Different tax rules apply under UK law depending upon whether the business is life insurance or pension business. Tax on the life insurance business is based on investment returns less expenses attributable to that business. Tax on the pension business is based on the shareholders' profits or losses attributable to that business. The shareholders' portion of the long-term business is taxed at the shareholders' rate with the remaining portion taxed at rates applicable to the policyholders.

Deferred tax is measured at the tax rates that are expected to apply to the period when the asset is realised or the liability settled, based on tax rates (and laws) that have been enacted or are substantively entailed at the end of the reporting period.

Basis of presentation of tax charges

Tax charges in the income statement reflect the aggregate of the shareholder tax on the long-term business result and on the Prudential Group's other results.

Under UK Listing Authority rules, profit before tax is required to be presented. This requirement, coupled with the fact that IFRS does not contemplate tax charges which are attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies, necessitates the reporting of total tax charges within the presented results. The result before all taxes (i.e. 'profit before tax' as shown in the income statement) represents income net of post-tax transfers to unallocated surplus of with-profits funds, before tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders. Separately within the income statement, 'profit before tax attributable to shareholders' is shown after deduction of taxes attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. Tax charges on this measure of profit reflect the tax charges attributable to shareholders. In determining the tax charges attributable to shareholders, the Prudential Group has applied a methodology consistent with that previously applied under UK GAAP reflecting the broad principles underlying the tax legislation of life assurance companies.

Property, plant and equipment

All property, plant and equipment such as owner occupied property, computer equipment and furniture and fixtures, are carried at depreciated cost. Costs including expenditure directly attributable to the acquisition of the assets are capitalised. Depreciation is calculated and charged on a straight-line basis over an asset's estimated useful life. The residual values and useful lives are reviewed at each statement of financial position date. If the carrying amount of an asset is greater than its recoverable amount then its carrying value is written down to that recoverable amount.

Leasehold improvements to owner occupied property are depreciated over the shorter of the economic life and the life of the lease. Assets held under finance leases are capitalised at their fair value.

Business acquisitions and disposals

Business acquisitions are accounted for by applying the purchase method of accounting, which adjusts the net assets of the acquired company to fair value at the date of purchase. The excess of the costs of acquisition over the fair value of the assets and liabilities of the acquired entity is recorded as goodwill. Should the fair value of the identifiable assets and liabilities of the entity exceed the cost of acquisition then this amount is recognised immediately in the income statement. Income and expenses of acquired entities are included in the income statement from the date of acquisition. Income and expenses of entities sold during the period are included in the income statement up to the date of disposal. The gain or loss on disposal is calculated as the difference between sale proceeds, net of selling costs, less the net assets of the entity at the date of disposal.

For life insurance company acquisitions, the adjusted net assets include an identifiable intangible asset for the present value of in-force business which represents the profits that are expected to emerge from the acquired insurance business. The present value of in-force business is calculated using best estimate actuarial assumptions for interest, mortality, persistency and expenses and is amortised over the anticipated lives of the related contracts in the portfolio. The net carrying amount of insurance liabilities acquired less the value of in-force business, represents the fair value of the insurance liabilities acquired. An intangible asset may also be recognised in respect of acquired investment management contracts representing the fair value of contractual rights acquired under these contracts.

Prudential uses the economic entity method to purchase minority interests. Under the economic entity method any difference between consideration and the share of net assets acquired is recorded directly in equity.

Goodwill

Goodwill arising on acquisitions of subsidiaries and businesses is capitalised and carried on the Prudential Group statement of financial position as an intangible asset at initial value less any accumulated impairment losses. Goodwill impairment testing is conducted annually and when there is an indication of impairment. For the purposes of impairment testing, goodwill is allocated to cash generating units. These cash generating units reflect the smallest group of assets that includes the goodwill and generates cash flows that are largely independent of the cash inflows from other groups of assets. If the carrying amount of the cash generating unit exceeds its recoverable amount then the goodwill is considered impaired. Impairment losses are recognised immediately in the income statement and may not be reversed in future periods.

Acquired intangible assets

Intangible assets acquired on the purchase of a subsidiary or portfolio of contracts are valued at acquisition and carried at cost less amortisation and any accumulated impairment losses. Amortisation is charged over the estimated useful life of the assets on a basis reflecting the pattern in which the assets' future economic benefits are expected to be consumed. The residual values and useful lives are reviewed at each statement of financial position date.

Cash and cash equivalents

Cash and cash equivalents consist of cash at bank and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days maturity from the date of acquisition.

Rights of offset

Assets and liabilities in the consolidated financial information are only reported on a net basis when there is a legally enforceable right to offset and there is an intention to settle on a net basis.

Segments

Under IFRS 8, adopted in 2009, the Prudential Group determines and presents operating segments based on the information that internally is provided to the Group Executive Committee ("GEC"), which is the Prudential Group's chief operating decision maker.

An operating segment is a component of the Prudential Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Prudential Group's other components. An operating segment's operating results are reviewed regularly by the GEC to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

The operating segments identified by the Prudential Group reflect the Prudential Group's organisational structure, which is by both geography (Asia, US and UK) and by product line (insurance operations and asset management). Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type.

Insurance operations comprise principally of products that contain both significant and insignificant elements of insurance risk. The products are managed together and there is no distinction between these two categories other than for accounting purposes. This segment also includes the commission earned on general insurance business and investment subsidiaries held for supporting the Prudential Group's insurance operations

Asset management comprises both internal and third party asset management services, inclusive of portfolio and mutual fund management, where the Prudential Group acts as an advisor, and broker-dealer activities. The nature of the products and the managing of the business differ from the risks inherent in the insurance operations segments, and the regulatory environment of the asset management industry differs from that of the insurance operations segments.

The Prudential Group's operating segments as determined under IFRS 8 are:

Insurance operations

- Asia
- US (Jackson)
- UK

Asset management operations

- M&G
- Asian asset management
- US broker-dealer and asset management (including Curian Capital LLC)

Prudential Capital has been incorporated into the M&G operating segment for the purposes of segment reporting.

The performance measure of operating segments utilised by Prudential is IFRS operating profit attributable to shareholders based on longer-term investment returns. This measure excludes the recurrent items of short-term fluctuations in investment returns and the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes. In addition, for 2009 this measure excludes the non-recurrent cost of hedging the Prudential Group IGD capital surplus included within short-term fluctuations in investment returns (see note B1). In 2009 the Company sold its Taiwan agency business. In order to facilitate comparisons on a like for like basis, the loss on sale and the results of the Taiwan agency business during the period of ownership (including those for the 2007 and 2008 comparatives) are shown separately within the supplementary analysis of profit. Further details on the determination of the performance measure of "operating profit based on longer-term investment returns" is provided below in note A4 (d).

Segment results that are reported to the GEC include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items are mainly in relation to the Group Head Office and Asia Regional Head Office.

Shareholders' dividends

Dividends to shareholders are recognised as a liability in the period in which they are declared. Where scrip dividends are issued, the value of such shares, measured as the amount of the cash dividend alternative, is credited to reserves and the amount in excess of the nominal value of the shares issued is transferred from the share premium account to retained earnings.

Share capital

Where there is no obligation to transfer assets, shares are classified as equity. The difference between the proceeds received on issue of the shares, net of share issue costs, and the nominal value of the shares issued, is credited to share premium. Where the Prudential Group purchases shares for the purposes of employee incentive plans, the consideration paid, net of issue costs, is deducted from retained earnings. Upon issue or sale any consideration received is credited to retained earnings net of related costs.

Foreign exchange

The Prudential Group's consolidated financial information is currently presented in the parent company's functional currency. Accordingly, the results and financial position of foreign subsidiaries must be translated into the presentation currency of the Prudential Group from their functional currencies, i.e. the currency of the primary economic environment in which the entity operates. All assets and liabilities of foreign subsidiaries are converted at year end exchange rates whilst all income and expenses are converted at average exchange rates where this is a reasonable approximation of the rates prevailing on transaction dates. The impact of these currency translations is recorded as a separate component in the statement of comprehensive income.

Foreign currency borrowings that have been used to provide a hedge against Prudential Group equity investments in overseas subsidiaries are translated at year end exchange rates and movements recognised in other comprehensive income. Other foreign currency monetary items are translated at year end exchange rates with changes recognised in the income statement.

Foreign currency transactions are translated at the spot rate prevailing at the time.

d Operating profit based on longer-term investment returns

Consistent with the Prudential Group's segmental reporting for its current businesses, the Prudential Group provides supplementary analysis of profit before tax attributable to shareholders that distinguishes operating profit based on longer-term investment returns from other constituent elements of the total profit.

In determining its segmental results, the Prudential Group uses operating profit based on longer-term investment returns to measure the performance of its operational segments. For the purposes of measuring operating profit, investment returns on shareholder-financed business (including the shareholders' share of participating business other than UK style with-profits funds) are based on the expected longer-term rates of return. This reflects the particular features of long-term insurance business where assets and liabilities are held for the long-term and for which the accounting basis for insurance liabilities under current IFRS is not generally conducive to demonstrating trends in underlying performance for life businesses exclusive of changes in market conditions. In determining profit on this basis the following key elements are applied to the segment operating results of the Prudential Group's shareholder-financed operations.

i Debt and equity securities

Longer-term investment returns comprise income and longer-term capital returns. For debt securities the longer-term capital returns comprise two elements. These are a risk margin reserve ("RMR") based charge for expected defaults, which is determined by reference to the credit quality of the portfolio, and amortisation of interest-related realised gains and losses to operating results based on longer-term investment returns to the date when sold bonds would have otherwise matured. The shareholder-backed operation for which the risk margin reserve charge is most significant is Jackson National Life. The RMR charge for Jackson is based on long-term average default and recovery data as published by Moody's. During 2009, refinements were made to the RMR process following the National Association of Insurance Commissioners ("NAIC") issuing RBC valuation data for more than 20,000 RMBS securities. Longer-term equity returns comprise aggregate long-term income and capital returns.

ii Derivative value movements

Value movements for Jackson's equity-based derivatives and variable annuity product embedded derivatives are included in operating profits based on longer-term investment returns. The inclusion of these movements is so as to broadly match with the results on the Jackson variable annuity book that pertain to equity market movements, subject to some limitations for GMDB products where US GAAP does not fully reflect the economic features being hedged. These accounting mis-matches are magnified in periods of significant market movements.

Other derivative value movements are excluded from operating results based on longer-term investment returns. These derivatives are primarily held by Jackson as part of a broadly-based hedging programme for features of Jackson's bond portfolio (for which value movements are booked in the statement of comprehensive income rather than income statement) and product liabilities (for which US GAAP accounting does not reflect the economic features being hedged).

These key elements are of most importance in determining the operating results based on longer-term investment returns of Jackson.

There are two exceptions to the basis described above for determining operating results based on longer-term investment returns. These are for:

- Unit linked and US variable annuity business.

For such business the policyholder liabilities are directly reflective of the asset value movements. Accordingly, all asset value movements are recorded in the operating results based on longer-term investment returns.

- Assets covering non-participating business liabilities that are interest rate sensitive.

For UK annuity business policyholder liabilities are determined by reference to current interest rates. The value movements of the assets covering liabilities are closely correlated with the related change in liabilities. Accordingly, asset value movements are recorded within the 'operating results based on longer-term investment returns'.

Policyholder liabilities include a margin for credit risk as explained in note D2(f)(iii). Variations between actual and best estimate expected impairments are recorded as a component of short-term fluctuations in investment returns.

iii Liabilities to policyholders and embedded derivatives for product guarantees

Under IFRS, the degree to which the carrying values of liabilities to policyholders are sensitive to current market conditions varies between territories depending upon the nature of the 'grandfathered' measurement basis. In general, in those instances where the liabilities are particularly sensitive to routine changes in market conditions, the accounting basis is such that the impact of market movements on the assets and liabilities are broadly equivalent in the income statement, and operating profit based on longer-term investment returns is not distorted. In these circumstances there is no need for the movement in the liability to be bifurcated between the element that relates to longer-term market conditions and short-term effects.

However, some types of business movements in liabilities do require bifurcation to ensure that at the net level (i.e. after allocated investment returns and change for policyholder benefits) the operating result reflects longer-term market returns.

Examples where such bifurcation is necessary are:

a Asia

Vietnamese participating business

For the participating business in Vietnam the liabilities include policyholders' interest in investment appreciation and other surplus. Bonuses paid in a reporting period and accrued policyholder interest in investment appreciation and other surpluses primarily reflect the level of realised investment gains above contract specific hurdle levels. For this business operating profit based on longer-term investment returns includes the aggregate of longer-term returns on the relevant investments, a credit or charge equal to movements on the liability for the policyholders' interest in realised investment gains (net of any recovery of prior deficits on the participating pool), less amortisation over five years of current and prior movements on such credits or charges.

The overall purpose of these adjustments is to ensure that investment returns included in operating results equal longer-term returns but that in any one reporting period movements on liabilities to policyholders caused by investment returns are substantially matched in the presentation of the segmental analysis of profit before tax attributable to policyholders.

Non-participating business

Liabilities are bifurcated so that the movement in the carrying value of liabilities is split between that which is included in operating results based on longer-term investment returns, and the residual element for the effect of using year end rates is included in short-term fluctuations and in the income statement.

Guaranteed Minimum Death Benefit (GMDB) product features

For unhedged GMDB liabilities accounted for under IFRS using 'grandfathered' US GAAP, such as in the Japanese business, the change in carrying value is determined under SOP 03-01, which partially reflects changes in market conditions. Under the company's segmental basis of reporting the operating profit reflects the change in liability based on longer-term market conditions with the difference between the charge to the operating result and the movement reflected in the total result included in short-term fluctuations in investment returns.

b US operations — embedded derivatives for variable annuity guarantee features

Under IFRS, the Guaranteed Minimum Withdrawal Benefit ("GMWB") and Guaranteed Minimum Income Benefit ("GMIB") reinsurance are required to be fair valued as embedded derivatives. The movements in carrying values are affected by changes in the level of observed implied equity volatility and changes to the discount rate applied from year to year. For these embedded derivatives, as described in note D3(i), the discount rate applied reflects AA corporate bond curve rates. For the purposes of determining operating profit based on longer-term investment returns the charge for these features is determined using historical longer-term equity volatility levels and long-term average AA corporate bond rate curves.

c UK shareholder-backed annuity business

With one exception, the operating result based on longer-term investment returns reflects the impact of all value movements on policyholder liabilities for annuity business in PRIL and the PAC non-profit sub-fund.

The exception is for the impact on credit risk provisioning of actual downgrades during the year. As this feature arises due to short-term market conditions the effect of downgrades, if any, in a particular period, on the overall provisions for credit risks is included in the category of short-term fluctuations in investment returns.

The effects of other changes to credit risk provisioning are included in the operating result, as is the net effect of changes to the valuation rate of interest applied to portfolio rebalancing to align more closely with management benchmark.

iv Fund management and other non-insurance businesses

For these businesses, the particular features applicable for life insurance noted above do not apply. For these businesses, it is inappropriate to include returns in the operating result on the basis described above. Instead it is appropriate to generally include realised gains and losses (including impairments) in the operating result with unrealised gains and losses being included in short-term fluctuations. For this purpose impairments are calculated as the credit loss determined by comparing the projected cash flows discounted at the original effective interest rate to the carrying value. In some instances it may also be appropriate to amortise realised gains and losses on derivatives and other financial instruments to operating results over a time period that reflects the underlying substance of the arrangements.

A5: New accounting pronouncements

The following standards, interpretations and amendments have either been effective and adopted in 2009 or have been issued but are not yet effective in 2009 including those which have not yet been adopted by the EU. This is not intended to be a complete list as only those standards, interpretations and amendments that are anticipated to have an impact upon the Prudential Group's financial information has been discussed.

Accounting pronouncements adopted in 2009

IFRS 8, 'Operating Segments'

IFRS 8 superseded IAS 14 'Segment Reporting' for accounting periods beginning on or after 1 January 2009 and requires the Prudential Group to adopt the 'management approach' to reporting the financial performance of its operating segments.

In accordance with IFRS 8, the Group determines and presents operating segments based on the information that internally is provided to the Group Executive Committee, which is the Prudential Group's chief operating decision maker. Further details on the operating segments and their related performance measure are provided in note A4(c) in "Segments".

The adoption of IFRS 8 has resulted in presentational and disclosure changes in the Prudential Group's financial information. This standard has no impact on the results or financial position of the Prudential Group.

Amendments to IAS 1, 'Presentation of Financial information: A Revised Presentation'

The revised version of IAS 1, which includes non-mandatory changes to the titles of some of the financial information, has resulted in a number of changes in presentation and disclosure.

As a result of the adoption of this revised IAS 1, the Prudential Group has changed the titles of its "consolidated balance sheet" to "consolidated statement of financial position" and its "consolidated cash flow statement" to "consolidated statement of cash flows".

The Prudential Group has also introduced a consolidated statement of comprehensive income in accordance with the revised IAS 1. Components of comprehensive income recognised outside of the income statement, for example exchange movements and the unrealised valuation movement of Jackson's available-for-sale debt securities, are now presented separately from changes in equity and are disclosed in the statement of comprehensive income. Consequent to this presentational change, the Prudential Group has altered the exchange translation method of the unrealised valuation movement of Jackson's available-for-sale debt securities from the previous application of closing exchange rate to the average exchange rate, consistent with the translation method of foreign subsidiaries' income statement items. There is no impact on shareholders' equity or the income statement from this change.

Improvements to IFRSs

The improvements issued by the IASB in May 2008 include amendments to a number of standards. The only amendment that has impacted the financial information is the amendment to IAS 40, 'Investment property' (and consequential amendments to IAS 16, 'Property, Plant and Equipment') which now states that property that is under construction or development for future use as investment property is within the scope of IAS 40 and so should be measured at fair value where this is reliably measurable. Previously, these properties were within the scope of IAS 16 and were measured at cost.

As a result of this amendment, the Prudential Group has reclassified its properties under development for future use as investment properties from Property, plant and equipment to Investment properties. This amendment is effective on a prospective application basis from 1 January 2009 and whilst IAS 40 permits retrospective application provided that the fair values of investment properties under construction were determined at those dates, Prudential has not sought to adjust 2007 and 2008 comparatives due to the relative immateriality of any such adjustments. At 1 January 2009, properties under development with a cost of £131 million were reclassified to Investment properties and revalued to a fair value of £152 million. The fair value adjustment of a gain of £21 million was recorded in the income statement but as the relevant properties were held by the PAC with-profits fund, the gain was absorbed by the liability for unallocated surplus and has no direct effect on the profit or loss attributable to shareholders or shareholders' equity. There was no deferred tax impact on this fair value adjustment.

Amendments to IFRS 7, 'Improving Disclosures about Financial Instruments'

In March 2009, the IASB issued amendments to IFRS 7 which requires enhanced disclosures about fair value measurements and liquidity risk. The amendments include the introduction of a three-level hierarchy for fair value measurement disclosures and require additional disclosures about the relative reliability of fair value measurements. This has been included in note G1. Prudential has applied the amendments to IFRS 7 for periods beginning on 1 January 2009. Additional supplementary 2008 disclosures have been prepared in certain instances.

In addition, the Prudential Group has also adopted the following accounting pronouncements in 2009 but their adoption has had no material impact on results and financial position of the Prudential Group:

- Amendment to IFRS 2, 'Share-based Payment: Vesting Conditions and Cancellations'
- Amendment to IAS 23 'Borrowing costs'
- Amendments to IAS 32 and IAS 1, 'Puttable Financial Instruments and Obligations Arising on Liquidation'
- IFRIC 16, 'Hedges of a Net Investment in A Foreign Operation'

Accounting pronouncement endorsed by the EU but not yet effective

The following accounting pronouncements potentially relevant to the Prudential Group have been issued and endorsed for use in the EU but are not mandatory for adoption for 31 December 2009 year ends.

Revised IFRS 3, 'Business Combinations' and Amendments to IAS 27, 'Consolidated and Separate Financial information'

The revised IFRS 3 and amended IAS 27 are the outcomes of the second phase of the IASB's and the US Financial Accounting Standards Board's (FASB) joint business combination project. The more significant changes from the revised IFRS 3 include:

- The immediate expensing of acquisition-related costs rather than inclusion in goodwill; and
- recognition and measurement at fair value of contingent consideration at acquisition date with subsequent changes to income.

The amendments to IAS 27 reflect changes to the accounting for non-controlling (minority) interests.

The revised IFRS 3 and amended IAS 27 are effective for business combinations occurring in the accounting period beginning on or after 1 July 2009.

Amendment to IAS 39, 'Financial instruments: Recognition and Measurement' — Eligible Hedged Items

This amendment to IAS 39 clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. This amendment is effective for EU compliant financial information for accounting periods beginning on or after 1 July 2009. The Prudential Group is currently assessing the impact of this amendment but it is not expected to have a material impact on the financial information of the Prudential Group.

Accounting pronouncements not yet endorsed by the EU

The following accounting pronouncements potentially relevant to the Prudential Group have been issued but not yet endorsed for use in the EU.

Improvements to IFRSs (2009)

In April 2009, the IASB published amendments to a number of standards as part if its annual improvements projects. These amendments are effective for Prudential's 2010 financial information. The Prudential Group is currently assessing the impact of these improvements to its financial information.

Amendment to IFRS 2 — Group Cash-Settled Share-based Payment Transactions

In June 2009 the IASB issued further amendments to IFRS 2 which sets out the accounting requirements for share-based payments. These amendments clarified existing guidance, in particular by specifying that an entity that receives goods or services in a share-based payment arrangement must account for those goods or services no matter which entity in the group settles the transaction and no matter whether the transaction is settled in shares or cash. Prudential is still assessing the impact of the standard but it is not expected to have a material impact on the Prudential Group's financial information.

IFRIC 19 Extinguishing financial liabilities with equity instruments

In November 2009 the IFRIC issued guidance on how to account for the extinguishment of a financial liability by the issue of equity instruments. This standard is likely to be effective for EU compliant financial information for accounting periods beginning on or after 1 July 2010. This interpretation is not considered to have a material effect on the Prudential Group's financial information.

IFRS 9 Financial Instruments: Classification and Measurement

In November 2009 the IASB issued a new standard which altered the classification and measurement of financial instruments. Under the new standard only two possible classifications arise, rather than the four existing classifications currently available under IAS 39, and will result in all financial assets being valued at amortised cost or fair value through profit and loss. Financial liabilities are excluded from the scope of the standard.

The standard is not mandatory before 2013 year-ends and is yet to be endorsed by the EU. The Prudential Group is still assessing the full impact of this standard.

B: SUMMARY OF RESULTS

B1: Segment disclosure — income statement

The determination of the operating segments and performance measure of the operating segments of the Prudential Group are as detailed in note A4.

	2007	2008	2009
	£m	£m	£m
Asian operations			
Insurance operations:(note ii)			
Underlying results before exceptional credit	140	257	353
Exceptional credit for Malaysia operations(note D4(h))	—	—	63
Total Asian insurance operations	140	257	416
Development expenses	(15)	(26)	(6)
Total Asian insurance operations after development expenses	125	231	410
Asian asset management	72	52	55
Total Asian operations	197	283	465
US operations			
Jackson (US insurance operations)(notes ii,iv)	444	406	459
Broker-dealer and asset management(note iv)	8	7	4
Total US operations	452	413	463

	2007	2008	2009
	£m	£m	£m
UK operations			
UK insurance operations:(note ii)			
Long-term business	524	545	606
General insurance commission(note v)	4	44	51
Total UK insurance operations	528	589	657
M&G	254	286	238
Total UK operations	782	875	895
Total segment profit	1,431	1,571	1,823
Other income and expenditure			
Investment return and other income	86	89	22
Interest payable on core structural borrowings	(168)	(172)	(209)
Corporate expenditure:			
Group Head Office	(129)	(130)	(146)
Asia Regional Head Office	(38)	(41)	(57)
Charge for share-based payments for Prudential schemes(note viii)	(11)	(6)	(5)
Total	(260)	(260)	(395)
Restructuring costs	(19)	(28)	(23)
Operating profit based on longer-term investment returns(note i)	1,152	1,283	1,405
Short-term fluctuations in investment returns on shareholder-backed business(note vi)	(51)	(1,721)	36
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes(note vii)	(1)	(13)	(74)
Loss on sale and results for Taiwan agency business(note iii)	(37)	1	(621)
Profit (loss) from continuing operations before tax attributable to shareholders	1,063	(450)	746

Notes

i Operating profit based on longer-term investment returns: Operating profit based on longer-term investment returns is a supplemental measure of results and is the basis on which management regularly reviews the performance of the Prudential Group's segments as defined by IFRS 8. For the purposes of measuring operating profit, investment returns on shareholder-financed business are based on expected long-term rates of return as discussed in note A4. The expected long-term rates of return are intended to reflect historical real rates of return and, where appropriate, current inflation expectations adjusted for consensus economic and investment forecasts. The most significant operation that requires adjustment for the difference between actual and long-term investment returns is Jackson. The amounts included in operating results for long-term capital returns for Jackson's debt securities comprise two components. These are a risk margin reserve based charge for long-term expected defaults, which is determined by reference to the credit quality of the portfolio, and amortisation of interest-related realised gains and losses to operating results based on longer-term results to the date when sold bonds would otherwise have matured. Consistent with the policy of including longer-term investment returns in the measure of operating profit, movements in policyholder liabilities are also, where appropriate, delineated between amounts included in operating profits and movements arising from short-term market conditions, which are recorded in short-term fluctuations in investment returns.

ii Effect of changes to assumptions, estimates and bases of determining life assurance liabilities: The results of the Prudential Group's long-term business operations are affected by changes to assumptions and bases of preparation. These are described in notes D2(h), D3(h) and D4(h).

iii Sale of Taiwan agency business: In order to facilitate comparisons of operating profit based on longer-term investment returns that reflect the Group's retained operations, the results attributable to the Taiwan business for which the sale process was completed in June 2009 are included separately within the supplementary analysis of profit.

iv Jackson operating results based on longer-term investment returns: IFRS basis operating profits for US operations include the following amounts (net of related change in amortisation of deferred acquisition costs, where applicable) so as to derive longer-term investment returns;

	2007	2008	2009
	£m	£m	£m
Debt securities:			
Amortisation of interest related realised gains and losses	31	24	47
Risk margin reserve charge for longer-term credit related losses (see below)	(37)	(41)	(60)
Equity type investments:			
Longer-term returns	47	62	69

The risk margin reserve ("RMR") charge for longer-term credit related losses included in operating profit based on longer-term investment returns is based on an average annual RMR of 22, 23 and 27 basis points, for 2007, 2008 and 2009 respectively, on average book values for the year as shown below.

Moody's rating category (or equivalent under NAIC rating of RMBS)	2007 Average book value	2007 RMR	2007 Annual expected losses		2008 Average book value	2008 RMR	2008 Annual expected losses		2009 Average book value	2009 RMR	2009 Annual expected losses	
	US $m	bps	US $m	£m	US $m Average	bps	US $m	£m	US $m	bps	US $m	£m
A3 or higher	20,231	0.03	(6)	(3)	21,098	0.03	(6)	(3)	19,509	0.03	(5)	(3)
Baa1, 2, 3	20,306	0.22	(46)	(23)	20,145	0.23	(46)	(25)	21,072	0.23	(47)	(30)
Ba1, 2, 3	1,687	1.13	(19)	(9)	1,635	1.11	(18)	(10)	2,035	1.13	(23)	(15)
B1, 2, 3	530	2.88	(15)	(7)	514	2.80	(14)	(8)	594	2.86	(17)	(11)
Below B3	240	4.00	(10)	(5)	373	3.98	(15)	(8)	691	3.91	(27)	(17)
Total	42,994	0.22	(96)	(47)	43,765	0.23	(99)	(54)	43,901	0.27	(119)	(76)
Related change to amortisation of deferred acquisition costs (see below)			20	10			23	13			25	16
Risk margin reserve charge to operating profit for longer-term credit related losses			(76)	(37)			(76)	(41)			(94)	(60)

During 2009 the National Association of Insurance Commissioners ("NAIC") changed its approach to the determination of regulatory ratings of residential mortgage-backed securities ("RMBS"). This recognised the complexities associated with these investments and the limitations of the credit rating previously applied. The new ratings framework has been applied by an external third party, PIMCO, and provides regulatory ratings details for more than 20,000 RMBS securities owned by US insurers at the end of 2009. Jackson has decided to use the ratings resulting from this model to determine the average annual RMR for 2009 as this is considered more relevant information for the RMBS securities concerned. If the previous approach of using ratings by Nationally Recognised Statistical Ratings Organisation ("NRSROS") such as Moody's, Standard and Poor's or Fitch for these investments had been used this would have resulted in an annual RMR of 31 basis points for 2009, an additional £11 million of annual expected losses for the year. It should be noted that this change has no impact on the valuation applied to these securities within the IFRS statement of financial position and there is no impact to IFRS profit before tax or shareholders' equity as a result of this change.

The longer-term rates of return for equity-type investments ranged from 8.1% to 10.1% for 2007, 6.3%to 8.4% for 2008, and 6.7% to 7.9% for 2009 depending on the type of investments. These rates are currently based on spreads over 10 year US treasury rates of 400 to 600 basis points.

Market value movements on equity-based derivatives and embedded derivatives are also recorded within operating profits based on longer-term investment returns so as to be consistent with the market related effects on fees and reserve movements for equity-based products. Market value movements on other derivatives are excluded from operating profit, and are included in short-term fluctuations in investment returns.

Consistent with the basis of measurement of insurance assets and liabilities for US GAAP investment contracts applied to Jackson's IFRS results, the charges and credits to operating profits based on longer-term investment returns are partially offset by related changes to amortisation of deferred acquisition costs.

v UK operations transferred its general insurance business to Churchill in 2002, with general insurance commission representing the commission receivable net of expenses for Prudential-branded general insurance products as part of this arrangement.

vi Short-term fluctuations in investment returns on shareholder-backed business;

	2007	2008	2009
	£m	£m	£m
Insurance operations:			
Asia	15	(138)	31
US	(18)	(1,058)	27
UK	(47)	(212)	108
IGD hedge costs	—	—	(235)
Other	(1)	(313)	105
	(51)	(1,721)	36

General overview of defaults

There were no default losses in 2007. The Prudential Group incurred defaults of £206 million in 2008 and £11 million in 2009 on its debt securities portfolio. The defaults of £11 million in 2009 were experienced by the UK shareholder-backed annuity business. Jackson experienced less than £1 million of default losses during 2009. Defaults in 2008 of £206 million (including losses on sale) arose primarily in respect of Lehman Brothers (£110 million) and Washington Mutual (£91 million), the majority of which arose in Jackson.

Asian insurance operations

For 2007, the £15 million of short-term fluctuations primarily reflect strong equity market movements in Vietnam. For 2008, fluctuations primarily related to £(81) million for Vietnam, reflecting a significant fall in the Vietnamese bond and equity markets. The fluctuations for Asian operations in 2009 primarily relate to strong market performance in Taiwan and Japan partially offset by the fall in the Vietnamese bond markets.

US insurance operations

The short-term fluctuations in investment returns for US insurance operations for the year comprise of the following items:

	2007	2008	2009
	£m	£m	£m
Short-term fluctuations related to debt securities			
Charges in the year*			
Defaults	—	(78)	—
Losses on sales of impaired and deteriorating bonds	(51)	(130)	(6)
Bond write downs	(35)	(419)	(630)
Recoveries/reversals	8	3	5
	(78)	(624)	(631)
Less: risk margin charge included in operating profit based on longer-term investment returns	48	54	76
	(30)	(570)	(555)
Interest related gains (losses)			
Arising in the year	31	(25)	125
Less: amortisation gains and losses arising in current and prior years to operating profit based on longer-term investment returns	(37)	(28)	(59)
	(6)	(53)	66
Related change to amortisation of deferred acquisition costs	9	88	75
Total short-term fluctuations related to debt securities	(27)	(535)	(414)
Derivatives (other than equity related): market value movements (net of related change to Amortisation of deferred acquisition costs)[†]	(19)	(369)	385
Equity type investments: actual less longer-term return (net of related change to amortisation of deferred acquisition costs)	42	(69)	(59)
Other items (net of related change to amortisation of deferred acquisition costs)[‡]	(14)	(85)	115
Total	(18)	(1,058)	27

* Additional supplementary detailed disclosure of changes by type of security has been provided for 2008 and 2009. The charges on the debt securities of Jackson comprise the following:

	2008				
	Defaults	Losses on sale of impaired and deteriorating bonds	Bond write downs	Recoveries/ reversals	Total
			£m		
Residential mortgage-backed securities					
Prime	—	—	25	—	25
Alt-A	—	—	138	—	138
Sub-prime	—	—	4	—	4
Total residential mortgage-backed securities	—	—	167	—	167
Corporate debt securities	78	130	233	—	441
Other	—	—	19	(3)	16
Total	78	130	419	(3)	624

	2009				
	Defaults	Losses on sale of impaired and deteriorating bonds	Bond write downs	Recoveries/ reversals	Total
			£m		
Residential mortgage-backed securities					
Prime	—	—	268	—	268
Alt-A	—	(10)	192	—	182
Sub-prime	—	—	49	—	49
Total residential mortgage-backed securities	—	(10)	509	—	499
Corporate debt securities	—	16	91	—	107
Other	—	—	30	(5)	25
Total	—	6	630	(5)	631

As disclosed above total 2007 defaults, losses on sale, write downs and recoveries were £(78) million compared to £(624) million in 2008 and £(631) million in 2009. Given the smaller scale of losses in 2007 a break down by type of debt security has not been provided.

Other bond write downs and defaults of £30 million relates to Piedmont Securities in 2009. Piedmont is an investment vehicle investing in certain asset-backed and mortgage-backed securities in the US.

† Market value movements of (£19) million, (£369) million and £385 million, for 2007, 2008 and 2009 respectively, relate to freestanding derivatives held to manage the fixed annuity and other general account business. Under IAS 39, unless hedge accounting is applied, value movements on derivatives are recognised in the income statement.

Derivative value movements in respect of equity risk within variable annuity business are included within the operating profit based on longer-term investment returns to broadly match with the commercial effects to which the variable annuity derivative programme relates, (subject to some limitations to GMDB liabilities where US GAAP does not fully reflect the economic features being hedged.) Other derivative value movements are separately identified within short-term fluctuations in investment returns.

For the derivatives programme attaching to the fixed annuity and other general account business the Prudential Group has continued its approach of not seeking to apply hedge accounting under IAS 39. This decision reflects the inherent constraints of IAS 39 for hedge accounting investments and life assurance assets and liabilities under 'grandfathered' US GAAP under IFRS 4.

‡ The charge of £85 million and the gain of £115 million, for 2008 and 2009 respectively, in relation to other items shown above contains a charge of £70 million and a gain of £85 million in 2008 and 2009 respectively, in respect of the difference between the charge for embedded derivatives included in the operating result and the charge to the total result, and a charge of £15 million and a gain of £30 million in 2008 and 2009 respectively, in respect of other items. For embedded derivatives, the operating result reflects the application of 10-year average AA corporate bond rate curves and a static historical equity volatility assumption.

For 2008 and 2009, the total result reflects the application of year end AA corporate bond rate curves and current equity volatility levels.

In addition, for US insurance operations, included within the statement of comprehensive income, is an increase in net unrealised losses of £244 million and £2,104 million for 2007 and 2008 respectively, and reduction in net unrealised losses on debt securities classified as available-for-sale of £2,669 million for 2009. These temporary market value movements do not reflect defaults or impairments. Additional details on the movement in the value of the Jackson portfolio are included in note D3.

UK insurance operations

The short-term fluctuation charge for 2007 were mostly PRIL. The fluctuation principally reflected the impact of widened credit spreads on the corporate bond securities backing the shareholders' equity of the business. The 2008 charge of £212 million reflected £170 million for asset value movements, principally for shareholder-backed annuity business, and £42 million for the effect of credit downgrades on the calculation of liabilities for shareholder-backed annuity business in PRIL and the PAC non-profit sub-fund. The short-term fluctuations gain for UK insurance operations of £108 million in 2009 reflects principally asset value movements principally for shareholder-backed annuity business.

IGD hedge costs

During the severe equity market conditions experienced in the first quarter of 2009 coupled with historically high equity volatility the Prudential Group entered into exceptional short-dated hedging contracts to protect against potential tail-events on the IGD capital position, in addition to the regular operational hedging programmes. The hedge contracts have expired and have not been renewed.

Other

Short-term fluctuations of other operations, in addition to the previously discussed IGD hedge costs, arise from:

	2007	2008	2009
	£m	£m	£m
Unrealised value movements on swaps held centrally to manage Group assets and liabilities	(18)	(38)	28
Unrealised value movements on Prudential Capital's bond portfolio	(24)	(190)	66
Unrealised value movements on investments held by other operations	9	(14)	11
Amounts related to Asian investment in India mutual fund	32	(71)	—
	(1)	(313)	105

vii Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes

	2007	2008	2009
	£m	£m	£m
Actuarial gains and losses			
Actual less expected return on scheme assets	4	(97)	23
Experience gains (losses) on scheme liabilities	(4)	19	17
Gains (losses) on changes of assumptions for scheme liabilities	(7)	71	(147)
	(7)	(7)	(107)
Less: amount attributable to the PAC with-profits sub-fund	6	(2)	47
	(1)	(9)	(60)
Other gains and losses			
Movement in the provision for deficit funding of PSPS	—	(13)	(48)
Less: amount attributable to the PAC with-profits sub-fund	—	9	34
	—	(4)	(14)
Total	(1)	(13)	(74)

The actuarial gains and losses shown in the table above relate to the Scottish Amicable, M&G and until 2009 the small Taiwan defined benefit pension scheme. The amounts did not include actuarial gains and losses for the Prudential Staff Pension Scheme (PSPS) for which the Prudential Group has not recognised its interest in the scheme's underlying surplus.

The losses of £147 million in 2009 on change of assumptions comprise mainly the effect of a decrease in the risk discount rate combined with the effect of an increase in inflation rates. The gains of £71 million in 2008 on change in assumptions comprises the effect of an increase in the risk discount rate combined with the effect of decreases in inflation rates.

Other gains and losses relate to the change in the year of the provision for deficit funding obligation for PSPS

Further details on the Prudential Group's defined benefit pension schemes and the effect of the accounting policy change are shown in note I2.

viii Share-based payments

The charge for share-based payments for Prudential schemes is for the SAYE and Group performance-related schemes.

ix Restructuring costs are incurred in the UK as part of EEV covered business (2007: £7 million, 2008: £10 million, 2009: £16 million) and as part of central operations (EEV non-covered business) (2007: £12 million, 2008: £18 million, 2009: £7 million).

B2: Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year, excluding those held in employee share trusts, which are treated as cancelled.

For diluted earnings per share, the weighted average number of shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The Prudential Group's only class of dilutive potential ordinary shares are those share options granted to employees where the exercise price is less than the average market price of Prudential's ordinary shares during the year. No adjustment is made if the impact is anti-dilutive overall.

	2007					
	Before tax note B1	Tax note F5	Minority interests	Net of tax and minority interests	Basic earnings per share	Diluted earnings per share
	£m	£m	£m	£m	Pence	Pence
Based on operating profit based on longer-term investment returns	1,152	(352)	(4)	796	32.5p	32.5p
Short-term fluctuations in investment returns on shareholder-backed business	(51)	20	1	(30)	(1.2)p	(1.2)p
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	(1)	1	—	—	0.0p	0.0p
Adjustment for result of Taiwan agency business	(37)	(23)	—	(60)	(2.5)p	(2.5)p
Based on profit for the year from continuing operations	1,063	(354)	(3)	706	28.8p	28.8p
Adjustments for post-tax results of discontinued operations*	222	19	—	241	9.9p	9.8p
Based on profit for the year	1,285	(335)	(3)	947	38.7p	38.6p

* Discontinued operations in 2007 related entirely to UK Banking operations following the sale on 1 May 2007 of Egg Banking plc to Citibank Overseas Investment Corporation, a subsidiary of Citigroup Inc.

	2008					
	Before tax note B1	Tax note F5	Minority interests	Net of tax and minority interests	Basic earnings per share	Diluted earnings per share
	£m	£m	£m	£m	Pence	Pence
Based on operating profit based on longer-term investment returns	1,283	(292)	(4)	987	39.9p	39.9p
Short-term fluctuations in investment returns on shareholder-backed business	(1,721)	352	(1)	(1,370)	(55.4)p	(55.4)p
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	(13)	3	—	(10)	(0.4)p	(0.4)p
Adjustment for result of sold Taiwan agency business	1	(4)	—	(3)	(0.1)p	(0.1)p
Based on loss for the year	(450)	59	(5)	(396)	(16.0)p	(16.0)p

	2009					
	Before tax note B1	Tax note F5	Minority interests	Net of tax and minority interests	Basic earnings per share	Diluted earnings per share
	£m	£m	£m	£m	Pence	Pence
Based on operating profit based on longer-term investment returns	1,405	(318)	(2)	1,085	43.4p	43.3p
Short-term fluctuations in investment returns on shareholder-backed business	36	224	1	261	10.4p	10.4p
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(74)	21	—	(53)	(2.1)p	(2.1)p
Adjustment from loss on sale and result of Taiwan agency business	(621)	18	—	(603)	(24.1)p	(24.0)p
Based on profit for the year from continuing operations	746	(55)	(1)	690	27.6p	27.6p
Adjustments for post-tax results of discontinued operations (note I9)	(14)	—	—	(14)	(0.6)p	(0.6)p
Based on profit for the year	732	(55)	(1)	676	27.0p	27.0p

Parent company profits

The consolidated profit after tax attributable to equity shareholders of the company includes a loss of £26 million, a profit of £475 million and profit of £908 million, in respect of the standalone company (including dividends from subsidiaries), for 2007, 2008 and 2009 respectively.

Number of shares

A reconciliation of the weighted average number of ordinary shares used for calculating basic and diluted earnings per share is set out as below:

	2007 m	2008 m (note i)	2009 m
Weighted average shares for calculation of basic earnings per share	2,445	2,472	2,501
Shares under option at end of year	9	—	12
Number of shares that would have been issued at fair value on assumed option exercise	(6)	—	(7)
Weighted average shares for calculation of diluted earnings per share	2,448	2,472	2,506

Note i

For the year ended 31 December 2008 there were 7 million shares under option offset by 6 million shares that would have been issued at fair value on assumed option exercise. The net one million shares have not been included in the 2008 diluted earnings per share calculation as their inclusion would have decreased the loss per share.

B3: Dividends

	2007	2008	2009
	£m	£m	£m
Dividends declared and paid in reporting period			
Parent company:			
Interim dividend (2007: 5.70p, 2008: 5.99p, 2009: 6.29p per share)	140	149	159
Final dividend for prior period (2007: 11.72p, 2008: 12.30p, 2009: 12.91p per share)	286	304	322
Subsidiary company dividend payments attributable to minority interests	5	2	—
Total	431	455	481

As a result of shares issued in lieu of dividends of £176 million, £157 million and £137 million, dividends paid in cash, as set out in the consolidated statement of cash flows, were £255 million, £297 million and £344 million for 2007, 2008 and 2009 respectively.

	2007	2008	2009
	£m	£m	£m
Parent company dividends relating to reporting period:			
Interim dividend (2007: 5.70p, 2008: 5.99p, 2009: 6.29p per share)	140	149	159
Final dividend (2007: 11.72p, 2008: 12.91p, 2009: 13.56p per share)	304	322	343
Total	444	471	502

B4: Exchange translation

Exchange movement recognised in other comprehensive income

	2007	2008	2009
	£m	£m	£m
Asian operations	16	456	(189)
US operations	(43)	581	(244)
Unallocated to a segment (central funds)	38	(646)	227
	11	391	(206)

The movements for Asian and US operations reflect the application of year end exchange rates to the assets and liabilities and average exchange rates to the income statement on translation of these operations into the presentation currency of the Prudential Group. The movement unallocated to a segment mainly reflects the translation of currency borrowings and forward contracts which have been designated as a net investment hedge against the currency risk of the net investment in Jackson.

The exchange rates applied were:

Local currency: £	Opening rate at 1 Jan 2007	Closing rate at 31 Dec 2007	Average for 2007	Closing rate at 31 Dec 2008	Average for 2008	Closing rate at 31 Dec 2009	Average for 2009
Hong Kong	15.22	15.52	15.62	11.14	14.42	**12.52**	**12.14**
Indonesia	17,601.63	18,696.71	18,295.63	15,799.22	17,749.22	**15,171.52**	**16,173.28**
Japan	233.20	222.38	235.64	130.33	192.09	**150.33**	**146.46**
Malaysia	6.90	6.58	6.88	5.02	6.15	**5.53**	**5.51**
Singapore	3.00	2.87	3.02	2.07	2.61	**2.27**	**2.27**
Taiwan	63.77	64.56	65.75	47.28	58.24	**51.65**	**51.65**
US	1.96	1.99	2.00	1.44	1.85	**1.61**	**1.57**

B5: New business

Insurance products and investment products(note i)

	Insurance products gross premiums			Investment products gross inflows (note ii)			Total		
	2007	2008	2009	2007	2008	2009	2007	2008	2009
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Asian operations	2,901	2,422	2,019	38,954	46,957	71,176	41,855	49,379	73,195
US operations	6,534	6,941	8,909	60	36	6	6,594	6,977	8,915
UK operations	6,879	7,183	5,014	14,745	16,154	24,875	21,624	23,337	29,889
Group total	16,314	16,546	15,942	53,759	63,147	96,057	70,073	79,693	111,999

Insurance products — new business premiums and contributions(note i)

	Single			Regular			Annual premium and contribution equivalents		
	2007	2008	2009	2007	2008	2009	2007	2008	2009
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Asian operations(note iv)									
China (Group's 50% interest)	45	63	72	24	32	38	29	38	45
Hong Kong	501	507	94	117	154	232	167	205	241
India (Group's 26% interest)	26	60	47	177	202	163	180	208	168
Indonesia	118	94	41	109	167	186	121	176	190
Japan	122	115	57	22	30	46	34	42	52
Korea	179	78	38	241	211	118	259	219	122
Malaysia	41	28	63	78	99	140	82	102	146
Singapore	593	341	297	67	78	98	126	112	128
Taiwan(note iii)	10	36	104	21	55	97	22	58	107
Other	36	18	29	55	54	59	58	56	62
Total Asian operations	1,671	1,340	842	911	1,082	1,177	1,078	1,216	1,261
US operations(note iv)									
Fixed annuities	573	1,724	1,053	—	—	—	57	172	105
Fixed index annuities	446	501	1,433	—	—	—	45	50	143
Variable annuities	4,554	3,491	6,389	—	—	—	455	349	639
Life	7	7	10	19	24	24	20	25	25
Total US operations — Retail	5,580	5,723	8,885	19	24	24	577	596	912
Guaranteed investment contracts and Medium Term Notes	935	1,194	—	—	—	—	94	120	—
Total US operations	6,515	6,917	8,885	19	24	24	671	716	912
UK operations									
Product summary									
Internal vesting annuities	1,399	1,600	1,357	—	—	—	140	160	136
Direct and partnership annuities	842	703	590	—	—	—	84	70	59
Intermediated annuities	555	497	242	—	—	—	56	50	24
Total individual annuities	2,796	2,800	2,189	—	—	—	280	280	219
Income drawdown	34	75	91	—	—	—	3	8	9
Equity release	156	242	127	—	—	—	16	24	13
Individual pensions	38	115	198	1	3	7	5	14	27
Corporate pensions	283	221	81	84	88	86	112	110	94
Unit-linked bonds	243	109	122	—	—	—	24	11	12
With-profits bonds	297	869	1,264	—	—	—	30	87	126
Protection	—	—	—	5	6	17	5	6	17
Offshore products	434	551	317	4	4	3	47	59	35
PruHealth	—	—	—	13	16	11	13	16	11
Total retail retirement	4,281	4,982	4,389	107	117	124	535	615	563
Corporate pensions	198	227	111	115	116	105	135	139	116
Other products	190	132	79	25	21	17	44	34	25
DWP rebates	143	153	127	—	—	—	14	15	13
Total mature life and pensions	531	512	317	140	137	122	193	188	154
Total retail	4,812	5,494	4,706	247	254	246	728	803	717
Wholesale annuities	1,799	1,417	39	—	—	—	180	142	4
Credit life	21	18	23	—	—	—	2	2	2
Total UK operations	6,632	6,929	4,768	247	254	246	910	947	723
Channel summary									
Direct and partnership	2,385	2,352	1,814	212	215	201	451	450	382
Intermediated	2,284	2,990	2,765	35	39	45	263	338	322
Wholesale	1,820	1,434	62	—	—	—	182	144	6
Sub-total	6,489	6,776	4,641	247	254	246	896	932	710
DWP rebates	143	153	127	—	—	—	14	15	13
Total UK operations	6,632	6,929	4,768	247	254	246	910	947	723
Group total	14,818	15,186	14,495	1,177	1,360	1,447	2,659	2,879	2,896

Investment products — funds under management(note (ii) and (iv))

	2007				
	1 Jan 2007	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2007
	£m				
Asian operations	12,253	38,954	(35,993)	2,179	17,393
US operations	—	60	(4)	(1)	55
UK operations	44,946	14,745	(9,787)	1,317	51,221
Group total	57,199	53,759	(45,784)	3,495	68,669

	2008				
	1 Jan 2008	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2008
	£m				
Asian operations	17,393	46,957	(46,102)	(3,016)	15,232
US operations	55	36	(32)	(9)	50
UK operations	51,221	16,154	(12,747)	(7,631)	46,997
Group total	68,669	63,147	(58,881)	(10,656)	62,279

	2009				
	1 Jan 2009	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2009
	£m				
Asian operations	15,232	71,176	(69,177)	2,243	**19,474**
US operations	50	6	(66)	10	**—**
UK operations	46,997	24,875	(11,397)	9,831	**70,306**
Group total	62,279	96,057	(80,640)	12,084	**89,780**

Notes

i The tables shown above are provided as an indicative volume measure of transactions undertaken in the reporting period that have the potential to generate profits for shareholders. The amounts shown are not, and not intended to be, reflective of premium income recorded in the IFRS income statement.

Annual Premium Equivalents (APEs) are calculated as the aggregate of regular new business amounts and one-tenth of single new business amounts. New business premiums for regular premium products are shown on an annualised basis. Department of Work and Pensions (DWP) rebate business is classified as single recurrent business. Internal vesting business is classified as new business where the contracts include an open market option.

The format of the tables shown above is consistent with the distinction between insurance and investment products as applied for previous financial reporting periods. With the exception of some US institutional business, products categorised as 'insurance' refer to those classified as contracts of long-term insurance business for regulatory reporting purposes, i.e. falling within one of the classes of insurance specified in Part II of Schedule 1 to the Regulated Activities Order under FSA regulations.

The details shown above for insurance products include contributions for contracts that are classified under IFRS 4 'Insurance Contracts' as not containing significant insurance risk. These products are described as investment contracts or other financial instruments under IFRS. Contracts included in this category are primarily certain unit-linked and similar contracts written in UK insurance operations and Guaranteed Investment Contracts and similar funding agreements written in US operations.

ii Investment products referred to in the table for funds under management above are unit trusts, mutual funds and similar types of retail fund management arrangements. These are unrelated to insurance products that are classified as 'investment contracts' under IFRS 4, as described in the preceding paragraph, although similar IFRS recognition and measurement principles apply to the acquisition costs and fees attaching to this type of business.

iii The tables above include new business for the Taiwan bank distribution operation. New business of the Taiwan Agency business, which was sold in June 2009 (as explained in note I1) are excluded from the tables. Comparative figures have been adjusted accordingly.

iv New business and market gross inflows and redemption have been translated at the average exchange rate for the year applicable. Funds under management at points in time are translated at the exchange rate applicable at those dates.

B6: Group statement of financial position

To explain more comprehensively the assets, liabilities and capital of the Prudential Group's businesses it is appropriate to provide an analysis of the Prudential Group's statement of financial position by operating segment and type of business. The tables below aggregate the three asset management segments for ease of presentation and hence should be read in conjunction with the associated tables on asset management in note E2.

B6 (a) Group statement of financial position by operating segment

This analysis is shown below for the Prudential Group statement of financial position by operating segment.

(i) ***Position at 31 December 2007***

	2007							
	Insurance operations							
By operating segment	UK D2	US D3	Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2007 group total
	£m							
Assets								
Intangible assets attributable to shareholders:								
Goodwill	—	—	111	111	1,230	—	—	1,341
Deferred acquisition costs and other intangible assets	157	1,928	745	2,830	6	—	—	2,836
Total(H1)	157	1,928	856	2,941	1,236	—	—	4,177
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	192	—	—	192	—	—	—	192
Deferred acquisition costs and other intangible assets	19	—	—	19	—	—	—	19
Total(H2)	211	—	—	211	—	—	—	211
Total	368	1,928	856	3,152	1,236	—	—	4,388
Deferred tax assets(H4)	105	657	73	835	95	21	—	951
Other non-investment and non-cash assets(H3-H6)	4,110	994	689	5,793	426	4,292	(5,499)	5,012
Investment of long-term business and other operations:								
Investment properties	13,666	8	14	13,688	—	—	—	13,688
Investments accounted for using the equity method	—	—	—	—	—	12	—	12
Financial investments:								
Loans(note c)	1,245	3,258	1,087	5,590	2,334	—	—	7,924
Equity securities and portfolio holdings in unit trusts	60,829	15,507	9,804	86,140	17	—	—	86,157
Debt securities(note c)	57,180	19,002	6,920	83,102	882	—	—	83,984
Other investments	3,391	762	42	4,195	155	46	—	4,396
Deposits	7,228	258	377	7,863	26	—	—	7,889
Total investments(G1,H7,H8)	143,539	38,795	18,244	200,578	3,414	58	—	204,050
Properties held for sale(H9)	30	—	—	30	—	—	—	30
Cash and cash equivalents(H10)	1,869	169	679	2,717	1,840	394	—	4,951
Total assets	150,021	42,543	20,541	213,105	7,011	4,765	(5,499)	219,382

By operating segment	Insurance operations UK D2	Insurance operations US D3	Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2007 group total
	2007 £m							
Equity and liabilities								
Equity								
Shareholders' equity(H11)	1,364	2,690	1,369	5,423	1,677	(1,038)	—	6,062
Minority interests	42	1	7	50	52	—	—	102
Total equity	1,406	2,691	1,376	5,473	1,729	(1,038)	—	6,164
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Insurance contract liabilities(H12)	82,938	32,926	16,912	132,776	—	—	—	132,776
Investment contract liabilities with discretionary participation features(G1)	29,466	—	84	29,550	—	—	—	29,550
Investment contract liabilities without discretionary participation features(G1)	12,073	1,922	37	14,032	—	—	—	14,032
Unallocated surplus of with-profits funds(D2fii,H12)	13,813	—	146	13,959	—	—	—	13,959
Total policyholder liabilities and unallocated surplus of with-profits funds(note d)	138,290	34,848	17,179	190,317	—	—	—	190,317
Core structural borrowings of shareholder-financed operations:(H13)								
Subordinated debt	—	—	—	—	—	1,570	—	1,570
Other	—	125	—	125	—	797	—	922
Total	—	125	—	125	—	2,367	—	2,492
Operational borrowings attributable to shareholder-financed operations(G1,H13)	12	591	—	603	1	2,477	—	3,081
Borrowings attributable to with-profits operations(G1,H13)	987	—	—	987	—	—	—	987
Other non-insurance liabilities:(G1,H4,H14,H15)								
Obligations under funding, securities lending and sale and repurchase agreements	1,360	2,721	—	4,081	—	—	—	4,081
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	1,751	65	506	2,322	1,234	—	—	3,556
Deferred tax liabilities	2,383	639	362	3,384	11	7	—	3,402
Current tax liabilities	507	—	24	531	36	670	—	1,237
Accruals and deferred income	289	—	111	400	199	—	—	599
Other creditors	1,913	333	627	2,873	3,440	206	(5,499)	1,020
Provisions	326	19	33	378	166	31	—	575
Derivative liabilities	699	158	2	859	176	45	—	1,080
Other liabilities	98	353	321	772	19	—	—	791
Total	9,326	4,288	1,986	15,600	5,281	959	(5,499)	16,341
Total liabilities	148,615	39,852	19,165	207,632	5,282	5,803	(5,499)	213,218
Total equity and liabilities	150,021	42,543	20,541	213,105	7,011	4,765	(5,499)	219,382

(ii) *Position at 31 December 2008*

By operating segment	Insurance operations UK D2	Insurance operations US D3	Insurance operations Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2008 Group total
	2008 £m							
Assets								
Intangible assets attributable to shareholders:								
Goodwill	—	—	111	111	1,230	—	—	1,341
Deferred acquisition costs and other intangible assets	134	3,962	1,247	5,343	6	—	—	5,349
Total(H1)	134	3,962	1,358	5,454	1,236	—	—	6,690
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	174	—	—	174	—	—	—	174
Deferred acquisition costs and other intangible assets	13	—	113	126	—	—	—	126
Total(H2)	187	—	113	300	—	—	—	300
Total	321	3,962	1,471	5,754	1,236	—	—	6,990
Deferred tax assets(H4)	513	1,969	101	2,583	160	143	—	2,886
Other non-investment and non-cash assets(H3-H6)	4,962	1,819	1,416	8,197	135	3,553	(5,608)	6,277
Investment of long-term business and other operations:								
Investment properties	11,959	13	20	11,992	—	—	—	11,992
Investments accounted for using the equity method	—	—	—	—	—	10	—	10
Financial investments:								
Loans(note c)	1,902	5,121	1,705	8,728	1,763	—	—	10,491
Equity securities and portfolio holdings in unit trusts	38,880	15,142	8,077	62,099	23	—	—	62,122
Debt securities(note c)	58,871	24,249	11,113	94,233	991	—	—	95,224
Other investments	4,160	1,256	144	5,560	462	279	—	6,301
Deposits	6,090	390	750	7,230	64	—	—	7,294
Total investments(G1,H7,H8)	121,862	46,171	21,809	189,842	3,303	289	—	193,434
Properties held for sale(H9)	—	—	—	—	—	—	—	—
Cash and cash equivalents(H10)	2,571	246	1,501	4,318	1,472	165	—	5,955
Total assets	130,229	54,167	26,298	210,694	6,306	4,150	(5,608)	215,542

By operating segment	Insurance operations UK D2	Insurance operations US D3	Insurance operations Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group Eliminations	31 Dec 2008 Group total
	2008 £m							
Equity and liabilities								
Equity								
Shareholders' equity(H11)	1,655	1,698	2,167	5,520	1,642	(2,104)	—	5,058
Minority interests	47	—	7	54	1	—	—	55
Total equity	1,702	1,698	2,174	5,574	1,643	(2,104)	—	5,113
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Insurance contract liabilities(H12)	72,756	42,476	20,798	136,030	—	—	—	136,030
Investment contract liabilities with discretionary participation features(G1)	23,367	—	79	23,446	—	—	—	23,446
Investment contract liabilities without discretionary participation features(G1)	11,584	2,885	32	14,501	—	—	—	14,501
Unallocated surplus of with-profits funds (D2fii,H12)	8,254	—	160	8,414	—	—	—	8,414
Total policyholder liabilities and unallocated surplus of with-profits funds(note d)	115,961	45,361	21,069	182,391	—	—	—	182,391
Core structural borrowings of shareholder-financed operations:(H13)								
Subordinated debt	—	—	—	—	—	1,987	—	1,987
Other	—	173	—	173	—	798	—	971
Total	—	173	—	173	—	2,785	—	2,958
Operational borrowings attributable to shareholder-financed operations(G1,H13)	54	511	130	695	4	1,278	—	1,977
Borrowings attributable to with-profits operations(G1,H13)	1,308	—	—	1,308	—	—	—	1,308
Other non-insurance liabilities:(G1,H4,H14,H15)								
Obligations under funding, securities lending and sale and repurchase agreements	2,251	3,321	—	5,572	—	—	—	5,572
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	1,536	88	1,154	2,778	1,065	—	—	3,843
Deferred tax liabilities	1,421	1,337	441	3,199	11	19	—	3,229
Current tax liabilities	127	—	76	203	40	599	—	842
Accruals and deferred income	265	—	130	395	205	30	—	630
Other creditors	1,619	529	796	2,944	2,898	1,262	(5,608)	1,496
Provisions	267	23	37	327	97	37	—	461
Derivative liabilities	3,401	863	32	4,296	292	244	—	4,832
Other liabilities	317	263	259	839	51	—	—	890
Total	11,204	6,424	2,925	20,553	4,659	2,191	(5,608)	21,795
Total liabilities	128,527	52,469	24,124	205,120	4,663	6,254	(5,608)	210,429
Total equity and liabilities	130,229	54,167	26,298	210,694	6,306	4,150	(5,608)	215,542

(iii) ***Position at 31 December 2009***

By operating segment	Insurance operations UK D2	Insurance operations US D3	Insurance operations Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2009 Group total
	2009 £m							
Assets								
Intangible assets attributable to shareholders:								
Goodwill	—	—	80	80	1,230	—	—	1,310
Deferred acquisition costs and other intangible assets	127	3,092	822	4,041	8	—	—	4,049
Total(H1)	127	3,092	902	4,121	1,238	—	—	5,359
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	124	—	—	124	—	—	—	124
Deferred acquisition costs and other intangible assets	9	—	97	106	—	—	—	106
Total(H2)	133	—	97	230	—	—	—	230
Total	260	3,092	999	4,351	1,238	—	—	5,589
Deferred tax assets(H4)	292	1,944	132	2,368	132	208	—	2,708
Other non-investment and non-cash assets(H3-H6)	3,074	1,404	880	5,358	718	4,393	(5,044)	5,425
Investment of long-term business and other operations:								
Investment properties	10,861	33	11	10,905	—	—	—	10,905
Investments accounted for using the equity method	4	—	2	6	—	—	—	6
Financial investments:								
Loans(note c)	1,815	4,319	1,207	7,341	1,413	—	—	8,754
Equity securities and portfolio holdings in unit trusts	37,051	20,984	11,182	69,217	137	—	—	69,354
Debt securities(note c)	67,772	22,831	9,984	100,587	1,164	—	—	101,751
Other investments	3,630	955	258	4,843	113	176	—	5,132
Deposits	11,557	454	746	12,757	63	—	—	12,820
Total investments(G1,H7,H8)	132,690	49,576	23,390	205,656	2,890	176	—	208,772
Properties held for sale(H9)	—	3	—	3	—	—	—	3
Cash and cash equivalents(H10)	2,265	340	837	3,442	970	895	—	5,307
Total assets	138,581	56,359	26,238	221,178	5,948	5,672	(5,044)	227,754

By operating segment	Insurance operations UK D2	US D3	Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2009 Group total
	2009 £m							
Equity and liabilities								
Equity								
Shareholders' equity(H11)	1,939	3,011	1,462	6,412	1,659	(1,800)	—	6,271
Minority interests	28	—	1	29	3	—	—	32
Total equity	1,967	3,011	1,463	6,441	1,662	(1,800)	—	6,303
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Insurance contract liabilities(H12)	77,655	46,346	21,712	145,713	—	—	—	145,713
Investment contract liabilities with discretionary participation features(G1)	24,780	—	100	24,880	—	—	—	24,880
Investment contract liabilities without discretionary participation features(G1)	13,794	1,965	46	15,805	—	—	—	15,805
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds) (D2dii,H12)	9,966	—	53	10,019	—	—	—	10,019
Total policyholder liabilities and unallocated surplus of with-profits funds(note(d))	126,195	48,311	21,911	196,417	—	—	—	196,417
Core structural borrowings of shareholder-financed operations:(H13)								
Subordinated debt	—	—	—	—	—	2,691	—	2,691
Other	—	154	—	154	—	549	—	703
Total	—	154	—	154	—	3,240	—	3,394
Operational borrowings attributable to shareholder-financed operations(G1,H13)	158	203	210	571	142	2,038	—	2,751
Borrowings attributable to with-profits operations(G1,H13)	1,284	—	—	1,284	—	—	—	1,284
Other non-insurance liabilities:(G1,H4,H14,H15)								
Obligations under funding, securities lending and sale and repurchase agreements	2,108	1,374	—	3,482	—	—	—	3,482
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	2,534	47	818	3,399	410	—	—	3,809
Deferred tax liabilities	1,606	1,858	384	3,848	5	19	—	3,872
Current tax liabilities	426	89	85	600	35	580	—	1,215
Accruals and deferred income	271	—	105	376	209	9	—	594
Other creditors	726	532	760	2,018	3,292	1,346	(5,044)	1,612
Provisions	406	10	50	466	127	50	—	643
Derivative liabilities	709	461	146	1,316	49	136	—	1,501
Other liabilities	191	309	306	806	17	54	—	877
Total	8,977	4,680	2,654	16,311	4,144	2,194	(5,044)	17,605
Total liabilities	136,614	53,348	24,775	214,737	4,286	7,472	(5,044)	221,451
Total equity and liabilities	138,581	56,359	26,238	221,178	5,948	5,672	(5,044)	227,754

B6 (b) Group statement of financial position by business type

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type at 31 December:

			2009						
			Shareholder-backed business						
By business type	31 Dec 2007 Group total	31 Dec 2008 Group total	Participating funds	Unit-linked and variable annuity	Non-linked business D4	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2009 Group total
	£m								
Assets									
Intangible assets attributable to shareholders:									
Goodwill	1,341	1,341	—	—	80	1,230	—	—	1,310
Deferred acquisition costs and other intangible assets	2,836	5,349	—	—	4,041	8	—	—	4,049
Total(H1)	4,177	6,690	—	—	4,121	1,238	—	—	5,359
Intangible assets attributable to with-profits funds:									
In respect of acquired subsidiaries for venture fund and other investment purposes	192	174	124	—	—	—	—	—	124
Deferred acquisition costs and other intangible assets	19	126	106	—	—	—	—	—	106
Total(H2)	211	300	230	—	—	—	—	—	230
Total	4,388	6,990	230	—	4,121	1,238	—	—	5,589
Deferred tax assets(H4)	951	2,886	156	—	2,212	132	208	—	2,708
Other non-investment and non-cash assets(H3-H6)	5,012	6,277	2,017	630	2,711	718	4,393	(5,044)	5,425
Investment of long-term business and other operations:									
Investment properties	13,688	11,992	8,759	662	1,484	—	—	—	10,905
Investments accounted for using the equity method	12	10	—	—	6	—	—	—	6
Financial investments:									
Loans(note c)	7,924	10,491	1,887	27	5,427	1,413	—	—	8,754
Equity securities and portfolio holdings in unit trusts	86,157	62,122	29,962	38,620	635	137	—	—	69,354
Debt securities(note c)	83,984	95,224	47,327	8,848	44,412	1,164	—	—	101,751
Other investments	4,396	6,301	3,448	110	1,285	113	176	—	5,132
Deposits	7,889	7,294	9,638	746	2,373	63	—	—	12,820
Total investments (notes G1,H7,H8)	204,050	193,434	101,021	49,013	55,622	2,890	176	—	208,722
Properties held for sale	30	—	—	—	3	—	—	—	3
Cash and cash equivalents(H10)	4,951	5,955	1,421	1,174	847	970	895	—	5,307
Total assets	219,382	215,542	104,845	50,817	65,516	5,948	5,672	(5,044)	227,754

By business type	31 Dec 2007 £m Group total	31 Dec 2008 £m Group total	2009 Participating funds	Shareholder-backed Unit-linked and variable annuity	Non-linked business D4	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2009 Group total
			£m						
Equity and liabilities									
Equity									
Shareholders' equity(H11)	6,062	5,058	—	—	6,412	1,659	(1,800)	—	6,271
Minority interests	102	55	28	—	1	3	—	—	32
Total equity	6,164	5,113	28	—	6,413	1,662	(1,800)	—	6,303
Liabilities									
Policyholder liabilities and unallocated surplus of with-profits funds:									
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	176,358	173,977	86,337	49,391	50,670	—	—	—	186,398
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds)(D2fii,H12)	13,959	8,414	10,019	—	—	—	—	—	10,019
Total policyholder liabilities and unallocated surplus of with-profits funds(note b)	190,317	182,391	96,356	49,391	50,670	—	—	—	196,417
Core structural borrowings of shareholder-financed operations:(H13)									
Subordinated debt	1,570	1,987	—	—	—	—	2,691	—	2,691
Other	922	971	—	—	154	—	549	—	703
Total	2,492	2,958	—	—	154	—	3,240	—	3,394
Operational borrowings attributable to shareholder-financed operations(G1,H13)	3,081	1,977	—	—	571	142	2,038	—	2,751
Borrowings attributable to with-profits funds(G1,H13)	987	1,308	1,284	—	—	—	—	—	1,284
Deferred tax liabilities	3,402	3,229	1,420	12	2,416	5	19	—	3,872
Other non insurance liabilities	12,939	18,566	5,757	1,414	5,292	4,139	2,175	(5,044)	13,733
Total liabilities	213,218	210,429	104,817	50,817	59,103	4,286	7,472	(5,044)	221,451
Total equity and liabilities	219,382	215,542	104,845	50,817	65,516	5,948	5,672	(5,044)	227,754

B6 (c) Debt securities and loans

i Information on the credit risks of debt securities

Position at 31 December:

	2007					
	Insurance operations			Total insurance operations	Asset management	Group total
	UK	US	Asia			
	£m	£m	£m	£m	£m	£m
S&P — AAA	21,556	3,896	2,284	27,736	278	28,014
S&P — AA+ to AA−	6,173	1,187	1,994	9,354	319	9,673
S&P — A+ to A−	12,557	3,657	675	16,889	198	17,087
S&P — BBB+ to BBB−	5,409	5,415	193	11,017	—	11,017
S&P — Other	942	1,113	149	2,204	—	2,204
	46,637	15,268	5,295	67,200	795	67,995
Moody's — Aaa	1,021	549	201	1,771	46	1,817
Moody's — Aa1 to Aa3	587	118	45	750	—	750
Moody's — A1 to A3	944	47	28	1,019	—	1,019
Moody's — Baa1 to Baa3	490	79	19	588	—	588
Moody's — Other	410	78	58	546	—	546
	3,452	871	351	4,674	46	4,720
Fitch	682	380	1	1,063	—	1,063
Other	6,409	2,483	1,273	10,165	41	10,206
Total debt securities	57,180	19,002	6,920	83,102	882	83,984

	2008					
	Insurance operations			Total insurance operations	Asset management	Group total
	UK	US	Asia			
	£m	£m	£m	£m	£m	£m
S&P — AAA	18,981	5,321	2,632	26,934	342	27,276
S&P — AA+ to AA−	6,012	853	3,746	10,611	274	10,885
S&P — A+ to A−	15,929	5,244	808	21,981	319	22,300
S&P — BBB+ to BBB−	7,413	7,077	902	15,392	—	15,392
S&P — Other	1,033	1,321	253	2,607	—	2,607
	49,368	19,816	8,341	77,525	935	78,460
Moody's — Aaa	681	458	494	1,633	24	1,657
Moody's — Aa1 to Aa3	833	100	108	1,041	15	1,056
Moody's — A1 to A3	678	111	398	1,187	—	1,187
Moody's — Baa1 to Baa3	454	100	60	614	—	614
Moody's — Other	162	95	50	307	—	307
	2,808	864	1,110	4,782	39	4,821
Fitch	560	464	41	1,065	—	1,065
Other	6,135	3,105	1,621	10,861	17	10,878
Total debt securities	58,871	24,249	11,113	94,233	991	95,224

	2009					
	Insurance operations			Total insurance operations	Asset management	Group total
	UK	US	Asia			
	£m	£m	£m	£m	£m	£m
S&P — AAA	16,091	3,287	2,259	21,637	469	22,106
S&P — AA+ to AA−	6,472	846	1,594	8,912	148	9,060
S&P — A+ to A−	19,693	5,192	1,496	26,381	468	26,849
S&P — BBB+ to BBB−	12,183	7,659	682	20,524	57	20,581
S&P — Other	2,667	895	917	4,479	—	4,479
	57,106	17,879	6,948	81,933	1,142	83,075
Moody's — Aaa	463	273	134	870	—	870
Moody's — Aa1 to Aa3	276	43	349	668	19	687
Moody's — A1 to A3	801	32	309	1,142	2	1,144
Moody's — Baa1 to Baa3	815	64	40	919	—	919
Moody's — Other	339	57	15	411	—	411
	2,694	469	847	4,010	21	4,031
Implicit ratings of RMBS based on NAIC valuations (see below)						
— NAIC 1	—	747	—	747	—	747
— NAIC 2	—	105	—	105	—	105
— NAIC 3-6	—	473	—	473	—	473
	—	1,325	—	1,325	—	1,325
Fitch	1,022	281	39	1,342	—	1,342
Other	6,950	2,877	2,150	11,977	1	11,978
Total debt securities	67,772	22,831	9,984	100,587	1,164	101,751

In the tables above, with the exception of residential mortgage backed securities within Jackson, Standard & Poor's ("S&P") ratings have been used where available. For securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative. During 2009, the National Association of Insurance Commissioners in the US revised the regulatory ratings process for more than 20,000 residential mortgage-backed securities. The table above includes those securities, held by Jackson, using the regulatory ratings levels established by an external third party (PIMCO). Notes D2(c), D3(c), D4(c) and E2 provide further details on the credit risks of debt securities by segment.

ii Group exposure to holdings in asset-backed securities

Additional supplementary disclosure has been provided for 2008 and 2009. The Prudential Group's exposure to holdings in asset-backed securities which comprise residential mortgage-backed securities ("RMBS"), commercial mortgage backed securities ("CMBS"), collateralised debt obligation ("CDO") funds and other asset-backed securities ("ABS"), at 31 December is as follows:

	2008	2009
	£m	£m
Shareholder-backed operations:		
UK insurance operations(note i)	1,075	2,044
US insurance operations(note ii)	7,464	6,376
Asian insurance operations(note iii)	15	59
Other operations(note iv)	407	326
	8,961	8,805
With-profits operations:		
UK insurance operations(note i)	4,977	6,451
Asian insurance operations(note iii)	328	378
	5,305	6,829
Total	14,266	15,634

i UK insurance operations

The UK insurance operations' exposure to asset-backed securities at 31 December is analysed as follows:

	2008	2009
	£m	£m
Shareholder-backed business (2008: 70% AAA, 19% AA; 2009: 29% AAA, 24% AA)	1,075	2,044
With-profits operations (2008: 74% AAA, 10% AA; 2009: 33% AAA, 14% AA)	4,977	6,451
	6,052	8,495

All of the £1,075 million and £2,044 million, for 2008 and 2009 respectively, exposure of the shareholder-backed business relates to the UK market and primarily relate to investments held by PRIL. £2,721 million of the £4,977 million and £4,695 million of the £6,451 million exposure of the with-profits operations relates to exposure to the UK market while the remaining £2,256 million and £1,756 million relates to exposure to the US market, for 2008 and 2009 respectively.

ii US insurance operations

US insurance operations' exposure to asset-backed securities at 31 December comprises:

	2008	2009
	£m	£m
RMBS†		
Sub-prime (2008: 91% AAA, 3% AA; 2009: 76% AAA, 1% AA)	291	194
Alt-A 2007 (2008: 60% AAA, 15% AA; 2009: 24% AAA, 5% AA)	646	443
Prime (2008: 87% AAA, 5% AA; 2009: 82% AAA, 4% AA)	3,572	2,679
CMBS (2008: 85% AAA, 9% AA; 2009: 46% AAA, 14% AA)	1,869	2,104
CDO funds (2008: 34% AAA, 14% AA; 2009: 29% AAA, 10% AA),* including £6 million exposure to sub-prime in 2008 and £3 million in 2009	320	79
Other ABS (2008: 31% AAA, 16% AA; 2009: 25% AAA, 18% AA), including £51 million exposure to sub-prime in 2008 and nil 2009	766	877
Total	7,464	6,376

† RMBS ratings refer to the rating implicit within NAIC risk-based capital valuation (see B6(c)(i)).

* Including the Group's economic interest in Piedmont and other consolidated CDO funds. Further details on Jackson's RMBS sub-prime and Alt-A securities are given in note D3(c).

iii Asian insurance operations

The Asian insurance operations' exposure to asset-backed securities is primarily held by the with-profits operations.

The £328 million and £378 million, at 31 December 2008 and at 31 December 2009 respectively, asset-backed securities exposure of the Asian with-profits operations comprises:

	2008	2009
	£m	£m
RMBS — all without sub-prime exposure	46	—
CMBS	88	91
CDO funds and ABS	194	287
Total	328	378

The £328 million and £378 million includes £259 million and £228 million, for 2008 and 2009 respectively, held by investment funds are consolidated under IFRS in recognition of the control arrangements for those funds. The consolidated funds include an amount not owned by the Prudential Group with a corresponding liability of £32 million and £61 million (at 31 December 2008 and at 31 December 2009 respectively) on the statement of financial position for net asset value attributable to external unit-holders in respect of these funds, which are non-recourse to the Prudential Group. Of the £328 million and £378 million, 70% and 72% are investment graded by Standard & Poor's as at 31 December 2008 and 31 December 2009 respectively.

iv Other operations

Other operations' exposure to asset-backed securities at 31 December is held by Prudential Capital and comprises:

	2008	2009
	£m	£m
RMBS: Prime (2008: 75% AAA, 10% AA; 2009: 92% AAA, 8% AA)	106	91
CMBS (2008: 68% AAA, 20% AA; 2009: 48% AAA, 18% AA)	230	193
CDO funds and other ABS	71	42
Total	407	326

(iii) Loans

Information on the credit quality of the portfolio of loans, which almost wholly is for amounts which are neither past due or impaired is shown in notes D2, D3, D4 and E2. Details of allowances for loans, losses and amounts past due are shown in notes G1 and G2. No additional analysis is provided of the element of loans and receivables that were neither past due nor impaired from those of the total portfolio on the grounds of the immateriality of the difference between the neither past due nor impaired element and the total portfolio.

(d) Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of the Group from the beginning of the year to the end of the year is as follows:

	Insurance operations			Total insurance operations
	UK	US	Asia	
	£m	£m	£m	£m
At 1 January 2007	133,904	31,746	12,889	178,539
Premiums	8,853	6,352	3,958	19,163
Surrenders	(4,528)	(3,476)	(1,032)	(9,036)
Maturities/Deaths	(6,787)	(490)	(395)	(7,672)
Shareholders' transfers post tax	(279)	—	(21)	(300)
Investment-related items and other movements	7,194	1,225	1,458	9,877
Foreign exchange translation differences	(67)	(509)	322	(254)
At 31 December 2007/1 January 2008	138,290	34,848	17,179	190,317
Premiums	9,372	6,728	4,162	20,262
Surrenders	(4,281)	(3,852)	(1,191)	(9,324)
Maturities/Deaths	(8,324)	(564)	(354)	(9,242)
Shareholders' transfers post tax	(284)	—	(23)	(307)
Investment-related items and other movements	(16,331)	(4,552)	(4,293)	(25,176)
Foreign exchange translation differences	(2,481)	12,753	5,589	15,861
At 31 December 2008/1 January 2009	115,961	45,361	21,069	182,391
Premiums	6,867	9,177	3,807	19,851
Surrenders	(3,971)	(3,255)	(1,201)	(8,427)
Maturities/Deaths	(7,239)	(733)	(342)	(8,314)
Shareholders' transfers post tax	(202)	—	(20)	(222)
Changes in reserving basis in Malaysia	—	—	(63)	(63)
Assumption changes (shareholder-backed business)	(46)	—	(4)	(50)
Investment-related items and other movements	14,118	2,986	4,242	21,346
Foreign exchange translation differences	707	(5,225)	(2,069)	(6,587)
Disposal of Taiwan agency business	—	—	(3,508)	(3,508)
At 31 December 2009	126,195	48,311	21,911	196,417

The items above represent the amount attributable to changes in policyholder liabilities and unallocated surplus of with-profits funds as a result of each of the components listed.

Premiums, surrenders, and maturities/deaths represent the amounts impacting policyholder liabilities and may not represent the total cash paid/received (for example, premiums are net of any deductions to cover acquisition costs).

C: GROUP RISK MANAGEMENT

a Overview

As a provider of financial services, including insurance, the Prudential Group's business is the managed acceptance of risk. The control procedures and systems established within the Group are designed to manage, rather than eliminate, the risk of failure to meet business objectives. They can only provide reasonable and not absolute assurance against material misstatement or loss, and focus on aligning the levels of risk-taking with the achievement of business objectives.

The Prudential Group's internal control processes are detailed in the Group Governance Manual. This is supported by the Group risk framework, which provides an overview of the group-wide philosophy and approach to risk management. Where appropriate, more detailed policies and procedures have been developed at Prudential Group and/or business unit levels. These include group-wide mandatory policies on certain operational risks, including: health, safety, fraud, money laundering, bribery, business continuity, information security and operational security, and policies on certain financial risks. Additional guidelines are provided for some aspects of actuarial and finance activity.

Prudential's risk governance framework requires that all of the Prudential Group's businesses and functions establish processes for identifying, evaluating and managing the key risks faced by the Prudential Group. The risk governance framework is based on the concept of 'three lines of defence': Risk management, risk oversight and independent assurance. Primary responsibility for strategy, performance management and risk control lies with the Board, the Group Chief Executive and the chief executives of each business unit. Risk oversight is provided by group-level risk committees, chaired by the Group Chief Risk Officer or the Group Chief Financial Officer. Independent assurance on the Prudential Group's and business unit internal control and risk management systems is provided by group-wide Internal Audit reporting to the Prudential Group and business unit audit committees.

The Prudential Group's risk reporting framework forms an important part of the Prudential Group's business planning process. Business units review their risks as part of the annual preparation of their business plans and review opportunities and risks against business objectives regularly with Prudential Group executive management.

Additional information on the Prudential Group's risk framework is included in the risk and capital management section of the Prudential Group's business review.

The management of the risk attached to the Prudential Group's financial instruments and insurance liabilities, together with the inter-relationship with the management of capital may be summarised in the following sections.

b Group risk appetite

The Prudential Group risk appetite framework sets out the Group's tolerance to risk management and return optimisation. The Prudential Group defines and monitors aggregate risk limits for its earnings volatility and its capital requirements based on financial and non-financial stresses.

i Earnings volatility:

The objectives of the limits are to ensure that (a) the volatility of earnings is consistent with stakeholder expectations, (b) the Prudential Group has adequate earnings (and cash flows) to service debt and expected dividends and (c) that earnings (and cash flows) are managed properly across geographies and are consistent with the Prudential Group's funding strategies. The two measures used currently are European Embedded Value ("EEV") operating profit based on longer-term investment returns and International Financial Reporting Standards ("IFRS") operating profit based on longer-term investment returns. Additionally, EEV and IFRS total profits are also assessed.

ii Capital requirements:

The objectives of the limits are to ensure that (a) the Prudential Group meets the internal economic capital requirements at all times, (b) the Prudential Group achieves its desired target rating to meet its business objectives and (c) supervisory intervention is avoided. The two measures used are EU Insurance Groups Directive ("IGD") capital requirements and internal economic capital requirements. In addition, the Prudential Group also monitors capital requirement on a local statutory basis.

Business units must establish suitable market, credit, underwriting and liquidity limits that maintain financial risk exposures within the defined Prudential Group risk appetite.

The Prudential Group's risk appetite framework forms an integral part of its annual business planning cycle. Throughout the year, the Group risk function monitors the Prudential Group's risk profile against the agreed limits. Using submissions from business units, Group risk function calculates the Prudential Group's aggregated position (allowing for diversification effects between business units) relative to the limits implied by the risk appetite statements.

Market risk is managed such that as conditions evolve the risk profile is maintained within risk appetite in addition to business unit operational limits on credit risk, the Prudential Group sets counterparty risk limits at group level. Limits on the total group-wide exposures to a single counterparty are specified within different credit rating 'categories'. Actual exposures are monitored against these limits on a monthly basis.

c Risk mitigation and hedging

The Prudential Group manages its actual risk profile against its tolerance of risk. To do this, it maintains risk registers that include details of the identified risks and of the controls and mitigating actions employed in managing them. Any mitigation strategies involving large transactions, such as a material derivative transaction, are subject to scrutiny at group level before implementation.

It uses a range of risk management and mitigation strategies. The most important of these include: adjusting asset portfolios to reduce investment risks (such as duration mismatches or overweight counterparty exposures); using derivatives to hedge market risks; implementing reinsurance programmes to limit insurance risk; implementing corporate insurance programmes to limit the impact of operational risks; and revising business plans where appropriate.

i Use of derivatives

In the UK and Asia, Prudential uses derivatives to reduce equity and credit risk, interest rate and currency exposures, and to facilitate efficient investment management. In the US, Prudential uses derivatives to reduce interest rate risk, to facilitate efficient portfolio management and to match liabilities under annuity policies, and for certain equity-based product management activities.

Further details of the Prudential Group's use of derivatives are explained in note G3.

ii Asset/liability management

Prudential manages its assets and liabilities locally, in accordance with local regulatory requirements and reflecting the differing types of liabilities of each business unit. Stochastic asset/liability modelling is carried out locally by business units to perform dynamic solvency testing and assess capital requirements. Reserve adequacy testing under a range of scenarios and dynamic solvency analysis is carried out, including under certain scenarios mandated by the US, the UK and Asian regulators.

A stochastic approach models the inter-relationship between asset and liability movements, taking into account asset correlation and policyholder behaviour, under a large number of possible scenarios. These scenarios are projected forward over a period of time, typically 25 years, and the liabilities and solvency position of the fund are calculated in each scenario in each future year. This allows the identification of which extreme scenarios will have the most adverse effects and what the best estimate outcome may be. The fund's policy on management actions, including bonus and investment policy, are then set in order that they are consistent with the available capital and the targeted risk of default. This differs from a deterministic model, which would only consider the results from one carefully selected scenario.

For businesses that are most sensitive to interest rate changes, such as immediate annuity business, Prudential uses cash flow analysis to create a portfolio of fixed income securities whose value changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits and the capital position from changing interest rates. In the UK, the cash flow analysis is used in Prudential Group's annuity business while, in the US, it is used for its interest-sensitive and fixed index annuities and stable value products such as Guaranteed Investment Contracts ("GICs"). Perfect matching is not possible, for example because of the nature of the liabilities (which might include guaranteed surrender values) and options for prepayment contained in the assets or the unavailability of assets with a sufficiently long duration.

For businesses that are most sensitive to equity price changes, Prudential uses stochastic modelling and scenario testing to look at the expected future returns on its investments under different scenarios that best reflect the large diversity in returns that equities can produce. This allows Prudential to devise an investment and with-profits policyholder bonus strategy that, on the model assumptions, allows it to optimise returns to its policyholders and shareholders over time, while maintaining appropriate financial strength. Prudential uses this method extensively in connection with its UK with-profits business.

All of Prudential Group's investments are held either for risk management or investment purposes. This is because almost all of the investments support policyholder or customer liabilities of one form or another. Any assets that the Prudential Group holds centrally that are not supporting customer liabilities are predominantly invested in short-term fixed income and fixed maturity securities.

The Prudential Group has contingency plans in place for a range of operational risk scenarios, including incident management and business continuity plans. As a contingency plan for liquidity risk, the Prudential Group has arranged access to committed revolving credit facilities and committed securities lending facilities.

d Risk exposures

The Group publishes separately within 'Additional Information' of its Group Annual Report a section on key risk factors, which discusses inherent risks in the business and trading environment.

i Market risks

Market risk is the risk that arises from adverse changes in the value of, or income from, assets and changes in interest rates or exchange rates.

Equity and interest rate risk

Prudential faces equity risk and interest rate risk because most of its assets are investments that are either equity type investments and subject to equity price risk, or bonds, mortgages or cash deposits, the values of which are subject to interest rate risk. The amount of risk borne by Prudential's shareholders depends on the extent to which its customers share the investment risk through the structure of the Prudential Group's products.

The split of the Prudential Group's investments between equity investments and interest-sensitive instruments depends principally on the type of liabilities supported by those investments and the amount of capital the Prudential Group has available. The nature of some liabilities allows it to invest a substantial portion of its investment funds in equity and property investments that Prudential believes produce greater returns over the long term. On the other hand the Prudential Group has some liabilities that contain guaranteed returns and allow instant access (for example, interest-sensitive fixed annuities and immediate annuities), which generally will be supported by fixed income investments.

Foreign exchange risk

Prudential faces foreign exchange risk, primarily because its presentation currency is pounds sterling, whereas approximately 45%, 53% and 62% of the Prudential Group operating profit from continuing operations based on longer-term investment returns, as described in note B1, for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, came from the US and Asian operations. The exposure relating to the translation of reported earnings is not separately managed although its impact is reduced by interest payments on foreign currency borrowings and by the adoption of average exchange rates for the translation of foreign currency revenues.

Approximately 70%, 83% and 77% of the Prudential Group's IFRS basis shareholders' equity at 31 December 2007, 31 December 2008 and 31 December 2009 respectively arose in Prudential's US and Asian operations. To mitigate the exposure of the US component US$1.55 billion, US$1.55 billion and US$1.55 billion of borrowings were held centrally, which are formally designated as net investment hedges, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Net of the currency position arising from these borrowings some 40%, 49% and 52% of the Group's shareholders' funds are represented by net assets in currencies other than sterling as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

Additional details on the market risks' exposures of the UK, US and Asian insurance operations are provided in notes D2, D3 and D4, respectively.

ii Credit risk

Credit risk is the risk of loss to the Prudential Group if another party fails to perform its obligations, or fails to perform them in a timely manner. Credit risk is the Prudential Group's most significant financial risk.

Some of the Prudential Group businesses, in particular Jackson, the PAC with-profits fund and the Prudential Group UK pension annuity business hold large amounts of interest-sensitive investments that contain credit risk on which a certain level of defaults is expected. These expected losses are considered when Prudential determines the crediting rates, deposit rates and premium rates for the products that will be supported by these assets. The key shareholder business exposed to credit risks is Jackson. Certain over-the-counter derivatives contain a credit risk element that is controlled through evaluation of collateral agreements and master netting agreements on interest rate and currency swaps. Prudential is also exposed to credit-related losses in the event of non-performance by counterparties.

Further analysis of the credit quality of debt securities held by the Prudential Group is shown in note B6. Additional details on the credit quality of the debt security portfolios of UK, US and Asian insurance operations are shown in notes D2, D3 and D4, respectively.

iii Liquidity risk

The assets of insurers are in general relatively liquid whilst liabilities to policyholders are mainly illiquid. Accordingly, for insurers, the focus is on parent capital and liquidity measures. Prudential regularly monitors and analyses its liquidity position at the parent (group centre) level and performs stress tests of this position. For Prudential, liquidity risk is the risk that though solvent on a statement of financial position basis, the Prudential Group either does not have the financial resources to meet its obligations as they fall due or can secure the resources only at excessive cost. The liquidity of the Prudential Group is monitored on a monthly basis by comparing the predicted cash needs of the Prudential Group centre to meet corporate and financing costs (net of expected dividends from the business units) to the liquid resources available to it. These liquid resources include cash held and cash that could be raised through internal resources (for example by repoing unencumbered bonds). Base costs and stress scenarios reported monthly to the Balance Sheet and Capital Management Committee. The main stress is the assumption that the external financing markets are completely closed to Prudential, no new external funding can be obtained, and existing funding cannot be rolled over. In addition Group liquidity risk reports are prepared regularly. In summary, these address the accuracy of external back-up lines, internal sources of liquidity, and monitor how external liabilities and other commitments over the next 12 months compare with internal and external sources. The parent company has significant internal resources of liquidity which are sufficient to meet all of its foreseeable future needs without having to utilise external funding. The Prudential Group maintains committed facilities that at 31 December 2009 include £1.4 billion of undrawn syndicated committed banking facility and two £100 million bi-lateral facilities on the same terms, maturing in 2011 and 2012 respectively, as well as a committed £500 million annually renewable securities lending back-up facility.

iv Insurance risk

Insurance risk is the inherent uncertainty as to the occurrence, amount and timing of insurance liabilities. This includes adverse mortality, morbidity and persistency experience.

Prudential needs to make assumptions about a number of factors in determining the pricing of its products and for reporting the results of its long-term business operations. In common with other industry participants, the profitability of the Group's businesses depends on a mix of factors including mortality and morbidity trends, voluntary discontinuance rates, investment performance, unit cost of administration and new business acquisition expenses.

For example, the assumption that Prudential makes about future expected levels of mortality is particularly relevant for its UK annuity business where, in exchange for their accumulated pension fund, pension annuity policyholders receive a guaranteed payment, for as long as they live. Prudential conducts rigorous research into longevity risk using data from its substantial annuitant portfolio. As part of its pension annuity pricing and reserving policy, Prudential UK assumes that current rates of mortality continuously improve over time at levels based on adjusted data from the Continuous Mortality Investigations (CMI) projections as published by the Institute and Faculty of Actuaries.

Prudential's voluntary discontinuance (persistency) assumptions reflect recent past experience for each relevant line of business, and any expectations of future persistency. Where appropriate, allowance is also made for the relationship, which is either assumed or historically observed, between persistency and investment returns and the resulting additional risk is allowed for.

v Non-financial risks — operational, business environment and strategic risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, systems or from external events. Business environment risk may arise from exposure to forces in the external environment that could significantly change the fundamentals that drive the business's overall objectives and strategy. Strategic risk may arise from ineffective, inefficient or inadequate senior management processes for the development and implementation of business strategy in relation to the business environment and the Prudential Group's capabilities.

Prudential Group is exposed to operational, business environment and strategic risk in the course of running its businesses. The Prudential Group processes a large number of complex transactions across numerous and diverse products, and is subject to a number of different legal and regulatory regimes. The Prudential Group has a significant number of third-party relationships that are important to the distribution and processing of its products, as market counterparties and as business partners.

The Prudential Group uses the qualitative and quantitative analysis of operational risk exposures material to the Prudential Group to support business decisions, to inform overall levels of capital held and to assess the adequacy of the corporate insurance programme.

e Regulatory capital requirements

Regulatory capital requirements apply at an individual company level for the Prudential Group's life assurance and asset management business. These are described in sections D5 and E3 respectively.

In addition, the Prudential Group as a whole is subject to the capital adequacy requirements of the Insurance Groups Directive ("IGD") as implemented by the FSA. The IGD pertains to groups whose activities are primarily concentrated in the insurance sector. Under this test the surplus capital held in each of the regulated subsidiaries is aggregated with the free assets of non-regulated subsidiaries. From this total Prudential Group borrowings are deducted, other than subordinated debt issues which qualify as capital. No credit for the benefit of diversification is allowed for under this approach. The test is passed when this aggregate number is positive: a negative result at any point in time is a notifiable breach of UK regulatory requirements.

Due to the geographically diverse nature of the Prudential Group's operations, the application of these requirements to Prudential is complex. In particular, for many of the Prudential Group's Asian operations the assets, liabilities and capital requirements have to be recalculated based on FSA regulations as if the companies were directly subject to FSA regulation.

The FSA has established a structure for determining how much hybrid debt can count as capital which is similar to that used for banks. It categorises capital as Tier 1 (equity and preference shares), Upper Tier 2 and Lower Tier 2. Up to 15% of Tier 1 capital can be in the form of hybrid debt and is called 'Innovative Tier 1'. At 31 December 2007, 31 December 2008 and 31 December 2009 the Prudential Group held £763 million, £1,059 million and £1,422 million respectively of Innovative Tier 1 capital in the form of perpetual securities and £nil of Upper Tier 2 for all years. At 31 December 2007, 31 December 2008 and 31 December 2009, Prudential held £807 million, £928 million and £1,269 million respectively of Lower Tier 2 capital. In addition, Jackson held £125 million, £173 million and £154 million of surplus notes at the end of each of the financial years respectively which, although the US does not have a similar capital categorisation under its regulatory framework, are akin to the FSA's Lower Tier 2 capital and have been disclosed as such in note H13. The increase in these amounts arises from the issue in May 2009 of £400 million of subordinated debt (Lower Tier 2), the issue in July 2009 of US$750 million perpetual subordinated capital securities (Innovative Tier 1) and exchange rate movements during 2008 and 2009 (no issuance was made during 2007 and 2008). Further details on these amounts and other Group borrowings are shown in note H13.

At 31 December 2007 and 31 December 2008, the Prudential Group met the requirements of the IGD with £1.9 billion and £1.5 billion respectively of surplus capital before allowing for the 2007 and 2008 final dividend respectively. The IGD position as at 31 December 2009 is that the surplus capital under the test was £3.4 billion before allowing for the 2009 final dividend giving a solvency ratio of 283%. The main components of the increase in IGD surplus during 2009 are:

- net capital generation mainly through operating earnings (in-force releases less investment in new business) of £1.1 billion;
- the sale of the Taiwan agency business (increasing IGD surplus by £0.8 billion);
- the hybrid debt issues in May and July (increasing IGD surplus by £0.9 billion);
- an additional recognition of £0.4 billion in respect of part of the shareholders' interest in the future transfers from the PAC with-profits fund, recognition of £0.2 billion of future profits in the UK and Hong Kong and other intra-group capital efficiencies of £0.3 billion;
- offset by dividend payments, external financing costs and other central costs, credit related impacts in the US, impacts from regulatory changes and foreign exchange movements.

Prudential's approach to capital allocation takes into account a range of factors, especially risk adjusted returns on capital, the impact of alternative capital measurement bases (accounting, regulatory, economic and ratings agency assessments), tax efficiency and wider strategic objectives.

The Prudential Group optimises capital allocation across the Group by using a consistent set of capital performance metrics across all business units to ensure meaningful comparison. Capital utilisation, return on capital and new business value creation are measured at a product level. The use of these capital performance metrics is embedded into our decision-making processes for product launches, product design and product pricing.

The Prudential Group capital performance metrics are based on economic capital, which provides a realistic and consistent view of our capital requirements across the Group, allowing for diversification benefits. Economic capital also provides valuable insights into our risk profile and is used both for risk measurement and capital management.

The Prudential Group detailed understanding of risk adjusted performance allows the Prudential Group to manage proactively its allocation of capital to write new business to maximise risk adjusted value creation.

D: LIFE ASSURANCE BUSINESSES

D1: Group overview

a Products and classification for IFRS reporting

The measurement basis of assets and liabilities of long-term business contracts is dependent upon the classification of the contracts under IFRS. Under IFRS 4, contracts are initially classified as being either 'insurance' contracts, if the level of insurance risk in the contracts is significant, or investment contracts, if the risk is insignificant.

Insurance contracts

Insurance contracts are permitted to be accounted for under previously applied GAAP. The Prudential Group has chosen to adopt this approach. However, as an improvement to accounting policy, permitted by IFRS 4, the Prudential Group has applied the measurement principles for with-profits contracts of UK regulated entities and disclosures of the UK Standard FRS 27 from 1 January 2005. An explanation of the provisions under FRS 27 is provided in note D2.

Under the previously applied GAAP, UK GAAP, the assets and liabilities of contracts are reported in accordance with the MSB of reporting as set out in the ABI SORP.

The insurance contracts of the Prudential Group's shareholder-backed business fall broadly into the following categories:

- UK insurance operations
  — bulk and individual annuity business, written primarily by Prudential Retirement Income Limited and other categories of non-participating UK business;
- Jackson
  — fixed and variable annuity business and life insurance; and
- Prudential Corporation Asia
  — non-participating term, whole life, and unit-linked policies, together with accident and health policies.

Investment contracts

Investment contracts are further delineated under IFRS 4 between those with and without discretionary participation features. For those contracts with discretionary participation features, IFRS 4 also permits the continued application of previously applied GAAP. The Prudential Group has adopted this approach, again subject to the FRS 27 improvement.

For investment contracts that do not contain discretionary participation features, IAS 39 and, where the contract includes an investment management element, IAS 18, apply measurement principles to assets and liabilities attaching to the contract that may diverge from those previously applied.

Contracts of the Prudential Group, which are classified as investment contracts that do not contain discretionary participation features, can be summarised as:

- UK
  — certain unit-linked savings and similar contracts;
- Jackson
  — GICs and funding agreements
  — minor amounts of 'annuity certain' contracts; and
- Prudential Corporation Asia
  — minor amounts for a number of small categories of business.

The accounting for the investment contracts of UK insurance operations and Jackson's GICs and funding agreements are considered in turn below:

i Certain UK unit-linked savings and similar contracts

Deferred acquisition costs

Acquisition costs are deferred to the extent that it is appropriate to recognise an asset that represents the entity's contractual right to benefit from providing investment management services and are amortised as the entity recognises the related revenue. IAS 18 further reduces the costs potentially capable of deferral to incremental costs only. Deferred acquisition costs are amortised to the income statement in line with service provision.

Deferred income reserves

These are required to be established under IAS 18 with amortisation over the expected life of the contract. The majority of the relevant UK contracts are single premium with the initial deferred income reflecting the 'front-end load' i.e. the difference between the premium paid and the amount credited to the unit fund. Deferred income is amortised to the income statement in line with service provision. The amortisation profile is either on a straight-line basis or, if more appropriate, a further deferral of income recognition is applied.

Sterling reserves

Prudent provisions established for possible future expenses not covered by future margins at a policy level reflecting the regulatory approach in the UK are not permitted for those contracts with insignificant insurance risk that are classified as investment contracts.

ii Jackson — GICs and funding arrangements

Under a traditional GIC, the policyholder makes a lump sum deposit. The interest rate paid is fixed and established when the contract is issued. Funding agreements are of a similar nature but the interest rate may be floating, based on a rate linked to an external index. The US GAAP accounting requirements for such contracts are very similar to those under IFRS on the amortised cost model for liability measurement.

b Concentration of risk

i Business accepted

The Prudential Group's exposure to life assurance risks is well-diversified. This is achieved through the geographical spread of the Prudential Group's operations and, within those operations, through a broad mix of product types.

As part of the risk management framework, the Prudential Group regularly monitors concentration of risk using a variety of risk monitoring tools including:

- Scenario testing and sensitivity analysis for the Prudential Group capital and profitability metrics involving IGD, Prudential Group economic capital, EEV and IFRS help identify concentrations of risks by risk types, products and business units, as well as the benefits of diversification of risks.

An example of the diversification benefits for Prudential Group is that adverse scenarios do not affect all business units in the same way, providing natural hedges within the group. For example, the US business is sensitive to increasing interest rates, whereas, in contrast, several business units in Asia benefit from increasing rates. Conversely, these Asian business units are sensitive towards low interest rates, whereas certain products in the US benefit from falling interest rates. The economic capital framework also takes into account situations where factors are correlated, for example the extent of correlation between UK and US economies.

- Business units are also required to disclose to the group risk function all material risks, along with information on their severity and likelihood, and mitigating actions taken or planned.

Credit risk remains one of the largest risk exposures. This reflects the relative size of exposure in Jackson and the UK Shareholder annuities business. The Prudential Group manages concentration of credit risks by setting limits on the maximum exposure to each counterparty based on their credit ratings.

ii Ceded business

The Prudential Group cedes certain business to other insurance companies. Although the ceding of insurance does not relieve the Prudential Group of liability to its policyholders, the Prudential Group participates in such agreements for the purpose of managing its loss exposure. The Prudential Group evaluates the financial condition of its reinsurers and monitors concentration of credit risk from similar geographic regions, activities or economic characteristics of the reinsurers to minimise its exposure from reinsurer insolvencies. There are no significant concentrations of reinsurance risk. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively the Prudential Group's UK and US operations ceded 98%, 98% and 98% of the reinsurance recoverable insurance assets. Of those amounts, 88%, 93% and 92% were from reinsurers with Standard & Poor's rating A- and above as at 31 December 2007, 31 December 2008 and 31 December 2009.

c Guarantees

Notes D2(d), D3(d) and D4(d) provide details of guarantee features of the Prudential Group's life assurance products. In the UK, guarantees of the with-profits products are valued for accounting purposes on a market consistent basis in 2007, 2008 and 2009 as described in section D2(f)(ii). The UK business also has products with guaranteed annuity option features, mostly within SAIF, as described in section D2(d). There is little exposure to financial options and guarantees in the shareholder-backed business of the UK operations. The US business annuity products have a variety of option and guarantee features as described in section D3(d). Jackson's derivative programme seeks to manage the exposures as described in section D3(e). The Prudential Group's exposure to guarantees was significantly reduced during 2009 as a result of the disposal of the Taiwan agency business.

d Sensitivity of EEV basis profit and equity for market and other risks

The Prudential Group prepares supplementary EEV basis financial information for half yearly and annual publication. These statements include sensitivity disclosures which are part of the market risk information provided to key management.

e Sensitivity of IFRS basis profit or loss and equity to market and other risks

i Overview of risks by business unit

The financial assets and liabilities attaching to the Prudential Group's life assurance business are, to varying degrees, subject to market and insurance risk and other changes of experience assumptions that may have a material effect on IFRS basis profit or loss and equity.

Market risk is the risk that the fair value or future cash flows of a financial instrument or, in the case of liabilities of insurance contracts, their carrying value will fluctuate because of changes in market prices. Market risk comprises three types of risk, namely:

- Currency risk: due to changes in foreign exchange rates;
- interest rate risk: due to changes in market interest rates; and
- other price risk: due to fluctuations in market prices (other than those arising from interest rate risk or currency risk).

Policyholder liabilities relating to the Prudential Group's life assurance businesses are also sensitive to the effects of other changes in experience, or expected future experience, such as for mortality, other insurance risk and lapse risk.

In addition, the profitability of the Prudential Group's life assurance businesses and, as described in Section E, asset management business, is indirectly affected by the performance of the assets covering policyholder liabilities and related capital.

Three key points are to be noted, namely:

- the Prudential Group's with-profit and unit-linked funds absorb most market risk attaching to the fund's investments. Except for second order effects, for example on asset management fees and shareholders' share of cost of bonuses for with-profits business, shareholder results are not directly affected by market value movements on the assets of these funds;
- the Prudential Group's shareholder results are most sensitive to market risks for assets of shareholder-backed business; and
- the main exposures of the Prudential Group's IFRS basis results to market risk for life assurance operations on investments of shareholder-backed business are for debt securities.

The most significant items for which the IFRS basis shareholders' profit or loss and equity for the Prudential Group's life assurance business is sensitive to these variables are shown in the following tables. The distinction between direct and indirect exposure is not intended to indicate the relative size of the sensitivity.

Type of business	Market and credit risk			
	Investments/derivatives	Liabilities/unallocated	Other exposure	Insurance and lapse risk
UK insurance operations (see also section D2(i))				
With-profits business (including Prudential Annuities Limited)	Net neutral direct exposure (Indirect exposure only)		Investment performance subject to smoothing through declared bonuses	Persistency risk to future shareholder transfers
SAIF sub-fund	Net neutral direct exposure (Indirect exposure only)		Asset management fees earned by M&G	

Type of business	Market and credit risk			Insurance and lapse risk
	Investments/derivatives	Liabilities/unallocated	Other exposure	
Unit-linked business	Net neutral direct exposure (Indirect exposure only) Asset/liability mismatch risk		Investment performance through asset management fees	Persistency risk
Shareholder-backed annuity business	Credit risk Interest rate risk for assets in excess of liabilities i.e. representing shareholder capital			Mortality experience and assumptions for longevity
US insurance operations (see also section D3(i))				
All business	Currency risk			Persistency risk
Variable annuity business	Net effect of market risk arising from incidence of guarantee features and variability of asset management fees offset by derivative hedging programme			
Fixed index annuity business	Derivative hedge programme to the extent not fully hedged against liability and fund performance	Incidence of equity participation features		
Fixed index annuity, Fixed annuity and GIC business	Credit risk Interest rate risk These risks are reflected in volatile profit or loss and shareholders' equity for derivative value movements and impairment losses, and, in addition, for shareholders' equity for value movements on fixed income securities classified as 'available for sale' under IAS 39		Spread difference between earned rate and rate credited to policyholders	Lapse risk but the effects of extreme events are mitigated by the use of swaption contracts
Asian insurance operations (see also section D4(i))				Mortality and morbidity risk
All business	Currency risk			Persistency risk
With-profits business	Net neutral direct exposure (Indirect exposure only)		Investment performance subject to smoothing through declared bonuses	
Unit-linked business	Net neutral direct exposure (Indirect exposure only)		Investment performance through asset management fees	
Non-participating business	Interest rate and price risk	Long-term interest rates		

ii IFRS shareholder results — Exposures for market and other risk

Key Group exposures

The IFRS operating profit based on longer-term investment returns for UK insurance operations has high potential sensitivity for changes to longevity assumptions affecting the carrying value of liabilities to policyholders for shareholder-backed annuity business. In addition, at the total IFRS profit level the result is sensitive to temporary value movements on assets backing IFRS equity.

For Jackson at the level of operating profit based on longer-term investment returns, the results are sensitive to market conditions to the extent of income earned on spread-based products and equity-based exposure not mitigated by the equity and interest derivative programmes. Further information is given below under the US operations section of market and credit risk.

Jackson's derivative programme is used to substantially mitigate equity market risk attaching to its equity-based products and interest rate risk associated with its spread-based products. Movements in interest rates and credit spreads materially affect the carrying value of derivatives which are used to manage the liabilities to policyholders and backing investment assets of fixed annuity and other general account business. Combined with the use of US GAAP measurement (as grandfathered under IFRS 4) for the asset and liabilities for the insurance contracts liabilities, which is largely insensitive to current period market movements, the Jackson total profit (i.e. including short-term fluctuations in investment returns) is very sensitive to market movements. In addition to these effects the Jackson IFRS equity is sensitive to the impact of interest rate and credit spread movements on the value of fixed income securities. Movements in unrealised appreciation on these securities are included as movement in equity (i.e. outside the income statement).

For Asian operations, the operating profit based on longer-term investment returns is mainly affected by the impact of market levels on unit-linked business persistency, and other insurance risk.

At the total IFRS profit level the Asian result is affected by short-term value movements on the asset portfolio for non-linked shareholder-backed business.

M&G profits are affected primarily by movements in the growth in funds under management and of the effect any impairment on the loan book and fair value movements on debt securities held by Prudential Capital.

Market and credit risk

UK insurance operations

With-profits business

- **With-profits business**

Shareholder results of UK with-profits business are sensitive to market risk only through the indirect effect of investment performance on declared policyholder bonuses.

The investment assets of the PAC with-profits fund are subject to market risk. However, changes in their carrying value, net of related changes to asset-share liabilities of with-profit contracts, affect the level of unallocated surplus of the fund. As unallocated surplus is accounted for as a liability under IFRS, movements in its value do not affect shareholders' profit or equity.

The shareholder results of the UK with-profits fund correspond to the shareholders' share of the cost of bonuses declared on the with-profits business. This currently corresponds to one-ninth of the cost of bonuses declared.

Investment performance is a key driver of bonuses, and hence the shareholders' share of cost of bonuses. Due to the 'smoothed' basis of bonus declaration the sensitivity to investment performance in a single year is low. However, over multiple periods it is important.

- Prudential Annuities Limited (PAL)

PAL's business is not with-profits, it writes annuity business. However, as PAL is owned by the PAC with-profits sub-fund, changes in the carrying value of PAL's assets and liabilities are reflected in the liability for unallocated surplus which as described above, do not affect shareholder results.

- Scottish Amicable Insurance Fund (SAIF)

SAIF is a ring-fenced fund in which, apart from asset management fees, shareholders have no interest. Accordingly, the Prudential Group's IFRS profit and equity are insensitive to the direct effects of market risk attaching to SAIF's assets and liabilities.

Shareholder-backed business

The factors that may significantly affect the IFRS results of UK shareholder-backed business are the mortality experience and assumptions and credit risk attaching to the annuity business of Prudential Retirement Income Limited and the PAC non-profit sub-fund.

- Prudential Retirement Income Limited (PRIL)

The assets covering PRIL's liabilities are principally debt securities and other investments that are held to match the expected duration and payment characteristics of the policyholder liabilities. These liabilities are valued for IFRS reporting purposes by applying discount rates that reflect the market rates of return attaching to the covering assets.

Except to the extent of any asset/liability duration mismatch which is reviewed regularly, and exposure to credit risk, the sensitivity of the Group's results to market risk for movements in the carrying value of PRIL's liabilities and covering assets is broadly neutral on a net basis.

The main market risk sensitivity for PRIL arises from interest rate risk on the debt securities which substantially represent IFRS equity. This equity comprises the net assets held within the long-term fund of the company that cover regulatory basis liabilities that are not recognised for IFRS reporting purposes, for example contingency reserves, and shareholder capital held outside the long-term fund.

The principal items affecting the IFRS results for PRIL are mortality experience and assumptions and credit risk.

- PAC non-profit sub-fund

The PAC non-profit sub-fund principally comprises annuity business previously written by SAL, credit life, unit-linked and other non-participating business.

The financial assets covering the liabilities for those types of business are subject to market risk. However, for the annuity business the same considerations as described above for PRIL apply, whilst the liabilities of the unit-linked business change in line with the matching linked assets. Other liabilities of the PAC non-profit sub-fund are broadly insensitive to market risk.

- Other shareholder-backed unit-linked business

Due to the matching of policyholder liabilities to attaching asset value movements the UK unit-linked business is not directly affected by market or credit risk. The principal factor affecting the IFRS results is investment performance through asset management fees.

US insurance operations (Jackson)

The IFRS basis results of Jackson are highly sensitive to market risk on the assets covering liabilities other than variable annuity business segregated in the separate accounts.

Invested assets covering liabilities (other than the separate accounts) and related capital comprise principally debt securities classified as available-for-sale. Value movements for these securities are reflected as movements in shareholders' equity through the statement of comprehensive income. Other invested assets and derivatives are carried at fair value with the value movements reflected in the income statement.

By contrast, the IFRS insurance liabilities for business written by Jackson, by the application of grandfathered GAAP under IFRS 4, are measured on US GAAP bases which with the exception of certain items covered by the equity hedging programme, are generally insensitive to temporary changes in market conditions or the short-term returns on the attaching asset portfolios.

These differences in carrying value of debt securities, other invested assets, derivatives and insurance liabilities give rise to potentially significant volatility in the IFRS income statement and shareholders' equity. As with other shareholder-backed business the profit or loss for Jackson is presented in the Prudential Group's segmental analysis of profit as described in note B1, by distinguishing the result for the year between an operating result based on longer-term investment returns and short-term fluctuations in investment returns. In this way the most significant direct effect of market changes that have taken place to the Jackson result are separately identified.

Excluding these short-term effects, the factors that most significantly affect the Jackson IFRS operating result based on long-term investment returns are:

- Variable annuity business — net effect of market risk arising from the incidence and valuation of guarantee features and variability of asset management fees offset by derivative hedging performance, in 2008 and 2009. The net effect of market risk in Jackson's guarantees and derivatives included in operating result excludes the impact of changes in market implied volatility in addition to those years. Further movements in reserves for guarantees reflected in operating result are also based on a discount rate using a long-term average Corporate AA credit curve instead of the actual Corporate AA credit curve at the valuation date. The derivative hedging programme is designed to be economically effective and there can be some accounting mis-matches for those guarantee features which are not economically valued under grandfathered US GAAP, for example guaranteed minimum death benefits. These accounting mis-matches are magnified in periods of market dislocation:
- fixed annuity business — the spread differential between the earned rate and the rate credited to policyholders; and
- fixed index annuity business — the spread differential between the earned rate and the rate credited to policyholders and incidence of equity index participation features, net of the related hedging performance.

In addition, the total profit for Jackson is affected by the level of impairment losses on the debt securities portfolios, short-term value movements on derivatives held to manage the fixed annuity and other general account business, other temporary value movements on portfolio investments classified as fair value through profit and loss, and those arising on revaluing the embedded derivative components of variable annuity liabilities for the effects of short-term movements in AA corporate bond rate curves and equity volatility levels.

Asian insurance operations

For Asian with-profits business the same features apply as described above for UK with-profits business. Similarly, as for other parts of the Prudential Group, for unit-linked business the main factor affecting IFRS basis results is investment performance through asset management fees.

The sensitivity of the IFRS basis results of the Prudential Group's Asian operations to market risk is primarily restricted to the non-participating business.

This sensitivity is primarily reflected through the volatility of asset returns coupled with the fact that the accounting carrying value of liabilities to policyholders are only partially sensitive to changed market conditions. As for UK shareholder-backed operations and Jackson, the IFRS profit is distinguished in the Prudential Group's segmental analysis so as to distinguish operating profits based on longer-term investment return and short-term fluctuations in investment returns.

Insurance and lapse risk

The features described above cover the main sensitivities of IFRS profit and loss and equity for market, insurance and credit risk. Lapse and longevity risk may also be a key determination of IFRS basis results with variable impacts.

In the UK, adverse persistency experience can affect the level of profitability from with-profits and unit-linked business.

For with-profits business in any given year, the amount represented by the shareholders' share of cost of bonus may be only marginally affected. However, altered persistency trends may affect future expected shareholder transfers.

By contrast, Prudential Group IFRS operating profit is particularly sensitive to longevity outlook that result in changes of assumption for the UK shareholder-backed annuity business.

Jackson is sensitive to lapse risk. However, Jackson uses swaption derivatives to ameliorate the effect of a sharp rise in interest rates, which would be the most likely cause of a sudden change in policyholder behaviour.

In Asia adverse persistency experience can impact the IFRS profitability of certain business written in the region. This risk is managed at a business unit level through monthly monitoring of experience and the implementation of management actions as necessary. These actions could include product enhancements, increased management focus on premium collection as well as other customer retention efforts. The potential financial impact of lapses is often mitigated through the specific features of the products, e.g. surrender charges.

iii Impact of diversification on risk exposure

The Prudential Group enjoys significant diversification benefits. This arises because not all risk scenarios will happen at the same time and across all geographic regions. The Prudential Group tests the sensitivities of results to different correlation factors such as:

Correlation across geographic regions

- Financial risk factors
- Non-financial risk factors.

Correlation across risk factors

- Longevity risk
- Expenses
- Persistency
- Other risks.

The effect of group diversification is to significantly reduce the aggregate standalone volatility risk to IFRS operating profit based on longer-term investment returns. The effect is almost wholly explained by the correlations across risk types, in particular longevity risk.

f Duration of liabilities

Under the terms of the Prudential Group's contracts, as for life assurance contracts generally, the contractual maturity date is the earlier of the end of the contract term, death, other insurable events or surrender. The Prudential Group has therefore chosen to provide details of liability duration that reflect the actuarially determined best estimate of the likely incidence of these factors on contract duration. Details are shown in sections D2(j), D3(j) and D4(j).

In the years 2005 to 2009, claims paid on the Prudential Group's life assurance contracts including those classified as investment contracts under IFRS 4 ranged from £13 billion to £19 billion. Indicatively, it is to be expected that, of the Prudential Group's policyholder liabilities (excluding unallocated surplus) at 31 December 2009 of £186.4 billion, the amounts likely to be paid in 2010 will be of a similar magnitude.

D2: UK insurance operations

a Summary statement of financial position

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type. In order to explain the different types of UK business and fund structure, the statement of financial position of the UK insurance operations may be analysed by the assets and liabilities of the Scottish Amicable Insurance Fund (SAIF), the PAC with-profits sub-fund, unit-linked assets and liabilities and annuity (principally PRIL) and other business. The assets and liabilities of these funds and subsidiaries as at 31 December are shown in the table below.

	UK insurance operations		PAC with-profits sub-fund note i				Other funds and subsidiaries			UK insurance operations
	2007 Total	2008 Total	Scottish Amicable Insurance Fund note ii	Excluding Prudential Annuities Limited	Prudential Annuities Limited note iii	Total note iv	Unit-linked assets and liabilities	Annuity and other long-term business	Total	2009 Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets										
Intangible assets attributable to shareholders:										
Deferred acquisition costs and other intangible assets	157	134	—	—	—	—	—	127	127	127
	157	134	—	—	—	—	—	127	127	127
Intangible assets attributable to PAC with-profits fund:										
In respect of acquired subsidiaries for venture fund and other investment purposes	192	174	—	124	—	124	—	—	—	124
Deferred acquisition costs	19	13	2	7	—	7	—	—	—	9
	211	187	2	131	—	131	—	—	—	133
Total	368	321	2	131	—	131	—	127	127	260
Deferred tax assets	105	513	2	84	70	154		136	136	292
Other non-investment and non-cash assets	4,110	4,962	419	1,020	344	1,364	547	744	1,291	3,074
Investments of long-term business and other operations:										
Investment properties	13,666	11,959	710	7,330	719	8,049	662	1,440	2,102	10,861
Investments accounted for using the equity method	—	—	—	—	—	—	—	4	4	4
Financial investments:										
Loans(note v)	1,245	1,902	138	825	143	968	—	709	709	1,815
Equity securities and portfolio holdings in unit trusts	60,829	38,880	2,994	23,062	215	23,277	10,757	23	10,780	37,051
Debt securities(note D2(c))	57,180	58,871	4,797	25,358	12,184	37,542	6,386	19,047	25,433	67,772
Other investments(note vi)	3,391	4,160	340	2,879	156	3,035	66	189	255	3,630
Deposits	7,228	6,090	869	8,378	377	8,755	550	1,383	1,933	11,557
Total investments	143,539	121,862	9,848	67,832	13,794	81,626	18,421	22,795	41,216	132,690
Properties held for sale	30	—	—	—	—	—	—	—	—	—
Cash and cash equivalents	1,869	2,571	214	948	34	982	939	130	1,069	2,265
Total assets	150,021	130,229	10,485	70,015	14,242	84,257	19,907	23,932	43,839	138,581

	UK insurance operations		PAC with-profits sub-fund note i				Other funds and subsidiaries			UK insurance operations
	2007 Total	2008 Total	Scottish Amicable Insurance Fund note ii	Excluding Prudential Annuities Limited	Prudential Annuities Limited note iii	Total note iv	Unit-linked assets and liabilities	Annuity and other long-term business	Total	2009 Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Equity and liabilities										
Equity										
Shareholders' equity	1,364	1,655	—	—	—	—	—	1,939	1,939	1,939
Minority interests	42	47	—	28	—	28	—	—	—	28
Total equity	1,406	1,702	—	28	—	28	—	1,939	1,939	1,967
Liabilities										
Policyholder liabilities and unallocated surplus of with-profits funds:										
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	124,477	107,707	9,972	55,588	11,969	67,557	19,035	19,665	38,700	116,229
Unallocated surplus of with-profits funds (reflecting application of 'realistic' provisions for UK regulated with-profits funds)	13,813	8,254	—	8,421	1,545	9,966	—	—	—	9,966
Total	138,290	115,961	9,972	64,009	13,514	77,523	19,035	19,665	38,700	126,195
Operational borrowings attributable to shareholder-financed operations	12	54	—	—	—	—	—	158	158	158
Borrowings attributable to with-profits funds	987	1,308	118	1,166	—	1,166	—	—	—	1,284
Deferred tax liabilities	2,383	1,421	66	807	281	1,088	—	452	452	1,606
Other non-insurance liabilities	6,943	9,783	329	4,005	447	4,452	872	1,718	2,590	7,371
Total liabilities	148,615	128,527	10,485	69,987	14,242	84,229	19,907	21,993	41,900	136,614
Total equity and liabilities	150,021	130,229	10,485	70,015	14,242	84,257	19,907	23,932	43,839	138,581

Notes

i For the purposes of this table and subsequent explanation, references to the PAC WPSF also include, for convenience, the amounts attaching to the Defined Charges Participating Sub-fund, which includes the with-profits annuity business transferred to Prudential from the Equitable Life Assurance Society on 1 December 2007 (with assets of approximately £1.7 billion at that date). Profits to shareholders on this with-profits annuity business emerge on a 'charges less expenses' basis and policyholders are entitled to 100% of the investment earnings.

ii SAIF is a separate sub-fund within the PAC long-term business fund.

iii Wholly-owned subsidiary of the PAC WPSF that writes annuity business.

iv Excluding policyholder liabilities of the Hong Kong branch of PAC.

v The loans of the Group's UK insurance operations of £1,245 million, £1,902 million and £1,815 million as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise loans held by the PAC WPSF of £946 million, £1,345 million and £1,106 million, for 31 December 2007, 31 December 2008 and 31 December 2009 respectively, and loans held by shareholder-backed business of £299 million, £557 million, and £709 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. The loans held by the PAC WPSF at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise mortgage loans of £156 million, £150 million and £145 million, policy loans of £35 million, £29 million and £24 million and other loans of £755 million, £1,166 million and £937 million respectively. The mortgage loans are collateralised by properties. Other loans held by the PAC with-profits fund are all commercial loans and comprise mainly syndicated loans. The loans held by the UK shareholder-backed business at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise mortgage loans collateralised by properties of £293 million, £551 million, and £702 million and other loans of £6 million, £6 million and £7 million.

vi Other investments comprise:

	2007	2008	2009
	£m	£m	£m
Derivative assets*(note G3)	571	1,326	910
Partnerships in investment pools and other**	2,820	2,834	2,720
	3,391	4,160	3,630

* In the UK, Prudential uses derivatives to reduce equity and credit risk, interest rate and currency exposures, and to facilitate efficient portfolio management. After derivative liabilities of £689 million, £3,401 million and £709 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which are also included in the statement of financial position, the overall derivative position was a net liability of £118 million, a

net liability of £2,075 million, and a net asset of £201 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

** Partnerships in investment pools and other comprise mainly investments held by the PAC with-profits fund. These investments are primarily venture fund investments and investment in property funds and limited partnerships.

b Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of UK insurance operations from the beginning of the year to the end of the year is as follows:

	SAIF and PAC with-profits sub-fund	Other funds and Subsidiaries		UK insurance operations Total
		Unit-linked liabilities	Annuity and other long-term business	
	£m	£m	£m	£m
At 1 January 2007	101,616	18,187	14,101	133,904
Premiums	4,459	2,115	2,279	8,853
Surrenders	(2,879)	(1,636)	(13)	(4,528)
Maturities/Deaths	(4,987)	(790)	(1,010)	(6,787)
Net cash flows	(3,407)	(311)	1,256	(2,462)
Shareholders transfers post tax	(279)	—	—	(279)
Switches	(352)	352	—	—
Assumption changes (shareholder-backed business)(note D2(h), note c)	—	—	(34)	(34)
Investment-related items and other movements	6,256	749	223	7,228
Foreign exchange translation differences	(62)	—	(5)	(67)
At 31 December 2007/1 January 2008	103,772	18,977	15,541	138,290
Premiums	3,157	2,435	3,780	9,372
Surrenders	(2,336)	(1,838)	(107)	(4,281)
Maturities/Deaths	(6,309)	(666)	(1,349)	(8,324)
Net cash flows (note a)	(5,488)	(69)	2,324	(3,233)
Shareholders transfers post tax	(284)	—	—	(284)
Switches	(360)	360	—	—
Assumption changes (shareholder-backed business)(note D2(h), note c)	—	—	447	447
Investment-related items and other movements(note b)	(13,049)	(2,952)	(777)	(16,778)
Foreign exchange translation differences	(2,483)	2	—	(2,481)
At 31 December 2008/1 January 2009	82,108	16,318	17,535	115,961
Premiums	3,271	1,860	1,736	6,867
Surrenders	(2,394)	(1,535)	(42)	(3,971)
Maturities/Deaths	(5,147)	(670)	(1,422)	(7,239)
Net cash flows(note a)	(4,270)	(345)	272	(4,343)
Shareholders transfers post tax	(202)	—	—	(202)
Switches	(270)	270	—	—
Assumption changes (shareholder-backed business)(note D2(h), note c)	—	—	(46)	(46)
Investment-related items and other movements(note b)	9,365	2,849	1,904	14,118
Foreign exchange translation differences	764	(57)	—	707
At 31 December 2009	87,495	19,035	19,665	126,195

Notes

(a) Net cash flows of negative £4,343 million have increased from negative £3,233 million in 2008, principally as a result of a decrease in premiums following the decision to limit bulk annuity transactions in the period.

(b) Investment-related items and other movements of £14,118 million across fund types reflected the strong performance of UK equity markets in 2009, as well as the increase in value of debt securities and the reversal of unrealised losses on property investments recorded in 2008.

(c) Assumption changes principally represent the net impact of changes to the deflation reserve, expense assumptions and modelling changes.

c Information on credit risk of debt securities

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type. The following table summarises by rating the securities held by UK insurance operations as at 31 December:

	UK insurance Operations		Scottish Amicable Insurance Fund	PAC with-profits sub-fund			Other funds and subsidiaries			UK insurance operations
			2009							
	2007 Total	2008 Total		Excluding Prudential Annuities Limited	Prudential Annuities Limited	Total	Unit-linked assets and liabilities	PRIL	Other annuity and long-term business	2009 Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
S&P — AAA	21,556	18,981	1,018	4,594	2,531	7,125	2,451	4,702	795	16,091
S&P — AA+ to AA−	6,173	6,012	399	2,242	1,131	3,373	765	1,716	219	6,472
S&P — A+ to A−	12,557	15,929	1,210	6,954	3,685	10,639	1,788	5,366	690	19,693
S&P — BBB+ to BBB−	5,409	7,413	1,124	6,141	1,287	7,428	905	2,276	450	12,183
S&P — Other	942	1,033	316	1,618	168	1,786	360	182	23	2,667
	46,637	49,368	4,067	21,549	8,802	30,351	6,269	14,242	2,177	57,106
Moody's — Aaa	1,021	681	59	252	51	303	4	76	21	463
Moody's — Aa1 to Aa	587	833	18	108	40	148	—	85	25	276
Moody's — A1 to A3	944	678	36	181	290	471	—	251	43	801
Moody's — Baa1 to Baa3	490	454	65	324	258	582	—	141	27	815
Moody's — Other	410	162	27	140	61	201	—	102	9	339
	3,452	2,808	205	1,005	700	1,705	4	655	125	2,694
Fitch	682	560	46	300	331	631	—	314	31	1,022
Other	6,409	6,135	479	2,504	2,351	4,855	113	1,423	80	6,950
Total debt securities	57,180	58,871	4,797	25,358	12,184	37,542	6,386	16,634	2,413	67,772

Where no external ratings are available, internal ratings produced by the Prudential Group's asset management operation, which are prepared on Prudential assessment of a comparable basis to external ratings, are used where possible. Of the £6,409 million, £6,135 million and £6,950 million total debt securities held at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which are not externally rated, £2,972 million, £2,325 million and £2,190 million were internally rated AAA to A-, £2,844 million, £3,149 million and £3,445 million were internally rated BBB to B- and £593 million, £661 million and £1,315 million were rated below B- or unrated. The majority of unrated debt security investments were held in SAIF and the PAC with-profits fund and relate to convertible debt and other investments which are not covered by ratings analysts nor have an internal rating attributed to them. Of the £1,503 million PRIL and other annuity and long-term business investments which are not externally rated, £15 million were internally rated AAA, £88 million AA, £495 million A, £647 million BBB, £123 million BB and £135 million were internally rated B+ and below at 31 December 2009.

As detailed in note D2(i) below, the primary sensitivity of IFRS basis profit or loss and shareholders' equity relates to non-linked shareholder-backed business which covers "PRIL" and "other annuity and long-term business" in the table above.

d Products and guarantees

Prudential's long-term products in the UK consist of life insurance, pension products and pension annuities.

These products are written primarily in:

- One of three separate sub-funds of the PAC long-term fund, namely the with-profits sub-fund, SAIF, and the non-profit sub-fund;
- Prudential Annuities Limited, which is owned by the PAC with-profits sub-fund;
- Prudential Retirement Income Limited, a shareholder-owned subsidiary; or
- Other shareholder-backed subsidiaries writing mainly non-profit unit-linked business.

i With-profits products and PAC with-profits sub-fund

Within the statement of financial position of UK insurance operations at 31 December 2007, 31 December 2008 and 31 December 2009, as shown in note D2(a), there are policyholder liabilities and unallocated surplus of £90.5 billion, £72.1 billion and £77.5 billion, respectively, that relate to the WPSF. These amounts include the liabilities and capital of

Prudential Annuities Limited, a wholly owned subsidiary of the fund. The WPSF mainly contains with-profits business but it also contains some non-profit business (unit-linked, term assurances and annuities). The WPSF's profits are apportioned 90% to its policyholders and 10% to shareholders as surplus for distribution is determined via the annual actuarial valuation.

The WPSF held a provision of £45 million at 31 December 2007, £42 million at 31 December 2008 and £31 million at 31 December 2009 to honour guarantees on a small amount of guaranteed annuity products. SAIF's exposure to guaranteed annuities is described below.

Beyond the generic guarantees described above, there are very few explicit options or guarantees such as minimum investment returns, surrender values or annuities at retirement and any granted have generally been at very low levels.

With-profits products provide returns to policyholders through bonuses that are 'smoothed'. There are two types of bonuses: 'annual' and 'final'. Annual bonuses are declared once a year, and once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, final bonuses are guaranteed only until the next bonus declaration.

The main factors that influence the determination of bonus rates are the return on the investments of the with-profits fund, inflation, taxation, the expenses of the fund chargeable to policyholders and the degree to which investment returns are smoothed. The overall rate of return earned on investments and the expectation of future investment returns are the most important influences on bonus rates. A high proportion of the assets backing the with-profits business are invested in equities and real estate. If the financial strength of the with-profits business is affected, then a higher proportion of fixed interest or similar assets might be held by the fund.

Further details on the determination of the two types of the bonuses: "regular" and "final", the application of significant judgement, key assumptions and the degree of smoothing of investment returns in determining the bonus rates are provided below.

Regular bonus rates

For regular bonuses, the bonus rates are determined for each type of policy primarily by targeting the bonus level at a prudent proportion of the long-term expected future investment return on underlying assets. The expected future investment return is reduced as appropriate for each type of policy to allow for items such as expenses, charges, tax and shareholders' transfers. However, the rates declared may differ by product type, or by the date of payment of the premium or date of issue of the policy or if the accumulated annual bonuses are particularly high or low relative to a prudent proportion of the achieved investment return.

When target bonus levels change the PAC board has regard to the overall strength of the long-term fund when determining the length of time over which it will seek to achieve the amended prudent target bonus level.

In normal investment conditions, PAC expects changes in regular bonus rates to be gradual over time, and these are not expected to exceed 1% per annum over any year. However, the PAC Directors retain the discretion whether or not to declare a regular bonus each year, and there is no limit on the amount by which regular bonus rates can change.

Final bonus rates

A final bonus which is normally declared yearly, may be added when a claim is paid or when units of a unitised product are realised.

The rates of final bonus usually vary by type of policy and by reference to the period, usually a year, in which the policy commences or each premium is paid. These rates are determined by reference to the asset shares for the sample policies but subject to the smoothing approach, explained below.

In general, the same final bonus scale applies to maturity, death and surrender claims except that:

- the total surrender value may be impacted by the application of a Market Value Reduction — MVR — (for accumulating with-profits policies) and is affected by the surrender bases (for conventional with-profits business); and

- for the SAIF and Scottish Amicable Life ("SAL"), the final bonus rates applicable on surrender may be adjusted to reflect expected future bonus rates.

Application of significant judgement

The application of the above method for determining bonuses requires the PAC board of directors to apply significant judgement in many respects, including in particular the following:

- Determining what constitutes fair treatment of customers: Prudential is required by UK law and regulation to consider the fair treatment of its customers in setting bonus levels. The concept of determining what constitutes fair treatment, while established by statute, is not defined.
- Smoothing of investment returns: This is an important feature of with-profits products. Determining when particular circumstances, such as a significant rise or fall in market values, warrant variations in the standard bonus smoothing limits that apply in normal circumstances requires the PAC Board to exercise significant judgement.
- Determining at what level to set bonuses to ensure that they are competitive: The overall return to policyholders is an important competitive measure for attracting new business.

Key assumptions

As noted above, the overall rate of return on investments and the expectation of future investment returns are the most important influences in bonus rates, subject to the smoothing described below. Prudential determines the assumptions to apply in respect of these factors, including the effects of reasonably likely changes in key assumptions, in the context of the overarching discretionary and smoothing framework that applies to its with-profits business as described above. As such, it is not possible to specifically quantify the effects of each of these assumptions or of reasonably likely changes in these assumptions.

Prudential's approach, in applying significant judgement and discretion in relation to determining bonus rates, is consistent conceptually with the approach adopted by other firms that manage a with-profits business. It is also consistent with the requirements of UK law, which require all UK firms that carry out a with-profits business to define, and make publicly available, the Principles and Practices of Financial Management ("PPFM") that are applied in the management of their with-profits funds.

Accordingly, Prudential's PPFM contains an explanation of how it determines regular and final bonus rates within the discretionary framework that applies to all with-profits policies, subject to the general legislative requirements applicable. The purpose of Prudential's PPFM is therefore to:

- explain the nature and extent of the discretion available;
- show how competing or conflicting interests or expectations of:

  — different groups and generations of policyholders, and

  — policyholders and shareholders are managed so that all policyholders and shareholders are treated fairly, and
- provide a knowledgeable observer (e.g. a financial adviser) with an understanding of the material risks and rewards from starting and continuing to invest in a with-profits policy with Prudential.

Furthermore, in accordance with industry-wide regulatory requirements, the PAC board has appointed:

- an Actuarial Function Holder who provides the PAC board with all actuarial advice;
- a With-Profits Actuary whose specific duty is to advise the PAC board on the reasonableness and proportionality of the manner in which its discretion has been exercised in applying the PPFM and the manner in which any conflicting interests have been addressed; and
- a With-Profits Committee of independent individuals, which assesses the degree of compliance with the PPFM and the manner in which conflicting rights have been addressed.

Smoothing of investment return

In determining bonus rates for the UK with-profits policies, smoothing is applied to the allocation of the overall earnings of the UK with-profits fund of which the investment return is a significant element. The smoothing approach differs between accumulating and conventional with-profits policies to reflect the different contract features. In normal circumstances, Prudential does not expect most payout values on policies of the same duration to change by more than 10% up or down from one year to the next, although some larger changes may occur to balance payout values between different policies. Greater flexibility may be required in certain circumstances, for example following a significant rise or fall in market values, and in such situations the PAC board may decide to vary the standard bonus smoothing limits in order to protect the overall interests of policyholders.

The degree of smoothing is illustrated numerically by comparing in the following table the relatively "smoothed" level of policyholder bonuses declared as part of the surplus for distribution with the more volatile movement in investment return and other items of income and expenditure of the UK component of the PAC with-profits fund for each period presented.

	2007	2008	2009
	£m	£m	£m
Net income of the fund:			
Investment return	5,881	(14,595)	**10,461**
Claims incurred	(6,512)	(7,068)	**(6,253)**
Movement in policyholder liabilities	(2,307)	13,504	**(3,692)**
Add back policyholder bonuses for the year (as shown below)	2,522	2,565	**1,827**
Claims incurred and movement in policyholder liabilities (including charge for provision for asset shares and excluding policyholder bonuses)	(6,297)	9,001	**(8,118)**
Earned premiums, net of reinsurance	4,181	2,927	**3,063**
Other income	1,417	(36)	**(2)**
Acquisition costs and other operating expenditure	(2,105)	(408)	**(842)**
Tax credit (charge)	(24)	1,191	**(640)**
Net income of the fund before movement in unallocated surplus	3,053	(1,920)	**3,922**
Movement in unallocated surplus	(252)	4,769	**(1,893)**
Surplus for distribution	2,801	2,849	**2,029**
Surplus for distribution allocated as follows:			
— 90% policyholders bonus (as shown above)	2,522	2,565	**1,827**
— 10% shareholders' transfers	279	284	**202**
	2,801	2,849	**2,029**

ii Annuity business

Prudential's conventional annuities include level, fixed increase and retail price index (RPI) annuities. They are mainly written within the subsidiaries PAL, PRIL, Prudential Pensions Limited and the PAC with-profits sub-fund, but there are some annuity liabilities in the non-profit sub-fund and SAIF.

Prudential's fixed-increase annuities incorporate automatic increases in annuity payments by fixed amounts over the policyholder's life. The RPI annuities that the Prudential Group offers provide for a regular annuity payment to which an additional amount is added periodically based on the increase in the UK RPI.

Prudential's with-profits annuities, which are written in the WPSF, combine the income features of annuity products with the investment smoothing features of with-profits products and enable policyholders to obtain exposure to investment return on the WPSF's equity shares, property and other investment categories over time. Policyholders select an 'anticipated bonus' from the specific range the Prudential Group offers for the particular product. The amount of the annuity payment each year depends upon the relationship between the anticipated bonus rate selected by the policyholder when the product is purchased and the bonus rates the Prudential Group subsequently declares each year during the term of the product. If the total bonus rates fall below the anticipated rate, then the annuity income falls.

At 31 December 2007, 31 December 2008 and 31 December 2009, £29.5 billion, £29.4 billion and £32.3 billion, respectively, of investments relate to annuity business of PAL and PRIL. These investments are predominantly in debt securities (including retail price index-linked bonds to match retail price index-linked annuities), loans and deposits and are duration matched with the estimated duration of the liabilities they support.

iii SAIF

SAIF is a ring-fenced sub-fund of the PAC long-term fund formed following the acquisition of the mutually owned Scottish Amicable Life Assurance Society in 1997. No new business may be written in SAIF, although regular premiums are still being paid on policies in force at the time of the acquisition and incremental premiums are permitted on these policies.

The fund is solely for the benefit of policyholders of SAIF. Shareholders have no interest in the profits of this fund although they are entitled to asset management fees on this business.

The process for determining policyholder bonuses of SAIF with-profits policies, which constitute the vast majority of obligations of the funds, is similar to that for the with-profits policies of the WPSF. However, in addition, the surplus assets in SAIF are allocated to policies in an orderly and equitable distribution over time as enhancements to policyholder benefits i.e. in excess of those based on asset share.

Provision is made for the risks attaching to some SAIF unitised with-profits policies that have MVR-free dates and for those SAIF products which have a guaranteed minimum benefit on death or maturity of premiums accumulated at 4% per annum.

The Prudential Group's main exposure to guaranteed annuities in the UK is through SAIF and a provision of £563 million, £391 million, and £284 million was held in SAIF at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, to honour the guarantees. As SAIF is a separate sub-fund solely for the benefit of policyholders of SAIF this provision has no impact on the financial position of the Prudential Group's shareholders' equity.

iv Unit-linked (non-annuity) and other non-profit business

The Prudential Group's UK insurance operations also have an extensive book of unit-linked policies of varying types and provide a range of other non-profit business such as credit life and protection contracts. These contracts do not contain significant financial guarantees.

There are no guaranteed maturity values or guaranteed annuity options on unit-linked policies except for minor amounts for certain policies linked to cash units within SAIF.

e Exposure to market risk

i Non-linked life and pension business

For with-profits business, the absence of guaranteed surrender values and the flexibility given by the operation of the bonus system means that a high proportion of the investments backing the with-profits business are in equities and real estate with the balance in debt securities, deposits and loans.

The investments supporting the protection business are small in value and tend to be assets with a fixed term duration reflecting the guaranteed nature of the liabilities.

ii Pension annuity business

Prudential's UK annuity business mainly employs fixed income investments (including UK retail price index-linked assets) because the liabilities consist of guaranteed payments for as long as each annuitant or surviving partner is alive. Retail price index-linked assets are used to back pension annuities where the payments are linked to the RPI.

iii Unit-linked business

Except through the second order effect on asset management fees, the unit-linked business of the UK insurance operations is not exposed to market risk. The lack of exposure arises from the contract nature whereby policyholder benefits reflect asset value movements of the unit-linked funds.

f Process for setting assumptions and determining contract liabilities

i Overview

The calculation of the contract liabilities involves the setting of assumptions for future experience. This is done following detailed review of the relevant experience including, in particular, mortality, expenses, tax, economic assumptions and where applicable, persistency.

For with-profits business written in the WPSF or SAIF, a market consistent valuation is performed (as described in section (ii) below). Additional assumptions required are for persistency and the management actions under which the fund is managed. Assumptions used for a market consistent valuation typically do not contain margins, whereas those used for the valuation of other classes of business do.

Mortality assumptions are set based on the results of the most recent experience analysis looking at the experience over recent years of the relevant business. For non-profit business, a margin for adverse deviation is added. Different assumptions are applied for different product groups. For annuitant mortality, assumptions for current mortality rates are based on recent experience investigations and expected future improvements in mortality. The expected future improvements are based on recent experience and projections of the business and industry experience generally.

Maintenance and, for some classes of business, termination expense assumptions are expressed as per policy amounts. They are set based on the expenses incurred during the year, including an allowance for ongoing investment expenditure and allocated between entities and product groups in accordance with the operation's internal cost allocation model. For non-profit business a margin for adverse deviation is added to this amount. Expense inflation assumptions are set consistent with the economic basis and based on the difference between yields on nominal gilts and index-linked gilts.

The actual renewal expenses charged to SAIF continued to be based on the tariff arrangement specified in the Scottish Amicable Life Assurance Society Scheme up to 31 December 2007, when the tariff arrangement terminated. This provided an additional margin in SAIF as the unit costs derived from actual expenses (and used to derive the recommended assumptions) were generally significantly greater than the tariff costs.

From 1 January 2008, when the previous tariff arrangement terminated, the actual renewal expenses incurred on behalf of SAIF by other group companies are recharged in full to SAIF.

The assumptions for asset management expenses are based on the charges specified in agreements with the Prudential Group's asset management operations, plus a margin for adverse deviation for non-profit business.

Tax assumptions are set equal to current rates of taxation.

For non-profit business excluding unit-linked business, the valuation interest rates used to discount the liabilities are based on the yields as at the valuation date on the assets backing the technical provisions. For fixed interest securities the gross redemption yield is used except for the PAL and PRIL annuity business where the internal rate of return of the assets backing the liabilities is used. Properties are valued using the rental yield, and for equities it is the greater of the dividend yield and the average of the dividend yield and the earnings yield. An adjustment is made to the yield on non risk-free fixed interest securities and property to reflect credit risk. To calculate the non-unit reserves for linked business, assumptions have been set for the gross unit growth rate and the rate of inflation of maintenance expenses, as well as for the valuation interest rate as described above.

ii WPSF and SAIF

The policyholder liabilities reported for the WPSF are primarily for two broad types of business. These are accumulating and conventional with-profits contracts. The policyholder liabilities of the WPSF are accounted for under FRS 27.

The provisions have been determined on a basis consistent with the detailed methodology included in regulations contained in the FSA's rules for the determination of reserves on the FSA's 'realistic' Peak 2 basis. In aggregate, the regime has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances. These contracts are a combination of insurance and investment contracts with discretionary participation features, as defined by IFRS 4.

The FSA's Peak 2 calculation under the realistic regime requires the value of liabilities to be calculated as:

- the with-profits benefits reserve (WPBR); plus
- future policy related liabilities (FPRL); plus
- the realistic current liabilities of the fund.

The WPBR is primarily based on the retrospective calculation of accumulated asset shares but is adjusted to reflect future expected policyholder benefits and other outgoings. Asset shares are calculated as the accumulation of all items of income and outgo that are relevant to each policy type. Income comprises credits for premiums, investment returns (including unrealised gains), and miscellaneous profits. Outgo comprises charges for tax (including an allowance for tax on unrealised gains), guarantees and smoothing, mortality and morbidity, shareholders' profit transfers, miscellaneous losses, and expenses and commission (net of any tax relief).

The FPRL must include a market consistent valuation of costs of guarantees, options and smoothing, less any related charges, and this amount must be determined using either a stochastic approach, hedging costs or a series of deterministic projections with attributed probabilities.

The assumptions used in the stochastic models are calibrated to produce risk-free returns on each asset class. Volatilities of, and correlations between, investment returns from different asset classes are as determined by the Group's Portfolio Management Group and aim to be market consistent.

The cost of guarantees, options and smoothing is very sensitive to the bonus, market value reduction ("MVR"), and investment policy employed and therefore the stochastic modelling incorporates a range of management actions that would help to protect the fund in adverse investment scenarios. Substantial flexibility has been included in the modelled management actions in order to reflect the discretion that is retained in adverse investment conditions, thereby avoiding the creation of unreasonable minimum capital requirements. The management actions assumed are consistent with the Prudential Group's management policy for with-profits funds and the Prudential Group's disclosures in the publicly available PPFM.

The contract liabilities for with-profits business also require assumptions for persistency. These are set based on the results of recent experience analysis.

iii Annuity business

Credit risk provisions

For IFRS reporting, the results for UK shareholder-backed annuity business are particularly sensitive to the allowances made for credit risk. The allowance is reflected in the deduction from the valuation rate of interest for discounting projected future annuity payments to policyholders that would have otherwise applied. Since mid-2007 there has been a significant increase in the actual and perceived credit risk associated with corporate bonds as reflected in the significant widening that has occurred in corporate bond spreads. Although bond spreads over swap rates have narrowed from their peak in March 2009, they are still high compared with the levels seen in the years immediately preceding the start of the dislocated markets in 2007. The allowance that should therefore be made for credit risk remains a particular area of judgement.

The additional yield received on corporate bonds relative to swaps can be broken into the following constituent parts:

— the expected level of future defaults;

— the credit risk premium that is required to compensate for the potential volatility in default levels; and

— the liquidity premium that is required to compensate for the lower liquidity of corporate bonds relative to swaps

The credit risk allowance is a function of the asset mix and the credit quality of the underlying portfolio. At 31 December 2008 and 2009, respectively, 75% and 80% of the assets backing the shareholder annuity and other business were debt securities as shown in D2(a). This comprises both government and corporate bonds. Government bonds are generally given a credit default allowance of zero. For corporate bonds the credit allowance varies by credit rating. An analysis of the credit ratings of debt securities is included in note D2(c).

Given that the normal business model for Prudential's annuity business is to hold bonds to match long-term liabilities, the valuation rate that is applied includes a liquidity premium that reflects the residual element of current bond spreads over swap rates after providing for the credit risk.

Historically, until the second half of 2007, when corporate bond spreads widened significantly, the allowance for credit risk was calculated as the long-term expected defaults and a long-term credit risk premium. This long-term credit risk was supplemented by a short-term allowance from 31 December 2007 to allow for the concern that credit ratings applied by the rating agencies may be downgraded and defaults in the short term might be higher than the long-term assumptions.

The weighted components of the bond spread over swap rates for shareholder-backed fixed and linked annuity business for PRIL at 31 December 2007, 31 December 2008 and 31 December 2009 based on the asset mix at the relevant balance sheet date are as follows:

	2007		
	Pillar 1 Regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)
Bond spread over swap rates(note i)	76	—	76
Credit risk allowance			
Long-term expected defaults(note ii)	13	—	13
Long-term credit risk premium(note iii)	10	(3)	7
Short-term allowance for credit risk(note iv)	10	(10)	—
Total credit risk allowance	33	(13)	20
Liquidity premium	43	13	56

	2008		
	Pillar 1 Regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)
Bond spread over swap rates(note i)	323	—	323
Credit risk allowance			
Long-term expected defaults(note ii)	15	—	15
Long-term credit risk premium(note iii)	11	—	11
Short-term allowance for credit risk(note iv)	54	(25)	29
Total credit risk allowance	80	(25)	55
Liquidity premium	243	25	268

	2009		
	Pillar 1 Regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)
Bond spread over swap rates(note i)	175	—	175
Credit risk allowance			
Long-term expected defaults(note ii)	19	—	19
Long-term credit risk premium(note iii)	13	—	13
Short-term allowance for credit risk(note iv)	39	(24)	15
Total credit risk allowance	71	(24)	47
Liquidity premium	104	24	128

Notes

i Bond spread over swap rates reflect market observed data.

ii Long-term expected defaults are derived by applying Moody's data from 1970 to 2004 uplifted by between 100% (B) and 200% (AAA) according to credit rating on the annuity asset portfolio. The credit rating assigned to each asset held is based on external credit rating and for this purpose the credit rating assigned to each asset held is the lowest credit rating published by Moody's, Standard and Poors and Fitch.

iii The long-term credit risk premium provides compensation against the risk of potential volatility in the level of defaults and is derived by applying the 95th percentile from Moody's data from 1970 to 2004 to the annuity asset portfolio.

iv During the second half of 2007, corporate bond spreads widened significantly and the methodology was reviewed to ensure that it still made appropriate allowance for credit risk. As a result of this review a short-term allowance for credit risk was established in the Pillar 1 reserves at 31 December 2007 to allow for the concern that credit ratings applied by rating agencies to individual bonds might be over optimistic and that default experience in the short-term might be higher than the long-term assumptions.

The short-term allowance for credit risk assumed in the Pillar 1 solvency valuations at 31 December 2007 and 31 December 2008 were determined as 25% of the increase in corporate bond spreads (as estimated from the movements in published corporate bond indices) since 31 December 2006.

The very prudent Pillar 1 regulatory basis reflects the overriding objective of ensuring sufficient provisions and capital to ensure payments to policyholders can be made. The approach for IFRS, on the other hand, aims to establish liabilities that are closer to 'best estimate'. In years prior to 2008 long-term IFRS default assumptions had been set mid-way between the EEV and Pillar 1 assumptions. At 31 December 2008, in light of the increased uncertainty surrounding future credit default experience, the IFRS long-term assumptions were strengthened to bring them into line with the long-term Pillar 1 default assumptions. In addition a short-term allowance for credit risk was established but at a lower level than allowed for in the Pillar 1 regulatory basis.

Factors affecting the credit risk allowance at 31 December 2009

The main factors influencing the credit risk allowance at 31 December 2009 are as follows:

a) Credit downgrades and default experience

As highlighted above, the short term allowance at 31 December 2008 was intended to cover both short term credit downgrades and losses in excess of the longer term expectations. Downgrades in 2009 have been within the opening Pillar 1 assumptions and hence the increase in the long term allowance as a result of credit downgrades has been offset by an equal decrease in the short term allowance. Defaults for the UK shareholder-backed annuity business totaled £11 million during 2009, below the amount allowed for within the short term allowance. The allowance (in bps terms) has been adjusted to eliminate any experience profits that would have otherwise arisen.

b) Asset trading in relation to subordinated financial debt

During the second half of 2009, the Prudential Group decided to trade out of subordinated financial debt into higher quality assets. This resulted in a gross transaction loss arising from the lower expected yield on the newly purchased assets. The reduction in subordinated financial debt holdings improved the overall credit quality of the corporate bond portfolio and so allowed a release of long-term credit reserves to offset this loss. In addition the allowance for the short-term defaults above has been notionally allocated to the highest yielding assets and so the allowance attaching to the subordinated debt sold has also been released.

On a Pillar 1 basis this transaction had no overall impact on the solvency surplus of PRIL, the PAC non-participating sub-fund and PAL. On an IFRS basis, a lower short-term default reserve was held at 31 December 2008 and the release of the reserves in respect of the subordinated debt is therefore lower. Overall the reduction in subordinated financial debt holdings generated a pre-tax IFRS operating loss of £51 million.

c) Asset purchases in respect of new business

The assets purchased during 2009 to back new business have been of better average credit quality than the assets held at 31 December 2008, in particular no subordinated bank debt or sub-investment grade assets have been bought to back new business. As a result of the lower credit risk of the new business assets, the overall allowance for credit risk required at 31 December 2009 is reduced when the new business assets and in-force assets are aggregated together.

d) Overall impact on the PRIL credit risk allowance

After taking account of the factors noted above the movement on the average basis points allowances for PRIL on the Pillar 1 regulatory and IFRS bases are as follows:

	Pillar 1 Regulatory basis (bps)			IFRS (bps)		
	Long term	**Short term**	**Total**	**Long term**	**Short term**	**Total**
Total allowance for credit risk at 31 December 2008	26	54	80	26	29	55
Credit downgrades	14	(14)	—	14	(14)	—
Retention of surplus from favourable default experience	—	5	5	—	1	1
Asset trading	(8)	(4)	(12)	(8)	(1)	(9)
New business	—	(2)	(2)	—	(1)	(1)
Other	—	—	—	—	1	1
Total allowance for credit risk at 31 December 2009	32	39	71	32	15	47

Overall this has led to the credit allowance for Pillar 1 purposes to be 41% (2008: 25%) of the bond spread over swap rates. For IFRS purposes it represents 27% of the bond spread over swap rates (2008: 17%).

Mortality

The mortality assumptions are set in light of recent population and internal experience. The assumptions used are percentages of standard actuarial mortality tables with an allowance for future mortality improvements. Where annuities have been sold on an enhanced basis to impaired lives an additional age adjustment is made. The percentages of the standard table used are selected according to the source of business. The range of percentages used is set out in the following tables:

	PAL		PRIL	
2007	**Males**	**Females**	**Males**	**Females**
In payment	106% — 126% PNMA00 (C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	84% — 117% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120	99% — 114% PNMA00 (C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	85% — 103% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

	PAL		PRIL	
2008	**Males**	**Females**	**Males**	**Females**
In payment	102% — 126% PNMA00 (C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	84% — 117% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120	97% — 102% PNMA00(C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	88% — 98% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

	PAL		PRIL	
2009	**Males**	**Females**	**Males**	**Females**
In payment	102% — 126% PNMA00 (C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	84% — 117% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120	96% — 102% PNMA00(C = 2000) with medium cohort improvement table with a minimum annual improvement of 2.25% up to age 90, tapering to zero at age 120	87% — 98% PNFA00 (C = 2000) with 75% of medium cohort improvement table with a minimum annual improvement of 1.25% up to age 90, tapering to zero at age 120
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

iv Unit-linked (non-annuity) and other non-profit business

The majority of other long-term business written in the UK insurance operations is unit-linked business or other business with similar features. For these contracts the attaching liability reflects the unit value obligation and provision for expenses and mortality risk. The latter component is determined by applying mortality assumptions on a basis that is appropriate for the policyholder profile.

For unit-linked business, the assets covering unit liabilities are exposed to market risk, but the residual risk when considering the unit-linked liabilities and assets together is limited to the effect on fund-based charges.

For those contracts where the level of insurance risk is insignificant the assets and liabilities arising under the contracts are distinguished between those that relate to the financial instrument liability and acquisition costs and deferred income that relate to the component of the contract that relates to investment management. Acquisition costs and deferred income are recognised consistent with the level of service provision in line with the requirements of IAS 18.

g Reinsurance

The Prudential Group's UK insurance business cedes only minor amounts of business outside the Prudential Group. Reinsurance premiums for externally ceded business were £59 million, £61 million and £122 million for 2007, 2008 and 2009 respectively and reinsurance recoverable insurance assets were £335 million, £416 million and £502 million in aggregate, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. This resulted in a one-off benefit of £34 million to IFRS profit before tax. The gains and losses recognised in profit and loss for these contracts were immaterial.

h Effect of changes in assumptions used to measure insurance assets and liabilities

2007

For UK insurance operations, the 2007 results were determined after making changes to mortality assumptions for the annuity business and other assumptions for the WPSF and releasing excess margins in the aggregate liabilities that had previously been set aside as an indirect extra allowance for longevity related risks, as shown below.

	2007	
	With-profits sub-fund	**Shareholder-backed business**
	£m	**£m**
Effect of (strengthening) weakening of mortality assumptions(note a)	(435)	(276)
Modelling of management actions(note b)	(167)	—
Strengthening of other assumptions(note c)	(62)	—
	(664)	(276)
Release of other margins:		
Projected benefit related(note d)	13	104
Investment related:(note e)		
Default margins	199	48
Asset management fees	60	—
	259	48
Expense related(note c, f)	—	68
Other(note c, g)	—	90
	272	310
Net charge to unallocated surplus	(392)	—
Net credit to shareholder result		34

Notes

a The mortality assumptions have been strengthened by increasing the minimum level of future improvement rate.

b Given the continuing strong financial position of the fund, the assumed management actions relating to with-profits business have been revised in order to better reflect the benefits to policyholders that can be supported by the fund.

c The effects of the strengthening of other assumptions for the WPSF of £62 million is net of a release of PAL's expense reserve of £11 million and other additional margins in PAL's liabilities of £40 million.

d The release of projected benefit related margins primarily relates to modelling improvements that have been made during 2007.

e The release of investment-related margins includes £48 million in respect of default margins for shareholder-backed business and £199 million for PAL. The resulting assumptions for expected defaults, after allowing for the release of margins, remain appropriate given economic conditions at 31 December 2007. In addition, for PAL, there is a release of £60 million in respect of asset management fees.

f A release of expense reserves has been made following recent expense reductions.

g This amount reflects the release of other additional margins in the liabilities that are no longer appropriate in light of the explicit strengthening of the mortality assumptions.

2008

Mortality

Overall mortality experience was in line with expectations and no change was therefore required to the overall strength of mortality assumptions at 31 December 2008. However, mortality assumptions were rebalanced across different categories of business so as to more closely align to the actual experience of each product category. The overall effect of rebalancing the assumptions between different product groups was financially neutral.

Credit risk

In total, for 2008, the effect of changes to the allowance for credit risk and the effect of portfolio rebalancing gave rise to a charge of £23 million. For shareholder-backed annuity and lifetime mortgage business, the operating profit based on longer-term investment returns included a charge of £413 million for the additional credit risk allowance for the annuity portfolio as a whole. Partially offsetting this was £390 million for the impact of £2.8 billion of portfolio rebalancing to more closely align management benchmark. The credit reflecting the additional yield expected after allowing for additional credit risk arising from the rebalancing.

Aggregate effect of assumptions changes

For UK insurance operations, the effects of assumptions changes for 2008 were as follows:

	2008	
	With-profits sub-fund	Shareholder-backed business
	£m	£m
Effect of (strengthening) weakening of mortality assumptions	(60)	(4)
Modelling of management actions[note a]	421	—
(Strengthening) weakening of other assumptions	75	—
	436	(4)
Release of other margins:		
Projected benefit related	10	10
Investment related:		
Additional credit default margins	(369)	[note b](413)
Deflation risk margins	(30)	(32)
Expense related	36	(8)
Net credit to unallocated surplus	83	—
Net charge to shareholder result	—	(447)

Notes

a The £421 million credit for modelling of management actions relates primarily to enhancements for actions in the event of solvency distress scenarios.

b Net of additional credit risk allowance attaching to effect of portfolio balancing described above.

c In 2008, no changes to mortality assumptions were made or necessary.

2009

Mortality

Recent mortality has been in line with expectations and no change is therefore required to the overall strength of mortality assumptions at 31 December 2009.

Credit risk

The approach for reserving for credit risk is set out in note (f)(iii).

Aggregate effect of assumptions changes

For UK insurance operations, the effects of assumptions changes for 2009 were as follows:

	2009	
	With-profits sub-fund note a	Shareholder-backed business note b
	£m	£m
Effect of changing expense assumptions for the with-profits sub-fund	51	(9)
Release of investment-related margins:		
Deflation risk margins	—	32
Asset management fees	—	14
Weakening of other assumptions	14	9
Net credit to unallocated surplus	65	—
Net credit to shareholder result	—	46

Notes

a Charges and expenses of the with-profits sub-fund have been updated to reflect the experience in 2009. The changes vary by product and the overall impact is a £51 million credit.

b The assumption changes in 2009 for the shareholder-backed business primarily relate to changes to the deflation reserve, expense assumptions and modelling changes.

i Sensitivity of IFRS basis profit or loss and equity to market and other risks

The risks to which the IFRS basis results of the UK insurance operations are sensitive are asset/liability matching, mortality experience and payment assumptions for shareholder-backed annuity business. Further details are described below.

i With-profits business

SAIF

Shareholders have no interest in the profits of SAIF but are entitled to the asset management fees paid on the assets of the fund.

With-profits sub-fund business

For with-profits business (including non-participating business of PAL which is owned by the WPSF) adjustments to liabilities and any related tax effects are recognised in the income statement. However, except for any impact on the annual declaration of bonuses, shareholders' profit for with-profits business is unaffected. This is because IFRS basis profits for with-profits business, which are determined on the same basis as on preceding UK GAAP, solely reflect one-ninth of the cost of bonuses declared for the year.

The main factors that influence the determination of bonus rates are the return on the investments of the fund, the effect of inflation, taxation, the expenses of the fund chargeable to policyholders and the degree to which investment returns are smoothed. Mortality and other insurance risk are relatively minor factors.

Unallocated surplus represents the excess of assets over policyholder liabilities of the fund. As unallocated surplus of the WPSF is recorded as a liability, movements in its value do not affect shareholders' profits or equity.

The level of unallocated surplus is particularly sensitive to the level of investment returns on the portion of the life fund assets that represents the surplus. The effects for 2007, 2008 and 2009 are demonstrated in note D5.

ii Shareholder-backed annuity business

Profits from shareholder-backed annuity business are most sensitive to:

- The extent to which the duration of the assets held closely matches the expected duration of the liabilities under the contracts. Assuming close matching, the impact of short-term asset value movements as a result of interest rate movements will broadly offset changes in the value of liabilities caused by movements in valuation rates of interest;
- actual versus expected default rates on assets held;
- the difference between long-term rates of return on corporate bonds and risk-free rates;
- the variance between actual and expected mortality experience;

- the extent to which expected future mortality experience gives rise to changes in the measurement of liabilities; and
- changes in renewal expense levels.

A decrease in assumed mortality rates of 1% would decrease gross profits by approximately £35 million, £35 million and £44 million, for 2007, 2008 and 2009 respectively. A decrease in credit default assumptions of five basis points would increase gross profits by £72 million, £71 million and £91 million, for 2007, 2008 and 2009 respectively. A decrease in renewal expenses (excluding asset management expenses) of 5% would increase gross profits by £13 million, £15 million and £17 million, for 2007, 2008 and 2009 respectively. The effect on profits would be approximately symmetrical for changes in assumptions that are directionally opposite to those explained above.

iii Unit-linked and other business

Unit-linked and other business represents a comparatively small proportion of the in-force business of the UK insurance operations.

Profits from unit-linked and similar contracts primarily arise from the excess of charges to policyholders, for management of assets under the Company's stewardship, over expenses incurred. The former is most sensitive to the net accretion of funds under management as a function of new business and lapse and timing of death. The accounting impact of the latter is dependent upon the amortisation of acquisition costs in line with the emergence of margins (for insurance contracts) and amortisation in line with service provision (for the investment management component of investment contracts). By virtue of the design features of most of the contracts which provide low levels of mortality cover, the profits are relatively insensitive to changes in mortality experience.

iv Shareholder exposure to interest rate risk and other market risk

By virtue of the fund structure, product features and basis of accounting described in note D2(e) and (g), the policyholder liabilities of the UK insurance operations are, except for pension annuity business, not generally exposed to interest rate risk. For pension annuity business, liabilities are exposed to fair value interest rate risk. However, the net exposure to the PAC WPSF (for PAL) and shareholders (for liabilities of PRIL and the non-profit sub-fund) is very substantially ameliorated by virtue of the close matching of assets with appropriate duration. The level of matching from period to period can vary depending on management actions and economic factors so it is possible for a degree of mis-matching profits or losses to arise.

The close matching by the Group of assets of appropriate duration to annuity liabilities is based on maintaining economic and regulatory capital. The measurement of liabilities under capital reporting requirements and IFRS is not the same, with contingency reserves and some other margins for prudence within the assumptions required under the FSA regulatory solvency basis not included for IFRS reporting purposes. As a result IFRS equity is higher than regulatory capital and therefore more sensitive to interest rate risk.

The estimated sensitivity of the UK non-linked shareholder-backed business (principally pension annuities business) to a movement in interest rates is as follows.

	2007		2008				2009			
	A decrease of 1%	An increase of 1%	A decrease of 2%	A decrease of 1%	An increase of 1%	An increase of 2%	A decrease of 2%	A decrease of 1%	An increase of 1%	An increase of 2%
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Carrying value of debt securities and derivatives	1,930	(1,634)	4,362	1,983	(1,676)	(3,108)	5,372	2,422	(2,020)	(3,731)
Policyholder liabilities	(1,777)	1,467	(3,974)	(1,798)	1,503	2,773	(5,125)	(2,304)	1,905	3,498
Related deferred tax effects	(43)	47	(109)	(52)	48	94	(69)	(33)	32	65
Net sensitivity of profit after tax and shareholders' equity	110	(120)	279	133	(125)	241	178	85	(83)	(168)

In addition the shareholder-backed portfolio of UK non-linked insurance operations covering liabilities and shareholders' equity includes equity securities and investment property. Excluding any second order effects on the measurement of the liabilities for future cash flow to the policyholder, a fall in their value would have given rise to the following effects on pre-tax profit, profit after tax, and shareholders' equity.

	2007	2008			2009	
	A decrease of 10%	A decrease of 40%	A decrease of 20%	A decrease of 10%	A decrease of 20%	A decrease of 10%
	£m	£m	£m	£m	£m	£m
Pre-tax profit	(86)	(508)	(254)	(127)	(292)	(146)
Related deferred tax assets	24	142	71	35	82	41
Net sensitivity of profit after tax and shareholders' equity	(62)	(366)	(183)	(92)	(210)	(105)

A 10%, 20% or 40% increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above. The market risk sensitivities shown above reflect the impact of temporary market movements and, therefore, the primary effect of such movements would, in the Prudential Group's segmental analysis of profits, be included within the short-term fluctuations in investment returns. The disclosure of the effect of a 40% fall for the 2008 year end was included because of the exceptional market conditions at that time. These conditions have now abated and the disclosure is no longer appropriate.

In the equity risk sensitivity analysis given above the Prudential Group has, for 2009, considered the impact of an instantaneous 20% fall in equity markets. If equity markets were to fall by more than 20%, the Prudential Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Prudential Group would be able to put in place mitigating management actions.

j Duration of liabilities

With the exception of most unitised with-profits bonds and other whole of life contracts the majority of the contracts of the UK insurance operations have a contract term. However, in effect, the maturity term of contracts reflects the earlier of death, maturity, or lapsation. In addition, with-profit contract liabilities as noted in note D2(f) include projected future bonuses based on current investment values. The actual amounts payable will vary with future investment performance of SAIF and the WPSF.

The tables below show the carrying value of the policyholder liabilities. Separately, the Group uses cash flow projections of expected benefit payments as part of the determination of the value of in-force business when preparing EEV basis results. The tables below also show the maturity profile of the cash flows used for 2007, 2008 and 2009 respectively, for that purpose for insurance contracts, as defined by IFRS, i.e. those containing significant insurance risk, and investment contracts, which do not.

	2007 £m									
	With-profits business			Annuity business (Insurance contracts)			Other			
	Insurance contracts	Investment contracts	Total	PAL	PRIL	Total	Insurance contracts	Investment contracts	Total	Total
Policyholder liabilities	47,915	29,480	77,395	12,564	13,402	25,966	9,057	12,059	21,116	124,477
	2007 %									
Expected maturity:										
0 to 5 years	47	25	38	32	31	32	32	31	31	
5 to 10 years	27	23	26	24	23	24	23	22	23	
10 to 15 years	13	19	16	18	17	17	18	20	19	
15 to 20 years	7	15	10	12	12	12	12	13	12	
20 to 25 years	4	11	6	7	8	7	8	6	7	
Over 25 years	2	7	4	7	9	8	7	8	8	

	2008 £m									
	With-profits business			Annuity business (Insurance contracts)			Other			
	Insurance contracts	Investment contracts	Total	PAL	PRIL	Total	Insurance contracts	Investment contracts	Total	Total
Policyholder liabilities	39,010	23,367	62,377	11,477	12,513	23,990	9,756	11,584	21,340	107,707
	2008 %									
Expected maturity:										
0 to 5 years	47	26	38	30	29	29	31	32	32	
5 to 10 years	26	23	25	24	23	23	23	22	23	
10 to 15 years	13	19	15	18	17	18	18	18	18	
15 to 20 years	7	15	10	12	13	13	12	12	12	
20 to 25 years	4	11	7	8	8	8	8	7	7	
Over 25 years	3	6	5	8	10	9	8	9	8	

	2009 £m									
	With-profits business			Annuity business (Insurance contracts)			Other			
	Insurance contracts	Investment contracts	Total	PAL	PRIL	Total	Insurance contracts	Investment contracts	Total	Total
Policyholder liabilities	40,780	24,780	65,560	11,969	14,292	26,261	10,614	13,794	24,408	116,229
	2009 %									
Expected maturity:										
0 to 5 years	50	29	41	32	31	32	34	35	35	
5 to 10 years	26	25	26	25	23	24	25	22	23	
10 to 15 years	13	19	15	18	17	17	18	19	18	
15 to 20 years	6	14	9	11	12	12	11	11	11	
20 to 25 years	3	9	6	7	8	7	7	6	6	
Over 25 years	2	4	3	7	9	8	5	7	7	

Notes

i The cash flow projections of expected benefit payments used in the maturity profile tables above are from value of in-force business and exclude the value of future new business, including vesting of internal pension contracts.

ii Benefit payments do not reflect the pattern of bonuses and shareholder transfers in respect of the with-profits business.

iii Investment contracts under Other comprise certain unit-linked and similar contracts accounted for under IAS 39 and IAS 18.

iv For business with no maturity term included within the contracts, for example with-profits investment bonds such as Prudence Bond, an assumption is made as to likely duration based on prior experience.

v The maturity tables shown above have been prepared on a discounted basis. Details of undiscounted cash flow for investment contracts are shown in note G2.

D3: US insurance operations

a Summary results and statement of financial position

i Results and movements on shareholders' equity

	2007	2008	2009
	£m	£m	£m
Operating profit based on longer-term investment returns	444	406	459
Short-term fluctuations in investment returns	(18)	(1,058)	27
Profit (loss) before shareholder tax	426	(652)	486
Tax	(126)	72	102
Profit (loss) for the year	300	(580)	588

	2007	2008	2009
	£m	£m	£m
Profit (loss) for the year	300	(580)	588
Items recognised in other comprehensive income:			
Exchange movements	(42)	545	(231)
Unrealised valuation movements on securities classified as available-for-sale:			
Unrealised holding (losses) gains arising during the year	(231)	(2,482)	2,249
Less (gains) losses included in the income statement	(13)	378	420
Total unrealised valuation movements	(244)	(2,104)	2,669
Related change in amortisation of deferred income and acquisition costs	88	831	(1,069)
Related tax	54	442	(557)
Total other comprehensive income (loss)	(144)	(286)	812
Total comprehensive income (loss) for the year	156	(866)	1,400
Dividends and interest payments to Central companies	(122)	(126)	(87)
Net increase (decrease) in equity	34	(992)	1,313
Shareholders' equity at beginning of year	2,656	2,690	1,698
Shareholders' equity at end of year	2,690	1,698	3,011

Included within the movements in shareholders' equity is a net reduction in value of Jackson's debt securities classified as 'available-for-sale' under IAS 39 of £244 million, £2,104 million for 2007 and 2008 respectively, and a net increase in value of £2,669 million for 2009.

With the exception of debt securities for US insurance operations classified as 'available-for-sale' under IAS 39, unrealised value movements on the Prudential Group's investments are booked within the income statement. However, for debt securities classified as 'available-for-sale', unless impaired, fair value movements are recognised in other comprehensive income. Realised gains and losses, including impairments, are recorded in the income statement. This classification is applied for most of the debt securities of the Prudential Group's US operations. Jackson recorded £35 million, £497 million and £630 million, for 2007, 2008 and 2009 respectively, of impairment losses arising from:

	2007	2008	2009
	£m	£m	£m
Residential mortgage-backed securities	—	167	509
Public fixed income	21	311	91
Other	14	19	30
	35	497	630

Further details on the impairment losses recognised in the year are shown in note B1. Jackson's portfolio of debt securities is managed proactively with credit analysts closely monitoring and reporting on the credit quality of its holdings. Jackson continues to review its investments on a case-by-case basis to determine whether any decline in fair value represents an impairment. In addition, investment in structured securities where market prices are depressed are subject to a rigorous review of their future estimated cash flows, including expected and stress case scenarios, to identify potential shortfalls in contractual payments (both interest and principal). Impairment charges are recorded on structured securities when Prudential forecasts a contractual payment shortfall. Situations where such a short fall would not lead to recognition of a loss are rare. However, some structured securities do not have a single determined set of future cash flows and instead, there can be a reasonable range of estimates that could potentially emerge. With this variability, there could be instance where the projected cash flow shortfall under management's base case set of assumptions is so minor that relatively small and justifiable changes to the base case assumptions would eliminate the need for an impairment loss to be recognised. The impairment loss reflects the difference between the fair value and book value.

There was a movement in the statement of financial position value for debt securities classified as available-for-sale from a net unrealised gain of £110 million to a net unrealised loss of £136 million in 2007, a net unrealised loss of £136 million to a net unrealised loss of £2,897 million in 2008, and a net unrealised loss of £2,897 million to a net unrealised gain of £4 million, in 2009. The gross unrealised gain in the statement of financial position decreased from £303 million at 31 December 2007 to £281 million at 31 December 2008 then increased to £970 million at 31 December 2009 while the gross unrealised loss increased from £439 million at 31 December 2007 to £3,178 million at 31 December 2008 then decreased to £966 million at 31 December 2009. Details of the securities in an unrealised loss position are shown in D3(c) below.

These features are included in the table shown below of the movements in the values of available-for-sale securities:

	As at 31 December								
	2006	2007		2008			2009		
		Changes in unrealised appreciation†		Changes in unrealised appreciation†	Foreign exchange translation		Changes in unrealised appreciation†	Foreign exchange translation	
				Reflected as part of other comprehensive income			Reflected as part of other comprehensive income		
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets fair valued at below book value									
Book value*	11,258	—	10,730	—	—	20,600	—	—	8,220
Unrealised loss	(256)	(183)	(439)	(1,997)	(742)	(3,178)	1,925	287	(966)
Fair value (as included in statement of financial position)	11,002	—	10,291	—	—	17,422	—	—	7,254
Assets fair valued at or above book value									
Book value*	8,208	—	8,041	—	—	6,296	—	—	14,444
Unrealised gain	366	(63)	303	(107)	85	281	744	(55)	970
Fair value (as included in statement of financial position)	8,574	—	8,344	—	—	6,577	—	—	15,414
Total									
Book value*	19,466	—	18,771	—	—	26,896	—	—	22,664
Net unrealised (loss) gain	110	(246)	(136)	(2,104)	(657)	(2,897)	2,669	232	4
Fair value (as included in statement of financial position)**	19,576	—	18,635	—	—	23,999	—	—	22,668
Reflected as part of movement in other comprehensive income									
Movement in unrealised appreciation	—	—	(244)	—	—	(2,104)	—	—	2,669
Exchange movements	—	—	(2)	—	—	(657)	—	—	232
	—	—	(246)	—	—	(2,761)	—	—	2,901

* Book value represents cost/amortised cost of the debt securities.

** Debt securities for US operations as included in the statement of financial position of £19,002 million, £24,249 million and £22,831 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise £18,635 million, £23,999 million and £22,668 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, in respect of securities classified as 'available-for-sale' and £367 million, £250 million, £163 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, for securities of consolidated investment funds classified as 'fair value through profit and loss'.

† Translated at closing rate of US$2.00: £1 for 2007, the difference arising on exchange translation at 31 December 2007 between average and closing rate was not material. Translated at the average rate of US$1.85: £1 and US$1.57: £1, for 2008 and 2009 respectively.

Included within the movement in gross unrealised losses for the debt securities of Jackson of £183 million, £1,997 million and £1,925 million, for 2007, 2008 and 2009 respectively, as shown above was a value reduction of £55 million, £105 million and £72 million, for 2007, 2008 and 2009 respectively, relating to the sub-prime and Alt-A securities as referred to in section B6.

ii Statement of financial position

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type.

US insurance operations at 31 December:

	2007 Total	2008 Total	Variable annuity separate account assets and liabilities note i	Fixed annuity, GIC and other business note i	2009 Total
	£m	£m	£m	£m	£m
Assets					
Intangible assets attributable to shareholders:					
Deferred acquisition costs and other intangible assets	1,928	3,962	—	3,092	3,092
Total	1,928	3,962	—	3,092	3,092
Deferred tax assets	657	1,969	—	1,944	1,944
Other non-investment and non-cash assets	994	1,819	—	1,404	1,404
Investments of long-term business and other operations:					
Investment properties	8	13	—	33	33
Financial investments:					
Loans(note ii)	3,258	5,121	—	4,319	4,319
Equity securities and portfolio holdings in unit trusts	15,507	15,142	20,639	345	20,984
Debt securities(noteD3c)	19,002	24,249	—	22,831	22,831
Other investments(note iii)	762	1,256	—	955	955
Deposits	258	390	—	454	454
Total investments	38,795	46,171	20,639	28,937	49,576
Properties held for sale	—	—	—	3	3
Cash and cash equivalents	169	246	—	340	340
Total assets	42,543	54,167	20,639	35,720	56,359
Equity and liabilities					
Equity					
Shareholders' equity	2,690	1,698	—	3,011	3,011
Minority interests	1	—	—	—	—
Total equity	2,691	1,698	—	3,011	3,011
Liabilities					
Policyholder liabilities:(note iv)					
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	34,848	45,361	20,639	27,672	48,311
Total	34,848	45,361	20,639	27,672	48,311
Core structural borrowings of shareholder-financed operations	125	173	—	154	154
Operational borrowings attributable to shareholder-financed operations	591	511	—	203	203
Deferred tax liabilities	639	1,337	—	1,858	1,858
Other non-insurance liabilities	3,649	5,087	—	2,822	2,822
Total liabilities	39,852	52,469	20,639	32,709	53,348
Total equity and liabilities	42,543	54,167	20,639	35,720	56,359

Notes

i Assets and liabilities attaching to variable annuity business that are not held in the separate account are shown within other business.

ii Loans

The loans of the Group's US insurance operations of £3,258 million, £5,121 million and £4,319 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise mortgage loans of £2,841 million, £4,534 million and £3,774 million and policy loans of £417 million, £587 million and £530 million and other loans of nil, nil, and £15 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. All of the mortgage loans are commercial mortgage loans which are collateralised by properties. The property types are mainly industrial, multi-family residential, suburban office, retail and hotel. The breakdown by property type as at 31 December is as follows:

	2007	2008	2009
	%	%	%
Industrial	28	29	32
Multi-family	23	21	18
Office	22	21	20
Retail	18	17	19
Hotels	8	10	10
Other	1	2	1
	100	100	100

The US insurance operations' commercial mortgage loan portfolio does not include any single-family residential mortgage loans and is therefore not exposed to the risk of defaults associated with residential sub-prime mortgage loans. The average loan size as at 31 December 2009 is £6.3 million. The portfolio has a current estimated average loan to value of 74% which provides significant cushion to withstand substantial declines in value.

The policy loans are fully secured by individual life insurance policies or annuity policies. These loans are accounted for at amortised cost, less any impairment.

iii Other investments as at 31 December comprise:

	2007	2008	2009
	£m	£m	£m
Derivative assets(note G3*)	390	675	519
Partnerships in investment pools and other**	372	581	436
	762	1,256	955

* In the US, Prudential uses derivatives to reduce interest rate risk, to facilitate efficient portfolio management to match liabilities under annuity policies, and for certain equity-based product management activities. After taking account of the derivative liability of £158 million, £863 million and £461 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which is also included in the statement of financial position, the derivative position for US operations is a net asset of £232 million, net liability of £188 million and a net asset of £58 million for as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

** Partnerships in investment pools and other comprise primarily investments in limited partnerships. These include interest in the PPM America Private Equity Fund and diversified investments in 164, 157 and 159 other partnerships by independent money managers that generally invest in various equities and fixed income loans and securities, as at 31 December 2007, 31 December 2008 and 31 December 2009, respectively.

iv Summary policyholder liabilities (net of reinsurance) and reserves at 31 December 2007, 31 December 2008 and 31 December 2009 The policyholder liabilities, net of reinsurers' share of £436 million, £800 million and £667 million, reflect balances in respect of the following as at 31 December:

	2007	2008	2009
	£m	£m	£m
Policy reserves and liabilities on non-linked business:			
Reserves for future policyholder benefits and claims payable	916	2,518	1,645
Deposits on investment contracts (as defined under US GAAP)	16,784	24,962	23,706
Guaranteed investment contracts	1,685	2,543	1,654
Unit-linked (variable annuity) business	15,027	14,538	20,639
	34.412	44,561	47,644

In addition to the policyholder liabilities above, Jackson has entered into a programme of funding arrangements under contracts which, in substance, are almost identical to GICs . The liabilities under these funding arrangements totalled

£2,607 million, £3,233 million and £1,444 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively and are included in 'other non-insurance liabilities' in the statement of financial position above.

b Reconciliation of movement in policyholder liabilities

A reconciliation of the total policyholder liabilities of US insurance operations from the beginning of the year to the end of the year is as follows:

	Variable annuity separate account liabilities	Fixed annuity, GIC and other business	US insurance operations Total
	£m	£m	£m
At 1 January 2007	11,367	20,379	31,746
Premiums	3,970	2,382	6,352
Surrenders	(960)	(2,516)	(3,476)
Maturities/Deaths	(92)	(398)	(490)
Net cash flows[note b]	2,918	(532)	2,386
Investment-related items and other movements	914	311	1,225
Foreign exchange translation differences[note a]	(172)	(337)	(509)
At 31 December 2007/1 January 2008	15,027	19,821	34,848
Premiums	2,637	4,091	6,728
Surrenders	(1,053)	(2,799)	(3,852)
Maturities/Deaths	(161)	(403)	(564)
Net cash flows[note b]	1,423	889	2,312
Investment-related items and other movements	(6,288)	1,736	(4,552)
Foreign exchange translation differences[note a]	4,376	8,377	12,753
At 31 December 2008/1 January 2009	14,538	30,823	45,361
Premiums	4,667	4,510	9,177
Surrenders	(882)	(2,373)	(3,255)
Maturities/Deaths	(199)	(534)	(733)
Net cash flows[note b]	3,586	1,603	5,189
Transfers from general to separate account	984	(984)	—
Investment-related items and other movements[note c, b]	3,368	(382)	2,986
Foreign exchange translation differences[note a]	(1,837)	(3,388)	(5,225)
At 31 December 2009	20,639	27,672	48,311

Note

(a) Movements in the year have been translated at an average rate of 1.99, 1.85 and 1.57, for 2007, 2008 and 2009 respectively. The closing balance has been translated at closing rate of 1.96, 1.44 and 1.61, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Differences upon retranslation are included in foreign exchange translation differences.

(b) Net cash flows for the year were £5,189 million compared with £2,312 million in 2008, driven largely by increased new business volumes for the variable annuity business.

(c) Positive investment-related items and other movements in variable annuity separate account liabilities were impacted by the recovery of US equity markets during 2009. Negative movements in fixed annuity, GIC and other business of £382 million primarily represents a reduction in the liabilities for variable annuity guarantees following improvements in equity markets and increases in interest rates offset by interest credited to policyholder accounts.

c Information on credit risks of debt securities

As at 31 December:

	2007 Carrying value	2008 Carrying value	2009 Carrying value
	£m	£m	£m
Corporate security and commercial loans:			
Publicly traded and SEC Rule 144A traded	10,345	13,198	13,338
Non-SEC Rule 144A traded	2,613	3,273	3,117
Total	12,958	16,471	16,455
Residential mortgage-backed securities	3,177	4,509	3,316
Commercial mortgage-backed securities	1,532	1,869	2,104
Other debt securities	1,335	1,400	956
Total debt securities	19,002	24,249	22,831

i Credit quality

For statutory reporting in the US, debt securities are classified into six quality categories specified by the Securities Valuation Office of the National Association of Insurance Commissioners ("NAIC"). The categories range from Class 1 (the highest) to Class 6 (the lowest). Performing securities are designated as Classes 1 to 5. Securities in or near default are designated Class 6.

Securities designated as Class 3, 4, 5 and 6 are non-investment grade securities. Generally, securities rated AAA to A by nationally recognised statistical ratings organisations are reflected in Class 1, BBB in Class 2, BB in Class 3 and B and below in Classes 4 to 6. If a designation is not currently available from the NAIC, Jackson's investment adviser, PPM America, provides the designation for the purposes of disclosure below.

The following table shows the quality of the SEC Rule 144A publicly traded placement portfolio by NAIC classifications at 31 December:

	2007		2008		2009	
	£m	Carrying value % of total	£m	Carrying value % of total	£m	Carrying value % of total
NAIC designation:						
1	4,338	42	5,380	41	5,067	38
2	5,194	50	6,849	52	7,508	56
3	542	5	690	5	598	5
4	231	2	200	1	122	1
5	40	1	75	1	40	—
6	—	—	4	—	3	—
	10,345	100	13,198	100	13,338	100

The following table shows the quality of the non-SEC Rule 144A traded private placement portfolio by NAIC classifications at 31 December:

	2007		2008		2009	
	£m	Carrying value % of total	£m	Carrying value % of total	£m	Carrying value % of total
NAIC designation:						
1	1,011	39	1,268	39	1,084	35
2	1,351	52	1,655	50	1,792	57
3	206	8	285	9	162	5
4	45	1	54	2	54	2
5	—	—	11	0	20	1
6	—	—	—	—	5	—
	2,613	100	3,273	100	3,117	100

Included within other debt securities of £1,335 million, £1,400 million and £956 million in the summary shown above are £706 million, £893 million and £652 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of asset-backed securities held directly by Jackson. Of this balance £579 million, £663 million and £447 million were NAIC designation 1 and a further £127 million, £159 million and £152 million were NAIC designation 2 as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. In addition, other debt securities includes £316 million, £257 million and £172 million in respect of securities held by the Piedmont trust entity and £313 million, £250 million and £131 million from the consolidation of investment funds managed by PPM America as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

In addition to the ratings disclosed above, the following table summarises by rating the debt securities, as at 31 December using Standard and Poor's ("S&P"), Moody's, Fitch and implicit ratings of RMBS based on NAIC valuations:

	2007 Carrying value	2008 Carrying value	2009 Carrying Value
	£m	£m	£m
S&P — AAA	3,896	5,321	3,287
S&P — AA+ to AA−	1,187	853	846
S&P — A+ to A−	3,657	5,244	5,192
S&P — BBB+ to BBB−	5,415	7,077	7,659
S&P — Other	1,113	1,321	895
	15,268	19,816	17,879
Moody's — Aaa	549	458	273
Moody's — Aa1 to Aa3	118	100	43
Moody's — A1 to A3	47	111	32
Moody's — Baa1 to Baa3	79	100	64
Moody's — Other	78	95	57
	871	864	469
Implicit ratings of RMBS based on NAIC valuations (see below)			
NAIC 1	—	—	747
NAIC 2	—	—	105
NAIC 3-6	—	—	473
	—	—	1,325
Fitch	380	464	281
Other	2,483	3,105	2,877
Total debt securities	19,002	24,249	22,831

In the table above, with the exception of residential mortgage-backed securities for 2009, S&P ratings have been used where available. For securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative.

During 2009, the National Association of Insurance Commissioners ("NAIC") in the US revised the regulatory ratings process for more than 20,000 residential mortgage-backed securities. The table above includes these securities, where held by Jackson, using the regulatory rating levels established by an external third party (PIMCO).

The amounts within Other which are not rated by S&P, Moody's, Fitch nor are RMBS securities using the revised regulatory ratings have the following NAIC classifications as at 31 December:

	2007	2008	2009
	£m	£m	£m
NAIC 1	1,079	1,334	1,102
NAIC 2	1,311	1,650	1,623
NAIC 3-6	93	121	152
	2,483	3,105	2,877

ii Determining the fair value of debt securities when the markets are not active

Under IAS 39, unless categorised as 'held to maturity' or 'loans and receivables' debt securities are required to be fair valued. Where available, quoted market prices are used. However, where securities are in inactive markets, IAS 39 requires that valuation techniques be applied. Note G1 sets out further details of the Prudential Group's approach to determining fair value and classifies these fair values into a three level hierarchy as required by IFRS 7. As at 31 December 2008 and 2009, respectively, 15% and 3% of Jackson's debt securities were classified as level 3 being fair values where there are significant inputs which are not based on observable market data. The higher proportion at 31 December 2008 arises from the illiquidity of the market at that time and hence a greater use of internal valuation techniques.

In 2008, due to inactive and illiquid markets, beginning at the end of the third quarter of 2008 the external prices obtained for certain asset-backed securities were deemed not to reflect fair value in the dislocated market conditions at that time. For the valuations at 31 December 2008, Jackson had therefore utilised internal valuation models, provided by PPM America, as best estimate of fair values of all non-agency Residential Mortgage-backed Securities ("RMBS") and Asset backed Securities ("ABS") and certain Commercial Mortgage-backed securities ("CMBS").

During 2009, improvements were observed in the level of liquidity for these sectors of structured securities and this increased liquidity in the markets for certain tranches of non-agency RMBS and ABS resulted in Jackson being able to rely on external prices for the securities as the most appropriate measure of fair value.

Accordingly, at 30 June 2009 and 31 December 2009, nearly all of the non-agency RMBS, ABS and certain CMBS which at 31 December 2008 were valued using internal valuation models due to the dislocated market conditions in 2008, have now been valued using external prices.

iii Asset-backed securities funds exposures

Included within the debt securities of Jackson at 31 December 2007, 31 December 2008 and 31 December 2009 are exposures to asset-backed securities as follows:

	2007	2008	2009
	£m	£m	£m
RMBS Sub-prime (2007: 100% S&P AAA; 2008: 91% S&P AAA, 3% AA; 2009 76% S&P AAA, 1% AA) †	237	291	194
Alt-A (2007: 77% AAA, 17% AA; 2008: 60% AAA, 15% AA; 2009 24% AAA, 5%AA)	660	646	443
Prime (2007: 87% AAA; 2008: 87% AAA, 5% AA; 2009 82% AAA, 4% AA)	2,280	3,572	2,679
CMBS (2007: 83% AAA; 2008: 85% AAA, 9% AA; 2009 46% AAA, 14% AA)	1,532	1,869	2,104
CDO funds (2007: 65% AAA, 8% AA; 2008: 34% AAA, 14% AA; 2009: 29% AAA, 10% AA)* including £3m exposure to sub-prime	260	320	79
ABS (2007: 37% AAA, 12% AA; 2008: 31% AAA, 16% AA; 2009: 25% AAA, 18% AA)* including nil exposure to sub-prime	706	766	877
	5,675	7,464	6,376

* Including Group's economic interest in Piedmont and other consolidated CDO funds.

† RMBS ratings refer to the rating implicit within NAIC risk-based capital valuation.

Jackson defines its exposure to sub-prime mortgages as investments in residential mortgage-backed securities in which the underlying borrowers have a US Fair Isaac Credit Organisation ("FICO") credit score of 680 or lower.

iv Debt securities classified as available-for-sale in an unrealised loss position

a) Fair value of securities as a percentage of book value

The unrealised losses in Jackson's statement of financial position on unimpaired securities are £439 million, £3,178 million and £966 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. This relates to assets with fair market value of £10,291 million, £17,422 million, and £7,254 million as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively and a book value of £10,730 million £20,600 million and £8,220 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The following table shows the fair value of the debt securities in a gross unrealised loss position for various percentages of book value at 31 December:

	2007		2008		2009	
Fair value of securities as a percentage of book value	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
	£m		£m		£m	
Between 90% and 100%	9,370	(274)	8,757	(431)	5,127	(169)
Between 80% and 90%	784	(122)	4,581	(809)	1,201	(203)
Below 80%	137	(43)	4,084	(1,938)	926	(594)
	10,291	(439)	17,422	(3,178)	7,254	(966)

Included within the table above are amounts relating to sub-prime and Alt — A securities of:

Fair value of securities as a percentage of book value	2007 Fair value	2007 Unrealised loss	2008 Fair value	2008 Unrealised loss	2009 Fair value	2009 Unrealised loss
	£m		£m		£m	
Between 90% and 100%	572	(24)	479	(27)	102	(3)
Between 80% and 90%	132	(22)	120	(19)	160	(28)
Below 80%	28	(10)	192	(166)	159	(88)
	732	(56)	791	(212)	421	(119)

b) Unrealised losses by maturity of security

	2007 Unrealised loss	2008 Unrealised loss	2009 Unrealised loss
	£m	£m	£m
Less than 1 year	(1)	(21)	—
1 to 5 years	(54)	(537)	(29)
5 to 10 years	(164)	(1,236)	(127)
More than 10 years	(60)	(395)	(92)
Mortgage-backed and other debt securities	(160)	(989)	(718)
Total	(439)	(3,178)	(966)

c) Age analysis of unrealised losses for the periods indicated

The following table shows the aged analysis for all the unrealised losses in the portfolio by reference to the length of time the securities have been in an unrealised loss position:

Aged analysis of unrealised losses for the periods indicated	2007 Non-investment grade	2007 Investment grade	2007 Total	2008 Non-investment grade	2008 Investment grade	2008 Total	2009 Non-investment grade	2009 Investment grade	2009 Total
	£m			£m			£m		
Less than 6 months	(9)	(58)	(67)	(108)	(362)	(470)	(7)	(51)	(58)
6 months to 1 year	(21)	(115)	(136)	(125)	(1,164)	(1,289)	(25)	(59)	(84)
1 year to 2 years	(2)	(21)	(23)	(154)	(622)	(776)	(59)	(234)	(293)
2 years to 3 years	(34)	(140)	(174)	(15)	(91)	(106)	(125)	(199)	(324)
More than 3 years	(2)	(37)	(39)	(61)	(476)	(537)	(35)	(172)	(207)
	(68)	(371)	(439)	(463)	(2,715)	(3,178)	(251)	(715)	(966)

As at 31 December 2007, 2008 and 2009, the gross unrealised losses in the statement of financial position for the sub-prime and Alt-A securities in an unrealised loss position were £56 million, £212 million and £119 million, respectively. Of these losses, £37 million, £91 million and £21 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively have been in an unrealised loss position for less than one year with the remaining securities with unrealised losses of £19 million, £121 million, and £98 million respectively being in an unrealised loss position for more than one year.

d) Securities whose fair value were below 80% of the book value

As shown in table (a) above, £43 million, £1,938 million and £594 million of the £439 million, £3,178 million and £966 million of gross unrealised losses at 31 December 2007, 31 December 2008, and 31 December 2009 respectively related to securities whose fair values were below 80% of the book value. The analysis of the £43 million, £1,938 million and £594 million, for 2007, 2008 and 2009 respectively, by category of debt securities and by age analysis indicating the length of time for which their fair value was below 80% of the book value, are as follows:

	2007		2008		2009	
Category analysis	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
	£m		£m		£m	
Residential mortgage-backed securities						
Prime	2	(1)	287	(115)	322	(153)
Alt-A	27	(10)	144	(127)	77	(33)
Sub-prime	—	—	48	(39)	82	(55)
	29	(11)	479	(281)	481	(241)
Commercial mortgage-backed securities	4	(1)	811	(375)	87	(86)
Other asset-backed securities	4	(1)	198	(86)	183	(188)
Total structured securities	37	(13)	1,488	(742)	751	(515)
Corporates	100	(30)	2,596	(1,196)	175	(79)
Total	137	(43)	4,084	(1,938)	926	(594)

Age analysis of fair value being below 80% for the period indicated:

	2007		2008		2009	
Age analysis	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
	£m		£m		£m	
Less than 3 months	137	(43)	3,118	(1,364)	153	(45)
3 months to 6 months	—	—	696	(403)	5	(3)
More than 6 months	—	—	270	(171)	768	(546)
	137	(43)	4,084	(1,938)	926	(594)

d Products and guarantees

Jackson provides long-term savings and retirement products to retail and institutional customers throughout the US. Jackson offers fixed annuities (interest-sensitive, fixed indexed and immediate annuities), variable annuities (VA), life insurance and institutional products.

i Fixed annuities

Interest-sensitive annuities

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, interest-sensitive fixed annuities accounted for 25%, 29% and 24% of policy and contract liabilities of Jackson. Interest-sensitive fixed annuities are primarily deferred annuity products that are used for retirement planning and for providing income in retirement. They permit tax-deferred accumulation of funds and flexible payout options.

The policyholder of an interest-sensitive fixed annuity pays Jackson a premium, which is credited to the policyholder's account. Periodically, interest is credited to the policyholder's account and in some cases administrative charges are deducted from the policyholder's account. Jackson makes benefit payments at a future date as specified in the policy based on the value of the policyholder's account at that date.

The policy provides that at Jackson's discretion it may reset the interest rate, subject to a guaranteed minimum. The minimum guarantee varied from 1.5% to 5.5%, 1.5% to 5.5% and 1.5% to 5.5%, for 2007, 2008 and 2009 respectively, depending on the jurisdiction of issue and the date of issue, with 80%, 83% and 82%, for 2007, 2008 and 2009 respectively, of the fund at 3% or less. The average guarantee rate was 3.1%, 3.1% and 3.1%, for 2007, 2008 and 2009 respectively.

Approximately 30%, 34% and 61% of the interest-sensitive fixed annuities Jackson wrote in 2007, 2008 and 2009 respectively, provide for a market value adjustment, that could be positive or negative, on surrenders in the surrender period of the policy. This formula-based adjustment approximates the change in value that assets supporting the product would realise as interest rates move up or down. The minimum guaranteed rate is not affected by this adjustment.

Fixed indexed annuities

Fixed indexed annuities accounted for 7%, 8% and 10%, for 2007, 2008 and 2009 respectively, of Jackson's policy and contract liabilities at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Fixed indexed annuities vary in structure, but generally are deferred annuities that enable policyholders to obtain a portion of an equity-linked return (based on participation rates and caps) but provide a guaranteed minimum return. These guaranteed minimum rates are generally set at 1.25% to 3%.

Jackson hedges the equity return risk on fixed indexed products using futures and options linked to the relevant index. The cost of these hedges is taken into account in setting the index participation rates or caps. Jackson bears the investment and surrender risk on these products.

Immediate annuities

At 31 December 2007, 31 December 2008 and 31 December 2009, immediate annuities accounted for 2% of Jackson's policy and contract liabilities. Immediate annuities guarantee a series of payments beginning within a year of purchase and continuing over either a fixed period of years and/or the life of the policyholder. If the term is for the life of the policyholder, then Jackson's primary risk is mortality risk. The implicit interest rate on these products is based on the market conditions that exist at the time the policy is issued and is guaranteed for the term of the annuity.

ii Variable annuities

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, VAs accounted for 45%, 39% and 49% of Jackson's policy and contract liabilities. VAs are deferred annuities that have the same tax advantages and payout options as interest-sensitive and fixed indexed annuities.

The primary differences between VAs and interest-sensitive or fixed indexed annuities are investment risk and return. If a policyholder chooses a VA, the rate of return depends upon the performance of the selected fund portfolio. Policyholders may allocate their investment to either the fixed or variable account. Investment risk on the variable account is borne by the policyholder, while investment risk on the fixed account is borne by Jackson through guaranteed minimum fixed rates of return. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, approximately 9%, 18% and 14% of VA funds were in fixed accounts.

Jackson issues VA contracts where it contractually guarantees to the contractholder either a) return of no less than total deposits made to the contract adjusted for any partial withdrawals, b) total deposits made to the contract adjusted for any partial withdrawals plus a minimum return, or c) the highest contract value on a specified anniversary date adjusted for any withdrawals following the contract anniversary. These guarantees include benefits that are payable in the event of death (guaranteed minimum death benefit ("GMDB")), annuitisation (guaranteed minimum income benefit ("GMIB")), or at specified dates during the accumulation period (guaranteed minimum withdrawal benefit ("GMWB")) and guaranteed minimum accumulation benefit ("GMAB"). Jackson hedges these risks using equity options and futures contracts as described in note D3(e). The GMIB is no longer offered, with existing coverage being reinsured.

iii Life insurance

Jackson's life insurance products accounted for 9%, 10% and 9% of Jackson's policy and contract liabilities at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. The products offered include variable universal life insurance, term life insurance and interest-sensitive life insurance.

iv Institutional products

Jackson's institutional products consist of GICs, funding agreements (including agreements issued in conjunction with Jackson's participation in the US Federal Home Loan Bank programme) and medium-term note funding agreements. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, institutional products accounted for 12%, 12% and 6% of policy and contract liabilities. Under a traditional GIC, the policyholder makes a lump sum deposit. The interest rate paid is fixed and established when the contract is issued. If deposited funds are withdrawn earlier than the specified term of the contract, an adjustment is made that approximates a market value adjustment.

Under a funding agreement, the policyholder either makes a lump sum deposit or makes specified periodic deposits. Jackson agrees to pay a rate of interest, which may be fixed but which is usually a floating short-term interest rate linked to an external index. The average term of the funding arrangements is one to two years. Funding agreements terminable by the policyholder with less than 90 days' notice account for less than 1%, 1% and less than 1%, for 2007, 2008 and 2009 respectively, of total policyholder reserves.

Medium-term note funding agreements are generally issued to support trust instruments issued on non-US exchanges or to qualified investors (as defined by SEC Rule 144A). Through the funding agreements, Jackson agrees to pay a rate of interest, which may be fixed or floating, to the holders of the trust instruments.

e Exposure to market risk and risk management

Jackson's main exposures are to market risk through its exposure to interest rate risk and equity risk. Approximately 90%, 90% and 95%, for 2007, 2008 and 2009 respectively, of its general account investments support interest-sensitive and fixed indexed annuities, life business and surplus and 10%, 10% and 5%, for 2007, 2008 and 2009 respectively, support institutional business. All of these types of business contain considerable interest rate guarantee features and, consequently, require that the assets that support them are primarily fixed income or fixed maturity.

Prudential is exposed primarily to the following risks in the US arising from fluctuations in interest rates:

- the risk of loss related to meeting guaranteed rates of accumulation following a sharp and sustained fall in interest rates;
- the risk of loss related to policyholder withdrawals following a sharp and sustained increase in interest rates; and
- the risk of mismatch between the expected duration of certain annuity liabilities and prepayment risk and extension risk inherent in mortgage-backed securities.

Prudential is also exposed to the following risks in the US arising from equity market movements:

- the risk of loss related to the incidence of benefits related to guarantees issued in conjunction with its VA contracts; and
- the risk of loss related to meeting contractual accumulation requirements in FIA contracts.

Jackson enters into financial derivative transactions, including those noted below to reduce and manage business risks. These transactions manage the risk of a change in the value, yield, price, cash flows, or quantity of, or a degree of exposure with respect to assets, liabilities or future cash flows, which Jackson has acquired or incurred.

Jackson uses free-standing derivative instruments for hedging purposes. Additionally, certain liabilities, primarily trust instruments supported by funding agreements, fixed indexed annuities, certain GMWB variable annuity features and reinsured GMIB variable annuity features contain embedded derivatives as defined by IAS 39, 'Financial Instruments: Recognition and Measurement'. Jackson does not account for such derivatives as either fair value or cash flow hedges as might be permitted if the specific hedge documentation requirements of IAS 39 were followed. Financial derivatives, including derivatives embedded in certain host liabilities that have been separated for accounting and financial reporting purposes are carried at fair value.

Value movements on the derivatives are reported within the income statement. In preparing Jackson's segment profit as shown in note B1, value movements on Jackson's derivative contracts, other than for certain equity-based product management activities, are included within short-term fluctuations in investment returns and excluded from operating results based on longer-term investment returns (defined as segment profit). Value movements on derivative instruments used for certain equity-based product management activities, which for 2008 and 2009 is based on a static long-term volatility assumption and, for embedded liabilities, average Corporate AA interest rates, are included within operating results based on longer-term investment returns, as the value movements broadly offset the economic impact of changed levels of benefit payments and reserves as equity markets fluctuate, (subject to some limitations for GMDB where US GAAP does not fully reflect the economic features being hedged). Any differences in value movements on these derivatives between the static long-term volatility assumption and implied volatility or average Corporate AA interest rates and ending Corporate AA interest rates are reflected as a component of short-term fluctuations. The types of derivatives used by Jackson and their purpose are as follows:

- Interest rate swaps generally involve the exchange of fixed and floating payments over the period for when Jackson holds the instrument without an exchange of the underlying principal amount. These agreements are used for hedging purposes;
- put-swaption contracts provide the purchaser with the right, but not the obligation, to require the writer to pay the present value of a long-duration interest rate swap at future exercise dates. Jackson purchases and writes put-swaptions with maturities up to 10 years. On a net basis, put-swaptions hedge against significant upward movements in interest rates;
- equity index futures contracts and equity index call and put options are used to hedge Jackson's obligations associated with its issuance of fixed indexed immediate and deferred annuities and certain VA guarantees. These annuities and guarantees contain embedded options which are fair valued for financial reporting purposes;
- total return swaps in which Jackson receives equity returns or returns based on reference pools of assets in exchange for short-term floating rate payments based on notional amounts, are held for both hedging and investment purposes;
- cross-currency swaps, which embody spot and forward currency swaps and additionally, in some cases, interest rate swaps and equity index swaps, are entered into for the purpose of hedging Jackson's foreign currency denominated funding agreements supporting trust instrument obligations;

- spread cap options are used as a macro-economic hedge against declining interest rates. Jackson receives quarterly settlements based on the spread between the two-year and the 10-year constant maturity swap rates in excess of a specified spread; and
- credit default swaps, represent agreements under which Jackson has purchased default protection on certain underlying corporate bonds held in its portfolio. These contracts allow Jackson to sell the protected bonds at par value to the counterparty in the event of their default in exchange for periodic payments made by Jackson for the life of the agreement.

Note D3(i) parts (iii) and (iv) show the sensitivities of Jackson's results through its exposure to equity risk and interest rate risk.

f Process for setting assumptions and determining contract liabilities

Under the MSB of reporting applied under IFRS 4 for insurance contracts, providing the requirements of the Companies Act, UK GAAP standards and the ABI SORP are met, it is permissible to reflect the previously applied UK GAAP basis. Accordingly, and consistent with the basis explained in note A4, in the case of Jackson the carrying values of insurance assets and liabilities are consolidated into the group accounts based on US GAAP.

Under US GAAP, investment contracts (as defined for US GAAP purposes) are accounted for by applying in the first instance a retrospective deposit method to determine the liability for policyholder benefits. This is then augmented by potentially three additional amounts. These amounts are for:

- any amounts that have been assessed to compensate the insurer for services to be performed over future periods (i.e. deferred income);
- any amounts previously assessed against policyholders that are refundable on termination of the contract; and
- any probable future loss on the contract (i.e. premium deficiency).

Capitalised acquisition costs and deferred income for these contracts are amortised over the life of the book of contracts. The present value of the estimated gross profits is generally computed using the rate of interest that accrues to policyholder balances (sometimes referred to as the contract rate). Estimated gross profits include estimates of the following elements, each of which will be determined based on the best estimate of amounts of the following individual elements over the life of the book of contracts without provision for adverse deviation for:

- amounts expected to be assessed for mortality less benefit claims in excess of related policyholder balances;
- amounts expected to be assessed for contract administration less costs incurred for contract administration;
- amounts expected to be earned from the investment of policyholder balances less interest credited to policyholder balances;
- amounts expected to be assessed against policyholder balances upon termination of contracts (sometimes referred to as surrender charges); and
- other expected assessments and credits.

VA contracts written by Jackson may, as described above, provide for GMDB, GMIB, GMWB and GMAB features. In general terms, liabilities for these benefits are accounted for under US GAAP by using estimates of future benefits and fees under best estimate persistency assumptions.

In accordance with SOPO3-01 (Accounting and Reporting by Insurance Enterprises for Certain Non-traditional Long Duration Contracts and for Separate Accounts) which specifies how certain guarantee features should be accounted for under US GAAP, the GMDB liability is not fair valued but is instead determined each period end by estimating the expected value of death benefits in excess of the projected account balance and recognising the excess ratably over the life of the contract based on total expected assessments. At 31 December 2007, 31 December 2008 and 31 December 2009, the GMDB liability was valued using a series of deterministic investment performance scenarios, a mean investment return of 8.4% and assumptions for lapse, mortality and expense that are the same as those used in amortising the capitalised acquisition costs.

The direct GMIB liability is determined by estimating the expected value of the annuitisation benefits in excess of the projected account balance at the date of annuitisation and recognising the excess ratably over the accumulation period based on total expected assessments.

The assumptions used for calculating the direct GMIB liability at 31 December 2007, 2008 and 2009 are consistent with those used for calculating the GMDB liability.

Jackson regularly evaluates estimates used and adjusts the additional GMDB and GMIB liability balances, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

GMIB benefits are essentially fully reinsured, subject to annual claim limits. As this reinsurance benefit is net settled, it is considered to be a derivative under IAS 39 and is, therefore, recognised at fair value with the change in fair value included as a component of short-term derivative fluctuations.

Most GMWB features are considered to be embedded derivatives under IAS 39. Therefore, provisions for these benefits are recognised at fair value, with the change in fair value included in operating profit based on longer-term investment returns. Certain GMWB features guarantee payments over a lifetime and, therefore, include mortality risk. Provisions for these GMWB amounts are valued consistent with the GMDB valuation method discussed above.

For GMWB and GMIB reinsurance embedded derivatives that are fair valued under IAS 39, Jackson bases its volatility assumptions solely on implied market volatility with no reference to historical volatility levels and explicitly incorporates Jackson's own credit risk in determining discount rates.

For 2008 and 2009, volatility assumptions are based on a weighting of available market data on implied volatility for durations up to ten years, at which point the projected volatility is held constant. Non-performance risk is incorporated into the calculation through the use of discount interest rates sourced from a AA corporate credit curve. Other risk margins, particularly for market illiquidity and policyholder behaviour are also incorporated into the model through the use of explicitly conservative assumptions. On a periodic basis, Jackson rationalises the resulting fair values based on comparisons to other models and market movements.

With the exception of the GMDB, GMIB, GMWB and GMAB features of VA contracts, the financial guarantee features of Jackson's contracts are in most circumstances not explicitly valued, but the impact of any interest guarantees would be reflected as they are earned in the current account value (i.e. the US GAAP liability).

For traditional life insurance contracts, provisions for future policy benefits are determined under US GAAP using the net level premium method and assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviation.

Institutional products are accounted for as investment contracts under IFRS with the liability classified as being in respect of financial instruments rather than insurance contracts, as defined by IFRS 4. In practice, there is no material difference between the IFRS and US GAAP basis of recognition and measurement for these contracts.

Certain institutional products representing obligations issued in currencies other than US dollars have been hedged for changes in exchange rates using cross-currency swaps. The fair value of derivatives embedded in funding agreements, as well as foreign currency transaction gains and losses, are included in the carrying value of the trust instruments supported by funding agreements recorded in other non-insurance liabilities.

g Reinsurance

The principal reinsurance ceded by Jackson outside the Prudential Group is on term life insurance, direct and assumed accident and health business and GMIB variable annuity guarantees. In 2007, 2008 and 2009 respectively, the premiums for such ceded business amounted to £60 million, £68 million and £82 million. Net commissions received on ceded business and claims incurred ceded to external reinsurers totalled £10 million and £47 million, respectively, during 2007, £10 million and £49 million respectively, during 2008 and £12 million and £66 million respectively, during 2009. There were no deferred gains or losses on reinsurance contracts in 2007, 2008 or 2009. The reinsurance asset for business ceded outside the Prudential Group was £436 million, £800 million and £667 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

h Effect of changes in assumptions used to measure insurance assets and liabilities

a Measurement basis for embedded derivatives of variable annuity business and other policyholder liability

Certain variable annuity products sold by Jackson include Guaranteed Minimum Withdrawal Benefits ("GMWB") which, in accordance with the Prudential Group's accounting policies, are measured within the IFRS balance sheet at fair value. This requires a number of assumptions related to projected future cash flows, including those driven by policyholder behaviours such as lapses, fund selections and withdrawals utilisation. During 2009 the GMWB utilisation assumptions were revised to take account of the more recent experience of policyholder behaviour. Previously policyholder behaviour for the utilisation of GMWB was assumed to be largely driven by the extent to which benefits were 'in the money'. For 2009, the assumption has been altered to take account of recent experience which shows that the attained age of the policyholder is the key factor in determining utilisation levels. This has led to a release in policyholder liabilities of £96 million which is offset by a corresponding DAC amortisation charge of £68 million to give an overall impact on profit before tax of £28 million. This assumption change has been offset by sundry other assumption changes such that the overall impact on operating profit of policyholder liability assumption changes, after taking into account DAC amortisation offsets, is a charge of £4 million.

In 2008 there were no changes of assumptions that had a material effect on the Jackson results. There was a change in estimation technique relating to the measurement of the Guaranteed Minimum Withdrawal Benefit ("GMWB") features of Jackson's variable annuity products and the reinsurance of the Guaranteed Minimum Income Benefit

("GMIB"). In 2008 these features were valued using implied current equity volatility levels rather than historic long-term levels and the use of AA corporate bond rates rather than Libor based swap rates as the reference basis for determining the discount rate. The cumulative effect of these two changes was to reduce the total loss in 2008 by £47 million.

b Deferred acquisition costs

Income statement — amortisation for variable annuity business

Under IFRS 4, the Prudential Group applies US GAAP to the insurance assets and liabilities of Jackson. Under US GAAP, acquisition costs for Jackson's fixed and variable annuity business are deferred and then amortised in line with the expected emergence of margins. The amortisation profile is dependant on assumptions which, for variable annuity business, the key assumption is the expected level of equity market returns. For 2007, 2008 and 2009 a rate of 8.4% has been applied using, as is industry practice, a mean reversion methodology.

The mean reversion methodology is applied with the objective of adjusting the amortisation of deferred acquisition costs that would otherwise be highly volatile for the fact that the expected level of future gross profits fluctuates for altered variable annuity asset values arising from changes in equity market levels at the end of each reporting period.

The mean reversion methodology achieves this objective by dynamic adjustment to the level of expectations of short-term future investment returns. Under the methodology the projected returns for the next five years are, for the purposes of determining the amortisation profile, set so that normally combined with the actual returns for the current and preceding two years the average rate of return is 8.4%. The mean reversion methodology does, however, include a cap of 15% per annum on the projected return for each of the next five years. Projected returns after the next five years are set at 8.4%. For 2008 following the fall in equity markets in that year, this capping effect applied to restrict the projected returns below the rate of approximately 20% per annum level that would have otherwise applied to the first five years. Although equity markets rose during the year, the return in 2008 was such that the cap remains in place at 31 December 2009, albeit at a lower level.

The DAC amortisation reflected in the 2008 results, after incorporating the mean reversion, increased by some £140 million, of which £40 million arises due to the capping feature. In 2009, following improvements in equity markets, no such DAC acceleration arose during the period and DAC amortisation fell accordingly.

Statement of changes in equity — 'shadow DAC adjustments'

Consequent upon the unrealised valuation movement in 2007, 2008 and 2009 respectively, of negative £244 million, negative £2,104 million, and positive £2,669 million, there is a credit of £88 million, a credit of £831 million and a debit of £1,069 million, for 2007, 2008 and 2009 respectively, for altered 'shadow' amortisation booked within other comprehensive income. These adjustments reflect movement from period to period in the changes to the pattern of reported gross profits that would have happened if the assets had been sold, crystallising the loss, and the proceeds reinvested at yields currently available in the market. At 31 December 2008 and 2009, cumulative 'shadow DAC balance' was positive £1,192 million and negative £10 million, respectively.

i Sensitivity of IFRS basis profit and equity to market and other risks

i Currency fluctuations

Consistent with the Prudential Group's accounting policies, the profits of the Prudential Group's US operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2007, 2008 and 2009 respectively, the rates were US$2.00, US$1.85, and US$1.57 and US$1.99, US$1.44 and U$1.61 to £1 sterling, respectively.

A 10% increase or decrease in these rates would reduce or increase profit (loss) before tax attributable to shareholders, profit for the year and shareholders' equity attributable to US insurance operations respectively as follows:

	A 10% increase in exchange rates			A 10% decrease in exchange rates		
	2007	2008	2009	2007	2008	2009
	£m	£m	£m	£m	£m	£m
Profit (loss) before tax attributable to shareholders*	(39)	59	(44)	48	(72)	54
Profit (loss) for the year	(29)	51	(54)	35	(62)	65
Shareholders' equity attributable to US insurance operations	(242)	(158)	(274)	296	193	335

* Sensitivity on (loss) profit before tax i.e. aggregate of the operating profit based on longer-term investment returns and short-term fluctuations, as discussed in note B1.

ii Other sensitivities

The principal determinants of variations in operating profit based on longer-term returns are:

- Growth in the size of assets under management covering the liabilities for the contracts in-force;
- variations in fees and other income, offset by variations in market value adjustment payments and, where necessary, strengthening of liabilities;
- incidence of guarantees and the effectiveness of the related hedge programme; and
- spread returns for the difference between investment returns and rates credited to policyholders.

For the purpose of determining longer-term returns, adjustment is necessary for the normalisation of investment returns to remove the effects of short-term volatility in investment returns.

- amortisation of deferred acquisition costs.

For term business, acquisition costs are deferred and amortised in line with expected premiums. For annuity business, acquisition costs are deferred and amortised in line with expected gross profits on the relevant contracts. For interest-sensitive business, the key assumption is the expected long-term spread between the earned rate and the rate credited to policyholders, which is based on an annual spread analysis. In addition, expected gross profits depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges) all of which are based on a combination of actual experience of Jackson, industry experience and future expectations.

A detailed analysis of actual experience is measured by internally developed mortality and persistency studies. For variable annuity business, the key assumption is the expected long-term level of equity market returns, which for 2007, 2008 and 2009 was 8.4% per annum implemented using a mean reversion methodology. These returns affect the level of future expected profits through their effects on the fee income and the required level of provision for guaranteed minimum death benefit claims. The mean reversion methodology dampens the impact of equity market movements during a particular year, but does not fully eliminate the effects of movements in the equity markets.

In addition, the mean reversion methodology includes both a cap and a floor that determine the maximum impact that the methodology may have. Due to the significant market movements during 2008, Jackson exceeded the cap on future equity market returns, resulting in a higher level sensitivity to market movements than would have been recognised had the cap not been met at the end of 2008. Given the low market return in 2008 this cap remained in place at 31 December 2009 and so the higher level of sensitivity remains.

Except to the extent of mortality experience, which primarily affects profits through variations in claim payments and GMDB reserves, the profits of Jackson are relatively insensitive to changes in insurance risk.

iii Exposure to equity risk

As noted in note D3(e), Jackson is exposed to equity risk through the options embedded in the fixed indexed liabilities and GMDB and GMWB guarantees included in certain VA benefits. This risk is managed using a comprehensive equity hedging programme to minimise the risk of a significant economic impact as a result of increases or decreases in equity market levels while taking advantage of naturally offsetting exposures in Jackson's operations. Jackson purchases external futures and options that hedge the risks inherent in these products, while also considering the impact of rising and falling separate account fees.

As a result of this hedging programme, if the equity markets were to increase further in the future, Jackson's free-standing derivatives would decrease in value. However, over time, this movement would be broadly offset by increased separate account fees and reserve decreases, net of the related changes to amortisation of deferred acquisition costs. Due to the nature of the free-standing and embedded derivatives, this hedge while effective on an economic basis, may not completely mute the immediate impact of the market movements as the free-standing derivatives reset immediately while the hedged liabilities reset more slowly and fees are recognised prospectively. The opposite impacts would be observed if the equity markets were to decrease.

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, based on the hedges in place at that time, it is estimated that an immediate decrease in the equity markets of 10% would result in an accounting impact, net of related DAC amortisation, before tax of up to, £30 million benefit, £20 million charge and £60 million benefit, excluding the impact on future separate account fees. After related deferred tax there would have been an estimated change in shareholders' equity at 31 December 2007, 31 December 2008 and 31 December 2009, respectively of up to £20 million increase, £15 million decrease and £40 million increase. Jackson extended the range of reasonably possible movements in the value of equity securities, partnerships in investment pools and other financial derivatives at 31 December 2008 and 2009. Consequently an immediate decrease in the equity markets of 20% would result in an accounting charge, net of related DAC amortisation, before tax of up to, £40 million at 31 December 2008, and an accounting benefit of £110 million at 31 December 2009 respectively, excluding the impact on future separate account fees. After related deferred tax there would have been an estimated reduction in shareholders' equity at 31 December 2008, of up to £30 million and an increase in shareholders' equity of up to £80 million at 31 December 2009.

An immediate increase in the equity markets of 10% and 20% is estimated to result in an approximately equal and opposite estimated effect on profit and shareholders' equity as that disclosed above for a decrease.

The actual impact on financial results would vary contingent upon the volume of new product sales and lapses, changes to the derivative portfolio, correlation of market returns and various other factors including volatility, interest rates and elapsed time.

In addition, Jackson is also exposed to equity risk from its holding of equity securities, partnerships in investment pools and other financial derivatives.

A range of reasonably possible movements in the value of equity securities, partnerships in investment pools and other financial derivatives have been applied to Jackson's holdings at 31 December 2007, 31 December 2008 and 31 December 2009. The table below shows the sensitivity to reasonable per cent falls in value at each year end and the impact that this would have on pre-tax profit, net of related changes in amortisation of DAC, profit after tax and shareholders' equity.

	2007	2008			2009	
	A decrease of 10%	A decrease of 40%	A decrease of 20%	A decrease of 10%	A decrease of 20%	A decrease of 10%
	£m	£m			£m	
Pre-tax profit, net of related changes in amortisation of DAC	(76)	(255)	(141)	(98)	(117)	(58)
Related deferred tax effects	26	89	49	34	41	20
Net sensitivity of profit after tax and shareholders' equity	(50)	(166)	(92)	(64)	(76)	(38)

The disclosure of the effect of a 40% fall for the 2008 year-end was included because of the exceptional market conditions at that time. These conditions have now abated and the disclosure is no longer appropriate.

In the equity risk sensitivity analysis given above the Prudential Group has, for 2009, considered the impact of an instantaneous 20% fall in equity markets. If equity markets were to fall by more than 20%, the Prudential Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Prudential Group would be able to put in place mitigating management actions.

iv Exposure to interest rate risk

Notwithstanding the market risk exposure described in note D3(e), except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of fixed annuity liabilities of Jackson products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement described in notes D3(d) and D3(f). The GMWB features attaching to variable annuity business represents embedded derivatives which are fair valued and so will be sensitive to changes in interest rate.

Debt securities and related derivatives are marked to fair value. Value movements on derivatives, again net of related changes to amortisation of DAC and deferred tax, are recorded within profit and loss. Fair value movements on debt securities, net of related changes to amortisation of DAC and deferred tax, are recorded within other comprehensive income. At 31 December 2008 Jackson extended the range of the movements that were reasonably possible to occur to include both 1% and 2%. This continued at 31 December 2009.

The estimated sensitivity of the above items and policyholder liabilities to a 1%, and 2% decrease and increase in interest rates at 31 December, where applicable, is as follows:

	2007		2008				2009			
	A 1% decrease	A 1% increase	A 2% decrease	A 1% decrease	A 1% increase	A 2% increase	A 2% decrease	A 1% decrease	A 1% increase	A 2% increase
	£m		£m				£m			
Profit and loss										
Direct effect										
Derivatives value change	(116)	163	(575)	(268)	283	639	(319)	(148)	159	370
Policyholder liabilities	(38)	29	(517)	(218)	182	350	(418)	(185)	170	334
Related effect on amortisation of DAC	52	(58)	498	215	(193)	(395)	364	162	(156)	(328)
Pre-tax profit effect										
Operating profit based on longer-term investment returns	(15)	11	(128)	(59)	64	146	(144)	(62)	56	109
Short-term fluctuations in investment returns	(87)	123	(466)	(212)	208	448	(229)	(109)	117	267
	(102)	134	(594)	(271)	272	594	(373)	(171)	173	376
Related effect on charge for deferred tax	36	(47)	206	94	(95)	(207)	131	60	(60)	(131)
Net profit effect	(66)	87	(388)	(177)	177	387	(242)	(111)	113	245
Other comprehensive income										
Direct effect on carrying value of debt securities	848	(848)	2,476	1,238	(1,238)	(2,476)	2,183	1,179	(1,179)	(2,183)
Related effect on amortisation of DAC	(212)	212	(619)	(310)	310	619	(764)	(413)	413	764
Related effect on movement in deferred tax	(223)	223	(650)	(325)	325	650	(497)	(268)	268	497
Net effect	413	(413)	1,207	603	(603)	(1,207)	922	498	(498)	(922)
Total net effect on IFRS equity	347	(326)	819	426	(426)	(820)	680	387	(385)	(677)

j Duration of liabilities

The table below shows the carrying value of policyholder liabilities. Separately, the Group uses cash flow projections of expected benefit payments as part of the determination of the value of in-force business when preparing EEV basis results. The table below shows the maturity profile of the cash flows used for that purpose for 2007, 2008 and 2009:

	2007		2008		2009	
	Fixed annuity and other business (including GICs and similar contracts)	Variable annuity	Fixed annuity and other business (including GICs and similar contracts)	Variable annuity	Fixed annuity and other business (including GICs and similar contracts)	Variable annuity
	£m		£m		£m	
Policyholder liabilities	19,821	15,027	30,823	14,538	27,672	20,639
	%	%	%	%	%	%
Expected maturity:						
0 to 5 years	51	48	49	46	52	50
5 to 10 years	26	30	26	28	27	28
10 to 15 years	11	13	11	14	10	12
15 to 20 years	5	6	6	7	5	6
20 to 25 years	3	2	3	3	3	2
Over 25 years	4	1	5	2	3	2

The maturity tables shown above have been prepared on a discounted basis. Details of undiscounted cash flows for investment contracts are shown in note G2.

D4: Asian insurance operations

a Summary statement of financial position

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type as at 31 December.

	2007 Total	2008 Total	Asian insurance operations: With-profits business note i	Asian insurance operations: Unit-linked assets and liabilities	Asian insurance operations: Other	2009 Total
	£m	£m	£m	£m	£m	£m
Assets						
Intangible assets attributable to shareholders:						
Goodwill(note iii)	111	111	—	—	80	80
Deferred acquisition costs and other intangible assets	745	1,247	—	—	822	822
Total	856	1,358	—	—	902	902
Intangible assets attributable to with-profit funds:						
Deferred acquisition costs and other intangible assets	—	113	97	—	—	97
Deferred tax assets	73	101	—	—	132	132
Other non-investment and non-cash assets(note iii)	689	1,416	234	83	563	880
Investments of long-term business and other operations:						
Investment properties	14	20	—	—	11	11
Investment accounted for using the equity method	—	—	—	—	2	2
Financial investments:						
Loans(note ii)	1,087	1,705	781	27	399	1,207
Equity securities and portfolio holdings in unit trusts	9,804	8,077	3,691	7,224	267	11,182
Debt securities(note c)	6,920	11,113	4,988	2,462	2,534	9,984
Other investments	42	144	73	44	141	258
Deposits	377	750	14	196	536	746
Total investments	18,244	21,809	9,547	9,953	3,890	23,390
Cash and cash equivalents	679	1,501	225	235	377	837
Total assets	20,541	26,298	10,103	10,271	5,864	26,238
Equity and liabilities						
Equity						
Shareholders' equity	1,369	2,167	—	—	1,462	1,462
Minority interests	7	7	—	—	1	1
Total equity	1,376	2,174	—	—	1,463	1,463
Liabilities						
Policyholder liabilities and unallocated surplus of with-profits funds:						
Contract liabilities (including amounts in respect of contracts classifies as investment contract under IFRS 4)	17,033	20,909	8,808	9,717	3,333	21,858
Unallocated surplus of with-profits funds	146	160	53	—	—	53
Total	17,179	21,069	8,861	9,717	3,333	21,911
Other non-insurance liabilities:						
Operational borrowings attributable to shareholders-financed operations	—	130	—	—	210	210
Deferred tax liabilities	362	441	266	12	106	384
Other non-insurance liabilities	1,624	2,484	976	542	752	2,270
Total liabilities	19,165	24,124	10,103	10,271	4,401	24,775
Total equity and liabilities	20,541	26,298	10,103	10,271	5,864	26,238

Notes

i The statement of financial position for with-profits business comprises the with-profits assets and liabilities of the Hong Kong, Malaysia and Singapore with-profits operations. Assets and liabilities of other participating business are included in the column for 'other businesses'.

ii The loans of the Prudential Group's Asian insurance operations of £1,087 million, £1,705 million and £1,207 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, comprise mortgage loans of £132 million, £238 million and £13 million, policy loans of £430 million, £675 million and £437 million and other loans of £525 million, £792 million and £757 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. The mortgage and policy loans are secured by properties and life insurance policies respectively. The majority of the other loans are commercial loans held by the Malaysian operation and which are all investment graded by two local rating agencies.

iii Further segmental analysis

No goodwill attributable to any individual country included in the Asia total of £111 million, £111 million and £80 million, exceeds 10% of the Prudential Group goodwill attributable to shareholders of £1,341 million, £1,341 million and £1,310 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Included within "Other non-investment and non-cash assets" of £689 million, £1,416 million and £880 million, as at 31 December 2007, 31 December 2008 and 31 December 2009, was "Property, plant and equipment" of £98 million, £144 million and £94 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. No individual Country in Asia held property, plant and equipment at the end of the year which exceeds 10% of the Prudential Group total of £1,012 million, £635 million and £367 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

Summary policyholder liabilities (net of reinsurance) and unallocated surplus

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the policyholder liabilities net of reinsurance of £12 million, £24 million and £18 million and unallocated surplus for Asian operations of £17.2 billion, £21.0 billion and £21.9 billion comprised the following:

	2007	2008	2009
	£m	£m	£m
Singapore	5,462	5,426	6,960
Hong Kong	3,901	5,100	5,762
Taiwan	2,781	4,024	545
Malaysia	1,201	1,587	1,823
Japan	695	1,100	1,094
Other countries	3,127	3,808	5,709
Total Asian operations	17,167	21,045	21,893

b Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of Asian insurance operations from the beginning of the year to the end of the year is as follows:

	With-profits business	Unit-linked assets and liabilities	Other	Asian insurance operations Total
	£m	£m	£m	£m
At 1 January 2007	5,500	4,134	3,255	12,889
Premiums				
New business	372	1,676	160	2,208
In-force	488	781	481	1,750
	860	2,457	641	3,958
Surrenders	(146)	(689)	(197)	(1,032)
Maturities/Deaths	(183)	(52)	(160)	(395)
Net cash flows	531	1,716	284	2,531
Shareholders transfer post tax	(21)	—	—	(21)
Investment-related items and other movements	441	914	103	1,458
Foreign exchange translation differences(note (i))	96	207	19	322
At 31 December 2007/1 January 2008	6,547	6,971	3,661	17,179
Premiums				
New business	391	1,252	233	1,876
In-force	647	1,009	630	2,286
	1,038	2,261	863	4,162

	With-profits business	Unit-linked assets and liabilities	Other	Asian insurance operations Total
	£m	£m	£m	£m
Surrenders	(354)	(614)	(223)	(1,191)
Maturities/Deaths	(181)	(14)	(159)	(354)
Net cash flows	503	1,633	481	2,617
Shareholders transfer post tax	(23)	—	—	(23)
Investment-related items and other movements	(1,320)	(3,158)	185	(4,293)
Foreign exchange translation differences (note (i))	2,387	1,774	1,428	5,589
At 31 December 2008/1 January 2009	8,094	7,220	5,755	21,069
Premiums				
New business(note (ii))	46	643	517	1,206
In-force	777	1,223	601	2,601
	823	1,866	1,118	3,807
Surrenders	(361)	(666)	(174)	(1,201)
Maturities/Deaths	(253)	(19)	(70)	(342)
Net cash flows	209	1,181	874	2,264
Change in other reserving basis	—	—	(4)	(4)
Change in reserving basis in Malaysia(note (iii))	—	(9)	(54)	(63)
Shareholders' transfers post tax	(20)	—	—	(20)
Investment-related items and other movements(note (iv))	1,431	2,661	150	4,242
Foreign exchange translation differences(note (i))	(853)	(612)	(604)	(2,069)
Disposal of Taiwan agency business (note (v))	0	(724)	(2,784)	(3,508)
At 31 December 2009	8,861	9,717	3,333	21,911

i Movements in the year have been translated at the average exchange rate for the year ended 31 December 2007, 31 December 2008 and 31 December 2009. The closing balance has been translated at the closing spot rates as at 31 December 2007, 31 December 2008 and 31 December 2009. Differences upon retranslation are included in foreign exchange differences.

ii In 2009, the increase in policyholder liabilities due to new business premium for the with-profits business fell by £345 million to £46 million. This is predominantly driven by a fall in sales of single premium with-profits policies in Hong Kong following the withdrawal of the PruSaver product in 2009. The increase in policyholder liabilities due to new business premium for Asia unit-linked business was lower by £609 million in 2009, in line with decreases in single premium sales during the year.

iii The change in reserving basis in Malaysia of £63 million reflects the change made following the adoption of a risk based capital ("RBC") approach to the local regulatory reporting in that country.

iv The positive investment related items and other movements for with-profits (£1,431 million) and unit-linked business (£2,661 million) were mainly driven from Asian equity market gains in the period.

v The disposal of Taiwan agency business reflects the liabilities transferred at the date of disposal.

c Information on credit risks of debt securities

Additional supplementary disclosure has been provided in 2009 to set out the operating segment financial position by business type. The following table summarises the credit quality of the debt securities of the Asian insurance operations as at 31 December by rating agency rating:

	2007 Total	2008 Total	2009 With-profits business	2009 Unit-linked business	2009 Other business	2009 Total
	£m	£m	£m	£m	£m	£m
S&P — AAA	2,284	2,632	1,778	295	186	2,259
S&P — AA+ to AA−	1,994	3,746	657	345	592	1,594
S&P — A+ to A−	675	808	749	463	284	1,496
S&P — BBB+ to BBB−	193	902	472	103	107	682
S&P — Other	149	253	397	3	517	917
	5,295	8,341	4,053	1,209	1,686	6,948
Moody's — Aaa	201	494	86	33	15	134
Moody's — Aa1 to Aa3	45	108	38	32	279	349
Moody's — A1 to A3	28	398	12	283	14	309
Moody's — Baa1 to Baa3	19	60	17	16	7	40
Moody's — Other	58	50	—	—	15	15
	351	1,110	153	364	330	847
Fitch	1	41	—	38	1	39
Other	1,273	1,621	782	851	517	2,150
Total debt securities	6,920	11,113	4,988	2,462	2,534	9,984

Of the £598 million, £555 million and £517 million of debt securities for other business that are not rated in the table above, £317 million, £231 million and £225 million are in respect of government bonds, and £83 million, £221 million and £265 million are in respect of corporate bonds rated as investment grade by local external ratings agencies and £71 million, nil and £22 million of structured deposits issued by banks which are themselves rated but where the specific deposits have not been as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

d Products and guarantees

The life insurance products offered by the Group's Asian operations include a range of with-profits and non-participating term, whole life, endowment and unit-linked policies. The Asian operations also offer health, disability, critical illness and accident coverage to supplement its core life products.

The terms and conditions of the contracts written by the Asian operations and, in particular, the products' options and guarantees, vary from territory to territory depending upon local market circumstances.

In general terms, the Asian participating products provide savings and protection where the basic sum assured can be enhanced by a profit share (or bonus) from the underlying fund as determined at the discretion of the insurers. The Asian operations' non-participating term, whole life and endowment products offer savings and/or protection where the benefits are guaranteed or determined by a set of defined market-related parameters. Unit-linked products combine savings with protection, the cash value of the policy depends on the value of the underlying unitised funds. Health and protection policies provide mortality or morbidity benefits and include health, disability, critical illness and accident coverage. Health and protection products are commonly offered as supplements to main life policies but can be sold separately.

Subject to local market circumstances and regulatory requirements, the guarantee features described in note D2(d) in respect of UK business broadly apply to similar types of participating contracts written in the Hong Kong branch, Singapore and Malaysia. Participating products have both guaranteed and non-guaranteed elements.

Non-participating long-term products are the only ones where the insurer is contractually obliged to provide guarantees on all benefits. Investment-linked products have the lowest level of guarantee if any.

Product guarantees in Asia can be broadly classified into four main categories, namely premium rate, cash value and interest rate guarantees, policy renewability, and convertibility options.

The risks on death coverage through premium rate guarantees are low due to appropriate product pricing.

Cash value and interest rate guarantees are of three types:

- Maturity values

  Maturity values are guaranteed for non-participating products and on the guaranteed portion of participating products. Declared annual bonuses are also guaranteed once vested. Future bonus rates and cash dividends are not guaranteed on participating products.

- Surrender values

  Surrender values are guaranteed for non-participating products and on the guaranteed portion of participating products. The surrender value of declared reversionary bonuses are also guaranteed once vested. Market value adjustments and surrender penalties are used where the law permits such adjustments in cash values.

- Interest rate guarantees

  It is common in Asia for regulations or market-driven demand and competition to provide some form of capital value protection and minimum crediting interest rate guarantees. This would be reflected within the guaranteed maturity and surrender values.

  The guarantees are borne by shareholders for non-participating and investment-linked (non-investment guarantees only) products. Participating product guarantees are predominantly supported by the segregated life funds and their estates.

Whole of life contracts with floor levels of policyholder benefits that accrue at rates set at inception and do not vary subsequently with market conditions are written in the Korean life operations. This is to a much lesser extent than the policies written by the Taiwan agency business which was sold in the first half of 2009, as Korea has a much higher proportion of linked and health business. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the Korean business had non-linked liabilities of £261 million, £312 million and £349 million, and linked liabilities of £728 million, £742 million and £1,173 million respectively.

The other area of note in respect of guarantees is the Japanese business, where pricing rates are higher than current bond yields. Lapse risk is a feature in that policyholders could potentially surrender their policies on guaranteed terms if interest rates significantly increased leaving the potential for losses if bond values had depreciated significantly. However, the business is matched to a relatively short realistic liability duration.

The method for determining liabilities of insurance contracts for UK GAAP, and hence IFRS, purposes for some Asian operations is based on US GAAP principles and this method applies to contracts with cash value and interest rate guarantees. Following standard US GAAP procedure, premium deficiency reserve calculations are performed each year to establish whether the carrying values of the liabilities are sufficient.

On the US GAAP basis the calculations are deterministic, that is to say based on a single set of projections, and expected long-term rates of return are applied.

e Exposure to market risk

The Asian operations sell with-profits and unit-linked policies and, although the with-profits business generally has a lower terminal bonus element than in the UK, the investment portfolio still contains a proportion of equities and, to a lesser extent, property. Non-participating business is largely backed by debt securities or deposits. The exposure to market risk of the Group arising from its Asian operations is therefore at modest levels. This arises from the fact that the Asian operations have a balanced portfolio of with-profits, unit-linked and other types of business.

f Process for setting assumptions and determining liabilities

The future policyholder benefit provisions for Asian businesses in the Prudential Group's IFRS accounts and previously under the MSB, are determined in accordance with methods prescribed by local GAAP adjusted to comply, where necessary, with UK GAAP.

For Asian operations in countries where local GAAP is not well established and in which the business written is primarily non-participating and linked business, US GAAP is used as the most appropriate reporting basis. This basis is applied in Japan and Vietnam and, materially for 2007 and 2008 but less so for 2009 following the sale of the agency business, in Taiwan. The future policyholder benefit provisions for non-linked business are determined using the net level premium method, with an allowance for surrenders, maintenance and claims expenses. Rates of interest used in establishing the policyholder benefit provisions vary by operation depending on the circumstances attaching to each block of business.

g Reinsurance

The Asian businesses cede only minor amounts of business outside the Prudential Group with immaterial effects on reported profit. During 2007, 2008 and 2009 respectively, reinsurance premiums for externally ceded business were

£52 million, £76 million and £119 million and the reinsurance assets as at 31 December 2007, 31 December 2008 and 31 December 2009 were £12 million, £24 million and £18 million in aggregate.

h Effect of changes in bases, estimates and assumptions used to measure insurance assets and liabilities

a Exceptional credit of £63 million regarding the liability measurement for Malaysia long-term business

For the Malaysia life business, under the basis applied previously, 2008 IFRS basis liabilities were determined on the local regulatory basis using prescribed interest rates such that a high degree of prudence resulted.

As of 1 January 2009, the local regulatory basis has been replaced by the Malaysian authority's risk-based capital ("RBC") framework. In the light of this development, Prudential has remeasured the liabilities by reference to the method applied under the new RBC framework, which is more realistic than the previous approach, but with an overlay constraint to the method such that negative reserves derived at an individual policyholder level are not included. This change has resulted in a one-off release from liabilities at 1 January 2009 of £63 million.

b Changes in key assumptions

There were no changes of assumptions that had a material impact on the 2007 results for Asian operations. There were a number of individually small assumption changes impacting on the 2008 results by £21 million, in aggregate, for Asian operations. Excluding the change in Malaysia as explained above, the result for Asian operations was impacted in 2009 by the effect of a number of other individually small assumptions changes of, in aggregate, £4 million.

c Deferral and amortisation of acquisition costs

Under IFRS, the basis of accounting for insurance assets and liabilities reflects 'grandfathered' GAAP under the Modified Statutory Basis. In general, this requires the deferral and amortisation of acquisition costs in line with the emergence of margins. In 2008, the basis of deferral and amortisation was adjusted for a number of territories to better reflect the MSB requirement as follows:

For the India life operation, reflecting the initial development stage of the business, acquisition costs had previously not been deferred. In 2008, £19 million of deferred acquisition costs, net of amortisation in the year, were established.

For the Korea life business, refinements were made to move to a more appropriate basis which resulted in a credit of £35 million (£9 million of which related to the 1 January 2008 balance).

For Singapore, refinements were made with a £21 million benefit in 2008 (of which £7 million related to the 1 January 2008 position) where the local risk based capital approach does not provide an appropriate basis of implicit allowance for acquisition costs for certain products and in Hong Kong, adjustments were made with a net overall effect of £10 million in 2008.

i Sensitivity of IFRS basis profit and equity to market and other risks

Currency translation

Consistent with the Prudential Group's accounting policies, the profits of the Asian insurance operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2009, the rates for the most significant operations are given in note B4.

A 10% increase or decrease in these rates would have reduced or increased profit before tax attributable to shareholders, profit for the year and shareholders' equity, excluding goodwill, attributable to Asian operations respectively as follows:

	A 10% increase in exchange rates			A 10% decrease in exchange rates		
	2007	2008	2009	2007	2008	2009
	£m	£m	£m	£m	£m	£m
Profit before tax attributable to shareholders*	(16)	(14)	(40)	20	18	49
Profit for the year	(10)	(6)	(35)	13	8	43
Shareholders' equity, excluding goodwill, attributable to Asian operations	(124)	(202)	(129)	151	246	158

* Sensitivity on profit before tax i.e. aggregate of the operating profit based on longer-term investment returns, short-term fluctuations in investment returns, and actuarial gains and losses on defined benefit pension schemes but excluding for 2009 the loss on sale and results for Taiwan agency business, as discussed in note B1.

Other risks

i With-profits business

Similar principles to those explained for UK with-profits business apply to profit emergence for the Asian with-profits business. Correspondingly, the profit emergence reflects bonus declaration and is relatively insensitive to period by period fluctuations in insurance risk or interest rate movements.

ii Unit-linked business

As for the UK insurance operations, the profits and shareholders' equity related to the Asian operations is primarily driven by charges related to invested funds. For the Asian operations, substantially all of the contracts are classified as insurance contracts under IFRS 4, i.e. containing significant insurance risk. The sensitivity of profits and equity to changes in insurance risk is minor and, to interest rate risk, not material.

iii Other business

a) Interest rate risk for Taiwan

For 2008 the principal other business of Asian operations that was most sensitive to movements in interest rates was the whole of life business written in Taiwan. In June 2009 Prudential completed the sale of its agency distribution business and associated liabilities and its agency force in Taiwan to China Life Insurance Company Ltd. as explained in note I1. For 2009 the assets and liabilities of the element of Taiwan business retained by Prudential are relatively less sensitive to variances in interest rates, with a reasonably possible decrease in interest rates of 0.5% leading to an increase in IFRS pre-tax profits of £24 million. After adjusting these results for deferred tax the reasonably possible effect on shareholders' equity is £19 million. A 0.5% increase in interest rates is estimated to have an approximately equal and opposite effect on profit and shareholders' equity.

b) Interest rate risk for other business excluding Taiwan

Asian operations offer a range of insurance and investment products, predominately with-profits and non-participating term, whole life, endowment and unit-linked. Excluding with-profit and unit-linked business along with Taiwan, the results of the Asian business are sensitive to the vagaries of routine movements in interest rates.

For the purposes of analysing sensitivity to variations in interest rates, it has been determined for the majority of territories that a movement of 1% in the 10 year government bond rate can be considered reasonably possible. At 31 December 2009, 10 year government bond rates vary from territory to territory and range from 1.3% to 11.45% (2008: 1.17% to 10.18% and 2007: 1.5% to 9.1%). An exception to this arises in Japan where reasonably possible interest rate movements have been determined as 0.5% respectively. (2008: Japan 0.5%, Vietnam 1.5% and 2007: Japan 0.25%, Vietnam 1.5%). These reasonably possible changes would have the following impact:

	2007	2008	2009
	A decrease of 1%*	A decrease of 1%*	A decrease of 1%*
		£m	
Pre-tax	30	56	67
Related deferred tax (where applicable)	(8)	(11)	(17)
Net effect on profit and equity	22	45	50

* 1% sensitivity has been used in all territories except (2007: Japan 0.25% and Singapore 0.5%), (2008: Japan 0.5%, Vietnam 1.5%) and (2009: Japan 0.5%)

The pre-tax impacts, if they arose, would mostly be recorded within the category short-term fluctuations in investment returns in the Group's supplementary analysis of profit before tax.

At 31 December 2009, an increase in the rates of 1% (Japan (0.5%)) is estimated to have the effect of decreasing pre-tax profit by £87 million. After adjusting these results for deferred tax the reasonable possible effect on shareholders' equity is a decrease of £65 million.

c) Equity price risk

The non-linked shareholder business has limited exposure to equity and property investment (£278 million at 31 December 2009.) Generally changes in equity and property investment values are not automatically matched by investments in policyholder liabilities. However for the Vietnam business, to the extent that equity investment appreciation is realised through sales of securities then policyholders' liabilities are adjusted to the extent that policyholders' participate.

The estimated sensitivity to a 10% and 20% (2008: 10%, 20% and 40% and 2007: 10%) change in equity and property prices for shareholder-backed Asian other business, which would be reflected in the short-term fluctuation component of the Group's segmental analysis of profit before tax at 31 December 2007, 2008 and 2009 would be as follows:

	2007	2008			2009	
	A decrease of 10%	A decrease of 40%	A decrease of 20%	A decrease of 10%	A decrease of 20%	A decrease of 10%
	£m		£m		£m	
Pre-tax	(73)	(176)	(88)	(44)	(58)	(29)
Related deferred tax (where applicable)	5	5	3	1	8	4
Net effect on profit and equity	(68)	(171)	(85)	(43)	(50)	(25)

A 10% or 20% (2008: 10%, 20%, or 40% and 2007: 10%) increase in their value is estimated to have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above. The low tax rate effect, which is particularly evident in 2008, relates to the availability of losses in some of the territories.

The disclosure of the effect of a 40% fall for the 2008 year-end was included because of the exceptional market conditions at that time. These conditions have now abated and the disclosure is no longer appropriate.

In the equity risk sensitivity analysis given above the Prudential Group has, for 2009, considered the impact of an instantaneous 20% fall in equity markets. If equity markets were to fall by more than 20%, the Prudential Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Prudential Group would be able to put in place mitigating management actions.

d) Insurance risk

Many of the territories in Asia are exposed to mortality/morbidity risk and provision is made within IFRS policyholder liabilities on a prudent regulatory basis to cover the potential exposure. If these prudent assumptions were strengthened by 5% (estimated at one in ten year shock) then it is estimated that post tax IFRS profit would be impacted by approximately £9 million (with a corresponding change to IFRS shareholders' equity) in 2009. Mortality/morbidity has a symmetrical effect on portfolio and so a weakening of mortality/morbidity assumptions would have an approximately equal and opposite similar impact.

j Duration of liabilities

The table below shows the carrying value of policyholder liabilities. Separately the Group uses cash flow projections of expected benefit payments as part of the determination of the value of in-force business when preparing EEV basis results. The table below shows the maturity profile of the cash flows, taking account of expected future premiums and investment returns, is as follows:

	2007	2008	2009
	£m	£m	£m
Policyholder liabilities	17,033	20,909	21,858
	%	%	%
Expected maturity:			
0 to 5 years	22	23	24
5 to 10 years	22	21	21
10 to 15 years	16	15	15
15 to 20 years	13	13	12
20 to 25 years	9	10	9
Over 25 years	18	18	19

D5: Capital position statement for life assurance businesses

a Summary statement

The Prudential Group's estimated capital position for life assurance businesses with reconciliations to shareholders' equity is shown below. Available capital for each fund or group of companies is determined by reference to local regulation at 31 December 2007, 2008 and 2009.

	2007									
31 December 2007	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operations	M&G (including Prudential Capital)	Parent company and shareholders' equity of other subsidiaries and funds	Group total
	£m									
Group shareholders' equity										
Held outside long-term funds:										
Net assets	—	—	—	550	2,690	1,258	4,498	271	(862)	3,907
Goodwill	—	—	—	—	—	111	111	1,153	77	1,341
Total	—	—	—	550	2,690	1,369	4,609	1,424	(785)	5,248
Held in long-term funds(note iii)	—	—	—	814	—	—	814	—	—	814
Total Group shareholders' equity	—	—	—	1,364	2,690	1,369	5,423	1,424	(785)	6,062
Adjustments to regulatory basis										
Unallocated surplus of with-profits funds(note v)	—	13,813	13,813	—	—	146	13,959			
Shareholders' share of realistic liabilities	—	(4,178)	(4,178)	—	—	—	(4,178)			
Deferred acquisition costs of non-participating business not recognised for regulatory reporting purposes	(4)	(15)	(19)	(143)	(1,928)	(790)	(2,880)			
Jackson surplus notes(note iv)	—	—	—	—	125	—	125			
Investment and policyholder liabilities valuation differences between IFRS and regulatory basis for Jackson(note viii)	—	—	—	—	—	—	—			
Adjustment from IAS 19 basis pension deficit attributable to WPSF to pension liability for regulatory purposes(note vii)	—	(138)	(138)	—	—	—	(138)			
Valuation difference on PAL between IFRS basis and regulatory basis	—	(1,117)	(1,117)	—	—	—	(1,117)			
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis)(note v)	4	355	359	(239)	1,364	149	1,633			
Total adjustments	—	8,720	8,720	(382)	(439)	(495)	7,404			
Total available capital resources of life assurance businesses on local regulatory bases	—	8,720	8,720	982	2,251	874	12,827			

31 December 2007	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operations
				2007 £m			
Policyholder liabilities							
With-profits liabilities of UK regulated with-profits funds:							
Insurance contracts	12,672	34,029	46,701	—	—	3,307	50,008
Investment contracts (with discretionary participating features)	693	28,773	29,466	—	—	84	29,550
Total	13,365	62,802	76,167	—	—	3,391	79,558
Other liabilities:							
Insurance contracts:							
With-profits liabilities of non-UK regulated funds	—	—	—	—	—	2,973	2,973
Unit-linked, including variable annuity	—	2,029	2,029	8,338	15,027	6,971	32,365
Other life assurance business	255	11,494	11,749	14,121	17,899	3,661	47,430
Investment contracts without discretionary participation features (principally unit-linked and similar contracts in the UK and GIC liabilities of Jackson)(note vi)	—	14	14	12,059	1,922	37	14,032
Total	255	13,537	13,792	34,518	34,848	13,642	96,800
Total policyholder liabilities shown in the consolidated statement of financial position	13,620	76,339	89,959	34,518	34,848	17,033	176,358

31 December 2008	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operation	M&G (including Prudential Capital)	Parent company and shareholders' equity of other subsidiaries and funds	Group total
	2008									
	£m									
Group shareholders' equity										
Held outside long-term funds:										
Net assets	—	—	—	735	1,698	2,056	4,489	147	(1,839)	2,797
Goodwill	—	—	—	—	—	111	111	1,153	77	1,341
Total	—	—	—	735	1,698	2,167	4,600	1,300	(1,762)	4,138
Held in long-term funds(note iii)	—	—	—	920	—	—	920	—	—	920
Total Group shareholders' equity	—	—	—	1,655	1,698	2,167	5,520	1,300	(1,762)	5,058
Adjustments to regulatory basis										
Unallocated surplus of with-profits funds(note v)	—	8,254	8,254	—	—	160	8,414			
Shareholders' share of realistic liabilities	—	(2,028)	(2,028)	—	—	—	(2,028)			
Deferred acquisition costs of non-participating business not recognised for regulatory reporting purposes	(3)	(10)	(13)	(128)	(3,962)	(876)	(4,979)			
Jackson surplus notes(note iv)	—	—	—	—	173	—	173			
Investment and policyholder liabilities valuation differences between IFRS and regulatory basis for Jackson(note viii)	—	—	—	—	4,819	—	4,819			
Adjustment from IAS 19 basis pension deficit attributable to WPSF to pension liability for regulatory purposes(note vii)	—	(147)	(147)	—	—	—	(147)			
Valuation difference on PAL between IFRS basis and regulatory basis	—	(1,350)	(1,350)	—	—	—	(1,350)			
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis)(note v)	3	643	646	(474)	30	(41)	161			
Total adjustments	—	5,362	5,362	(602)	1,060	(757)	5,063			
Total available capital resources of life assurance businesses on local regulatory bases	—	5,362	5,362	1,053	2,758	1,410	10,583			

31 December 2008	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operations
	2008						
	£m						
Policyholder liabilities							
With-profits liabilities of UK regulated with-profits funds:							
Insurance contracts	9,260	26,466	35,726	—	—	4,416	40,142
Investment contracts (with discretionary participating features)	494	22,873	23,367	—	—	79	23,446
Total	9,754	49,339	59,093	—	—	4,495	63,588
Other liabilities:							
Insurance contracts:							
With-profits liabilities of non-UK regulated funds	—	—	—	—	—	3,407	3,407
Unit-linked, including variable annuity	—	1,872	1,872	6,041	14,538	7,220	29,671
Other life assurance business	264	12,625	12,889	16,228	27,938	5,755	62,810
Investment contracts without discretionary participation features (principally unit-linked and similar contracts in the UK and GIC liabilities of Jackson)(note vi)	—	—	—	11,584	2,885	32	14,501
Total	264	14,497	14,761	33,853	45,361	16,414	110,389
Total policyholder liabilities shown in the consolidated statement of financial position	10,018	63,836	73,854	33,853	45,361	20,909	173,977

31 December 2009	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operations	M&G (including Prudential Capital)	Parent company and shareholders' equity of other subsidiaries and funds	Group total
	2009									
	£m									
Group shareholders' equity										
Held outside long-term funds:										
Net assets	—	—	—	788	3,011	1,382	5,181	173	(1,507)	3,847
Goodwill	—	—	—	—	—	80	80	1,153	77	1,310
Total	—	—	—	788	3,011	1,462	5,261	1,326	(1,430)	5,157
Held in long-term funds(note iii)	—	—	—	1,114	—	—	1,114	—	—	1,114
Total Group shareholders' equity	—	—	—	1,902	3,011	1,462	6,375	1,326	(1,430)	6,271
Adjustments to regulatory basis										
Unallocated surplus of with-profits funds(note v)	—	9,966	9,966	—	—	53	10,019			
Shareholders' share of realistic liabilities	—	(3,001)	(3,001)	—	—	—	(3,001)			
Deferred acquisition costs of non-participating business not recognised for regulatory reporting purposes	(2)	(7)	(9)	(124)	(3,092)	(786)	(4,011)			
Jackson surplus notes(note iv)	—	—	—	—	154	—	154			
Investment and policyholder liabilities valuation differences between IFRS and regulatory basis for Jackson(note viii)	—	—	—	—	2,221	—	2,221			
Adjustment from IAS 19 basis pension deficit attributable to WPSF to pension liability for regulatory purposes(note vii)	—	65	65	—	—	—	65			
Valuation difference on PAL between IFRS basis and regulatory basis	—	(1,294)	(1,294)	—	—	—	(1,294)			
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis)(note v)	2	703	705	(171)	194	400	1,128			
Total adjustments	—	6,432	6,432	(295)	(523)	(333)	5,281			
Total available capital resources of life assurance businesses on local regulatory bases	—	6,432	6,432	1,607	2,488	1,129	11,656			

31 December 2009	SAIF	WPSF note i	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note ii	Jackson	Asian life assurance subsidiaries	Total life assurance operations
	2009						
				£m			
Policyholder liabilities							
With-profits liabilities of UK regulated with-profits funds:							
Insurance contracts	9,285	28,449	37,734	—	—	4,766	42,500
Investment contracts (with discretionary participating features)	396	24,384	24,780	—	—	100	24,880
Total	9,681	52,833	62,514	—	—	4,866	67,380
Other liabilities:							
Insurance contracts:							
With-profits liabilities of non-UK regulated funds	—	—	—	—	—	3,942	3,942
Unit-linked, including variable annuity	—	1,998	1,998	6,793	20,639	9,717	39,147
Other life assurance business	291	12,726	13,017	18,113	25,707	3,287	60,124
Investment contracts without discretionary participation features (principally unit-linked and similar contracts in the UK and GIC liabilities of Jackson)(note vi)	—	—	—	13,794	1,965	46	15,805
Total	291	14,724	15,015	38,700	48,311	16,992	119,018
Total policyholder liabilities shown in the consolidated statement of financial position	9,972	67,557	77,529	38,700	48,311	21,858	186,398

Notes

i WPSF unallocated surplus includes amounts related to the Hong Kong branch. Policyholder liabilities of the Hong Kong branch are included in the amounts of Asian life assurance subsidiaries.

ii Excluding PAC shareholders' equity that is included in 'parent company and shareholders' equity of other subsidiaries and funds'.

iii The term shareholders' equity held in long-term funds refers to the excess of assets over liabilities attributable to shareholders of funds which are required by law to be maintained with segregated assets and liabilities.

iv For regulatory purposes the Jackson surplus notes are accounted for as capital.

v Other adjustments to shareholders' equity and unallocated surplus include amounts for the value of non-participating business for UK regulated with-profits funds, deferred tax, admissibility and other items measured differently on the regulatory basis. For Jackson the principal reconciling item is deferred tax related to the differences between IFRS and regulatory basis as shown in the table above and other methodology differences.

vi Insurance business accounted for as financial instruments under IAS 39.

vii In determining the IAS 19 adjustment for the purposes of this table the deficit in the Group's main pension scheme used for the calculation includes amounts for investments in Prudential insurance policies (see note I2).

viii The investment and policyholder liabilities valuation difference between IFRS and regulatory bases for Jackson is mainly due to not all investments being carried at fair value under the regulatory basis and also for the valuation difference on annuity reserves.

b Basis of preparation, capital requirements and management

Each of the Prudential Group's long-term business operations is capitalised to a sufficiently strong level for its individual circumstances. Details by the Prudential Group's major operations are shown below.

i UK insurance operations

The FSA rules which govern the Prudential regulation of insurance form part of the Prudential Sourcebook for Insurers, the General Prudential Sourcebook and Interim Prudential Sourcebook for Insurers. Overall, the net requirements of the General Prudential Sourcebook are intended to align the capital adequacy requirements for insurance business more closely with those of banking and investment firms and building societies, for example, by addressing tiers of capital, rather than looking at net admissible assets. An insurer must hold capital resources equal at least to the Minimum Capital Requirement (MCR).

The Prudential Sourcebook for Insurers also contains rules on Individual Capital Assessments. Under these rules and the rules of the General Prudential Sourcebook all insurers must assess for themselves the amount of capital needed to back their business. If the FSA views the results of this assessment as insufficient, it may draw up its own Individual Capital Guidance for a firm, which can be superimposed as a requirement.

PAC WPSF and SAIF

Under FSA rules, insurers with with-profits liabilities of more than £500 million must hold capital equal to the higher of the MCR and the Enhanced Capital Requirement (ECR). The ECR is intended to provide a more risk responsive and 'realistic' measure of a with-profit insurer's capital requirements, whereas the MCR is broadly speaking equivalent to the previous required minimum margin under the Interim Prudential Sourcebook and satisfies the minimum EU Standards.

Determination of the ECR involves the comparison of two separate measurements of the firm's resources requirement, which the FSA refers to as the 'twin peaks' approach.

The two separate peaks are:

i The requirement comprised by the mathematical reserves plus the 'Long-Term Insurance Capital Requirement' (LTICR), together known as the 'regulatory peak'; and

ii a calculation of the 'realistic' present value of the insurer's expected future contractual liabilities together with projected 'fair' discretionary bonuses to policyholders, plus a risk capital margin, together known as the 'realistic peak'.

Available capital of the WPSF and SAIF of £8.7 billion, £5.4 billion and £6.4 billion, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, represents the excess of assets over liabilities on the FSA realistic basis. Unlike the previously discussed FRS 27 basis, realistic liabilities on the regulatory basis include the shareholders' share of future bonuses. These amounts are shown before deduction of the risk capital margin (RCM) which is estimated to be £2.0 billion, £2.1 billion and £1.4 billion, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The FSA's basis of setting the RCM is to target a level broadly equivalent to a Standard & Poor's credit rating of BBB and to judge this by ensuring there are sufficient assets to absorb a one in 200 year event. The RCM calculation achieves this by setting rules for the determination of margins to cover defined stress changes in asset values and yields for market risk, credit risk and termination risk for with-profits policies.

As noted in section D2(f)(ii), PAC has discretion in its management actions in the case of adverse investment conditions. Management actions encompass, but are not confined to, investment allocation decisions, levels of reversionary bonuses, crediting rates and total claim values. To illustrate the flexibility of management actions, rates of regular bonus are determined for each type of policy primarily by targeting them at a prudent proportion of the long-term expected future investment return on the underlying assets. The expected future investment return is reduced as appropriate for each type of policy to allow for items such as expenses, charges, tax and shareholders' transfers. However, the rates declared may differ by product type, or by date of payment of the premiums or date of issue of the policy, if the accumulated annual bonuses are particularly high or low relative to a prudent proportion of the achieved investment return.

When target bonus levels change, the PAC board has regard to the overall financial strength of the long-term fund when determining the length of time over which it will seek to achieve the amended product target bonus level.

In normal investment conditions, PAC expects changes to regular bonus rates to be gradual over time and changes are not expected to exceed 1% per annum over any year. However, discretion is retained as to whether or not a regular bonus is declared each year, and there is no limit on the amount by which regular bonus rates can be changed.

As regards smoothing of maturity and death benefits, in normal circumstances PAC does not expect most pay-out values on policies of the same duration to change by more than 10% up or down from one year to the next, although some larger changes may occur to balance pay-out values between different policies. Greater flexibility may be required in certain circumstances, for example, following a significant rise or fall in market values (either sudden or over a period of years) and in such situations the PAC board may decide to vary the standard bonus smoothing limits to protect the overall interests of policyholders.

For surrender benefits, any substantial fall in the market value of the assets of the with-profits sub-fund would lead to changes in the application of MVRs for accumulating with-profits policies, firstly to increase the size of MVRs already being applied and, secondly, to extend the range of policies for which an MVR is applied.

Other UK life assurance subsidiaries and funds

The available capital of £982 million, £1,053 million and £1,607 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, reflects the excess of regulatory basis assets over liabilities of the subsidiaries and funds, before deduction of the capital resources requirement of £841 million, £884 million and £952 million as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The capital resources requirement for these companies broadly reflects a formula which, for active funds, equates to a percentage of regulatory reserves plus a percentage of death strains. Death strains represent payments made to policyholders upon death in excess of amount explicitly allocated to fund the provisions for policyholders claims and maturities.

ii Jackson

The regulatory framework for Jackson is governed by the requirements of the US NAIC approved risk-based capital standards. Under these requirements life insurance companies report on a formula-based capital standard that they calculate by applying factors to various asset, premium and reserve items. The formula takes into account the risk characteristics of a company, including asset risk, insurance risk, interest rate risk and business risk.

The available capital of Jackson shown above of £2,251 million, £2,758 million and £2,488 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, reflects US regulatory basis assets less liabilities including asset valuation reserves. The asset valuation reserve is designed to provide for future credit-related losses on debt securities and losses on equity investments. Available capital includes a reduction for the effect of the interest maintenance reserve, which is designed by state regulators to defer recognition of non-credit related realised capital gains and losses and to recognise them rateably in the future.

Jackson's risk-based capital ratio is significantly in excess of regulatory requirements. Effective for 2008 reporting, the local regulator granted Jackson three permitted practices, which expired on 1 October 2009, unless extended by the local regulator. One permitted practice allows Jackson to carry interest rate swaps at book value, as if statutory hedge accounting were in place, instead of at fair value as would have been otherwise required. Jackson is also required to demonstrate the effectiveness of its interest rate swap programme pursuant to the Michigan Insurance Code. The local regulator also granted a permitted practice to allow Jackson to recognise book to tax differences that will reverse within the next three years (instead of one year as required by the NAIC) in determining the admissible tax asset (subject to a limitation of 15% of capital and surplus versus the 10% limitation imposed by the NAIC guidance). Finally, the local regulator granted a permitted practice to allow Jackson to use an average interest rate in calculating certain regulatory requirements. In 2009, the permitted practice with respect to the interest rate swaps was renewed until 1 October 2010 with the other two expired on 1 October 2009. The permitted practice requires that Jackson maintain certain minimum capital levels excluding the effect of the permitted practices. The total effect of these permitted practices was to increase statutory surplus by £117 million and £588 million at 31 December 2009 and 2008, respectively, and reduce authorised control level required capital by £57 million at 31 December 2008.

iii Asian operations

The available capital shown above of £874 million, £1,410 million and £1,129 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, represents the excess of local regulatory basis assets over liabilities before deduction of required capital of £265 million, £407 million and £438 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. These amounts have been determined applying the local regulations in each of the operations.

The businesses in Asia are subject to local capital requirements in the jurisdictions in which they operate. The Hong Kong business branch of PAC and its capital requirements are subsumed within those of the PAC long-term fund. For the other material Asian operations, the details of the basis of determining regulatory capital and regulatory capital requirements are as follows:

Singapore

In Singapore a risk-based regulatory framework applies rather than one based on a net premium approach.

For participating business, a gross premium reserve, determined using prudent best estimate assumptions and which makes allowance for future bonus, is held. The amount held is subject to a minimum of the higher of the assets attributed to participating business and a gross premium reserve calculated on specified assumptions, but without allowance for future bonus, that include prescribed provisions for adverse deviations (PADs).

For non-participating business, gross premium reserves are held. For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

Indonesia

Policy reserves for traditional business are determined on a modified net premium basis. The valuation interest rates are capped at 9% for local currency products and 5% for foreign currency products.

For linked business the value of units is held together with a non- unit reserve calculated in accordance with standard actuarial methodology. Solvency capital is determined using risk-based capital approach. Insurance companies in Indonesia are expected to maintain the level of net assets above 120% of solvency capital. Due to the 2008 financial crisis, the local regulator provided relief in solvency capital through 2008 and 2009 and the measure continues until further notice.

Japan

Mathematical reserves for traditional business are determined on a net premium basis using prescribed mortality and interest rates. Interest rates reflect the original pricing assumptions.

For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

With regard to solvency, the adjusted solvency capital assets of Prudential must exceed 200% of the risk related capital requirement value at risk. It is thus a risk-based capital approach.

Malaysia

For 2007 and 2008 the mathematical reserves for traditional business were determined on a modified net premium basis using prescribed mortality and interest rates (no higher than 4%).

For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

The capital requirement is determined as 4% of reserves plus a specified percentage of sums at risk. There is an overriding minimum capital requirement of 100 million Malaysian Ringgit.

A new risk-based capital framework was adopted from 1 January 2009 to replace the previous framework that used a net premium approach.

For participating business, a gross premium reserve on the guaranteed and non-guaranteed benefits determined using best estimate assumptions is held. The amount held is subject to a minimum of a gross premium reserve on the guaranteed benefits, determined using best estimate assumptions along with provisions of risk margin for adverse deviations (PRADs) discounted at the risk-free rate.

For non-participating business, gross premium reserves determined using best estimate assumptions along with provisions of risk margin for adverse deviations (PRADs) discounted at the risk-free rate are held. For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

The risk-free rate is derived from a yield curve of zero-coupon spot yields of Malaysian Government Securities.

Vietnam

Mathematical reserves are calculated using a modified net premium approach, using a stable set of assumptions agreed with the regulator.

The capital requirement is determined as 4% of reserves plus a specified percentage of 0.1% of sums at risk for policies with original term less than or equal to five years or 0.3% of sums at risk for policies with original term of more than five years. An additional capital requirement of Vietnamese Dong 200 billion is also required for companies transacting unit-linked business.

Korea

Policy reserves for traditional business are determined on net premium reserve basis using pricing mortality and prescribed standard interest rates.

For linked business, the value of units is held together with the non-unit reserves calculated in accordance with regulatory standard actuarial methodology.

For 2007 and 2008 the capital requirement in Korea were determined as 4% of the policy reserves and expected claims after reinsurance.

Insurance companies in Korea are expected to maintain a level of free surplus in excess of the capital requirements with the usual level of solvency margin being around 200% of the required capital.

The capital requirement in Korea has moved to a risk-based regulatory framework in April 2009 with a two-year transition period where insurers can choose between the prior and new framework. A risk-based regulatory framework is adopted immediately by Prudential. Under the new framework, insurance companies in Korea are expected to maintain a level of free surplus in excess of the capital requirements with the general target level of solvency margin being in excess of 150% of the risk-based capital.

iv Group capital requirements

In addition to the requirements at individual company level, FSA requirements under the IGD apply additional prudential requirements for the Prudential Group as a whole.

Discussion of the Prudential Group's estimated IGD position at 31 December 2009, together with market risk sensitivity disclosure provided to key management, is provided in the Risk capital management section of "Financial Information of the Prudential Group" and in Section C.

c Movements in total available capital

Total available capital for the Prudential Group's life assurance operations has changed during 2007, 2008 and 2009 as follows:

	2007				
	WPSF note i	Other UK life assurance subsidiaries and funds note iii	Jackson note ii	Asian life assurance subsidiaries note iv	Group total
			£m		
Available capital at 31 December 2006	**8,688**	**903**	**2,083**	**745**	**12,419**
Changes in assumptions	(335)	(33)	—	4	(364)
Changes in management policy	—	—	—	12	12
Changes in regulatory requirements	—	—	(7)	—	(7)
New business and other factors	367	112	175	113	767
Available capital at 31 December 2007	**8,720**	**982**	**2,251**	**874**	**12,827**

	2008				
	WPSF note i	Other UK life assurance subsidiaries and funds note iii	Jackson note ii	Asian life assurance subsidiaries note iv	Group total
			£m		
Available capital at 31 December 2007	**8,720**	**982**	**2,251**	**874**	**12,827**
Changes in assumptions	(149)	(624)	—	(7)	(780)
Changes in management policy	—	372	—	60	432
Changes in regulatory requirements	—	—	(57)	134	77
New business and other factors	(3,209)	323	564	349	(1,973)
Available capital at 31 December 2008	**5,362**	**1,053**	**2,758**	**1,410**	**10,583**

	2009				
	WPSF note i	Other UK life assurance subsidiaries and funds note iii	Jackson note ii	Asian life assurance subsidiaries note iv	Group total
			£m		
Available capital at 31 December 2008	**5,362**	**1,053**	**2,758**	**1,410**	**10,583**
Changes in assumptions	18	23	—	2	43
Changes in management policy	—	26	—	(101)	(75)
Changes in regulatory requirements	—	0	128	178	306
New business and other factors	1,052	505	(398)	(360)	799
Available capital at 31 December 2009	**6,432**	**1,607**	**2,488**	**1,129**	**11,656**

Notes

i WPSF

The increase in 2007 reflects investment return earned on the opening available capital partially offset by the £335 million effect of assumption changes and a £214 million impact from a change in the risk-free yield curve which affects the outlook for future investment returns. The £335 million effect of assumption changes on a regulatory basis compares to the £392 million effect of change in assumption on an IFRS basis as shown in note D2(i)

The decrease in 2008 reflects primarily the negative investment returns earned on the opening available capital and £149 million negative effect of changes in assumptions on a regulatory basis compared to the £83 million effect of change in assumptions on an IFRS basis as shown in note D(i).

The increase in 2009 reflects primarily the positive investment returns earned on the opening available capital and £18 million positive effect of changes in assumptions on a regulatory basis compared to the £65 million effect of change in assumptions on the IFRS basis as shown in note D2 (i).

ii Jackson

The increase of £168 million in 2007 reflects an underlying increase of £203 million (applying the 2007 year end exchange rate of $1.99:£1) and £35 million of exchange translation losses.

The increase of £507 million in 2008 reflects an underlying decrease of £358 million (applying the 2008 year end exchange rate of $1.44:£1) and £865 million of exchange translation gain.

The decrease of £270 million in 2009 reflects an underlying increase of £33 million (applying the 2009 year end exchange rate of $1.61:£1) and £303 million of exchange translation loss.

The underlying increase/decrease of the available capital of Jackson in 2007, 2008 and 2009 includes the effects of capital contributions, dividends paid to the parent company, impairment losses and also the effects of hedging transactions.

iii Other UK life assurance subsidiaries and funds

The effect from the changes in assumptions of valuation interest rates on insurance liabilities is broadly matched by the corresponding effect on assets leaving no significant impact on the available capital.

iv Asian life assurance subsidiaries

The decrease of £281 million in 2009 reflects an underlying decrease of £152 million (applying the relevant 2009 year end exchange rates) and £129 million of exchange translation loss. This underlying decrease of available capital includes the effects of the change to a risk-based capital framework in Malaysia from 1 January 2009 as explained in section b above and also the sale of the Taiwan agency business in June 2009 as described in note I1.

d Transferability of available capital

For PAC and all other UK long-term insurers, long-term business assets and liabilities must, by law, be maintained in funds separate from those for the assets and liabilities attributable to non-life insurance business or to shareholders. Only the 'established surplus' — the excess of assets over liabilities in the long-term fund determined through a formal valuation — may be transferred so as to be available for other purposes. Distributions from the with-profits sub-fund to shareholders reflect the shareholders' one-ninth share of the cost of declared policyholders' bonuses.

Accordingly, the excess of assets over liabilities of the PAC long-term fund is retained within that company. The retention of the capital enables it to support with-profits and other business of the fund by, for example, providing the benefits associated with smoothing and guarantees. It also provides investment flexibility for the fund's assets by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies.

For other UK long-term business subsidiaries, the amounts retained within the companies are at levels which provide an appropriate level of capital strength in excess of the regulatory minimum.

For Jackson, capital retention is maintained at a level consistent with an appropriate rating by Standard & Poor's. Jackson can pay dividends on its capital stock only out of earned surplus unless prior regulatory approval is obtained. Furthermore, dividends which exceed the greater of 10% of Jackson's statutory surplus or statutory net gain from operations for the prior year require prior regulatory approval.

For Asian subsidiaries, the amounts retained within the companies are at levels that provide an appropriate level of capital strength in excess of the local regulatory minimum. For ring-fenced with-profits funds, the excess of assets over liabilities is retained with distribution tied to the shareholders' share of bonuses through declaration of actuarially determined surplus. The Singapore and Malaysian businesses may, in general, remit dividends to the UK, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations.

Available capital of the non-insurance business units is transferable to the life assurance businesses after taking account of an appropriate level of operating capital, based on local regulatory solvency targets, over and above basis liabilities. The economic capital model described in section D1 (concentration of risks) takes into account restrictions on mobility of capital across the Prudential Group with capital transfers to and from business units triggered at a solvency level consistent with these targets. The model takes into account restrictions on the availability to the Prudential Group of the estate of the various with-profits funds throughout the group.

e Sensitivity of liabilities and total capital to changed market conditions and capital management policies

Prudential manages its assets, liabilities and capital locally, in accordance with local regulatory requirements and reflecting the different types of liabilities Prudential has in each business. As a result of the diversity of products offered by the Prudential Group and the different regulatory requirements in which it operates, Prudential employs differing methods of asset/liability and capital management, depending on the business concerned.

Stochastic modelling of assets and liabilities is undertaken in the UK, Jackson and Asia to assess the economic capital requirements under different confidence intervals and time horizons. In addition, reserve adequacy testing under a range of scenarios and dynamic solvency testing is carried out, including under certain scenarios mandated by the UK, the US and Asian regulators.

A stochastic approach models the inter-relationship between asset and liability movements, taking into account asset correlation, management actions and policyholder behaviour under a large number of alternative economic scenarios. These scenarios are projected forward over a period of time, typically 25 years or longer, and the liabilities and solvency position of the fund are calculated in each scenario in each future year. The fund's policy on management actions, including bonus and investment policy, continue to be set in order that they are consistent with the available capital and the targeted risk of default.

The sensitivity of liabilities and other components of total capital vary depending upon the type of business concerned and this conditions the approach to asset/liability management.

For example, for businesses that are most sensitive to interest rate changes, such as immediate annuity business, Prudential uses cash flow analysis to create a portfolio of debt securities whose value changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. This type of analysis is used in the UK for annuity business and by Jackson for its interest-sensitive and fixed indexed annuities and stable value products.

For businesses that are most sensitive to equity price changes, Prudential uses stochastic modelling and scenario testing to look at the future returns on its investments under different scenarios which best reflect the large diversity in returns that equities can produce. This allows Prudential to devise an investment and with-profits policyholder bonus strategy that, on the model assumptions, allows it to optimise returns to its policyholders and shareholders over time while maintaining appropriate financial strength. Prudential uses this methodology extensively in connection with its UK with-profits business.

f Intra-group arrangements in respect of SAIF

Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations to the policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency.

Due to the quality and diversity of the assets in SAIF and the ability of SAIF to revise guaranteed benefits in the event of an asset shortfall, the directors believe that the probability of either the PAC long-term fund or the Prudential Group's shareholders' funds, under their obligation to maintain the capital position of long-term funds generally, having to contribute to SAIF is remote.

E: ASSET MANAGEMENT (INCLUDING US BROKER-DEALER) AND OTHER OPERATIONS

The Prudential Group's asset management operations are based in the UK, Asia and the US where they operate different models and under different brands tailored to their markets.

Asset management in the UK is undertaken through M&G which is made up of three distinct businesses, being Retail, Wholesale and Finance, and whose operations include retail asset management, institutional fixed income, pooled life and pension funds, property and private finance.

Asset management in Asia serves both the life companies in Asia by managing the life funds and funds underlying the investment linked products and third-party customers through mutual fund business. Asia offers mutual fund investment products in a number of countries within the region, allowing customers to participate in debt, equity and money market investments.

Asset management in the US is undertaken through PPM America which manages assets for the Prudential Group's US, UK and Asian affiliates plus also provides investment services to other affiliated and unaffiliated institutional clients including CDOs, private investment funds, institutional accounts and mutual funds. In addition, broker-dealer activities are undertaken in the US where trades in securities are carried out for both third-party customers and for its own account.

Other operations covers unallocated corporate activities and includes the head office functions.

E1: Income statement for asset management operations

a) The profit included in the income statement in respect of asset management operations for the year is as follows:

	Asset management operations 2007			
	M&G	US	Asia	Total
	£m			
Revenue*	810	386	201	1,397
Charges	(547)	(377)	(129)	(1,053)
Profit before tax	**263**	**9**	**72**	**344**
Profit before tax for asset management operations comprise:				
Operating profit based on longer-term investment returns†	254	8	72	334
Short-term fluctuations in investment returns‡	4	1	—	5
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	5	—	—	5
Profit before tax	**263**	**9**	**72**	**344**

	Asset management operations 2008			
	M&G	US	Asia	Total
	£m			
Revenue*	53	409	202	664
Charges	28	(402)	(150)	(524)
Profit before tax	**81**	**7**	**52**	**140**
Profit before tax for asset management operations comprise:				
Operating profit based on longer-term investment returns†	286	7	52	345
Short-term fluctuations in investment returns‡	(195)	—	—	(195)
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	(10)	—	—	(10)
Profit before tax	**81**	**7**	**52**	**140**

	Asset management operations 2009			
	M&G	US	Asia	Total
	£m			
Revenue*	799	500	217	1,516
Charges	(505)	(496)	(162)	(1,163)
Profit before tax	**294**	**4**	**55**	**353**
Profit before tax for asset management operations comprise:				
Operating profit based on longer-term investment returns†	238	4	55	297
Short-term fluctuations in investment returns‡	70	—	—	70
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	(14)	—	—	(14)
Profit before tax	**294**	**4**	**55**	**353**

* Included within revenue for M&G are realised and unrealised net losses of £26 million, £673 million and £176 million, for 2007, 2008 and 2009 respectively, in respect of consolidated investment funds and Prudential Capital. The investment funds are managed on behalf of third-parties and are consolidated under IFRS in recognition of the control arrangements for the funds. The investment losses in respect of the investment funds are non-recourse to M&G and the Group and are added back through charges and consequently there is no impact on the profit before tax. Excluding the anomaly in respect of the consolidated investment funds the revenue for M&G would be £686 million, £494 million, and £697 million and the charges, £423 million, £413 million and £403 million, for 2007, 2008 and 2009 respectively.

† In 2008 Operating profit based on longer-term investment returns includes a £28 million charge for an impairment loss on a holding in Lehman Brothers. There were no impairment losses in 2007 and 2009.

‡ Short-term fluctuations for M&G are primarily in respect of unrealised value movements on Prudential Capital's bond portfolio.

b) M&G operating profit based on longer-term investment returns

	2007	2008	2009
	£m	£m	£m
Asset management fee income	482	455	457
Other income	30	25	13
Staff costs	(224)	(184)	(205)
Other costs	(113)	(111)	(100)
Underlying profit before performance-related fees	175	185	165
Performance-related fees	28	43	12
Operating profit from asset management operations	203	228	177
Operating profit from Prudential Capital	51	58	61
Total M&G operating profit based on longer-term investment returns	254	286	238

The difference between the fees and other income shown above in respect of asset management operations, and the revenue figure for M&G shown in the main table primarily relates to income and investment gains (losses) earned by Prudential Capital and by investment funds controlled by the asset management operations which are consolidated under IFRS.

E2: Statement of financial position for asset management operations

Assets, liabilities and shareholders' funds included in the Prudential Group's consolidated statement of financial position in respect of asset management operations are as follows as at 31 December:

	Asset management operations 2007			
	M&G	US	Asia	Total
	£m			
Assets				
Intangible assets:				
Goodwill	1,153	16	61	1,230
Deferred acquisition costs	6	—	—	6
Total	1,159	16	61	1,236
Other non-investment and non-cash assets	304	132	85	521
Financial investments:				
Loans(note i)	2,334	—	—	2,334
Equity securities and portfolio holdings in unit trusts	11	—	6	17
Debt securities(note ii)	857	—	25	882
Other investments(note v)	132	19	4	155
Deposits	—	15	11	26
Total investments	3,334	34	46	3,414
Cash and cash equivalents(note v)	1,751	33	56	1,840
Total assets	**6,548**	**215**	**248**	**7,011**
Equity and liabilities				
Equity				
Shareholders' equity(note iii)	1,424	81	172	1,677
Minority interests	52	—	—	52
Total equity	1,476	81	172	1,729
Liabilities				
Intra Group debt represented by operational borrowings at Group level(note iv)	2,477	—	—	2,477
Net asset value attributable to external holders of consolidated funds(note v)	1,234	—	—	1,234
Other non-insurance liabilities	1,361	134	76	1,571
Total liabilities	5,072	134	76	5,282
Total equity and liabilities	**6,548**	**215**	**248**	**7,011**

	Asset management operations 2008			
	M&G	US	Asia	Total
	£m			
Assets				
Intangible assets:				
Goodwill	1,153	16	61	1,230
Deferred acquisition costs	6	—	—	6
Total	1,159	16	61	1,236
Other non-investment and non-cash assets	27	169	99	295
Financial investments:				
Loans(note i)	1,763	—	—	1,763
Equity securities and portfolio holdings in unit trusts	11	—	12	23
Debt securities(note ii)	975	—	16	991
Other investments(note v)	432	24	6	462
Deposits	35	16	13	64
Total investments	3,216	40	47	3,303
Cash and cash equivalents(note v)	1,329	39	104	1,472
Total assets	**5,731**	**264**	**311**	**6,306**
Equity and liabilities				
Equity				
Shareholders' equity(note iii)	1,300	114	228	1,642
Minority interests	1	—	—	1
Total equity	1,301	114	228	1,643
Liabilities				
Intra Group debt represented by operational borrowings at Group level(note iv)	1,278	—	—	1,278
Net asset value attributable to external holders of consolidated funds(note v)	1,065	—	—	1,065
Other non-insurance liabilities	2,087	150	83	2,320
Total liabilities	4,430	150	83	4,663
Total equity and liabilities	**5,731**	**264**	**311**	**6,306**

	Asset management operations 2009			
	M&G	US	Asia	Total
	£m			
Assets				
Intangible assets:				
Goodwill	1,153	16	61	1,230
Deferred acquisition costs	8	—	—	8
Total	1,161	16	61	1,238
Other non-investment and non-cash assets	607	161	82	850
Financial investments:				
Loans(note i)	1,413	—	—	1,413
Equity securities and portfolio holdings in unit trusts	129	—	8	137
Debt securities(note ii)	1,149	—	15	1,164
Other investments(note v)	106	2	5	113
Deposits	38	13	12	63
Total investments	2,835	15	40	2,890
Cash and cash equivalents(note v)	820	40	110	970
Total assets	**5,423**	**232**	**293**	**5,948**
Equity and liabilities				
Equity				
Shareholders' equity(note iii)	1,326	111	222	1,659
Minority interests	3	—	—	3
Total equity	1,329	111	222	1,662
Liabilities				
Intra Group debt represented by operational borrowings at Group level(note iv)	2,038	—	—	2,038
Net asset value attributable to external holders of consolidated funds(note v)	410	—	—	410
Other non-insurance liabilities	1,646	121	71	1,838
Total liabilities	4,094	121	71	4,286
Total equity and liabilities	**5,423**	**232**	**293**	**5,948**

Notes

i Loans

The M&G loans of £2,334 million, £1,763 million and £1,413 million, at 31 December 2007, 2008 and 2009 respectively, relate to loans and receivables managed by Prudential Capital. These assets are generally secured but have no external credit ratings. Internal ratings prepared by the Prudential Group's asset management operations as part of the risk management process rating are; £951 million, nil and £92 million as A+ to A−; £738 million, £1,100 million and £835 million as BBB+ to BBB−; £645 million, £663 million, and £330 million, as BB+ to BB−; and nil, nil and £156 million as B+ to B−, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

ii Debt securities

Of the total debt securities of £882 million, £991 million and £1,164 million for M&G £841 million, £959 million and £1,072 million were rated AAA to A− by Standard and Poor's or Aaa rated by Moody's, at 31 December 2007, 31 December 2008, and 31 December 2009.

iii M&G includes those assets and liabilities in respect of Prudential Capital.

iv Intra Group debt represented by operational borrowings at Group level

Operational borrowings for M&G are in respect of Prudential Capital's short-term fixed income security programme and comprise £2,422 million, £1,269 million and £2,031 million, at 31 December 2007, 2008 and 2009 respectively, of commercial paper and £55 million, £9 million, £7 million, at 31 December 2007, 2008 and 2009 respectively, of medium-term notes.

v Consolidated investment funds

The M&G statement of financial position shown above includes investment funds which are managed on behalf of third-parties. In respect of these funds, the statement of financial position includes cash and cash equivalents, other investments, other net assets and liabilities and the net asset value attributable to external unit holders which are non-recourse to M&G and the Group at 31 December as presented in the table below.

	2007	2008	2009
	£m	£m	£m
Cash and cash equivalents	1,253	835	269
Other investments	—	345	158
Other net assets and liabilities	(19)	(115)	(17)
Net assets attributable to external unit holders*	1,234	1,065	410

* The net asset value attributable to external unit holders in respect of these funds, which are non-recourse to M&G and the Prudential Group.

E3: Regulatory capital positions

Asset management operations in the UK, Hong Kong, Singapore, Vietnam and China are subject to regulatory requirements based on fixed operating expenses and other operating considerations. The movement in the year of the surplus regulatory capital position of these operations, combined with the movement in the IFRS basis shareholders' funds for other asset management operations, is as follows:

	Asset management operations			
	M&G	US	Asia	Total
	£m			
Capital surplus position — 2007				
Beginning of year	114	57	72	243
Exchange movement	—	(1)	—	(1)
Movement in capital requirement	(6)	—	(3)	(9)
Gains during the year	105	25	59	189
Distributions made	(114)	—	(36)	(150)
End of year	99	81	92	272
Capital surplus position — 2008				
Beginning of year	99	81	92	272
Exchange movement	(3)	39	31	67
Movement in capital requirement	(28)	—	25	(3)
Gains during the year	89	1	46	136
Distributions made	—	(8)	(34)	(42)
End of year	157	113	160	430
Capital surplus position — 2009				
Beginning of year	157	113	160	430
Exchange movement	(1)	(4)	(11)	(16)
Movement in capital requirement	73	—	(6)	67
Gains during the year	(8)	5	41	38
Capital injection	—	—	1	1
Distributions made	—	(5)	(31)	(36)
End of year	221	109	154	484

The movement in the year reflects changes in regulatory requirements whilst gains are driven by profits generated during the year. Distributions consist of dividends paid up to the parent company.

The M&G figures include those for Prudential Capital.

E4: Sensitivity of profit and equity to market and other financial risk

i Currency translation

Consistent with the Prudential Group's accounting policies, the profits of the Asia and PPM America asset management operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2007, 2008 and 2009 the rates for the most significant operations are given in note B4. A 10% increase in the relevant Asian exchange rates would have reduced reported profit before tax attributable to shareholders and shareholders' equity, excluding goodwill attributable to Asia asset management operations, by £7 million, £5 million, and £5 million and PPM America asset management operations, by £18 million, £26 million, and £23 million for 2007, 2008 and 2009 respectively.

ii Other sensitivities to other financial risks for asset management operations

The principal sensitivities to other financial risk of asset management operations are credit risk on the bridging loan portfolio (as described in note E2) of M&G's Prudential Capital operation and the indirect effect of changes to market values of funds under management. Due to the nature of the asset management operations there is limited direct sensitivity to movements in interest rates. Total debt securities held at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, by asset management operations were £882 million, £991 million and £1,164 million, the majority of which are held by the Prudential Capital operation of M&G. Debt securities held by M&G are in general variable rate bonds and so market value is limited in sensitivity to interest rate movements and consequently any change in interest rates would not have a material impact on profit or shareholder's equity. Asset management operations do not hold significant investments in property or equities.

E5: Other operations

Other operations consist of unallocated corporate activities relating to Group Head Office and the Asia regional head office, with net charge (net of income and expenditure) for the year of £260 million, £260 million and £395 million, for 2007, 2008 and 2009 respectively, as detailed in note B1. An analysis of the assets and liabilities of other operations is shown in note B6.

F: INCOME STATEMENT NOTES

F1: Segmental information

Year ended 31 December 2007

	Insurance operations			Asset management			Total segment	Unallocated corporate	Group total
	UK	US	Asia	M&G	US	Asia			
	£m								
Gross premiums earned	7,477	5,860	5,022				18,359	—	18,359
Outward reinsurance premiums	(59)	(59)	(53)	—	—	—	(171)	—	(171)
Earned premiums, net of reinsurance	7,418	5,801	4,969				18,188	—	18,188
Investment return(note ii)	7,952	2,097	1,758	444	43	60	12,354	(129)	12,225
Other income	1,524	(13)	49	366	343	141	2,410	47	2,457
Total revenue, net of reinsurance	16,894	7,885	6,776	810	386	201	32,952	(82)	32,870
Benefits and claims	(13,606)	(7,161)	(5,457)				(26,224)		(26,224)
Outward reinsurers' share of benefits and claims	(109)	65	24	—	—	—	(20)	—	(20)
Movement in unallocated surplus of with-profits funds	(252)	—	(289)	—	—	—	(541)	—	(541)
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	(13,967)	(7,096)	(5,722)	—	—	—	(26,785)	—	(26,785)
Acquisition costs and other operating expenditure	(2,454)	(353)	(948)	(547)	(377)	(129)	(4,808)	(51)	(4,859)
Finance costs: interest on core structural borrowings of shareholder-financed operations	—	(10)	—	—	—	—	(10)	(158)	(168)
Total charges, net of reinsurance	(16,421)	(7,459)	(6,670)	(547)	(377)	(129)	(31,603)	(209)	(31,812)
Profit (loss) before tax *(being tax attributable to shareholders' and policyholders' returns)*(note i)	473	426	106	263	9	72	1,349	(291)	1,058
Tax credit attributable to policyholders' returns	8	—	(3)	—	—	—	5	—	5
Profit (loss) from continuing operations before tax attributable to shareholders	481	426	103	263	9	72	1,354	(291)	1,063

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Insurance operations			Asset management			Total segment	Unallocated corporate	Group Total
	UK	US	Asia	M&G	US	Asia			
						£m			
Operating profit based on longer-term investment returns	528	444	125	254	8	72	1,431	(279)	1,152
Short-term fluctuations in investment returns on shareholder-backed business	(47)	(18)	15	4	1	—	(45)	(6)	(51)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	5	—	—	5	(6)	(1)
Loss on sale and results for Taiwan agency business	—	—	(37)	—	—	—	(37)	—	(37)
Profit (loss) from continuing operations before tax attributable to shareholders	481	426	103	263	9	72	1,354	(291)	1,063

Year ended 31 December 2008

	Insurance operations			Asset management			Total segment	Unallocated corporate	Group Total
	UK	US	Asia	M&G	US	Asia			
						£m			
Gross premiums earned	7,628	6,032	5,333	—	—	—	18,993	—	18,993
Outward reinsurance premiums	(61)	(67)	(76)	—	—	—	(204)	—	(204)
Earned premiums, net of reinsurance	7,567	5,965	5,257	—	—	—	18,789	—	18,789
Investment return(note ii)	(20,134)	(5,449)	(4,229)	(301)	40	73	(30,000)	(202)	(30,202)
Other income	141	1	93	353	369	129	1,086	60	1,146
Total revenue, net of reinsurance(note iii)	(12,426)	517	1,121	52	409	202	(10,125)	(142)	(10,267)
Benefits and claims	7,048	(1,152)	(1,276)	—	—	—	4,620	—	4,620
Outward reinsurers' share of benefits and claims	146	205	38	—	—	—	389	—	389
Movement in unallocated surplus of with-profits funds	4,769	—	1,046	—	—	—	5,815	—	5,815
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	11,963	(947)	(192)	—	—	—	10,824	—	10,824
Acquisition costs and other operating expenditure	(739)	(211)	(882)	29	(402)	(150)	(2,355)	(104)	(2,459)
Finance costs: interest on core structural borrowings of shareholder-financed operations	—	(11)	—	—	—	—	(11)	(161)	(172)
Total charges, net of reinsurance(note iii)	11,224	(1,169)	(1,074)	29	(402)	(150)	8,458	(265)	8,193
(Loss) profit before tax (*being tax attributable to shareholders' and policyholders' returns*)(note i)	(1,202)	(652)	47	81	7	52	(1,677)	(407)	(2,074)
Tax credit attributable to policyholders' returns	1,579	—	45	—	—	—	1,624	—	1,624
(Loss) profit before tax attributable to shareholders	377	(652)	92	81	7	52	(53)	(407)	(450)

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Insurance operations			Asset management			Total segment	Unallocated corporate	Group total
	UK	US	Asia	M&G	US	Asia			
	£m								
Operating profit based on longer-term investment returns	589	406	231	286	7	52	1,571	(288)	1,283
Short-term fluctuations in investment returns on shareholder-backed business	(212)	(1,058)	(138)	(195)	—	—	(1,603)	(118)	(1,721)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	(2)	(10)	—	—	(12)	(1)	(13)
Results for the sold Taiwan agency business	—	—	1	—	—	—	1	—	1
(Loss) profit before tax attributable to shareholders	377	(652)	92	81	7	52	(43)	(407)	(450)

Year ended 31 December 2009

	Insurance operations			Asset management			Total segment	Unallocated corporate	Group total
	UK	US	Asia	M&G	US	Asia			
	£m								
Gross premiums earned	5,757	9,197	5,345	—	—	—	20,299	—	20,299
Outward reinsurance premiums	(122)	(82)	(119)	—	—	—	(323)	—	(323)
Earned premiums, net of reinsurance	5,635	9,115	5,226	—	—	—	19,976	—	19,976
Investment return(note ii)	17,366	5,070	4,357	420	68	74	27,355	(466)	26,889
Other income	176	(18)	110	379	432	143	1,222	12	1,234
Total revenue, net of reinsurance	23,177	14,167	9,693	799	500	217	48,533	(454)	48,099
Benefits and claims	(18,521)	(13,297)	(8,083)	—	—	—	(39,901)	—	(39,901)
Outward reinsurers' share of benefits and claims	214	12	39	—	—	—	265	—	265
Movement in unallocated surplus of with-profits funds	(1,893)	—	334	—	—	—	(1,559)	—	(1,559)
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	(20,200)	(13,285)	(7,710)	—	—	—	(41,195)	—	(41,195)
Acquisition costs and other operating expenditure	(1,508)	(383)	(1,536)	(505)	(496)	(162)	(4,590)	18	(4,572)
Finance costs: interest on core structural borrowings of shareholder-financed operations	—	(13)	—	—	—	—	(13)	(196)	(209)
Loss on sale of Taiwan agency business	—	—	(559)	—	—	—	(559)	—	(559)
Total charges, net of reinsurance	(21,708)	(13,681)	(9,805)	(505)	(496)	(162)	(46,357)	(178)	(46,535)
Profit (loss) before tax *(being tax attributable to shareholders' and policyholders' returns)*(note i)	1,469	486	(112)	294	4	55	2,196	(632)	1,564
Tax credit attributable to policyholders' returns	(750)	—	(68)	—	—	—	(818)	—	(818)
Profit (loss) from continuing operations before tax attributable to shareholders	719	486	(180)	294	4	55	1,378	(632)	746

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Insurance operations			Asset management			Total	Unallocated	Group
	UK	US	Asia	M&G	US	Asia	segment	corporate	total
						£m			
Operating profit based on longer-term investment returns	657	459	410	238	4	55	1,823	(418)	1,405
Short-term fluctuations in investment returns on shareholder-backed business	108	27	31	70	—	—	236	(200)	36
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(46)	—	—	(14)	—	—	(60)	(14)	(74)
Loss on sale and results for Taiwan agency business	—	—	(621)	—	—	—	(621)	—	(621)
Profit (loss) from continuing operations before tax attributable to shareholders	719	486	(180)	294	4	55	1,378	(632)	746

Notes

i The measure is the formal (loss) profit before tax measure under IFRS but is not the result attributable to shareholders.

ii Investment return principally comprises:

— Interest and dividends;

— Realised and unrealised gains and losses on securities and derivatives classified as fair value through profit and loss under IAS 39; and

— Realised gains and losses, including impairment losses, on securities classified as available-for-sale under IAS 39.

iii Total revenue for 2008 is negative £10,267 million whilst charges are a credit of £8,193 million. These abnormal effects arose from the basis of preparation whereby revenue includes investment appreciation, which is negative in 2008, and charges reflect the allocation, where appropriate, of investment return to policyholder benefits.

F2: Revenue

	2007	2008	2009
	£m	£m	£m
Long-term business premiums			
Insurance contract premiums	17,308	17,575	19,347
Investment contracts with discretionary participation feature premiums	874	964	789
Inwards reinsurance premiums	177	454	163
Less: reinsurance premiums ceded	(171)	(204)	(323)
Earned premiums, net of reinsurance(note iv)	18,188	18,789	19,976
Realised and unrealised gains and losses on securities at fair value through profit and loss	2,634	(34,157)	18,175
Realised and unrealised gains and losses on derivatives at fair value through profit and loss	270	(5,261)	1,164
Realised gains and losses on available-for-sale securities, previously recognised in other comprehensive income	13	(487)	(420)
Realised gains and losses on loans	47	210	(115)
Interest(notes i,ii)	5,857	6,739	5,575
Dividends	2,730	2,023	1,755
Other investment income	674	731	755
Investment income	12,225	(30,202)	26,889
Fee income from investment contract business and asset management(notes iii,iv)	1,039	1,109	1,234
Income from venture investments of the PAC with-profits funds	1,418	37	—
Other income	2,457	1,146	1,234
Total revenue	32,870	(10,267)	48,099

Notes

i The segmental analysis of interest income is as follows:

	2007	2008	2009
	£m	£m	£m
Insurance operations:			
UK	3,630	4,802	3,848
US	1,493	1,520	1,051
Asia	302	49	522
Asset management operations:			
M&G	389	310	140
US	1	1	2
Asia	2	2	2
Total segment	5,817	6,684	5,565
Unallocated corporate	40	55	10
Total	5,857	6,739	5,575

ii Interest income includes £2 million, £11 million and £17 million, for 2007, 2008 and 2009 respectively, accrued in respect of impaired securities.

iii Fee income includes £31 million, £7 million and £1 million, for 2007, 2008 and 2009 respectively, relating to financial instruments that are not held at fair value through profit and loss. These fees primarily related to prepayment fees, late fees and syndication fees.

iv The following table provides additional segmental analysis of revenue from external customers:

	2007				
	Asia	US	UK	Intragroup	Total
	£m	£m	£m	£m	£m
Revenue from external customers:					
Insurance operations	5,018	5,788	8,937	(4)	19,739
Asset management	199	388	527	(264)	850
Unallocated corporate	—	—	47	—	47
Intragroup revenue eliminated on consolidation	(58)	(45)	(165)	268	—
Total revenue from external customers	5,159	6,131	9,346	—	20,636

	2008				
	Asia	US	UK	Intragroup	Total
	£m	£m	£m	£m	£m
Revenue from external customers:					
Insurance operations	5,348	5,955	7,711	(10)	19,004
Asset management	202	414	497	(280)	833
Unallocated corporate	—	—	61	—	61
Intragroup revenue eliminated on consolidation	(73)	(45)	(172)	290	—
Total revenue from external customers	5,477	6,324	8,097	—	19,898

	2009				
	Asia	US	UK	Intragroup	Total
	£m	£m	£m	£m	£m
Revenue from external customers:					
Insurance operations	5,336	9,097	5,822	(11)	20,244
Asset management	213	499	513	(271)	954
Unallocated corporate	—	—	12	—	12
Intragroup revenue eliminated on consolidation	(70)	(67)	(145)	282	—
Total revenue from external customers	5,479	9,529	6,202	—	21,210

Revenue from external customers is made up of the following:

	2007	2008	2009
	£m	£m	£m
Earned premiums, net of reinsurance	18,188	18,789	19,976
Other income	2,446	1,109	1,234
Total revenue from external customers	20,634	19,898	21,210

In their capacity as fund managers to fellow Prudential Group subsidiaries, M&G, the US and the Asian asset management businesses earn fees for investment management and related services. Intragroup fees, for 2007, 2008 and 2009 respectively, included within asset management revenue were £264 million, £280 million and £271 million earned of which, £161 million, £162 million and £134 million by M&G, £45 million, £45 million and £67 million by the US asset management segment and £58 million, £73 million and £70 million by the Asian asset management segment. In 2007, 2008 and 2009 respectively, the remaining £4 million, £10 million and £11 million of intragroup revenue was recognised by UK insurance operations. These services are charged at appropriate arm's length prices, typically priced as a percentage of funds under management.

In Asia, revenue from external customers from no individual country exceeds 10% of the Prudential Group's total. The largest country is Hong Kong with a total revenue from external customers of £1,170 million and £1,013 million, for 2008 and 2009 respectively.

Due to the nature of the business of the Group, there is no reliance on any major customers.

F3: Acquisition costs and other operating expenditure

	2007	2008	2009
	£m	£m	£m
Acquisition costs(notes i,ii)	1,030	1,185	1,033
Staff and pension costs(I2)	1,402	913	1,172
Administrative and operating cost(note iii)	2,427	361	2,367
Total acquisition costs and other operating expenditure(notes iv,v)	4,859	2,459	4,572

Notes

i Acquisition costs in 2007, 2008 and 2009 respectively, comprise amounts related to insurance contracts of £939 million, £1,048 million, and £871 million and investment contracts and asset management contracts of £91 million, £137 million and £162 million. These costs include amortisation of £410 million, £520 million, and £290 million in respect of insurance contracts for 2007, 2008 and 2009 and £3 million, £15 million, and £15 million for investment contracts for 2007, 2008 and 2009 respectively.

ii Acquisition costs also include fee expenses relating to financial liabilities held at amortised cost of £1 million, £nil and £nil, for 2007, 2008 and 2009 respectively.

iii Administrative and operating costs include the movement in amounts attributable to external unit holders of the consolidated investment funds of the Group of a charge of £615 million (2008: a credit of £963 million, 2007: a charge of £122 million).

iv The total depreciation and amortisation expense is £523 million, £618 million, and £377 million, for 2007, 2008 and 2009 respectively. Of this amount, £413 million, £535 million, and £305 million, for 2007, 2008 and 2009 respectively, relates to amortisation of deferred acquisition costs of insurance contracts and asset management contracts, which is primarily borne by the insurance operations. The segmental analysis of total depreciation and amortisation expense is as follows:

	2007	2008	2009
	£m	£m	£m
Insurance operations:			
UK	75	29	25
US	315	283	88
Asia	122	279	246
Asset management operations:			
M&G	4	6	2
US	2	1	2
Asia	2	4	4
Total segment	520	602	367
Unallocated corporate	3	16	10
Total	523	618	377

v Interest expense, excluding interest on core structural borrowings of shareholder-financed operations, amounted to £436 million, £278 million, and £89 million, for 2007, 2008 and 2009 respectively, and is included within total acquisition costs and other operating expenditure as part of investment management expenses. The segmental analysis of this interest expense is as follows:

	2007	2008	2009
	£m	£m	£m
Insurance operations:			
UK	181	66	28
US	148	90	32
Asia	—	—	1
Asset management operations:			
M&G	—	34	—
US	—	—	—
Asia	—	—	—
Total segment	329	190	61
Unallocated corporate	107	88	28
Total	436	278	89

F4: Finance costs: Interest on core structural borrowings of shareholder-financed operations

Finance costs consist of interest on core debt of the parent company of £158 million, £161 million, and £196 million, for 2007, 2008 and 2009 respectively, and interest on US insurance operations' surplus notes of £10 million, £11 million, and £13 million, for 2007, 2008 and 2009 respectively.

F5: Tax

a Total tax credit (charge) by nature of expense

An analysis of the total tax benefit (expense) of continuing operations recognised in the income statement by nature of benefit (expense) is as follows:

	2007	2008	2009
	£m	£m	£m
Current tax benefit (expense):			
Corporation tax	(806)	(225)	(500)
Adjustments in respect of prior years	185	359	(29)
Total current tax	(621)	134	(529)
Deferred tax arising from:			
Origination and reversal of temporary differences	222	1,629	(340)
(Expense) benefit in respect of a previously unrecognised tax loss, tax credit or temporary difference from a prior period	50	(77)	(4)
Write down or reversal of a previous write down of a deferred tax asset	—	(3)	—
Total deferred tax credit	272	1,549	(344)
Total tax credit (charge)	(349)	1,683	(873)

Notes

i Total current tax includes £9 million, £7 million and £6 million, for 2007, 2008 and 2009 respectively, in respect of tax to be paid in Hong Kong. The current tax charge is calculated as either 17.5%, 16.5% and 16.5%, for 2007, 2008 and 2009 respectively, on 5% of the net insurance premium or 17.5%, 16.5% and 16.5%, for 2007, 2008 and 2009 respectively, on the estimated assessable profits depending on the nature of the business written.

The total tax benefit (expense) arises as follows:

	2007	2008	2009
	£m	£m	£m
Current tax benefit (expense):			
UK	(377)	280	(527)
Foreign	(244)	(146)	(2)
	(621)	134	(529)
Deferred tax credit:			
UK	349	1,478	(368)
Foreign	(77)	71	24
	272	1,549	(344)
Total	(349)	1,683	(873)

The total tax charge of £349 million for 2007, credit of £1,683 million for 2008 and charge of £873 million for 2009, comprises a charge of £28 million, credit of £1,758 million and charge of £895 million, respectively, for UK tax and a charge of £321 million, a charge of £75 million and a credit of £22 million respectively, for overseas tax. This tax charge and credit comprises tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders. The tax attributable to shareholders of a charge of £354 million for 2007, a credit of £59 million for 2008, and a charge of £55 million for 2009, comprises a charge of £148 million, a credit of £95 million and a charge of £176 million respectively, for UK tax and a charge of £206 million, a charge of £36 million and a credit of £121 million for overseas tax.

The prior year adjustments primarily relate to a change in assumptions regarding available foreign tax credits on overseas dividends and other changes that arose as a result of routine revision of tax returns.

The total deferred tax credit (charge) arises as follows:

	2007	2008	2009
	£m	£m	£m
Unrealised gains and losses on investments	225	1,521	(35)
Balances relating to investment and insurance contracts	41	(239)	(12)
Short-term timing differences	(10)	(29)	(105)
Capital allowances	4	2	1
Unused tax losses	12	294	(193)
Deferred tax credit (charge)	272	1,549	(344)

In 2007, 2008 and 2009 respectively, a deferred tax credit (charge) of £54 million, £561 million and £(546) million has been taken through other comprehensive income. Other movements in deferred tax totalling an aggregate credit/(charge) of £93 million, £(2) million and £69 million in 2007, 2008 and 2009 respectively is mainly comprised of foreign exchange movements. When these amounts are taken with the deferred tax credit (charge) shown above the result is a (increase) decrease of £0.4 billion, £2.1 billion and £(0.8) billion in the Prudential Group's net deferred tax liability at 31 December 2007, 2008 and 2009 respectively.

b Reconciliation of effective tax rate

The total tax expense is attributable to shareholders and policyholders as summarised in the income statement.

i Summary of pre-tax (loss) profit and tax credit (charge)

The income statement includes the following items:

	2007	2008	2009
	£m	£m	£m
Profit (loss) before tax	1,058	(2,074)	1,564
Tax attributable to policyholders' returns	5	1,624	(818)
Profit (loss) before tax attributable to shareholders	1,063	(450)	746
Tax attributable to shareholders' (losses) profits:			
Tax credit (charge)	(349)	1,683	(873)
Less: tax attributable to policyholders' returns	(5)	(1,624)	818
Tax attributable to shareholders' returns	(354)	59	(55)
Profit (loss) from continuing operations after tax	709	(391)	691

ii Overview

For the purposes of explaining the relationship between tax expense and accounting profit, it is appropriate to consider the sources of profit and tax by reference to those that are attributable to shareholders and policyholders, as follows:

	2007			2008			2009		
	Attributable to shareholders	Attributable to policyholders*	Total	Attributable to shareholders	Attributable to policyholders*	Total	Attributable to shareholders	Attributable to policyholders*	Total
	£m			£m			£m		
Profit (loss) before tax	1,063	(5)	1,058	(450)	(1,624)	(2,074)	746	818	1,564
Taxation charge:									
Expected tax rate	31%	100%	30%	42%	100%	87%	31%	100%	67%
Expected tax charge	(327)	5	(322)	188	1,624	1,812	(233)	(818)	(1,051)
Variance from expected tax charge(note v(ii))	(27)	—	(27)	(129)	—	(129)	178	—	178
Actual tax (charge) credit	(354)	5	(349)	59	1,624	1,683	(55)	(818)	(873)
Average effective tax rate	33%	100%	33%	13%	100%	81%	7%	100%	56%

* For the column entitled 'Attributable to policyholders', the profit before tax represents income, net of post-tax transfers to unallocated surplus of with-profits funds, before tax attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies.

Due to the requirements of the financial reporting standards IAS 1 and IAS 12, the profit (loss) before tax and tax charge reflect the aggregate of amounts that are attributable to shareholders and policyholders.

Profit (loss) before tax comprises profit attributable to shareholders and pre-tax profit attributable to policyholders of linked and with-profits funds and unallocated surplus of with-profits funds.

The total tax charge for linked and with-profits business includes tax expense on unit-linked and with-profits funds attributable to policyholders, the unallocated surplus of with-profits funds and the shareholders' profits. This feature arises from the basis of taxation applied to life and pension business, principally in the UK, but with similar bases applying in certain Asian operations, and is explained in note (iii) below.

Furthermore, the basis of preparation of Prudential's financial information incorporates the additional feature that, as permitted under IFRS 4, the residual equity of the Prudential Group's with-profits funds, i.e. unallocated surplus, is recorded as a liability with transfers to and from that liability reflected in pre-tax profits. This gives rise to anomalous effective tax rates for profits attributable to policyholders (as described in note (iv) below).

In meeting the reconciliation requirements set out in paragraph 81(c) of IAS 12, the presentation shown in this disclosure note seeks to ensure that the explanation of the relationship between tax expense and accounting profit draw properly the distinction between the elements of the profit and tax charge that are attributable to policyholders and shareholders as explained below in notes (iv) and (v) respectively. Due to the nature of the basis of taxation of UK life and pension business (as described in note (iii) below), and the significance of the results of the business to the Group, it is inappropriate to seek to explain the effective tax rate on profit before tax by traditional approach that would apply for other industries.

The shareholder elements are the components of the profit and tax charge that are of most direct relevance to investors, and it is this aspect that the IAS 12 reconciliation requirement is seeking to explain for companies that do not need to account for both with-profits and unit-linked funds, where tax is borne by Prudential on the policyholders' behalf and which is not contemplated by the IFRS requirement.

iii Basis of taxation for UK life and pension business

Different rules apply under UK tax law for taxing pension business and life insurance business and there are detailed rules for apportioning the investment return and profits of the fund between the types of business.

The investment return referable to pension business, and some other less significant classes of business, is exempt from taxation, but tax is charged on the profit that shareholders derive from writing such business at the corporate rate of tax. The rules for taxing life insurance business are more complex. Initially, the UK regime seeks to tax the regulatory basis investment return less management expenses (I-E) on this business as it arises. However, in determining the actual tax charge, a calculation of the shareholder profits for taxation purposes from writing life insurance business also has to be made and compared with the I-E profit.

If the shareholder profit is higher than the I-E amount, extra income is attributable to the I-E calculation until the I-E profit equals the shareholder profit. If on the other hand, the I-E profit is the greater, then an amount equal to the shareholder profit is taxed at the corporate rate of tax, with the remainder of the I-E profit being taxed at the lower policyholder rate of tax.

The purpose of this approach is to ensure that Prudential is always as a minimum taxed on the profit, as defined for taxation purposes by reference to Prudential's regulatory returns (rather than IFRS basis results), that it has earned. The shareholders' portion of the long-term business is taxed at the shareholders' rate, with the remaining portion taxed at rates applicable to the policyholders.

It is to be noted that the calculations described are determined using data from the regulatory basis returns rather than the IFRS basis results. The differences between the regulatory and accounting bases are very significant and extremely complex rendering any explanation in general purpose financial information to be of little if any use to users.

iv Profits attributable to policyholders and related tax

As noted above, it is necessary under IFRS requirements to include the total tax charge of Prudential (both policyholder and shareholder elements) in the tax charge disclosed in the income statement.

For with-profits business, total pre-tax profits reflect the aggregate of profits attributable to policyholders and shareholders. However, amounts attributable to the equity of with-profits funds are carried in the liability for unallocated surplus. Also, as described in note (iii), UK with-profits business is taxed on a basis that affects policyholders' unallocated surplus of with-profits funds and shareholders. For the PAC with-profits sub-fund, transfers to and from unallocated surplus are recorded in the income statement, so that after charging the total tax borne by the fund, the net balance reflects the statutory transfer from the fund for the year. The statutory transfer represents 10% of the actuarially determined surplus for the year that is attributable to shareholders.

For SAIF similar transfers are made. However, in the case of SAIF, a net nil balance is derived, reflecting the lack of shareholder interest in the financial performance of the fund (other than through asset management arrangements).

The accounting anomaly that arises under IFRS is that due to the fact that the net of tax profit attributable to with-profits policyholders is zero, Prudential's presentation of pre-tax profit attributable to policyholders reflects an amount that is the mirror image of the tax charge attributable to policyholders.

For unit-linked business, pre-tax profits also reflect the aggregate of profits attributable to policyholders and shareholders. The pre-tax profits attributable to policyholders represent fees earned that are used to pay tax borne by Prudential on policyholders' behalf. The net of tax profit attributable to policyholders for unit-linked business is thus zero.

The combined effect of these features is such that providing a reconciliation of the tax charge attributable to policyholders to an expected charge based on the standard corporate rate of tax on IFRS basis profits attributable to policyholders is not relevant.

In summary, for accounting purposes, in all cases and for all reporting periods, the apparent effective rate for profit attributable to policyholders and unallocated surplus is 100%. However, it is to be noted that the 100% rate does not reflect a rate paid on the profits attributable to policyholders. It instead reflects the basis of accounting for unallocated surplus coupled with the distinction made for performance reporting between sources of profit attributable to shareholders, policyholders and unallocated surplus and IFRS requirements in respect of reporting of all pre-tax profits and all tax charges irrespective of policyholder or shareholder economic interest.

v Reconciliation of tax charge on profits/(loss) attributable to shareholders

	2007				
	Asian insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m				
Profit before tax attributable to shareholders:					
Operating profit based on longer-term investment returns(note iii)	125	444	528	55	1,152
Short-term fluctuations in investment returns	15	(18)	(47)	(1)	(51)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	(1)	(1)
Results for sold Taiwan agency business	(37)	—	—	—	(37)
Total	103	426	481	53	1,063
Expected tax rate:(note i)					
Operating profit based on longer-term investment returns(note iii)	19%	35%	30%	28%	31%
Short-term fluctuations in investment returns	25%	35%	30%	28%	31%
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	20%	35%	30%	28%	28%
Results for sold Taiwan agency business	25%	—	—	—	25%
Expected tax credit (charge) based on expected tax rates:					
Operating profit based on longer-term investment returns(note iii)	(24)	(155)	(158)	(15)	(352)
Short-term fluctuations in investment returns	(4)	6	14	—	16
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	—	—
Results for sold Taiwan agency business	9	—	—	—	9
Total	(19)	(149)	(144)	(15)	(327)
Variance from expected tax charge:(note ii)					
Operating profit based on longer-term investment returns(note iii)	4	22	(25)	(1)	—
Short-term fluctuations in investment returns	(1)	1	(2)	6	4
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	1	1
Results for sold Taiwan agency business	(32)	—	—	—	(32)
Total	(29)	23	(27)	6	(27)
Actual tax credit (charge):					
Operating profit based on longer-term investment returns(note iii)	(20)	(133)	(183)	(16)	(352)
Short-term fluctuations in investment returns	(5)	7	12	6	20
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	1	1
Results for sold Taiwan agency business	(23)	—	—	—	(23)
Total	(48)	(126)	(171)	(9)	(354)
Actual tax rate: Operating profit based on longer-term investment returns	16%	30%	35%	29%	31%
Total	47%	30%	36%	17%	33%

Notes

i Expected tax rates for profit attributable to shareholders:

Expected tax rates shown in the table above reflect the corporate tax rates generally applied to taxable profits of the relevant country jurisdictions. For Asian operations the expected tax rates reflect the corporate tax rates weighted by reference to the source of profits of the operations contributing to the aggregate business result.

The tax rate of 28% in 2007 for other operations reflects the mix of business between UK and overseas operations, which are taxed at a variety of rates. The rate will fluctuate from year to year dependent on the mix of profits between jurisdictions.

ii Variances from expected tax charge for results attributable to shareholders:

For 2007, the principal variances arise from differences between the standard corporation tax rate and actual rates due to a number of factors, including:

a For Asian long-term operations, the tax rate has been adversely impacted by the fact that the Taiwan loss on disposal has no corresponding tax relief. In addition tax losses in several jurisdictions which are not expected to be available for relief against future profits, and losses on investments in jurisdictions which do not provide corresponding tax relief;

b For Jackson, the benefit of a deduction from taxable income of a proportion of dividends received attributable to the variable annuity business;

c For UK insurance operations, disallowed expenses and prior year adjustments arising from the routine revisions of tax returns; and

d For Other operations, the availability of capital losses brought forward on which no deferred tax had previously been recognised, which have been used against capital gains in the period.

iii Operating profit based on longer-term investment returns is net of attributable restructuring costs and development expenses.

	2008				
	Asian insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m				
(Loss) Profit before tax attributable to shareholders:					
Operating profit based on longer-term investment returns(note iii)	231	406	589	57	1,283
Short-term fluctuations in investment returns	(138)	(1,058)	(212)	(313)	(1,721)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(2)	—	—	(11)	(13)
Results for sold Taiwan agency business	1	—	—	—	1
Total	92	(652)	377	(267)	(450)
Expected tax rate:(note i)					
Operating profit based on longer-term investment returns(note iii)	23%	35%	28%	17%	29%
Short-term fluctuations in investment returns	28%	35%	28%	28%	32%
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	25%	—	—	28%	27%
Results for sold Taiwan agency business	25%	—	—	—	25%
Expected tax credit (charge) based on expected tax rates:					
Operating profit based on longer-term investment returns(note iii)	(54)	(142)	(165)	(10)	(371)
Short-term fluctuations in investment returns	38	370	59	88	555
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	1	—	—	3	4
Results for sold Taiwan agency business	—	—	—	—	—
Total	(15)	228	(106)	81	188
Variance from expected tax charge:(note ii)					
Operating profit based on longer-term investment returns(note iii)	(51)	17	57	56	79
Short-term fluctuations in investment returns	(3)	(173)	(8)	(19)	(203)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	—	—	—	(1)	(1)
Results for sold Taiwan agency business	(4)	—	—	—	(4)
Total	(58)	(156)	49	36	(129)
Actual tax credit (charge):					
Operating profit based on longer-term investment returns(note iii)	(105)	(125)	(108)	46	(292)
Short-term fluctuations in investment returns	35	197	51	69	352
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	1	—	—	2	3
Results for sold Taiwan agency business	(4)	—	—	—	(4)
Total	(73)	72	(57)	117	59
Actual tax rate: Operating profit based on longer-term investment returns	45%	31%	18%	(81)%	23%
Total	79%	11%	15%	44%	13%

Notes

i Expected tax rates for profit attributable to shareholders:

The tax rate of 23% reflects the mix of business between UK and overseas operations, which are taxed at a variety of rates. The rate will fluctuate from year to year dependent on the mix of profits between jurisdictions.

ii For 2008, the principal variances arise from differences between the standard corporation tax rate and actual rates due to a number of factors, including:

a For Asian long-term operations, tax losses in several jurisdictions which are not expected to be available for relief against future profits, and losses on investments in jurisdictions which do not provide corresponding tax relief;

b For Jackson, the inability to fully recognise deferred tax assets on losses being carried forward which has partially been offset by the benefit of a deduction from taxable income of a proportion of dividends received attributable to the variable annuity business;

c For UK insurance operations, prior year adjustments arising from the routine revisions of tax returns, the settlement of outstanding issues with HMRC at an amount below that previously provided and the different tax bases of UK life business; and

d For Other operations, the settlement of issues with HMRC at amounts below those previously provided and a reduction in amounts previously provided on outstanding issues with HMRC which has been partially offset by the inability to recognise a deferred tax asset on various tax losses.

iii Operating profit based on longer-term investment returns is net of attributable restructuring costs and development expenses.

	2009				
	Asian insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m				
Profit before tax attributable to shareholders:					
Operating profit based on longer-term investment returns(note iii)	410	459	657	(121)	1,405
Short-term fluctuations in investment returns	31	27	108	(130)	36
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	—	—	(46)	(28)	(74)
Loss on sale and results for Taiwan agency business	(621)	—	—	—	(621)
Total	(180)	486	719	(279)	746
Expected tax rate:(note i)					
Operating profit based on longer-term investment returns(note iii)	24%	35%	28%	28%	29%
Short-term fluctuations in investment returns	25%	35%	28%	36%	0%
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	—	—	28%	28%	28%
Loss on sale and results for Taiwan agency business	25%	—	—	—%	25%
Expected tax credit (charge) based on expected tax rates:					
Operating profit based on longer-term investment returns(note iii)	(98)	(161)	(184)	34	(409)
Short-term fluctuations in investment returns	(8)	(9)	(30)	47	—
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	—	—	13	8	21
Loss on sale and results for Taiwan agency business	155	—	—	—	155
Total	49	(170)	(201)	89	(233)
Variance from expected tax charge:(note ii)					
Operating profit based on longer-term investment returns(note iii)	35	77	(29)	8	91
Short-term fluctuations in investment returns	15	195	—	14	224
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	—	—	—	—	—
Loss on sale and results for Taiwan agency business	(137)	—	—	—	(137)
Total	(87)	272	(29)	22	178
Actual tax credit (charge):					
Operating profit based on longer-term investment returns(note iii)	(63)	(84)	(213)	42	(318)
Short-term fluctuations in investment returns	7	186	(30)	61	224
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	—	—	13	8	21
Loss on sale and results for Taiwan agency business	18	—	—	—	18
Total	(38)	102	(230)	111	(55)
Actual tax rate: Operating profit based on longer-term investment returns	15%	18%	32%	35%	23%
Total	(21)%	(21)%	32%	40%	7%

Notes

i Expected tax rates for profit attributable to shareholders:

The expected tax rates shown in the table above reflect the corporate tax rates generally applied to taxable profits of the relevant country jurisdictions.

For Asian operations the expected tax rates reflect the corporate tax rates weighted by reference to the source of profits of operations contributing to the aggregate business result.

The expected tax rate for Other operations reflects the mix of business between UK and overseas operations, which are taxed at a variety of rates. The rate will fluctuate from year to year dependent on the mix of profits.

ii For 2009, the principal variances arise from differences between the standard corporation tax rate and actual rates due to a number of factors, including:

a For Asian long-term operations, profits in certain countries which are not taxable partly offset by the inability to fully recognise deferred tax assets on losses being carried forward;

b For Jackson, the ability to fully recognise deferred tax assets on losses brought forward which we were previously unable to recognise together with income subject to a lower level of taxation and the benefit of a deduction from taxable income of a proportion of dividends received attributable to the variable annuity business;

c For UK insurance operations, adjustments in respect of the prior year tax charge and different tax bases of UK life business;

d For Other operations, the ability to now recognise a deferred tax asset on various tax losses which we were previously unable to recognise offset by adjustments in respect of the prior year tax charge; and

e The actual tax rate in relation to Asia excluding the result for the sold Taiwan agency business would have been 13% for the period.

iii Operating profit based on longer-term investment returns is net of attributable restructuring costs and development expenses.

F6: Allocation of investment return between policyholders and shareholders

Investment return is attributable to policyholders and shareholders. A key feature of the accounting policies under IFRS is that the investment return included in the income statement relates to all investment assets of the Prudential Group, irrespective of whether the return is attributable to shareholders, or to policyholders or the unallocated surplus of with-profits funds, the latter two of which have no net impact on shareholders' profit. The table below provides a breakdown of the investment return for each regional operation attributable to each type of business.

	2007	2008	2009
	£m	£m	£m
Asian operations			
Policyholders returns:			
Assets backing unit-linked liabilities	753	(2,552)	2,539
With-profits business	866	(1,611)	1,519
	1,619	(4,163)	4,058
Shareholder returns	199	7	373
Total	1,818	(4,156)	4,431
US operations			
Policyholders returns:			
Assets held to back (Separate Account) unit-linked liabilities	620	(5,925)	3,760
Shareholder returns:			
Realised gains and losses (including impairment losses on available-for-sale bonds)	(47)	(651)	(529)
Value movements on derivative hedging program for general account business	19	(311)	340
Interest/dividend income and value movements on other financial instruments for which fair value movements are booked in the income statement	1,548	1,478	1,567
Total	1,520	516	1,378
Total	2,140	(5,409)	5,138

	2007	2008	2009
	£m	£m	£m
UK operations			
Policyholder returns:			
Scottish Amicable Life Insurance Fund ("SAIF")	849	(2,095)	1,438
Assets held to back unit-linked liabilities	515	(2,971)	2,947
With-profits fund (excluding SAIF)	5,881	(14,595)	10,461
	7,245	(19,661)	14,846
Shareholder returns:			
Prudential Retirement Income Limited ("PRIL")	216	(684)	1,827
Other business	935	(90)	1,113
	1,151	(774)	2,940
Total	8,396	(20,435)	17,786
Unallocated corporate			
Shareholder returns	(129)	(202)	(466)
Group Total			
Policyholder returns	9,484	(29,749)	22,664
Shareholder returns	2,741	(453)	4,225
Total	12,225	(30,202)	26,889

The returns as shown in the table above, are delineated between those returns allocated to policyholders and those allocated to shareholders. In making this distinction, returns allocated to policyholders are those from investments in which shareholders have no direct economic interest, namely:

- Unit-linked business in the UK, Asia and SAIF in the UK, for which the investment return is wholly attributable to policyholders,
- Separate account business of US operations, the investment return of which is also wholly attributable to policyholders, and
- With-profits business (excluding SAIF) in the UK and Asia in which the shareholders' economic interest, and the basis of recognising IFRS basis profits, is restricted to a share of the actuarially determined surplus for distribution, in the UK 10%. Except for this surplus the investment return of the with-profit funds is attributable to policy holders (through the asset-share liabilities) or the unallocated surplus, which is accounted for as a liability under IFRS 4.

The investment return related to the types of business above does not impact shareholders' profits directly. However there is an indirect impact for example, investment-related feeds or the effect of investment return on the shareholders' share of the cost of bonuses of with-profits funds.

Investment returns for unit-linked and similar products have reciprocal impact on benefits and claims, with a decrease in market returns on the attached pool of assets affecting policyholder benefits on these products. Similarly for with-profits funds there is a close correlation between increases or decreases in investment returns and the level of combined charge for policyholder benefits and movement on unallocated surplus that arises from such returns.

Shareholder returns

For shareholder-backed non-participating business of the UK (comprising PRIL and other non-linked non-participating business) and of the Asian operations, the investment return is not directly attributable to policyholders and therefore does impact shareholders' profit directly. However, it should be noted that for UK shareholder-backed annuity business, principally PRIL, where the durations of asset and liability cash flows are closely matched, the discount rate applied to measure liabilities to policyholders (under grandfathered UK GAAP under IFRS 4) reflects movements in asset yields (after allowances for the future defaults) of the backing portfolios. Therefore, the net impact on the shareholders' profits of the investment return of the assets backing liabilities of the UK shareholder-backed annuity business is after taking into account the consequential effect on the movement in policyholder liabilities.

Changes in shareholder investment returns for US operations reflect primarily movements in the investment income, movements in the value of the derivative instruments held to manage the general account assets and liability portfolio, and realised gains and losses. However, separately reflecting Jackson's types of business an allocation is made to policyholders through the application of crediting rates. The shareholder investment return for US operations also includes the fair value movement of the derivatives and the movement on the related liabilities of the variable annuity guarantees under Jackson's dynamic hedging program.

The majority of the investments held to back the US non-participating business are debt securities for which the available-for-sale designation is applied for IFRS basis reporting. Under this designation the return included in the income statement reflects the aggregate of investment income and realised gains and losses (including impairment losses). However, movements in unrealised appreciation or depreciation are recognised in other comprehensive income. The return on these assets is attributable to shareholders.

F7: Benefits and claims and movements in unallocated surplus of with-profits funds net of reinsurance

Benefits and claims represent payments, including final bonuses, to policyholders in respect of maturities, surrenders and deaths plus the change in technical provisions (which primarily represents the movement in amounts owed to policyholders). Benefits and claims are amounts attributable to policyholders. The movement in unallocated surplus of with-profits funds represents the transfer to (from) the unallocated surplus each year through a charge (credit) to the income statement of the annual excess (shortfall) of income over expenditure of the with-profits funds, after declaration and attribution of the cost of bonuses to policyholders and shareholders.

Benefits and claims and movements in unallocated surplus of with-profits funds net of reinsurance can be further analysed as follows:

	2007			
	Asia	US	UK	Total
	£m			
Claims incurred	(1,429)	(3,032)	(10,266)	(14,727)
(Increase) decrease in policyholder liabilities	(4,004)	(4,064)	(3,449)	(11,517)
Movement in unallocated surplus of with-profits funds	(289)	—	(252)	(541)
	(5,722)	(7,096)	(13,967)	(26,785)

	2008			
	Asia	US	UK	Total
	£m			
Claims incurred	(1,552)	(3,666)	(10,992)	(16,210)
(Increase) decrease in policyholder liabilities	314	2,719	18,186	21,219
Movement in unallocated surplus of with-profits funds	1,046	—	4,769	5,815
	(192)	(947)	11,963	10,824

	2009			
	Asia	US	UK	Total
	£m			
Claims incurred	(1,814)	(4,092)	(9,875)	(15,781)
(Increase) decrease in policyholder liabilities	(6,230)	(9,193)	(8,432)	(23,855)
Movement in unallocated surplus of with-profits funds	334	—	(1,893)	(1,559)
	(7,710)	(13,285)	(20,200)	(41,195)

G: FINANCIAL ASSETS AND LIABILITIES

G1: Financial instruments — designation and fair values

The Prudential Group designates all financial assets as either fair value through profit and loss, available-for-sale, or as loans and receivables. Financial liabilities are designated as either fair value through profit and loss or amortised cost, or as investment contracts with discretionary participating features accounted for under IFRS 4 as described in note A4.

As at 31 December:

	2007				
	Fair value through profit and loss	Available-for-sale	Loans and receivables	Total carrying value	Fair value
			£m		
Financial assets					
Cash and cash equivalents	—	—	4,951	4,951	4,951
Deposits	—	—	7,889	7,889	7,889
Equity securities and portfolio holdings in unit trusts	86,157	—	—	86,157	86,157
Debt securities(note i)	65,349	18,635	—	83,984	83,984
Loans(note ii)	—	—	7,924	7,924	8,105
Other investments(note iii)	4,396	—	—	4,396	4,396
Accrued investment income	—	—	2,023	2,023	2,023
Other debtors	—	—	909	909	909
	155,902	18,635	23,696	198,233	

	2007				
	Fair value through profit and loss	Amortised cost	IFRS 4 basis value	Total carrying value	Fair value
			£m		
Financial liabilities					
Core structural borrowings of shareholder-financed operations(notes i,H13)	—	2,492	—	2,492	2,476
Operational borrowings attributable to shareholder-financed operations(H13)	—	3,081	—	3,081	3,081
Borrowings attributable to with-profits funds(H13)	204	783	—	987	1,006
Obligations under funding, securities lending and sale and repurchase agreements	—	4,081	—	4,081	4,100
Net asset value attributable to unit holders of consolidated unit trust and similar funds	3,556	—	—	3,556	3,556
Investment contracts with discretionary participating features(note iv)	—	—	29,550	29,550	—
Investment contracts without discretionary participating features	12,110	1,922	—	14,032	14,034
Other creditors	—	1,020	—	1,020	1,020
Derivative liabilities	1,080	—	—	1,080	1,080
Other liabilities	1	790	—	791	791
	16,951	14,169	29,550	60,670	

	2008				
	Fair value through profit and loss	Available-for-sale	Loans and receivables	Total carrying value	Fair value
			£m		
Financial assets					
Cash and cash equivalents	—	—	5,955	5,955	5,955
Deposits	—	—	7,294	7,294	7,294
Equity securities and portfolio holdings in unit trusts	62,122	—	—	62,122	62,122
Debt securities(note i)	71,225	23,999	—	95,224	95,224
Loans(note ii)	—	—	10,491	10,491	10,043
Other investments(note iii)	6,301	—	—	6,301	6,301
Accrued investment income	—	—	2,513	2,513	2,513
Other debtors	—	—	1,232	1,232	1,232
	139,648	23,999	27,485	191,132	

	2008				
	Fair value through profit and loss	Amortised cost	IFRS 4 basis value	Total carrying value	Fair value
	£m				
Financial liabilities					
Core structural borrowings of shareholder-financed operations(notes i,H13)	—	2,958	—	2,958	2,137
Operational borrowings attributable to shareholder-financed operations(H13)	—	1,977	—	1,977	1,977
Borrowings attributable to with-profits funds(H13)	158	1,150	—	1,308	1,320
Obligations under funding, securities lending and sale and repurchase agreements	—	5,572	—	5,572	5,676
Net asset value attributable to unit holders of consolidated unit trust and similar funds	3,843	—	—	3,843	3,843
Investment contracts with discretionary participating features(note iv)	—	—	23,446	23,446	—
Investment contracts without discretionary participating features	11,616	2,885	—	14,501	14,568
Other creditors	—	1,496	—	1,496	1,496
Derivative liabilities	4,832	—	—	4,832	4,832
Other liabilities	—	890	—	890	890
	20,449	16,928	23,446	60,823	

	2009				
	Fair value through profit and loss	Available-for-sale	Loans and receivables	Total carrying value	Fair value
	£m				
Financial assets					
Cash and cash equivalents	—	—	5,307	5,307	5,307
Deposits	—	—	12,820	12,820	12,820
Equity securities and portfolio holdings in unit trusts	69,354	—	—	69,354	69,354
Debt securities(note i)	79,083	22,668	—	101,751	101,751
Loans(note ii)	—	—	8,754	8,754	8,686
Other investments(note iii)	5,132	—	—	5,132	5,132
Accrued investment income	—	—	2,473	2,473	2,473
Other debtors	—	—	762	762	762
	153,569	22,668	30,116	206,353	

	2009				
	Fair value through profit and loss	Amortised cost	IFRS 4 basis value	Total carrying value	Fair value
	£m				
Financial liabilities					
Core structural borrowings of shareholder-financed operations(notes i,H13)	—	3,394	—	3,394	3,424
Operational borrowings attributable to shareholder-financed operations(H13)	—	2,751	—	2,751	2,751
Borrowings attributable to with-profits funds(H13)	105	1,179	—	1,284	1,281
Obligations under funding, securities lending and sale and repurchase agreements	—	3,482	—	3,482	3,540
Net asset value attributable to unit holders of consolidated unit trust and similar funds	3,809	—	—	3,809	3,809
Investment contracts with discretionary participating features(note iv)	—	—	24,880	24,880	—
Investment contracts without discretionary participating features	13,840	1,965	—	15,805	15,866
Other creditors	—	1,612	—	1,612	1,612
Derivative liabilities	1,501	—	—	1,501	1,501
Other liabilities	—	877	—	877	877
	19,255	15,260	24,880	59,395	

Notes

i As at 31 December 2007, 31 December 2008, and 31 December 2009 respectively, £722 million, £620 million, and £659 million of convertible bonds were included in debt securities and £278 million, £363 million, and £347 million were included in borrowings.

ii Loans and receivables are reported net of allowance for loan losses of £13 million, £27 million and £44 million, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

iii See note G3 for details of the derivative assets included. The balance also contains the PAC with-profits fund's participation in various investment funds and limited liability property partnerships.

iv It is impractical to determine the fair value of investment contracts with discretionary participation features due to the lack of a reliable basis to measure such features.

v For financial liabilities designated as fair value through profit and loss there was no impact on profit from movements in credit risk during 2009 and 2008.

Determination of fair value

The fair values of the financial assets and liabilities as shown on the table above have been determined on the following bases.

The fair values of the financial instruments for which fair valuation is required under IFRS are determined by the use of current market bid prices for quoted investments, or by using quotations from independent third-parties, such as brokers and pricing services or by using appropriate valuation techniques. Investments valued using valuation techniques include financial investments which by their nature do not have an externally quoted price based on regular trades and financial investments for which markets are no longer active as a result of market conditions e.g. market illiquidity. The valuation techniques used include comparison to recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation. These techniques may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments. When determining the inputs into the valuation techniques used priority is given to publicly available prices from independent sources, when available, but overall, the source of pricing is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date.

The fair value estimates are made at a specific point in time, based upon available market information and judgements about the financial instruments, including estimates of the timing and amount of expected future cash flows and the credit standing of counterparties. Such estimates do not reflect any premium or discount that could result from offering for sale at one time the Prudential Group's entire holdings of a particular financial instrument, nor do they consider the tax impact of the realisation of unrealised gains or losses from selling the financial instrument being fair valued. In some cases the fair value estimates cannot be substantiated by comparison to independent markets, nor can the disclosed value be realised in immediate settlement of the financial instrument.

At 31 December 2008 illiquid market conditions resulted in inactive markets for certain of the Prudential Group's financial instruments namely certain asset-backed securities issued by Jackson. As a result, there was generally limited observable market information for these instruments. Fair value estimates for financial instruments deemed to be in an illiquid market are based on judgements regarding current economic conditions, liquidity discounts, currency, credit and interest rate risks, loss experience and other factors. These fair values are estimates and involve considerable uncertainty and variability as a result of the inputs selected and may differ significantly from the values that would have been used had the ready market existed, and the differences could be material. At 31 December 2008 Jackson utilised internal valuation models as best estimate of fair values of all non-agency Residential Mortgage-Backed Securities ("RMBS") and Asset-Backed Securities ("ABS") and certain Commercial Mortgage-Backed Securities ("CMBS"). The use of internal models for these securities (which are accounted for on an available-for-sale basis) resulted in a fair value that was higher than those provided from pricing services and brokers of £760 million on a total amortised cost of £3.5 billion. During 2009, improvements were observed in the level of liquidity for these sectors of structured securities with the result that Jackson was able to rely on external prices for these securities as the most appropriate measure of fair value. At 31 December 2009 nearly all of the non-agency RMBS, ABS and certain CMBS which at 31 December 2008 were valued using internal models due to the dislocated market conditions in 2008 have now been valued using external prices.

The loans and receivables have been shown net of provisions for impairment. The fair value of loans has been estimated from discounted cash flows expected to be received. The rate of discount used was the market rate of interest.

The estimated fair value of derivative financial instruments reflects the estimated amount the Prudential Group would receive or pay in an arm's length transaction. This amount is determined using quoted prices if exchange listed, quotations from independent third-parties or valued internally using standard market practices. In accordance with the Prudential Group's risk management framework, all internally generated valuations are subject to assessment against external counterparties' valuations.

The fair value of borrowings is based on quoted market prices, where available.

Section A4 provides details of the determination of fair value for investment contracts without fixed and guaranteed terms (notably UK unit-linked policies). For investment contracts in the US with fixed and guaranteed terms the fair value is determined based on the present value of future cash flows discounted at current interest rates.

The fair value of other financial liabilities is determined using discounted cash flows of the amounts expected to be paid.

Level 1, 2 and 3 fair value measurement hierarchy of Prudential Group financial instruments

In March 2009 IFRS 7 *Financial Instruments: Disclosures* was amended by the IASB to require certain additional disclosures to be included in IFRS financial information. This includes, as is presented below, a table of financial instruments carried at fair value analysed by level of the IFRS 7 defined fair value hierarchy. This hierarchy is based on the inputs to the fair value measurement and reflects the lowest level input that is significant to that measurement. IFRS 7 does not require comparatives to be provided in the year of adoption but Prudential has chosen to provide the table at both 31 December 2009 and 31 December 2008.

The classification criteria and its application to Prudential can be summarised as follows:

Level 1 — quoted prices (unadjusted) in active markets for identical assets and liabilities

Level 1 principally includes exchange listed equities, mutual funds with quoted prices, exchange traded derivatives such as futures and options, and national government bonds unless there is evidence that trading in a given instrument is so infrequent that the market could not possibly be considered active. It also includes other financial instruments (including net assets attributable to unit holders of consolidated unit trusts and similar funds) where there is clear evidence that the year end valuation is based on a traded price in an active market.

Level 2 — inputs other than quoted prices included within level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices)

Level 2 principally includes corporate bonds and other non-national government debt securities which are valued using observable inputs, together with over-the-counter derivatives such as forward exchange contracts and non-quoted investment funds valued with observable inputs. It also includes net assets attributable to unit holders of consolidated unit trusts and similar funds and investment contract liabilities that are valued using observable inputs.

The nature of Prudential's operations in the US and the UK mean that a significant proportion of the assets backing non-linked shareholder-backed business are held in corporate bonds, structured securities and other non-national government debt securities. These assets, in line with market practice, are generally valued using independent pricing providers in the US and third party broker quotes in the UK and Asia either directly or via third parties such as IDC or Bloomberg. Such assets have generally been classified as level 2 as the nature of broker quotations means that it does not strictly meet the definition of a level 1 asset. However these valuations are determined using independent external quotations from multiple sources and are subject to a number of monitoring controls such as monthly price variances, stale price reviews and variance analysis on prices achieved on subsequent trades.

In addition level 2 includes debt securities that are valued internally using standard market practices. Of the total level 2 debt securities of £83,301 million at 31 December 2009, £6,426 million are valued internally. The majority of such securities use matrix pricing, which is based on assessing the credit quality of the underlying borrower to derive a suitable discount rate relative to government securities. Under matrix pricing, the debt securities are priced taking the credit spreads on comparable quoted public debt securities and applying these to the equivalent debt instruments factoring a specified liquidity premium. The majority of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

Level 3: Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs)

Level 3 principally includes investments in private equity funds, investment in property funds which are exposed to bespoke properties or risks, investments which are internally valued or subject to a significant number of unobservable assumptions and certain derivatives which are bespoke or long dated. It also includes debt securities which are rarely traded or traded only in privately negotiated transactions and hence where it is difficult to assert that these have been based on observable market data. The inherent nature of the vast majority of these assets means that, in normal market conditions, there is unlikely to be significant change in the specific underlying assets classified as level 3.

At 31 December 2009 the Prudential Group held £5,190 million, 3% of the fair valued financial instruments, within level 3. Of these amounts £3,510 million was held by the Prudential Group's participating funds and therefore shareholders' profit and equity are not impacted by movements in the valuation of these financial instruments. Total level 3 assets represented 3.7% of the total assets of the participating funds at 31 December 2009. Total level 3 liabilities were £348 million out of total participating fund liabilities of £104,817 million.

Of the £1,684 million level 3 items, net of derivative liabilities, which support non-linked shareholder-backed business (3.6% of the total assets net of derivative liabilities backing this business), £1,653 million are externally valued and £31 million are internally valued. Internal valuations, which represent only 0.04% of the total assets net of derivative liabilities supporting non-linked shareholder-backed business, are inherently more subjective than external valuations.

If the value of all level 3 investments backing non-linked shareholder-backed business was varied by 10%, the change in valuation would be £3 million, which would reduce shareholders' equity by this amount before tax. Of this amount a £5 million increase would pass through the income statement substantially as part of short term fluctuations outside of operating profit offset by a £8 million decrease included as part of other comprehensive income, being unrealised movements on assets classified as available-for-sale.

	31 December 2008			
	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
With-profits				
Equity securities and portfolio holdings in unit trusts	30,427	885	509	31,821
Debt securities	6,765	34,858	1,342	42,965
Other investments (including derivative assets)	77	1,569	2,122	3,768
Derivative liabilities	(166)	(2,861)	—	(3,027)
Total financial investments, net of derivative liabilities	37,103	34,451	3,973	75,527
Borrowing attributable to with-profits fund held at fair value	—	(158)	—	(158)
Investment contracts without discretionary participation features held at fair value	—	—	—	—
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,010)	(384)	(381)	(1,775)
Total	36,093	33,909	3,592	73,594
Percentage of total	49%	46%	5%	100%
Unit-linked and variable annuity				
Equity securities and portfolio holdings in unit trusts	29,097	114	—	29,211
Debt securities	2,650	3,615	33	6,298
Other investments (including derivative assets)	117	87	—	204
Derivative liabilities	—	—	—	—
Total financial investments, net of derivative liabilities	31,864	3,816	33	35,713
Borrowing attributable to with-profits fund held at fair value	—	—	—	—
Investment contracts without discretionary participation features held at fair value	—	(10,309)	—	(10,309)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(877)	—	—	(877)
Total	30,987	(6,493)	33	24,527
Percentage of total	126%	(26)%	0%	100%
Non-linked shareholder-backed				
Equity securities and portfolio holdings in unit trusts	745	27	318	1,090
Debt securities	6,514	35,451	3,996	45,961
Other investments (including derivative assets)	427	1,210	692	2,329
Derivative liabilities	(38)	(1,521)	(246)	(1,805)
Total financial investments, net of derivative liabilities	7,648	35,167	4,760	47,575
Borrowing attributable to with-profits fund held at fair value	—	—	—	—
Investment contracts without discretionary participation features held at fair value	—	(1,307)	—	(1,307)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(311)	(815)	(65)	(1,191)
Total	7,337	33,045	4,695	45,077
Percentage of total	16%	73%	11%	100%
Group total				
Equity securities and portfolio holdings in unit trusts	60,269	1,026	827	62,122
Debt securities	15,929	73,924	5,371	95,224
Other investments (including derivative assets)	621	2,866	2,814	6,301
Derivative liabilities	(204)	(4,382)	(246)	(4,832)
Total financial investments net of derivative liabilities	76,615	73,434	8,766	158,815
Borrowing attributable to with-profits fund held at fair value	—	(158)	—	(158)
Investment contract without discretionary participation held at fair value	—	(11,616)	—	(11,616)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(2,198)	(1,199)	(446)	(3,843)
Total	74,417	60,461	8,320	143,198
Percentage of total	52%	42%	6%	100%

	31 December 2009			
	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
With-profits				
Equity securities and portfolio holdings in unit trusts	28,688	799	475	29,962
Debt securities	7,063	39,051	1,213	47,327
Other investments (including derivative assets)	79	1,199	2,170	3,448
Derivative liabilities	(54)	(504)	(25)	(583)
Total financial investments, net of derivative liabilities	35,776	40,545	3,833	80,154
Borrowing attributable to the with-profits fund held at fair value	—	(105)	—	(105)
Investment contract without discretionary participation features held at fair value	—	—	—	—
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,354)	(305)	(323)	(1,982)
Total	34,422	40,135	3,510	78,067
Percentage of total	44%	51%	5%	100%
Unit-linked and variable annuity				
Equity securities and portfolio holdings in unit trusts	38,616	4	—	38,620
Debt securities	3,283	5,525	40	8,848
Other investments (including derivative assets)	30	80	—	110
Derivative liabilities	—	—	—	—
Total financial investments net of derivative liabilities	41,929	5,609	40	47,578
Investment contract without discretionary participation features held at fair value	—	(12,242)	—	(12,242)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,324)	(7)	(2)	(1,333)
Total	40,605	(6,640)	38	34,003
Percentage of total	119%	(19)%	0%	100%
Non-linked shareholder-backed				
Equity securities and portfolio holdings in unit trusts	557	36	179	772
Debt securities	5,783	38,725	1,068	45,576
Other investments (including derivative assets)	155	787	632	1,574
Derivative liabilities	(20)	(703)	(195)	(918)
Total financial investments, net of derivative liabilities	6,475	38,845	1,684	47,004
Investment contract without discretionary participation features held at fair value	—	(1,598)	—	(1,598)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(110)	(342)	(42)	(494)
Total	6,365	36,905	1,642	44,912
Percentage of total	14%	82%	4%	100%
Group total				
Equity securities and portfolio holdings in unit trusts	67,861	839	654	69,354
Debt securities	16,129	83,301	2,321	101,751
Other investments (including derivative assets)	264	2,066	2,802	5,132
Derivative liabilities	(74)	(1,207)	(220)	(1,501)
Total financial investments, net of derivative liabilities	84,180	84,999	5,557	174,736
Borrowing attributable to the with-profits fund held at fair value	—	(105)	—	(105)
Investment contract without discretionary participation features held at fair value	—	(13,840)	—	(13,840)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(2,788)	(654)	(367)	(3,809)
Total	81,392	70,400	5,190	156,982
Percentage of total	52%	45%	3%	100%

Reconciliation of movements in level 3 financial instruments measured at fair value

The following table reconciles the value of level 3 financial instruments at 1 January 2009 to that presented at 31 December 2009.

Total gains and losses recorded in the income statement in the period represents realised gains and losses, including interest and dividend income, unrealised gains and losses on financial instruments classified at fair value through profit and loss and foreign exchange movements on an individual entity's overseas investments. All these amounts are included within "investment return" within the income statement.

Total gains and losses recorded in other comprehensive income includes unrealised gains and losses on debt securities held as available for sale within Jackson and foreign exchange movements arising from the retranslation of the Prudential Group's overseas subsidiaries and branches.

As highlighted earlier in this note, at 31 December 2008 Jackson had utilised internal valuations for certain structured securities given the illiquidity of the market at that time. These assets have therefore been classified as level 3 given the unobservable nature of the assumptions within the internal valuation models used. During the first half of 2009 improvements were observed in the level of liquidity for these structured securities such that external prices based on observable inputs from pricing services or brokers were used to value nearly all of the structured securities at 31 December 2009. There is therefore a transfer of £2,072 million from level 3 to level 2 during 2009 in respect of these securities. The remaining transfers in or out of level 3 represent sundry individual asset reclassifications, none of which are materially significant as highlighted in the table below.

	At 1 Jan 2009	Total gains/losses in income statement	Total gains /losses recorded in other comprehensive income	Purchases	Sales	Settled	Transfers into level 3	Transfers out of level 3	At 31 Dec 2009
	£m	£m	£m	£m	£m	£m	£m	£m	£m
With-profits									
Equity securities and portfolio holdings in unit trusts	509	(3)	(1)	26	(56)	—	—	—	475
Debt securities	1,342	(14)	(11)	50	(225)	(17)	142	(54)	1,213
Other investments (including derivative assets)	2,122	(211)	(89)	403	(55)	—	—	—	2,170
Derivative liabilities	—	(2)	—	—	(23)	—	—	—	(25)
Total financial investments, net of derivative liabilities	3,973	(230)	(101)	479	(359)	(17)	142	(54)	3,833
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(381)	9	—	49	—	—	—	—	(323)
Total	3,592	(221)	(101)	528	(359)	(17)	142	(54)	3,510
Unit-linked and variable annuity									
Equity securities and portfolio holdings in unit trusts	—	—	—	—	—	—	—	—	—
Debt securities	33	2	1	16	—	(8)	—	(4)	40
Other investments (including derivative assets)	—	—	—	—	—	—	—	—	—
Derivative liabilities	—	—	—	—	—	—	—	—	—
Total financial investments, net of derivative liabilities	33	2	1	16	—	(8)	—	(4)	40
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	—	—	—	(1)	—	—	(1)	—	(2)
Total	33	2	1	15	—	(8)	(1)	(4)	38

	At 1 Jan 2009	Total gains/losses in income statement	Total gains /losses recorded in other comprehensive income	Purchases	Sales	Settled	Transfers into level 3	Transfers out of level 3	At 31 Dec 2009
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Non-linked shareholder-backed									
Equity securities and portfolio holding in unit trusts	318	(47)	(34)	21	(55)	—	—	(24)	179
Debt securities	3,996	(15)	(565)	104	(473)	(2)	200	(2,177)	1,068
Other investments (including derivative assets)	692	130	(76)	153	(308)	—	43	(2)	632
Derivative liabilities	(246)	93	—	(64)	23	—	(1)	—	(195)
Total financial investments, net of derivative liabilities	4,760	161	(675)	214	(813)	(2)	242	(2,203)	1,684
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(65)	17	6	—	—	—	—	—	(42)
Total	4,695	178	(669)	214	(813)	(2)	242	(2,203)	1,642
Group total									
Equity securities and portfolio holdings in unit trusts	827	(50)	(35)	47	(111)	—	—	(24)	654
Debt securities	5,371	(27)	(575)	170	(698)	(27)	342	(2,235)	2,321
Other investments (including derivative assets)	2,814	(81)	(165)	556	(363)	—	43	(2)	2,802
Derivative liabilities	(246)	91	—	(64)	—	—	(1)	—	(220)
Total financial investments net of derivative liabilities	8,766	(67)	(775)	709	(1,172)	(27)	384	(2,261)	5,557
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(446)	26	6	48	—	—	(1)	—	(367)
Total	8,320	(41)	(769)	757	(1,172)	(27)	383	(2,261)	5,190

Of the total gains and losses in the income statement of a loss of £(41) million in the period, £(205) million relates to financial instruments still held at the end of the year, which can be analysed as £(41) million for equity securities, £(44) million for debt securities, £(221) million for other investments, £76 million for derivative liabilities and £25 million for net asset value attributable to unit holders of consolidated unit trusts and similar funds.

Transfers between level 1 and level 2

There have been no significant transfers between level 1 and level 2 during the year.

Interest income and expense

The interest income on financial assets not at fair value through profit and loss for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, from continuing operations was £2,016 million, £2,532 million and £1,998 million.

The interest expense on financial liabilities not at fair value through profit and loss for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, from continuing operations was £699 million, £645 million, and £366 million.

G2: Market risk

Interest rate risk

The following table shows an analysis of the classes of financial assets and liabilities and their direct exposure to interest rate risk. Each applicable class of the Prudential Group's financial assets or liabilities is analysed between those exposed to fair value interest rate risk, cash flow interest rate risk and those with no direct interest rate risk exposure:

	2007			
	Fair value interest rate risk	Cash flow interest rate risk	Not directly exposed to interest rate risk	Total
	£m			
Financial assets				
Cash and cash equivalents	—	—	4,951	4,951
Deposits	678	7,211	—	7,889
Debt securities	76,481	7,503	—	83,984
Loans	4,319	3,605	—	7,924
Other investments (including derivatives)	664	285	3,447	4,396
	82,142	18,604	8,398	109,144
Financial liabilities				
Core structural borrowings of shareholder-financed operations	2,492	—	—	2,492
Operational borrowings attributable to shareholder-financed operations	2,743	331	7	3,081
Borrowings attributable to with-profits funds	451	441	95	987
Obligations under funding, securities lending and sale and repurchase agreements	594	3,487	—	4,081
Investment contracts without discretionary participation features	1,922	—	12,110	14,032
Derivative liabilities	244	145	691	1,080
Other liabilities	178	98	515	791
	8,624	4,502	13,418	26,544

	2008			
	Fair value interest rate risk	Cash flow interest rate risk	Not directly exposed to interest rate risk	Total
	£m			
Financial assets				
Cash and cash equivalents	—	—	5,955	5,955
Deposits	1,126	6,084	84	7,294
Debt securities	89,353	5,532	339	95,224
Loans	6,979	3,485	27	10,491
Other investments (including derivatives)	1,539	686	4,076	6,301
	98,997	15,787	10,481	125,265
Financial liabilities				
Core structural borrowings of shareholder-financed operations	2,958	—	—	2,958
Operational borrowings attributable to shareholder-financed operations	1,520	454	3	1,977
Borrowings attributable to with-profits funds	729	482	97	1,308
Obligations under funding, securities lending and sale and repurchase agreements	889	4,683	—	5,572
Investment contracts without discretionary participation features	2,885	—	11,616	14,501
Derivative liabilities	1,185	785	2,862	4,832
Other liabilities	218	105	567	890
	10,384	6,509	15,145	32,038

	2009			
	Fair value interest rate risk	Cash flow interest rate risk	Not directly exposed to interest rate risk	Total
	£m			
Financial assets				
Cash and cash equivalents	—	—	5,307	5,307
Deposits	896	11,884	40	12,820
Debt securities	95,817	5,550	384	101,751
Loans	5,923	2,816	15	8,754
Other investments (including derivatives)	1,381	368	3,383	5,132
	104,017	20,618	9,129	133,764
Financial liabilities				
Core structural borrowings of shareholder-financed operations	3,394	—	—	3,394
Operational borrowings attributable to shareholder-financed operations	2,128	620	3	2,751
Borrowings attributable to with-profits funds	804	312	168	1,284
Obligations under funding, securities lending and sale and repurchase agreements	611	2,871	—	3,482
Investment contracts without discretionary participation features	1,098	867	13,840	15,805
Derivative liabilities	647	286	568	1,501
Other liabilities	79	92	706	877
	8,761	5,048	15,285	29,094

Liquidity analysis

i) Contractual maturities of financial liabilities

The following table sets out the contractual maturities for applicable classes of financial liabilities, excluding derivative liabilities and investment contracts and that are separately presented. The financial liabilities are included in the column relating to the contractual maturities at the undiscounted cash flows (including contractual interest payments) due to be paid assuming conditions are consistent with those of year end.

	2007								
	Total carrying value	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total
	£m								
Financial liabilities									
Core structural borrowings of shareholder-financed operations(H13)	2,492	120	685	525	981	793	821	763	4,688
Operational borrowings attributable to shareholder-financed operations(H13)	3,081	2,625	133	319	19	19	72	—	3,187
Borrowings attributable to with-profits funds(H13)	987	444	233	250	—	—	83	100	1,110
Obligations under funding, securities lending and sale and repurchase agreements	4,081	4,081	—	—	—	—	—	—	4,081
Other liabilities	791	630	7	2	—	—	—	152	791
Net asset value attributable to unit holders of consolidated unit-trusts and similar funds	3,556	3,556	—	—	—	—	—	—	3,556
Other creditors	1,020	1,020	—	—	—	—	—	—	1,020
	16,008	12,476	1,058	1,096	1,000	812	976	1,015	18,433

	2008								
	Total carrying value	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total
	£m								
Financial liabilities									
Core structural borrowings of shareholder-financed operations(H13)	2,958	369	422	525	1,273	437	780	1,059	4,865
Operational borrowings attributable to shareholder-financed operations(H13)	1,977	1,590	357	18	18	18	65	—	2,066
Borrowings attributable to with-profits funds(H13)	1,308	232	807	249	—	—	78	113	1,479
Obligations under funding, securities lending and sale and repurchase agreements	5,572	5,572	—	—	—	—	—	—	5,572
Other liabilities	890	646	11	5	—	—	—	228	890
Net asset value attributable to unit holders of consolidated unit-trusts and similar funds	3,843	3,843	—	—	—	—	—	—	3,843
Other creditors	1,496	1,496	—	—	—	—	—	—	1,496
	18,044	13,748	1,597	797	1,291	455	923	1,400	20,211

	2009								
	Total carrying value	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total
	£m								
Financial liabilities									
Core structural borrowings of shareholder-financed operations(H13)	3,394	148	588	733	1,394	877	1,343	1,422	6,505
Operational borrowings attributable to shareholder-financed operations(H13)	2,751	2,351	435	9	9	9	31	—	2,844
Borrowings attributable to with-profits funds(H13)	1,284	228	882	102	—	—	—	205	1,417
Obligations under funding, securities lending and sale and repurchase agreements	3,482	3,482	—	—	—	—	—	—	3,482
Other liabilities	877	643	11	14	—	—	—	211	879
Net asset value attributable to unit holders of consolidated unit-trusts and similar funds	3,809	3,809	—	—	—	—	—	—	3,809
Other creditors	1,612	1,612	—	—	—	—	—	—	1,612
	17,209	12,273	1,916	858	1,403	886	1,374	1,838	20,548

ii) Maturity analysis of derivatives

The following table provides a maturity analysis of derivative assets and liabilities:

	2007					
	Total carrying value	1 year or less	After 1 year to 3 years	After 3 years to 5 years	After 5 years	Total
	£m					
Net derivative position	17	34	5	1	—	40

	2008					
	Total carrying value	1 year or less	After 1 year to 3 years	After 3 years to 5 years	After 5 years	Total
	£m					
Net derivative position	(2,462)	(2,464)	12	(1)	—	(2,453)

	2009					
	Total carrying value	1 year or less	After 1 year to 3 years	After 3 years to 5 years	After 5 years	Total
	£m					
Net derivative position	279	340	10	(1)	—	349

The net derivative positions as shown in the table above comprise the following derivative assets and liabilities:

	2007	2008	2009
	£m		
Derivative assets	1,097	2,370	1,780
Derivative liabilities	(1,080)	(4,832)	(1,501)
Net derivative position	17	(2,462)	279

The majority of derivative assets and liabilities have been included at fair value within the 1 year or less column representing the basis on which they are managed (i.e. to manage principally asset or liability value exposures). Contractual maturities are not considered essential for an understanding of the timing of the cash flows for these instruments and in particular the Prudential Group has no cash flow hedges. The only exception is certain identified interest rate swaps which are fully expected to be held until maturity solely for the purposes of matching cash flows on separately held assets and liabilities. For these instruments the undiscounted cash flows (including contractual interest amounts) due to be paid under the swap contract assuming conditions are consistent with those at year end are included in the column relating to the contractual maturity of the derivative.

The table below shows the maturity profile for investment contracts on an undiscounted basis to the nearest billion. This maturity profile has been based on the cash flow projections of expected benefit payments as part of the determination of the value of in-force business when preparing EEV basis results.

	2007							
	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	Total undiscounted value	Carrying value
	£bn							
Life assurance investment contracts	3	12	16	16	15	25	87	44

	2008							
	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	Total undiscounted value	Carrying value
	£bn							
Life assurance investment contracts	3	18	12	12	9	13	67	38

	2009							
	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	Total undiscounted value	Carrying value
	£bn							
Life assurance investment contracts	3	11	13	13	11	17	68	41

Most investment contracts have options to surrender early, albeit these are often subject to surrender or other penalties. It is therefore the case that most contracts could be said to have a contractual maturity of less than one year, but in reality the additional charges and term of the contracts means these are unlikely to be exercised in practice and the more useful information is to present information on expected payment.

The maturity profile above excludes certain corporate unit-linked business with gross policyholder liabilities of £8 billion at 31 December 2007, of £8 billion at 31 December 2008 and of £9 billion at 31 December 2009 respectively, which has no stated maturity but which is repayable on demand.

This table has been prepared on an undiscounted basis and accordingly the amounts shown for life assurance investment contracts differ from those disclosed on the statement of financial position. Durations of long-term business contracts, covering insurance and investment contracts, on a discounted basis are included in section D.

The vast majority of the Prudential Group's financial assets are held to back the Prudential Group's policyholder liabilities. Although asset/liability matching is an important component of managing policyholder liabilities (both those classified as insurance and those classified as investments), this profile is mainly relevant for managing market risk rather than liquidity risk. Within each business unit this asset/liability matching is performed on a portfolio by portfolio basis.

In terms of liquidity risk a large proportion of the policyholder liabilities contain discretionary surrender values or surrender charges, meaning that many of the Prudential Group's liabilities are expected to be held for the long term. Much of the Prudential Group's investment portfolio is in marketable securities, which can therefore be converted quickly to liquid assets.

For the reasons above an analysis of the Prudential Group's assets by contractual maturity is not considered necessary to evaluate the nature and extent of the Prudential Group's liquidity risk.

Credit risk

The Prudential Group's maximum exposure to credit risk before any allowance for collateral or allocation of losses to policyholders is represented by the carrying value of financial instruments on the balance sheet that have exposures to credit risk. These assets comprise cash and cash equivalents, deposits, debt securities, loans and derivative assets, the carrying value of which are disclosed at the start of this note and note G3 for derivative assets. The collateral in place in relation to derivatives is described in G4. Notes D2, D3, and D4, describe the security for these loans held by the Prudential Group, as disclosed at the start of this note.

Of the total loans and receivables held £5 million, £21 million and £64 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, are past their due date but have not been impaired. Of the total past due but not impaired, £5 million, £21 million and £53 million, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, are less than one year past their due date while £0.2 million, nil and £11 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively are more than six months but less than one year past their due date. The Prudential Group expects full recovery of these loans and receivables. No further analysis has been provided of the age of financial assets that are past due at the end of the reporting period but not impaired as the amounts are immaterial.

No further analysis has been provided of the element of loans and receivables that was neither past due nor impaired for the total portfolio. This is on the grounds of immateriality of the difference between the neither past due nor impaired elements and the total portfolio.

Financial assets that would have been past due or impaired had the terms not been renegotiated amounted to £55 million (2007: nil; 2008: £1 million).

There was no collateral held against loans that are past due and impaired or that are past due but not impaired at 31 December 2007, 31 December 2008 and 31 December 2009.

In addition, during 2007, 2008 and 2009 respectively, the Prudential Group took possession of £7 million, £66 million and £15 million of other collateral held as security, which mainly consists of assets that could be readily convertible into cash.

Currency risk

As at 31 December 2007, 31 December 2008 and 31 December 2009, the Prudential Group held 19%, 20%, and 19% and 13%, 13%, and 13% of its financial assets and financial liabilities respectively, in currencies, mainly US dollar and Euro, other than the functional currency of the relevant business unit.

The financial assets, of which 86%, 77%, and 74%, are held by the PAC with-profits fund, allow the PAC with-profits fund to obtain exposure to foreign equity markets, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The financial liabilities, of which 19%, 38%, and 34%, are held by the PAC with-profits fund, mainly relate to foreign currency borrowings, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The exchange risks inherent in these exposures are mitigated through the use of derivatives, mainly forward currency contracts (note G3 below).

The amount of exchange gains recognised in the income statement in 2007, 2008 and 2009 respectively, except for those arising on financial instruments measured at fair value through profit and loss, is £102 million gains, £638 million gains and £201 million losses. This constitutes £109 million gains, £32 million gains and £41 million losses on Medium Term Notes ("MTN") liabilities and £7 million of net losses, £606 million net gains and £160 million net losses, mainly arising on investments of the PAC with-profits fund in 2007, 2008 and 2009 respectively. The gains/losses on MTN liabilities are fully offset by value movements on cross-currency swaps, which are measured at fair value through profit and loss, for 2007, 2008 and 2009 respectively.

G3: Derivatives and hedging

Derivatives

The Prudential Group enters into a variety of exchange traded and over-the-counter derivative financial instruments, including futures, options, forward currency contracts and swaps such as interest rate swaps, cross-currency swaps, swaptions and credit default swaps.

All over-the-counter derivative transactions are conducted under standardised ISDA International Swaps and Derivatives Association Inc master agreements and the Prudential Group has collateral agreements between the individual Prudential Group entities and relevant counterparties in place under each of these market master agreements.

The total fair value balances of derivative assets and liabilities as at 31 December were as follows:

2007	UK insurance operations	US insurance operations	Asian insurance operations	Asset management	Unallocated to a segment	Group total
	£m					
Derivative assets	571	390	15	118	3	1,097
Derivative liabilities	(689)	(158)	(2)	(186)	(45)	(1,080)
	(118)	232	13	(68)	(42)	17

2008	UK insurance operations	US insurance operations	Asian insurance operations	Asset management	Unallocated to a segment	Group total
	£m					
Derivative assets	1,326	675	15	74	280	2,370
Derivative liabilities	(3,401)	(863)	(32)	(292)	(244)	(4,832)
	(2,075)	(188)	(17)	(218)	36	(2,462)

2009	UK insurance operations	US insurance operations	Asian insurance operations	Asset management	Unallocated to a segment	Group total
	£m					
Derivative assets	910	519	150	48	153	1,780
Derivative liabilities	(709)	(461)	(146)	(49)	(136)	(1,501)
	201	58	4	(1)	17	279

The above derivative assets are included in 'other investments' in the primary statements.

The notional amount of the derivatives, distinguishing between UK insurance and US operations, was as follows:

	2007			
	UK insurance operations Notional amount on which future payments are based		US insurance operations Notional amount on which future payments are based	
As at 31 December 2007	Asset	Liability	Asset	Liability
	£m			
Cross-currency swaps*	658	648	602	—
Equity index call options	—	23	—	—
Swaptions	1,125	—	25,620	1,005
Futures	1,905	2,176	—	371
Forwards*	17,243	17,635	—	—
Inflation swaps	1,758	1,319	—	—
Credit default swaps	4,181	59	—	—
Single stock options	—	—	—	—
Credit derivatives	—	—	3	20
Put options	—	—	3,642	—
Equity options	—	—	5,545	11
Total return swaps	956	955	226	—
Interest rate swaps*	4,335	4,663	1,708	3,587

	2008			
	UK insurance operations Notional amount on which future payments are based		US insurance operations Notional amount on which future payments are based	
As at 31 December 2008	Asset	Liability	Asset	Liability
	£m			
Cross-currency swaps*	838	1,014	448	218
Equity index call options	17	32	—	—
Swaptions	980	980	28,863	—
Futures	3,286	4,055	—	460
Forwards*	14,315	16,489	—	—
Inflation swaps	2,559	2,482	—	—
Credit default swaps	123	14	—	—
Single stock options	1	1	—	—
Credit derivatives	—	—	31	177
Put options	—	—	6,573	—
Equity options	2	4	3,785	5
Total return swaps	479	514	—	313
Interest rate swaps*	5,074	5,245	1,704	4,514

As at 31 December 2009	2009 UK insurance operations Notional amount on which future payments are based		2009 US insurance operations Notional amount on which future payments are based	
	Asset	Liability	Asset	Liability
	£m			
Cross-currency swaps*	808	881	376	168
Equity index call options	—	—	—	—
Swaptions	900	900	12,694	5,263
Futures	2,267	2,987	—	1,534
Forwards*	20,235	20,184	—	—
Inflation swaps	2,337	2,205	—	—
Credit default swaps	90	12	—	—
Single stock options	—	—	—	—
Credit derivatives	—	—	—	189
Put options	—	—	9,072	—
Equity options	30	552	3,246	562
Total return swaps	420	421	—	—
Interest rate swaps*	5,529	5,710	1,579	3,957

* In addition, for 2007, 2008 and 2009 respectively, the other operations, including the Group Treasury function and the Asian operations, have cross-currency swap assets and liabilities with notional amounts of £730 million, £1,503 million, and £819 million and £1,401 million, £605 million, and £122 million respectively, forward currency contracts assets and liabilities with notional amounts of £983 million, £1,419 million, and £570 million and £773 million, £2,310 million, and £958 million respectively, interest rate swaps assets and liabilities of £2,799 million, £1,407 million, and £793 million and £1,563 million, £2,316 million, and £522 million, respectively, and cliquet options assets of nil, £1,525 million, and £7 million.

These derivatives are used for efficient portfolio management to obtain cost effective and efficient exposure to various markets in accordance with the Prudential Group's investment strategies and to manage exposure to interest rate, currency, credit and other business risks. See also note D3 for use of derivatives by the Prudential Group's US operations.

The Prudential Group uses various interest rate derivative instruments such as interest rate swaps to reduce exposure to interest rate volatility.

The UK insurance operations use various currency derivatives in order to limit volatility due to foreign currency exchange rate fluctuations arising on securities denominated in currencies other than sterling. See also note G2 above. In addition, total return swaps and interest rate swaps are held for efficient portfolio management.

As part of the efficient portfolio management of the PAC with-profits fund, the fund may, from time to time, invest in cash-settled forward contracts over Prudential plc Shares, which are accounted for consistently with other derivatives. This is in order to avoid a mismatch of the with-profits investment portfolio with the investment benchmarks set for its equity-based investment funds. The contracts will form part of the long-term investments of the with-profits fund. These contracts are subject to a number of limitations for legal and regulatory reasons.

Some of the Prudential Group's products, especially those sold in the US, have certain guarantee features linked to equity indexes. A mismatch between product liabilities and the performance of the underlying assets backing them exposes the Prudential Group to equity index risk. In order to mitigate this risk, the relevant business units purchase swaptions, equity options and futures to match asset performance with liabilities under equity-indexed products.

The US operations and some of the UK operations hold large amounts of interest-rate sensitive investments that contain credit risks on which a certain level of defaults is expected. These entities have purchased some swaptions in order to manage the default risk on certain underlying assets and hence reduce the amount of regulatory capital held to support the assets.

Hedging

The Prudential Group has formally assessed and documented the effectiveness of the following hedges under IAS 39.

Fair value hedges

The Prudential Group uses interest rate derivatives to hedge the interest exposures on its US$300 million, 6.5% perpetual subordinated capital securities. In addition, the Prudential Group similarly used interest rate derivatives to hedge the exposure on its US$1 billion, 6.5% perpetual subordinated capital securities until this hedge was cancelled in March 2009. Where the hedge relationship is de-designated and re-designated, the fair value adjustment to the hedged item up to the point of de-designation continues to be reported as part of the basis of the hedged item and is amortised to the income statement based on a recalculated effective interest rate over the residual period to the first break clause date of the perpetual subordinated capital securities.

The Prudential Group has chosen to designate as a fair value hedge certain fixed to floating rate swaps which hedge the fair value exposure to interest rate movements of certain of the Prudential Group's operational borrowings.

The fair value of the derivatives designated as fair value hedges above at 31 December 2007, 31 December 2008, and 31 December 2009 were an asset of £5 million, £17 million, and £7 million and liabilities of £25 million, £nil, and £1 million. Movements in the fair value of the hedging instruments (net gain of £6 million, a net loss of £4 million, and a net loss of £11 million, for 2007, 2008, and 2009 respectively) and the hedged items (net loss of £4 million, a net gain of £7 million, and a net gain of £11 million, for 2007, 2008, and 2009 respectively) are recorded in the income statement in respect of the fair value hedges above.

Cash flow hedges

The Prudential Group has no cash flow hedges in place.

Net investment hedges

The Prudential Group entered into a series of rolling one to three-month period forward currency transactions which together formed a net investment hedge of the currency exposure of the net investments in the US operations. The programme ceased in August 2009. At December 2008, US$600 million of the forward currency contracts were designated as a partial net investment hedge of the currency exposure of the net investments in the US operations. The fair value of the forward currency contracts at 31 December 2007 and 31 December 2008 was a liability of £44 million and £56 million respectively, of which a liability of £44 million and £17 million respectively was designated as a net investment hedge of the currency exposure of the net investments in the US operations.

In addition, the Prudential Group has designated perpetual subordinated capital securities totalling US$1.55 billion as a net investment hedge to hedge the currency risks related to the net investment in Jackson. The carrying value of the subordinated capital securities was £763 million, £1,059 million, and £963 million as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. The foreign exchange gain of £13 million, loss of £299 million and of £118 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, on translation of the borrowings to pounds sterling at the statement of financial position date is recognised in the translation reserve in shareholders' equity.

The net investment hedges were 100% effective.

G4: Derecognition and collateral

Securities lending and reverse repurchase agreements

The Prudential Group has entered into securities lending (including repurchase agreements) whereby blocks of securities are loaned to third-parties, primarily major brokerage firms. The amounts above the fair value of the loaned securities required to be held as collateral by the agreements depend on the quality of the collateral, calculated on a daily basis. The loaned securities are not removed from the Prudential Group's consolidated statement of financial position, rather they are retained within the appropriate investment classification. Collateral typically consists of cash, debt securities, equity securities and letters of credit. At 31 December 2007, 31 December 2008 and 31 December 2009, the Prudential Group had lent £17,172 million, £12,617 million and £10,446 million respectively (of which £11,461 million, £9,701 million, and £7,910 million, respectively was lent by the PAC with-profits fund) of securities and at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, held collateral under such agreements of £18,125 million, £13,497 million and £10,669 million (of which £12,105 million, £9,924 million and £8,086 million, respectively was held by the PAC with-profits fund).

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the Prudential Group had entered into reverse repurchase transactions under which it purchased securities and had taken on the obligation to resell the securities for the purchase price of £1,361 million, £588 million and £1,587 million, together with accrued interest.

Collateral and pledges under derivative transactions

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the Prudential Group had pledged £260 million, £1,154 million and £644 million for liabilities and held collateral of £292 million, £829 million and £586 million in respect of over-the-counter derivative transactions.

G5: Impairment of financial assets

In accordance with the Prudential Group's accounting policy set out in note A4, impairment reviews were performed for available-for-sale securities and loans and receivables. In addition, impairment reviews were undertaken for the reinsurers' share of insurance contract liabilities.

During the year ended 31 December 2007, 31 December 2008, and 31 December 2009 respectively, impairment losses of £184 million, £525 million, and £647 million were recognised for available-for-sale securities and loans and receivables. These were £35 million, £497 million and £630 million in respect of available-for-sale securities held by Jackson and a further £149 million, £28 million and £17 million in respect of loans and receivables, for 2007, 2008 and 2009 respectively. The 2007 impairment charge of £149 million related to loans and advances to customers in the discontinued banking operations during the period of ownership. The 2008 impairment charge for loans and receivables of £28 million related primarily to loans held by the UK with-profits fund. The 2009 impairment charge for loans and receivables of £17 million relates to loans held by the UK with-profits fund and mortgage loans held by Jackson.

Impairment losses recognised on available-for-sale securities amounted to £35 million, £497 million and £630 million, for 2007, 2008 and 2009 respectively. Of this amount, 14%, 29% and 86% respectively, has been recorded on structured asset-backed securities, primarily due to reduced cash flow expectations on such securities that are collateralised by diversified pools of primarily below investment grade securities. Of the losses related to the impairment of fixed maturity securities the top five individual corporate issuers made up 57%, 27%, and 11%, for 2007, 2008 and 2009 respectively, reflecting a deteriorating business outlook of the companies concerned.

The impairment losses have been recorded in 'investment return' in the income statement.

In 2007, 2008 and 2009 respectively, the Prudential Group realised gross losses on sales of available-for-sale securities of £86 million, £184 million and £134 million with 46%, 55% and 60% of these losses related to the disposal of fixed maturity securities of six, six and five (2007, 2008 and 2009 respectively) individual issuers, which were disposed off to rebalance the portfolio in the US operations in response to the unstable mortgage lending.

The effect of those reasonably likely changes in the key assumptions underlying the estimates that underpin the assessment of whether impairment has taken place depends on the factors described in note A3. A key indicator of whether such impairment may arise in future, and the potential amounts at risk, is the profile of gross unrealised losses for fixed maturity securities accounted for on an available-for-sale basis by reference to the time periods by which the securities have been held continuously in an unrealised loss position and by reference to the maturity date of the securities concerned.

For 2007, 2008 and 2009 respectively the amounts of gross unrealised losses for fixed maturity securities classified as available-for-sale under IFRS in an unrealised loss position was £439 million, £3,178 million and £966 million. Notes B1 and D3 provide further details on the impairment charges and unrealised losses of Jackson's available-for-sale securities.

H: OTHER INFORMATION ON STATEMENT OF FINANCIAL POSITION ITEMS

H1: Intangible assets attributable to shareholders

a Goodwill

	2007	2008	2009
	£m	£m	£m
Cost			
At 1 January	1,461	1,461	1,461
Disposal of Taiwan Agency business	—	—	(44)
Additional consideration paid on previously acquired businesses	—	—	13
At 31 December	1,461	1,461	1,430
Aggregate impairment			
At 1 January and 31 December	(120)	(120)	(120)
Net book amount at 31 December	1,341	1,341	1,310

Impairment testing

Goodwill does not generate cash flows independently of other groups of assets and thus is assigned to cash generating units (CGUs) for the purposes of impairment testing. These CGUs are based upon how management monitors the business and represent the lowest level to which goodwill can be allocated on a reasonable basis. An allocation to CGUs of the Prudential Group's goodwill attributable to shareholders is shown below:

	2007	2008	2009
	£m	£m	£m
M&G	1,153	1,153	1,153
Other	188	188	157
	1,341	1,341	1,310

'Other' represents goodwill amounts allocated across CGUs in Asia and US operations. These goodwill amounts are not individually material.

Assessment of whether goodwill may be impaired

With the exception of M&G, the goodwill attributable to shareholders in the statement of financial position mainly relates to acquired life businesses. Prudential routinely compares the aggregate of net asset value and acquired goodwill on an IFRS basis of acquired life business with the value of the business as determined using the EEV methodology, as described in note D1. Any excess of IFRS over EEV carrying value is then compared with EEV basis value of current and projected future new business to determine whether there is any indication that the goodwill in the IFRS statement of financial position may be impaired. The assumptions underpinning the Prudential Group's EEV basis of reporting are included in the EEV basis supplementary information in Appendix IV to this listing document.

Goodwill is tested for impairment by comparing the CGUs carrying amount, excluding any goodwill, with its recoverable amount.

M&G

The recoverable amount for the M&G CGU has been determined by calculating its value in use. This has been calculated by aggregating the present value of future cash flows expected to be derived from the M&G operating segment (based upon management projections).

The discounted cash flow valuation has been based on a five-year (three-year plan for the year ended 31 December 2007) plan prepared by M&G, and approved by management, and cash flow projections for later years.

The value in use is particularly sensitive to a number of key assumptions as follows:

i The set of economic, market and business assumptions used to derive the five-year plan. The direct and secondary effects of recent developments, e.g. the fall in global equity markets, are considered by management in arriving at the expectations for the financial projections for the plan.

ii The assumed growth rate on forecast cash flows beyond the terminal year of the plan. A growth rate of 2.5%, 2.5%, and 2.5% as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, has been used to extrapolate beyond the plan period representing management's best estimate view of the long-term growth rate of the business after considering the future and past growth rates and external sources of data.

iii The risk discount rate (applicable across 2007, 2008 and 2009). Differing discount rates have been applied in accordance with the nature of the individual component businesses. For retail and institutional business a risk discount rate of 12% has been applied to post-tax cash flows. The pre-tax risk discount rate was 16%. Management have determined the risk discount rate by reference to an average implied discount rate for comparable UK listed asset managers calculated by reference to risk-free rates, equity risk premiums of 5% and an average 'beta' factor for relative market risk of comparable UK listed asset managers. A similar approach has been applied for the other component businesses of M&G.

iv That asset management contracts continue on similar terms.

Management believes that any reasonable change in the key assumptions would not cause the recoverable amount of M&G to fall below its carrying amount.

Japanese life company

The aggregate goodwill impairment of £120 million at 31 December 2007, 31 December 2008 and 31 December 2009 relates to the goodwill held in relation to the Japanese life operation which was impaired in 2005.

b Deferred acquisition costs and other intangible assets

Deferred acquisition costs and other intangible assets in the consolidated statement of financial position attributable to shareholders consist of:

	2007	2008	2009
	£m	£m	£m
Deferred acquisition costs (DAC) related to insurance contracts as classified under IFRS 4	2,644	5,097	3,823
Deferred acquisition costs related to investment management contracts, including life assurance contracts classified as financial instruments and investment management contracts under IFRS 4	113	108	107
	2,757	5,205	3,930
Present value of acquired in-force policies for insurance contracts as classified under IFRS 4	59	64	52
Present value of future profits of acquired investment management contracts, including life assurance contracts classified as financial instruments and investment management contracts under IFRS 4	4	1	1
Distribution rights	16	79	66
	79	144	119
Total of deferred acquisition costs and other intangible assets	2,836	5,349	4,049
Arising in:			
UK insurance operations	157	134	127
US insurance operations(note(i))	1,928	3,962	3,092
Asian insurance operations	745	1,247	822
Asset management operations	6	6	8
	2,836	5,349	4,049

The movement in the year comprises:

	2007	2008	2009
	£m	£m	£m
Balance at 1 January	2,497	2,836	5,349
Additions	717	959	1,071
Amortisation to income statement	(424)	(551)	(316)
Exchange differences	(42)	1,274	(550)
Change in shadow DAC (note D3(h))	88	831	(1,069)
DAC movement on sale of Taiwan agency business	—	—	(436)
Balance at 31 December	2,836	5,349	4,049

Amortisation is included in the 'acquisition costs and other operating expenditures' line in the income statement.

Deferred acquisition costs related to insurance contracts attributable to shareholders

The movement in deferred acquisition costs relating to insurance contracts attributable to shareholders is as follows:

	2007	2008	2009
	£m	£m	£m
Deferred acquisition costs at 1 January	2,315	2,644	5,097
Additions	694	887	1,054
Amortisation	(410)	(520)	(286)
Exchange differences	(44)	1,255	(537)
Change in shadow DAC	89	831	(1,069)
DAC movement on sale of Taiwan agency business	—	—	(436)
Deferred acquisition costs at 31 December	2,644	5,097	3,823

Deferred acquisition costs related to investment management contracts attributable to shareholders

Incremental costs associated with the origination of investment management contracts written by the Group's insurance and asset management businesses are capitalised and amortised as the related revenue is recognised.

	2007	2008	2009
	£m	£m	£m
At 1 January			
Gross amount	130	136	148
Accumulated amortisation	(20)	(23)	(40)
Net book amount	110	113	108
Additions (through internal development)	7	12	14
Amortisation	(3)	(17)	(15)
Other charges	(1)	—	—
At 31 December	113	108	107
Comprising:			
Gross amount	136	148	162
Accumulated amortisation	(23)	(40)	(55)
Net book amount	113	108	107

Present value of acquired in-force business of long-term business contracts attributable to shareholders

The present value of acquired in-force business (PVAIF) relating to investment contracts without discretionary participation features represents the contractual right to benefit from providing these investment management services in the future. The fair value is measured as the present value of the future profits of the asset management component of these contracts. These contracts are accounted for under the provisions of IAS 18. The remainder of the PVAIF balance relates to insurance contracts and is accounted for under UK GAAP as permitted by IFRS 4.

The present value of future profits of acquired asset management contracts relates to unit-linked contracts acquired as part of the M&G acquisition in 1999.

Amortisation is charged to the 'acquisition costs and other operating expenditure' line in the income statement over the period of provision of asset management services as those profits emerge.

	2007		2008		2009	
	Insurance contracts	Investment management	Insurance contracts	Investment management	Insurance contracts	Investment management
	£m		£m		£m	
At 1 January						
Cost	220	12	161	12	184	12
Accumulated amortisation	(154)	(6)	(102)	(8)	(120)	(11)
Net book amount	66	6	59	4	64	1
Exchange differences	2	—	14	—	(6)	—
Amortisation charge	(9)	(2)	(9)	(3)	(6)	—
At 31 December	59	4	64	1	52	1
Comprising:						
Cost	161	12	184	12	175	12
Accumulated amortisation	(102)	(8)	(120)	(11)	(123)	(11)
Net book amount	59	4	64	1	52	1

Distribution rights attributable to the Asian insurance operations

Distribution rights relate to facilitation fees paid in respect of the bancassurance partnership arrangements in Asia for the bank distribution of Prudential's insurance products for a fixed period of time. The distribution rights amounts are amortised over the term of the distribution contracts.

	2007	2008	2009
	£m	£m	£m
At 1 January			
Gross amount	—	16	84
Accumulated amortisation	—	0	(5)
	—	16	79
Additions	16	62	3
Amortisation charge	—	(4)	(9)
Exchange differences	—	5	(7)
At 31 December	16	79	66
Comprising:			
Gross amount	16	84	79
Accumulated amortisation	—	(5)	(13)
	16	79	66

H2: Intangible assets attributable to with-profits funds

a Goodwill in respect of acquired investment subsidiaries for venture fund and other investment purposes

	2007 £m	2008 £m	2009 £m
Goodwill			
Carrying value at 1 January	587	192	174
Additions	313	—	—
Deconsolidated venture fund investments	(708)	—	—
Impairment	—	(18)	(50)
At 31 December	192	174	124

All the goodwill relates to the UK insurance operations segment.

Following the sale by the Prudential Group of PPM Capital in November 2007, the only venture fund investment consolidated by the Prudential Group relates to an investment by PAC with-profits fund managed by M&G. Aside from this investment, the Prudential Group no longer controls venture fund investments and consequently ceased to consolidate these operations, resulting in the £708 million deconsolidation adjustment presented above in 2007. In 2008, following the impairment testing carried out, £18 million of the goodwill was deemed to be impaired and written off accordingly.

The only venture fund investment consolidated by the Prudential Group relates to an investment by PAC with-profits fund managed by M&G. The goodwill shown in the table above relates to this venture fund investment. Goodwill is tested for impairment for this investment by comparing the investment's carrying value including goodwill with its recoverable amount. The recoverable amount of the investment was determined by calculating its fair value less costs to sell. The fair value has been determined by using the discounted cash flow valuation. The valuation is based on cash flow projections to 2015 prepared by management after considering the historical experience and future growth rates of the business. The key assumption applied in the calculation is the risk discount rate of 14% which has been derived by reference to risk-free rates and an equity premium risk. In 2009, following the impairment testing carried out, £50 million (2008: £18 million) of the goodwill was deemed to be impaired and written off accordingly.

This impairment charge is recorded under 'acquisition costs and other operating expenditure' but is also taken account of in determining the charge/credit in the income statement for the transfer to the liability for unallocated surplus of with-profits funds. Accordingly, the charge does not affect shareholders' profits or equity.

b Deferred acquisition costs and other intangible assets

Other intangible assets in the Group consolidated statement of financial position attributable to with-profits funds consist of:

	2007	2008	2009
	£m	£m	£m
Deferred acquisition costs related to insurance contracts attributable to the PAC with-profits fund	19	13	9
Distribution rights attributable to with-profits funds of the Asian insurance operations	—	113	97
	19	126	106

Deferred acquisition costs related to insurance contracts attributable to the PAC with-profit fund

The movement in deferred acquisition costs relating to insurance contracts attributable to the PAC with-profits fund is as follows:

	2007	2008	2009
	£m	£m	£m
At 1 January	31	19	13
Additions	1	—	—
Amortisation charge	(13)	(6)	(4)
At 31 December	19	13	9

The above costs relate to non-participating business written by the PAC with-profits sub-fund.

No deferred acquisition costs are established for the participating business.

Distribution rights attributable to with-profit funds of the Asian insurance operations

Distribution rights relate to facilitation fees paid in relation to the bancassurance partnership arrangements in Asia for the bank distribution of Prudential's insurance products for a fixed period of time. The distribution rights amounts are amortised over the term of the distribution contracts.

	2007	2008	2009
	£m	£m	£m
At 1 January			
Gross amount	—	—	115
Accumulated amortisation	—	—	(2)
	—	—	113
Additions	—	115	—
Amortisation charge	—	(2)	(4)
Exchange differences	—	—	(12)
At 31 December	—	113	97
Comprising:			
Gross amount	—	115	103
Accumulated amortisation	—	(2)	(6)
	—	113	97

H3: Reinsurers' share of insurance contract liabilities

	2007	2008	2009
	£m	£m	£m
Insurance contract liabilities	724	1,176	1,114
Claims outstanding	59	64	73
	783	1,240	1,187

The movement on reinsurers' share of insurance contract liabilities is as follows:

	2007	2008	2009
	£m	£m	£m
At 1 January	878	724	1,176
Movement in the year	(147)	243	24
Foreign exchange translation differences	(7)	209	(86)
At 31 December	724	1,176	1,114

H4: Tax assets and liabilities

Assets

Of the £285 million, £657 million, and £636 million current tax recoverable, at 31 December 2007, 2008 and 2009 respectively, the majority is expected to be recovered in one year or less.

Deferred tax asset

	2007	2008	2009
	£m	£m	£m
Unrealised losses on investments	129	1,267	1,156
Balances relating to investment and insurance contracts	2	12	20
Short-term timing differences	770	1,282	1,228
Capital allowances	20	16	18
Unused deferred tax losses	30	309	286
Total	951	2,886	2,708

The deferred tax asset at 31 December 2007, 31 December 2008 and 31 December 2009 arises in the following parts of the Prudential Group.

	2007	2008	2009
	£m	£m	£m
UK insurance operations:			
SAIF	1	7	2
PAC with-profits fund (including PAL)	93	272	141
Other	11	234	149
US insurance operations	657	1,969	1,944
Asian insurance operations	73	101	132
Other operations	116	303	340
	951	2,886	2,708

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 available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted.

The taxation regimes applicable across the Prudential Group apply separate rules to trading and capital profits and losses. The distinction between temporary differences that arise from items of either a trading or capital nature may affect the recognition of deferred tax assets. Accordingly, for the 2007, 2008 and 2009 results and statement of financial position at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the possible tax benefit of approximately £280 million, £211 million and £257 million, which may arise from capital losses valued at approximately £1.4 billion, £1 billion and £1.2 billion, is sufficiently uncertain that it has not been recognised. In addition at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, a potential deferred tax asset of £112 million, £678 million and £607 million, which may arise from tax losses and other potential temporary differences totalling £350 million, £2.2 billion and £2.1 billion, for 2007, 2008 and 2009 respectively, is sufficiently uncertain that it has not been recognised. Forecasts as to when the tax losses and other temporary differences are likely to be utilised indicate that they may not be utilised in the short term.

Liabilities

The current tax liability was £1,237 million, £842 million and £1,215 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. The Prudential Group considers that whilst the UK tax provision established within the current tax liability represents an appropriate provision for matters under discussion with HM Revenue & Customs in the UK, it is not possible to estimate the amount of the tax liability expected to be settled in one year or less due to the uncertainty over when these issues will be agreed.

Deferred tax liability

	2007	2008	2009
	£m	£m	£m
Unrealised gains on investments	2,098	765	1,744
Balances relating to investment and insurance contracts	599	968	961
Short-term timing differences	693	1,490	1,159
Capital allowances	12	6	8
	3,402	3,229	3,872

Unprovided deferred income tax liabilities on temporary differences associated with investments in subsidiaries, associates and interests in joint ventures are considered to be insignificant due to the availability of various UK tax exemptions and reliefs.

Discounting

Deferred tax asset and liability balances have not been discounted.

H5: Accrued investment income and other debtors

	2007	2008	2009
	£m	£m	£m
Accrued investment income			
Interest receivable	1,434	1,775	1,718
Other	589	738	755
Total	2,023	2,513	2,473
Other debtors			
Premiums receivable:			
From policyholders	154	194	148
From intermediaries	13	17	17
From reinsurers	104	253	82
Other	638	768	515
Total	909	1,232	762
Total accrued investment income and other debtors	2,932	3,745	3,235

Of the £2,932 million, £3,745 million and £3,235 million of accrued investment income and other debtors, £64 million, £114 million and £134 million is expected to be settled after one year or more, for 2007, 2008 and 2009 respectively.

H6: Property, plant and equipment

Property, plant and equipment comprise Prudential Group occupied properties, development property and tangible assets. A reconciliation of the carrying amount of these items from the beginning of the year to the end of the year is as follows:

	Group occupied property	Development property	Tangible assets	Continuing operations	Discontinued operations	Total
	£m	£m	£m	£m	£m	£m
At 1 January 2007						
Cost	225	479	917	1,621	226	1,847
Accumulated depreciation	(33)	—	(518)	(551)	(163)	(714)
Net book amount	192	479	399	1,070	63	1,133
Year ended 31 December 2007						
Opening net book amount	192	479	399	1,070	63	1,133
Exchange differences	2	—	1	3	—	3
Depreciation charge	(48)	—	(50)	(98)	(9)	(107)
Additions	71	48	109	228	3	231
Arising on acquisition of subsidiaries	5	—	33	38	—	38
Disposal of subsidiaries	—	—	—	—	(57)	(57)
Deconsolidated venture fund investments	(69)	—	(261)	(330)	—	(330)
Disposals	(2)	—	(25)	(27)	—	(27)
Reclassification from (to) held for investment	—	120	—	120	—	120
Reclassification from held for sale	—	8	—	8	—	8
Closing net book amount	151	655	206	1,012	—	1,012
At 1 January 2008						
Cost	172	655	612	1,439	—	1,439
Accumulated depreciation	(21)	—	(406)	(427)	—	(427)
Net book amount	151	655	206	1,012	—	1,012

	Group occupied property	Development property	Tangible assets	Continuing operations	Discontinued operations	Total
	£m	£m	£m	£m	£m	£m
Year ended 31 December 2008						
Opening net book amount	151	655	206	1,012	—	1,012
Exchange differences	45	—	40	85	—	85
Depreciation charge	(3)	—	(67)	(70)	—	(70)
Additions	3	152	85	240	—	240
Disposals	(1)	—	(23)	(24)	—	(24)
Reclassification from (to) held for investment	68	(676)	—	(608)	—	(608)
Closing net book amount	263	131	241	635	—	635
At 1 January 2009						
Cost	292	131	717	1,140	—	1,140
Accumulated depreciation	(29)	—	(476)	(505)	—	(505)
Net book amount	263	131	241	635	—	635
Year ended 31 December 2009						
Opening net book amount	263	131	241	635	—	635
Exchange differences	(9)	—	(31)	(40)	—	(40)
Depreciation charge	(4)	—	(70)	(74)	—	(74)
Additions	2	—	89	91	—	91
Disposals (including amounts disposed of with the Taiwan agency business)	(99)	—	(15)	(114)	—	(114)
Reclassify as investment property*	—	(131)	—	(131)	—	(131)
Closing net book amount	153	—	214	367	—	367
At 31 December 2009						
Cost	173	—	661	834	—	834
Accumulated depreciation	(20)	—	(447)	(467)	—	(467)
Net book amount	153	—	214	367	—	367

* In line with changes issued by the IASB as part of its Annual Improvement Project in May 2008 as shown in note A5, all development properties have been reclassified as investment properties (see note H7). The total property, plant and equipment relates to continuing operations only.

Notes

i Owner occupied property can be analysed as follows:

	2007	2008	2009
	£m	£m	£m
Freehold	92	183	143
Long leases (>50 years)	58	78	9
Medium leases (10-50 years)	1	2	1
Total	151	263	153

No owner-occupied property is located in Hong Kong.

Capital expenditure: property, plant and equipment by segment

	2007	2008	2009
	£m	£m	£m
Insurance operations:			
UK	129	154	5
US	31	18	12
Asia	46	40	65
Asset management operations:			
M&G	5	3	—
US	2	2	1
Asia	4	8	2
Total segment	217	225	85
Unallocated corporate and discontinued operations	14	15	6
Total	231	240	91

H7: Investment properties

Investment properties principally relate to the PAC with-profits fund and are carried at fair value. A reconciliation of the carrying amount of investment properties at the beginning and end of the year is set out below:

	2007	2008	2009
	£m	£m	£m
At 1 January	14,491	13,688	11,992
Reclassification of development property*	—	—	131
Additions:			
Resulting from acquisitions	1,707	1,414	184
Resulting from expenditure capitalised	128	218	133
Resulting from acquisitions through business combinations	—	463	1
Disposals (including amounts disposed of with the Taiwan agency business)	(1,378)	(1,010)	(1,220)
Net loss from fair value adjustments	(1,128)	(3,784)	(203)
Net foreign exchange differences	14	395	(113)
Transfers to held for sale assets	(25)	—	—
Transfers to owner occupied properties	—	(68)	—
Other transfers from (to) property, plant and equipment	(121)	676	—
At 31 December	13,688	11,992	10,905

* In line with changes issued by the IASB as part of its Annual Improvement Project in May 2008 (as shown in note H6 and A5) all development properties with a total cost of £131 million have been reclassified as investment properties at 1 January 2009. At this date these investments had a fair value of £152 million. The initial gain of £21 million is included as part of 'net loss from fair value adjustments'.

Notes

i Investment property can be analysed as follows:

Hong Kong investment properties	2007	2008	2009
	£m	£m	£m
Medium leases (10-50 years)	35	42	41
Total	35	42	41

Other investment properties	2007	2008	2009
	£m	£m	£m
Freehold	10,332	8,427	7,696
Long leases (>50 years)	3,128	3,132	2,781
Medium leases (10-50 years)	189	388	387
Short leases (<10 years)	4	3	—
Total	13,653	11,950	10,864

The income statement includes the following items in respect of investment properties:

	2007	2008	2009
	£m	£m	£m
Rental income from investment properties	670	726	754
Direct operating expenses (including repairs and maintenance expenses) arising from investment properties:			
That generated rental income during the year	117	109	131
That did not generate rental income during the year	—	1	—
Total direct operating expenses	117	110	131

At 31 December 2007, 31 December 2008, and 31 December 2009 respectively, investment properties of £3,665 million, £3,559 million, and £3,177 million are held under finance leases. A reconciliation between the total of future minimum lease payments at the statement of financial position date, and their present value is shown below:

	2007	2008	2009
	£m	£m	£m
Future minimum lease payments at 31 December	979	963	1,683
Future finance charges on finance leases	(877)	(863)	(1,517)
Present value of minimum lease payments	102	100	166
Future minimum lease payments are due as follows:			
Less than 1 year	5	5	9
1 to 5 years	22	22	38
Over 5 years	952	936	1,636
Total	979	963	1,683
The present values of these minimum lease payments are:			
Less than 1 year	5	5	8
1 to 5 years	22	22	38
Over 5 years	75	73	120
Total	102	100	166

Contingent rent is that portion of the lease payments that is not fixed in amount but is based on the future value of a factor that changes other than with the passage of time. Contingent rent recognised as an expense in 2007, 2008 and 2009 respectively, amounted to £14 million, nil and nil. Contingent rents recognised as income in the year amounted to £26 million, nil, and nil, for 2007, 2008 and 2009 respectively.

The Prudential Group's policy is to rent investment properties to tenants through operating leases. Minimum future rentals to be received on non-cancellable operating leases are receivable in the following periods:

	2007	2008	2009
	£m	£m	£m
Less than 1 year	679	742	662
1 to 5 years	2,464	2,599	2,282
Over 5 years	8,266	9,106	7,792
Total	11,409	12,447	10,736

The total minimum future rentals to be received on non-cancellable sub-leases for land and buildings at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, are £2,746 million, £3,730 million and £3,684 million.

H8: Investments in associates and joint ventures

Investments in associates

The Prudential Group had four associates at 31 December 2007 and 2008, and three associates at 31 December 2009 that are accounted for using the equity method. The Prudential Group's associates are a 30% interest in The Nam Khang, a Vietnamese property developer, a 30% interest in Apollo Education and Training Organisation Vietnam and a 25% interest in OYO Developments Limited. The associate previously held in 2007 and 2008 was a 26.8% interest in IFonline Group Limited (IFonline). IFonline is no longer an associate of the Prudential Group following a restructuring of that entity in April 2009.

The Prudential Group also has investments in associates which meet the IAS 28 criteria for measurement at fair value through profit and loss in accordance with IAS 39.

Associates accounted for using the equity method

For 2007 and 2008 equity accounting is applied to IFonline based on its reporting period of the year to 30 November and is adjusted for material changes up to 31 December. Accordingly, the information is deemed to cover the same period as that of the Prudential Group.

A summary of the movements in investments in associates accounted for using the equity method in 2007, 2008 and 2009 is set out below:

	Share of capital	Share of reserves	Share of net assets	Goodwill	Total carrying value
	£m	£m	£m	£m	£m
Balance at 1 January 2007	4	(5)	(1)	7	6
Acquisitions	5	—	5	1	6
Exchange translations and other movements	—	—	—	—	—
Share of loss for the year after tax	—	—	—	—	—
Balance at 31 December 2007	9	(5)	4	8	12
Impairments of goodwill	—	—	—	(6)	(6)
Exchange translations and other movements	3	1	4	—	4
Share of loss for the year after tax	—	—	—	—	—
Balance at 31 December 2008	12	(4)	8	2	10
Exchange translation and other movements	(7)	4	(3)	(1)	(3)
Share of loss for the year after tax	—	—	—	—	(1)
Balance at 31 December 2009	5	—	5	1	6

There have been no changes recognised in the other comprehensive income of associates that would also be recognised in the other comprehensive income by the Prudential Group. Exchange translation and other movements for 2009 mainly related to the investment in IFonline mentioned above.

The Prudential Group's share of the assets, liabilities, revenues and profit and loss of associates accounted for using the equity method at 31 December 2007, 31 December 2008 and 31 December 2009 is as follows:

	2007	2008	2009
	£m	£m	£m
Financial position			
Total assets (excluding goodwill)	7	12	5
Total liabilities	(3)	(4)	—
Net assets	4	8	5
Results of operations			
Revenue	5	3	1
Profit in the year	—	—	—

Associates carried at fair value through profit and loss

The Prudential Group's associates that are carried at fair value through profit and loss comprise investments in OEICs, unit trusts, funds holding collateralised debt obligations, property unit trusts, and venture capital investments of the PAC with-profits fund where the Prudential Group has significant influence. These investments are incorporated both in the UK and overseas, and some have year ends which are non-coterminous with that of the Prudential Group. In these instances, the investments are recorded at fair value at 31 December 2007, 31 December 2008 and 31 December 2009 based on valuations or pricing information at that specific date. The aggregate fair value of associates carried at fair value through profit and loss where there are published price quotations is approximately £2 billion, £4 billion and £6 billion at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

The aggregate assets of these associates are approximately £9 billion, £8 billion and £9 billion in 2007, 2008 and 2009 respectively. Aggregate liabilities, excluding liabilities to unit holders and shareholders for unit trusts and OEICs, are approximately £2 billion, £2 billion and £2 billion, at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Fund revenues, with revenue arising in unit trusts and OEICs deemed to constitute the investment return for these vehicles, were approximately £0.5 billion, £0.8 billion and £0.8 billion at 31 December 2007, 31 December 2008 and 31 December 2009 respectively and in 2007, 2008 and 2009 respectively, excluding unit trusts and OEICs where all investment returns accrue to unit holders or shareholders respectively, were approximately a profit of £0.2 billion, profit of £0.3 billion and a loss of £0.2 billion.

Investments in joint ventures

Joint ventures represent activities over which the Prudential Group exercises joint control through contractual agreement with one or more parties. The Prudential Group's significant joint ventures, which are accounted for using proportionate consolidation, comprise various joint ventures relating to property investments where it has a 50% interest as well as the following interests, which have been held across the three years ended 31 December 2009:

Investment	% held	Principal activity	Country
ICICI Prudential Life Insurance Company Limited	26	Life assurance	India
BOCI — Prudential Asset Management Limited	36	Pensions	China
PruHealth	50	Private medical insurance	UK
CITIC — Prudential Life Insurance Company Limited	50	Life assurance	China
CITIC Prudential Fund Management Company Limited	49	Asset management	China
Prudential ICICI Asset Management Company Limited	49	Asset management	India
Prudential BSN Takaful Berhad	49	General and life insurance	Malaysia

The investments noted in the table above have the same accounting year end as the Prudential Group, except for ICICI Prudential Life Insurance Company Limited and Prudential ICICI Asset Management Company Limited. Although these investments have reporting periods ending 31 March, 12 months of financial information up to 31 December is recorded. Accordingly, the information covers the same period as that of the Prudential Group.

The summarised financial data for the Prudential Group's share of investments in joint ventures is as follows:

	2007	2008	2009
	£m	£m	£m
Financial position			
Current assets	1,277	250	386
Non-current assets	173	1,212	2,462
Total assets	1,450	1,462	2,848
Current liabilities	(115)	(159)	(150)
Non-current liabilities	(1,121)	(1,063)	(2,392)
Total liabilities	(1,236)	(1,222)	(2,542)
Net equity	214	240	306
Results of operations			
Revenues	500	656	974
Expenses	(546)	(649)	(945)
Net profit (loss)	(46)	7	29

There are several minor service agreements in place between the joint ventures and the Prudential Group. During 2007, 2008 and 2009 respectively, the aggregate amount of the transactions were £5.4 million, £15.9 million, and £14.1 million and the balance outstanding as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, was £4.7 million, £22.5 million and £54.6 million.

The joint ventures have no significant contingent liabilities to which the Prudential Group is exposed nor does it have any significant contingent liabilities in relation to its interest in the joint ventures.

H9: Properties held for sale

Investment properties are classified as held for sale when contracts have been exchanged but the sale has not been completed at the period end.

Assets held for sale in 2007 of £30 million comprised investment property of PAC with-profits fund.

There were no assets held for sale at 31 December 2008 and £3 million in assets held for sale at 31 December 2009.

Gains on disposal of held for sale assets are recorded in 'investment income' within the income statement.

H10: Cash and cash equivalents

Cash and cash equivalents consist of cash at bank and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days maturity from the date of acquisition. Cash and cash equivalents included in the cash flow statement comprise the following statement of financial position amounts:

	2007	2008	2009
	£m	£m	£m
Cash	4,528	5,362	5,071
Cash equivalents	423	593	236
Total cash and cash equivalents	4,951	5,955	5,307

Cash and cash equivalents held centrally are considered to be available for general use by the Prudential Group. These funds amount to £394 million, £165 million and £895 million at 31 December 2007, 31 December 2008 and 31 December 2009, respectively. The remaining funds are considered not to be available for general use by the Prudential Group, and include funds held for the benefit of policyholders.

H11: Shareholders' equity: share capital, share premium and reserves

	2007	2008	2009
	£m	£m	£m
Share capital and share premium			
Share capital	123	125	127
Share premium	1,828	1,840	1,843
Reserves			
Retained earnings	4,301	3,604	3,964
Translation reserve	(112)	398	203
Available-for-sale reserve	(78)	(909)	134
Total shareholders' equity	6,062	5,058	6,271

A summary of the ordinary shares in issue is set out below:

Share capital and share premium

	2007		
	Number of Ordinary shares	Share Capital	Share premium
		£m	£m
Issued shares of 5p each fully paid:			
At the beginning of the year	2,444,312,425	122	1,822
Shares issued under share option schemes	803,818	—	6
Shares issued in lieu of cash dividends	24,900,997	1	175
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	—	—	(175)
At end of the year	2,470,017,240	123	1,828

	2008		
Issued shares of 5p each fully paid:			
At the beginning of the year	2,470,017,240	123	1,828
Shares issued under share option schemes	2,307,469	—	12
Shares issued in lieu of cash dividends	24,622,979	2	156
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	—	—	(156)
At end of the year	2,496,947,688	125	1,840

			2009
Issued shares of 5p each fully paid:			
At the beginning of the year	2,496,947,688	125	1,840
Shares issued under share option schemes	605,721	—	13
Shares issued in lieu of cash dividends	34,674,062	2	136
Transfer to retained earnings in respect of shares issued in lieu of cash dividends	—	—	(136)
At end of the year	2,532,227,471	127	1,843

Amounts recorded in share capital represent the nominal value of the shares issued. The difference between the proceeds received on issue of shares, net of issue costs, and the nominal value of shares issued is credited to the share premium account.

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, there were options outstanding under Save As You Earn schemes to subscribe for 9,017,442 shares, 6,825,343 shares and 12,230,833 shares at prices ranging from 266 pence to 695 pence, 266 pence to 617 pence, and 266 pence to 572 pence, exercisable by the year 2014, 2015 and 2016 respectively. In addition at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, there are 2,037,220 conditional options, 967,652 conditional options and 17,292 conditional options outstanding under the RSP and 3,485,617 shares, 4,906,234 shares, and 6,644,203 shares under the GPSP exercisable at nil cost within a 10-year period.

The cost of own shares of £60 million, £75 million and £75 million as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, is deducted from retained earnings. Prudential has established trusts to facilitate the delivery of shares under employee incentive plans and savings-related share option schemes. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, 6.6 million, 6.4 million and 5.3 million Prudential shares with a market value of £47 million, £27 million and £34 million were held in such trusts. Of this total, 5.1 million, 6.0 million and 4.8 million shares were held in trusts under employee incentive plans. In 2007, 2008 and 2009 respectively, Prudential purchased 1.3 million, 5.4 million and 3.4 million shares in respect of employee incentive plans at a cost of £10 million, £27 million and £17 million, respectively.

Of the total shares held in trust at as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, 1.5 million, 0.4 million and 0.5 million shares were held by a qualifying employee share ownership trust. These shares are expected to be fully distributed in the future on maturity of savings-related share option schemes.

The maximum number of shares held in the year was 6.4 million, which was at the beginning of the year.

		Share Price		
2007	**no. of Shares**	**Low**	**High**	**Cost**
		£	**£**	**£**
January	9,975	7.12870	7.12870	71,110
February	9,693	7.18290	7.18790	69,661
March	17,410	6.69790	7.17790	118,318
April	12,239	7.49790	7.49790	91,767
May	25,458	7.75396	8.04200	203,147
June	10,936	7.14819	7.21819	78,456
July	11,021	7.30319	7.30819	80,544
August	598,924	6.99677	7.22819	4,266,196
September	10,435	6.94500	7.02970	73,355
October	587,121	7.66500	7.74000	4,511,614
November	10,451	7.05250	7.06250	73,708
December	11,876	7.13750	7.14375	84,817
2007 Total	1,315,539			9,722,693

2008	no. of Shares	Share Price Low	Share Price High	Cost
		£	£	£
January	8,718	6.69385	6.75385	58,704
February	11,934	5.93975	6.02975	71,469
March	567,163	3.30975	7.69000	3,723,404
April	33,239	6.29500	6.97970	231,210
May	755,425	6.67500	7.05800	5,045,623
June	740,840	6.28000	6.37300	4,652,961
July	245,412	5.16042	5.34000	1,308,962
August	8,317	5.79975	5.83395	48,392
September	211,596	4.83000	5.82500	1,033,080
October	11,247	4.44248	4.77380	53,018
November	15,494	3.57000	3.59540	55,042
December	2,827,057	3.30103	4.00541	11,175,373
2008 Total	5,436,442			27,457,238

2009	no. of Shares	Share Price Low	Share Price High	Cost
		£	£	£
January	19,852	3.82900	3.93583	76,575
February	19,926	3.52000	3.52000	70,140
March	1,112,209	2.02250	3.50122	3,837,968
April	22,164	3.37500	3.37500	74,859
May	32,416	4.45473	6.59000	173,242
June	26,594	4.43750	7.30870	145,230
July	342,062	3.85500	4.02750	1,374,929
August	14,059	4.84700	4.84700	68,144
September	12,435	5.50000	5.50000	68,393
October	10,332	6.33500	6.33500	65,453
November	10,576	6.04000	6.04000	63,879
December	1,739,591	6.05628	6.35000	10,941,847
2009 Total	3,362,216			16,960,659

The Prudential Group has consolidated a number of authorised investment funds where it is deemed to control these funds under IFRS. Some of these funds hold shares in Prudential. The total number of shares held by these funds as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively was 4.1 million, 9.2 million, and 10.6 million and the cost of acquiring these shares of £22 million, £47 million and £51 million, respectively, is included in the cost of own shares.

During 2007, 2008 and 2009 respectively, these funds made 772,896 net disposals, 5,060,985 net acquisitions and 1,414,263 net acquisitions of Prudential plc shares for a net decrease of £4 million, net increase of £26 million and a net increase of £3 million to book cost.

The market value of these shares as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively was £29 million, £37 million and £67 million.

All share transactions were made on an exchange other than the Stock Exchange of Hong Kong.

Reserves

The translation reserve represents cumulative foreign exchange translation differences taken directly to equity in accordance with IFRS, net of related tax. In accordance with IFRS 1, cumulative translation differences are deemed to be zero at 1 January 2004, the date of transition to IFRS.

The available-for-sale reserve represents gains or losses arising from changes in the fair value of available-for-sale securities of Jackson, net of the related change in amortisation of deferred income and acquisition costs and of the related tax.

Parent company profits and distributability of reserves

Under English company law, Prudential may pay dividends only if "distributable reserves" of the holding company are available for the purpose. The holding company prepares its own financial information in accordance with UK GAAP.

Even if distributable reserves are available, under English law Prudential may pay dividends only if the amount of its net assets is greater than the aggregate of its called up share capital and undistributable reserves (such as for example the share premium account) and the payment of the dividend does not reduce the amount of its net assets to less than that aggregate. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the UK GAAP retained earnings of the holding company from which distributable reserves may be derived, were £1,185 million, £1,280 million and £1,856 million.

H12: Insurance contract liabilities and unallocated surplus of with-profits funds

Movement in year

	Insurance contract liabilities	Unallocated surplus of with-profits funds
	£m	£m
At 1 January 2007	123,339	13,425
Income and expense included in the income statement	9,604	541
Foreign exchange translation differences	(167)	(7)
At 31 December 2007	132,776	13,959
At 1 January 2008	132,776	13,959
Income and expense included in the income statement	(12,760)	(5,815)
Foreign exchange translation differences	16,014	270
At 31 December 2008	136,030	8,414
At 1 January 2009	136,030	8,414
Income and expense included in the income statement	19,765	1,559
Foreign exchange translation differences	(6,574)	46
Disposal of Taiwan agency business	(3,508)	—
At 31 December 2009	145,713	10,019

Notes B6, D2b, D3b and D4b provide further analysis of the movement in the year of the Group's policyholder liabilities and unallocated surplus of the with-profits funds.

H13: Borrowings

Core structural borrowings of shareholder-financed operations

As at 31 December:

	2007			
	Innovative Tier 1*	Lower Tier 2*	Senior‡	Total
		£m		
Parent company				
Subordinated debt:				
€500m 5.75% Subordinated Notes 2021(note i)	—	365	—	365
€20m Medium-Term Subordinated Notes 2023(note ii)	—	15	—	15
£435m 6.125% Subordinated Notes 2031	—	427	—	427
US$1,000m 6.5% Perpetual Subordinated Capital Securities(note iii)	485	—	—	485
US$250m 6.75% Perpetual Subordinated Capital Securities(note iv)	124	—	—	124
US$300m 6.5% Perpetual Subordinated Capital Securities(note iv)	154	—	—	154
	763	807	—	1,570
Senior debt:				
£249m 5.5% Bonds 2009(note v)	—	—	248	248
£300m 6.875% Bonds 2023	—	—	300	300
£250m 5.875% Bonds 2029	—	—	249	249
	—	—	797	797
Total parent company(note x)	763	807	797	2,367
Jackson				
US$250m 8.15% Surplus Notes 2027(note vi)	—	125	—	125
Total(note vii)	763	932	797	2,492

	2008			
	Innovative Tier 1*	Lower Tier 2*	Senior‡	Total
	£m			
Parent company				
Subordinated debt:				
€500m 5.75% Subordinated Notes 2021(note i)	—	482	—	482
€20m Medium-Term Subordinated Notes 2023(note ii)	—	19	—	19
£435m 6.125% Subordinated Notes 2031	—	427	—	427
US$1,000m 6.5% Perpetual Subordinated Capital Securities(note iii)	696	—	—	696
US$250m 6.75% Perpetual Subordinated Capital Securities(note iv)	173	—	—	173
US$300m 6.5% Perpetual Subordinated Capital Securities(note iv)	190	—	—	190
	1,059	928	—	1,987
Senior debt:				
£249m 5.5% Bonds 2009(note v)	—	—	249	249
£300m 6.875% Bonds 2023	—	—	300	300
£250m 5.875% Bonds 2029	—	—	249	249
	—	—	798	798
Total parent company(note x)	1,059	928	798	2,785
Jackson				
US$250m 8.15% Surplus Notes 2027(note vi)	—	173	—	173
Total(notes vii,viii)	1,059	1,101	798	2,958

	2009			
	Innovative Tier 1*	Lower Tier 2*	Senior‡	Total
	£m			
Parent company				
Subordinated debt:				
€500m 5.75% Subordinated Notes 2021(note i)	—	443	—	443
€20m Medium-Term Subordinated Notes 2023(note ii)	—	18	—	18
£435m 6.125% Subordinated Notes 2031	—	428	—	428
£400m 11.375% Subordinated Notes 2039(note v)	—	380	—	380
US$1,000m 6.5% Perpetual Subordinated Capital Securities(note iii)	619	—	—	619
US$250m 6.75% Perpetual Subordinated Capital Securities(note iv)	155	—	—	155
US$300m 6.5% Perpetual Subordinated Capital Securities(note iv)	192	—	—	192
US$750m 11.75% Perpetual Subordinated Capital Securities(note ix)	456	—	—	456
	1,422	1,269	—	2,691
Senior debt:				
£300m 6.875% Bonds 2023	—	—	300	300
£250m 5.875% Bonds 2029	—	—	249	249
	—	—	549	549
Total parent company(note x)	1,422	1,269	549	3,240
Jackson				
US$250m 8.15% Surplus Notes 2027(note vi)	—	154	—	154
Total(notes vii, viii)	1,422	1,423	549	3,394

* These debt classifications are consistent with the treatment of capital for regulatory purposes, as defined in the FSA Handbook.

‡ The senior debt ranks above subordinated debt in the event of liquidation.

Notes

i The €500 million 5.75% borrowings have been swapped into borrowings of £333 million with interest payable at six month £LIBOR plus 0.962%.

ii The €20 million borrowings were issued at 20-year Euro Constant Maturity Swap (capped at 6.5%). These have been swapped into borrowings of £14 million with interest payable at three month £LIBOR plus 1.2%.

iii Interest on the US$1,000 million 6.5% borrowings was swapped into floating rate payments at three month US$LIBOR plus 0.80%. In January 2009, this swap was cancelled.

iv The US$250 million 6.75% borrowings and the US$300 million 6.5% borrowings can be converted, in whole or in part, at Prudential's option and subject to certain conditions, on any interest payment date falling on or after 23 March 2010 and 23 March 2011 respectively, into one or more series of Prudential preference shares.

v The £249 million 5.5% borrowings were repaid on maturity in May 2009. In the same month Prudential issued £400 million subordinated debt in part to replace the maturing debt.

vi The Jackson borrowings are unsecured and subordinated to all present and future indebtedness, policy claims and other creditor claims of Jackson.

vii Maturity analysis

The following table sets out the contractual maturity analysis of the Prudential Group's core structural borrowings as at 31 December:

	2007	2008	2009
	£m	£m	£m
Less than 1 year	—	249	—
1 to 2 years	248	—	—
2 to 3 years	—	—	—
3 to 4 years	—	—	—
4 to 5 years	—	—	—
Over 5 years	2,244	2,709	3,394
Total	2,492	2,958	3,394

Operational borrowings attributable to shareholder-financed operations

viii Management analyses the net core structural borrowings position as follows:

	2008 £m	2009 £m
Total core structural borrowings (as above)	2,958	3,394
Less: Holding company cash and short-term investments (recorded within the consolidated statement of financial position)	(1,165)	(1,486)
Net core structural borrowings of shareholder-financed operations	1,793	1,908

ix In July 2009, Prudential issued US$750 million perpetual subordinated capital securities.

x The total parent company's core structural borrowings as shown in the tables above represent the amounts in the context of the Prudential Group consolidated level. These amounts differ from the amounts included in the parent company's own financial information due to different dates of commencement of fair value hedge accounting on the US$300 million 6.5% borrowing.

	2007 £m	2008 £m	2009 £m
Borrowings in respect of short-term fixed income securities programmes			
Commercial paper	2,422	1,269	2,031
Medium-Term Notes 2008	48	—	—
Medium-Term Notes 2010	7	9	7
	2,477	1,278	2,038
Non-recourse borrowings of US operations(note i)			
Jackson(note ii)	126	104	—
Investment subsidiaries	9	23	20
Piedmont and CDO funds(note iii)	456	384	183
	591	511	203
Other borrowings			
Bank loans and overdrafts(note iv)	6	185	148
Obligations under finance leases	7	3	3
Other borrowings(note v)	—	—	359
	13	188	510
Total(notes vi, vii)	3,081	1,977	2,751

Notes

i In all instances the holders of the debt instruments issued by these subsidiaries and funds do not have recourse beyond the assets of those subsidiaries and funds.

ii This represents senior debt issued through the Federal Home Loan Bank of Indianapolis and is secured on collateral posted with FHLB by Jackson.

iii Piedmont is an investment trust investing in certain asset-backed and mortgage-backed securities in the US. These borrowings pertain to debt instruments issued to external parties.

iv Bank loans and overdrafts include a short-term loan of nil, £130 million and £130 million in respect of Asian operations as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

v Other borrowings represents amounts whose repayment to the lender is contingent on future surpluses emerging from certain contracts specified under the arrangement. If insufficient surplus emerges on contracts, there is no recourse to other assets of the Group and the liability is not payable to the degree of the shortfall.

vi In addition to the operational borrowings shown in the table above, Prudential plc has issued £200 million Floating Rate Notes 2010, which were wholly subscribed to by a Group subsidiary. These borrowings have been eliminated on consolidation.

vii Maturity analysis

The following table sets out the contractual maturity analysis of the Group's operational borrowings attributable to shareholder-financed operations:

	2007 £m	2008 £m	2009 £m
Less than 1 year	2,618	1,584	2,183
1 to 2 years	—	9	121
2 to 3 years	7	38	239
3 to 4 years	44	52	172
4 to 5 years	54	240	6
Over 5 years	358	54	30
Total	3,081	1,977	2,751

Borrowings attributable to with-profits operations

As at 31 December:

	2007 £m	2008 £m	2009 £m
Non-recourse borrowings of consolidated investment funds(note i)	789	1,161	1,016
£100m 8.5% Undated Subordinated Guaranteed Bonds of Scottish Amicable Finance plc(note ii)	100	100	100
Other borrowings (predominantly obligations under finance leases)	98	47	168
Total(note iii)	987	1,308	1,284

Notes

i In all instances the holders of the debt instruments issued by these funds do not have recourse beyond the assets of those funds.

ii The interests of the holders of the bonds issued by Scottish Amicable Finance plc, a subsidiary of the Scottish Amicable Life Insurance Fund, are subordinate to the entitlements of the policyholders of that fund.

iii Maturity analysis

The following table sets out the contractual maturity analysis of the Group's borrowings attributable to with-profits operations as at 31 December:

	2007 £m	2008 £m	2009 £m
Less than 1 year	103	272	33
1 to 2 years	16	12	77
2 to 3 years	62	150	706
3 to 4 years	—	418	1
4 to 5 years	154	—	1
Over 5 years	652	456	466
Total	987	1,308	1,284

H14: Provisions and contingencies

Provisions

As at 31 December:

	2007 £m	2008 £m	2009 £m
Provision in respect of defined benefit pension schemes: (I2)			
Deficit, gross of deferred tax, based on scheme assets held, including investments in Prudential insurance policies:			
Attributable to PAC with-profits fund (i.e. absorbed by the liability for unallocated surplus)	98	67	122
Attributable to shareholder-financed operations (i.e. to shareholders' equity)	85	82	128
	183	149	250
Add back: Investments in Prudential insurance policies	172	157	187
Provision after elimination of investments in Prudential insurance policies and matching policyholder liability from Group statement of financial position	355	306	437
Other provisions (see below)	220	155	206
Total provisions	575	461	643

Analysis of other provisions:

	2007 £m	2008 £m	2009 £m
At 1 January	238	220	155
Charged to income statement:			
Additional provisions	116	48	148
Unused amounts released	(23)	(24)	(13)
Used during the year	(112)	(101)	(75)
Exchange differences	1	12	(9)
At 31 December	220	155	206
Comprising:			
Legal provisions	19	23	15
Restructuring provisions	35	21	17
Other provisions	166	111	174
Total	220	155	206

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of the other provisions balance of £220 million, £155 million and £206 million, settlement of £77 million, £90 million and £148 millions expected to be made within one year. Employer contributions expected to be paid into defined benefit pension schemes within one year are shown in note I2.

Legal provisions

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the legal provisions of £19 million, £23 million and £15 million relate predominantly to Jackson. Jackson has been named in civil proceedings, which appear to be substantially similar to other class action litigation brought against many life insurers in the US, alleging misconduct in the sale of insurance products. During 2007, 2008 and 2009 respectively, £nil, £2 million and £9 million was paid.

Restructuring provisions

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, restructuring provisions of £35 million, £21 million and £17 million relate to restructuring activities of UK insurance operations.

In 2004 and 2005, UK insurance operations implemented restructurings relating to document management review, streamlining operations, and the relocation of activities to an offshore base in India. In December 2005, the Prudential Group announced an initiative for UK insurance operations to work more closely with M&G and in the process facilitate the realisation of substantial annualised pre-tax cost savings and opportunities for revenue synergies.

At 1 January 2007, a provision of £72 million was brought forward, and during 2007 an additional £21 million was provided, £14 million of unused provision was released, and £44 million was paid.

At 1 January 2008, a provision of £35 million was brought forward, and during 2008 an additional £4 million was provided, £7 million of unused provision was released, and £11 million was paid.

During 2009, £1 million of unused provision was released, and £3 million was paid.

Other provisions

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, other provisions of £166 million, £111 million and £174 million include provisions of £155 million, £95 million and £143 million relating to staff benefit schemes. In 2007, a provision of £134 million was brought forward, and additional £78 million was provided, £3 million of unused provision was released and £54 million was paid. In 2008, £155 million was brought forward, £37 million was provided and £15 million was released and £82 million was paid. In 2009, a provision of £95 million was brought forward, an additional £112 million was provided, £10 million of unused provision was released and £54 million was paid. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, other provisions also include £11 million, £16 million and £27 million relating to various onerous contracts where, in 2007 an additional £2 million was provided, £1 million was released and £8 million used, in 2008 an additional £10 million was provided and £5 million used and in 2009 an additional £15 million was provided and £4 million was used

Contingencies and related obligations

Litigation

In addition to the legal proceedings relating to Jackson mentioned above, the Prudential Group is involved in other litigation and regulatory issues and these legal proceedings are discussed in more detail in the section headed "Business — Legal and Regulatory Proceedings". Whilst the outcome of such matters cannot be predicted with certainty, Prudential believes that the ultimate outcome of such litigation and regulatory issues will not have a material adverse effect on the Prudential Group's financial condition, results of operations, or cash flows.

Pension mis-selling review

In 1988, the UK government introduced new pensions legislation intended to encourage more individuals to make their own arrangements for their pensions. During the period from April 1988 to June 1994, many individuals were advised by insurance companies, Independent Financial Advisers and other intermediaries to not join, to transfer from or to opt out of their occupational pension schemes in favour of private pension products introduced under the UK Income and Corporation Taxes Act 1988. The UK insurance regulator (previously the Personal Investment Authority, now the FSA), subsequently determined that many individuals were incorrectly advised and would have been better off not purchasing the private pension products sold to them. Industry participants are responsible for compensating the persons to whom private pensions were mis-sold. As a result, the FSA required that all UK life insurance companies review their potential cases of pension mis-selling and pay compensation to policyholders where necessary and, as a consequence, record a provision for the estimated costs. The Prudential Group met the requirement of the FSA to issue offers to all cases by 30 June 2002.

The table below summarises the change in the pension mis-selling provision for the years ended 31 December 2007, 31 December 2008 and 31 December 2009. The change in the provision is included in benefits and claims in the income statement and the movement in unallocated surplus of with-profits funds has been determined accordingly.

	2007	2008	2009
	£m	£m	£m
Balance at beginning of year	401	448	345
Changes to actuarial assumptions and method of calculation	71	(75)	20
Discount unwind	22	20	3
Redress to policyholders	(41)	(46)	(44)
Payment of administrative costs	(5)	(2)	(2)
Balance at end of year	448	345	322

The pension mis-selling provision is included within the liabilities in respect of investment contracts with discretionary participation features under IFRS 4.

The pension mis-selling provision at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, set out above of £448 million, £345 million and £322 million is stochastically determined on a discounted basis. The average discount rate implied in the movement in 2007, 2008 and 2009 respectively, is 4.6%, 4.0% and 4.6%. The undiscounted amounts at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, expected to be paid each of the years ending 31 December are as follows:

	2007	2008	2009
	£m	£m	£m
Year ended 31 December			
2008	51	—	—
2009	15	17	—
2010	15	8	29
2011	15	9	8
2012	22	13	11
2013	—	12	12
2014	—	—	15
Thereafter	707	572	513
Total undiscounted amount	825	631	588
Aggregate discount	(377)	(286)	(266)
Discounted pension mis-selling provision at 31 December 2007, 31 December 2008 and 31 December 2009, respectively	448	345	322

The liability accounting for the contracts which are the subject of the mis-selling provision is reflected in two elements, namely the core policyholder liability determined on the basis applied for other contract liabilities and the mis-selling provision. The overall liability for these contracts remains appropriate in the context of the accounting for policyholder liabilities that determines the calculation of both elements. However, the constituent elements are reallocated and remeasured for the changes arising from the application of the realistic Peak 2 basis of liabilities for the core policyholder liability, as reflected in the IFRS policy improvement to apply the UK GAAP standard FRS 27 as described in section A4.

The Financial Ombudsman Service periodically updates the actuarial assumptions to be used in calculating the compensation payments, including interest rates and mortality assumptions. The pension mis-selling provision represents the discounted value of future expected payments, including benefit payments and all internal and external legal and administrative costs of adjudicating, processing and settling those claims. To the extent that amounts have not been paid, the provision increases each year reflecting the shorter period of discount.

The directors believe that, based on current information, the provision, together with future investment return on the assets backing the provision, will be adequate to cover the costs of pension mis-selling as well as the costs and expenses of the Prudential Group's pension review unit established to identify and settle such cases. Such provision represents the best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

The costs associated with the pension mis-selling review have been met from the inherited estate (see below). Accordingly, these costs have not been charged to the asset shares used in the determination of policyholder bonus rates. Hence policyholders' pay-out values have been unaffected by pension mis-selling.

In 1998, Prudential stated that deducting mis-selling costs from the inherited estate would not impact its bonus or investment policy and it gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged. The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing.

This review was completed on 30 June 2002. The assurance will continue to apply to any policy in-force at 31 December 2003, both for premiums paid before 1 January 2004, and for subsequent regular premiums (including future fixed, RPI or salary related increases and Department of Work and Pensions rebate business). The assurance has not applied to new business since 1 January 2004. New business in this context consists of new policies, new members to existing pension schemes plus regular and single premium top-ups, transfers and switches to existing arrangements. The maximum amount of capital support available under the terms of the assurance will reduce over time.

The bonus and investment policy for each type of with-profits policy is the same irrespective of whether or not the assurance applies and this is expected to continue for the foreseeable future. Hence removal of the assurance for new business has had no impact on policyholder returns.

Mortgage endowment products review

In common with several other UK insurance companies, the Prudential Group used to sell low-cost endowment products related to repayment of residential mortgages. At sale, the initial sum assured is set at a level such that the projected benefits, including an estimate of the annual bonus receivable over the life of the policy, will equal or exceed the mortgage debt. Because of a decrease in expected future investment returns since these products were sold, the FSA is concerned that the maturity value of some of these products will be less than the mortgage debt. The FSA has worked with insurance companies to devise a programme whereby the companies write to customers indicating whether they may have a possible shortfall and outline the actions that the customers can take to prevent this possibility.

The Prudential Group is exposed to mortgage endowment products in respect of policies issued by Scottish Amicable Life plc ("SAL") and policies issued by Scottish Amicable Life Assurance Society (SALAS) which were transferred into SAIF. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, provisions of £5 million, £5 million and £4 million in SAL and £43 million, £40 million and £35 million in SAIF were held within policyholder liabilities to cover potential compensation in respect of mortgage endowment product mis-selling claims. As SAIF is a separate sub-fund of the Prudential Assurance long-term business fund, this provision has no impact on shareholders.

In addition, in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, Prudential Assurance's main with-profits fund paid compensation of £5 million, £1 million and £2 million in respect of mortgage endowment products mis-selling claims and at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, held a provision of £55 million, £54 million and £47 million in respect of further compensation. The movement in this provision has no impact on the Prudential Group's profit before tax.

In May 2006, the Prudential Group introduced a deadline for both Prudential and Scottish Amicable Life mortgage endowment complaints. Impacted customers have three years to lodge a mis-selling complaint in line with the time limit prescribed by the FSA and the ABI.

Guaranteed annuities

PAC used to sell guaranteed annuity products in the UK and at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, held a provision of £45 million, £42 million and £31 million within the main with-profits fund within policyholder liabilities to honour guarantees on these products. The Group's main exposure to guaranteed annuities in the UK is through SAIF and at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, a provision of £563 million, £391 million and £284 million was held in SAIF to honour the guarantees. As SAIF is a separate sub-fund of the PAC long-term business fund, the movement in this provision has no impact on shareholders.

Other matters

Inherited estate of the PAC long-term fund

The assets of the with-profits sub-fund (WPSF) within the long-term fund of PAC comprise the amounts that it expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the WPSF is equal to the policyholders' accumulated asset shares plus any additional payments that may be required by way of smoothing or to meet guarantees. The balance of the assets of the WPSF is called the 'inherited estate' and has accumulated over many years from various sources.

The inherited estate, as working capital, enables PAC to support with-profits business by providing the benefits associated with smoothing and guarantees, by providing investment flexibility for the fund's assets, by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of certain significant events or fundamental changes in its long-term business without affecting the bonus and investment policies. The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

Support for long-term business funds by shareholders' funds

As a proprietary insurance company, PAC is liable to meet its obligations to policyholders even if the assets of the long-term funds are insufficient to do so. The assets, represented by the unallocated surplus of with-profits funds, in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers ('the excess assets') in the long-term funds could be materially depleted over time by, for example, a significant or sustained equity market downturn, costs of significant fundamental strategic change or a material increase in the pension mis-selling provision. In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the Prudential Group's ability to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

In 1997, the business of SALAS, a mutual society, was transferred to PAC. In effecting the transfer, a separate sub-fund, SAIF, was established within PAC's long-term business fund. This sub-fund contains all the with-profits business and all other pension business that was transferred. No new business has been or will be written in the sub-fund and the sub-fund is managed to ensure that all the invested assets are distributed to SAIF policyholders over the lifetime of SAIF policies. With the exception of certain amounts in respect of the unitised with-profits life business, all future earnings arising in SAIF are retained for SAIF policyholders. Any excess (deficiency) of revenue over expense within SAIF during a period is offset by a transfer to (from) the SAIF unallocated surplus. Shareholders have no interest in the profits of SAIF but are entitled to the asset management fees paid on this business. With the exception of certain guaranteed annuity products mentioned earlier in this note, and certain products which include a minimum guaranteed rate of accumulation, the majority of SAIF with-profits policies do not guarantee minimum rates of return to policyholders.

Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations to the policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency. Due to the quality and diversity of the assets in SAIF and the ability of SAIF to revise guaranteed benefits in the event of an asset shortfall, the directors believe that the probability of either the PAC long-term fund or the Prudential Group's shareholders' funds having to contribute to SAIF is remote.

Guarantees and commitments

Guarantee funds in both the UK and the US provide for payments to be made to policyholders on behalf of insolvent life insurance companies. These guarantee funds are financed by payments assessed on solvent insurance companies based on location, volume and types of business. The Prudential Group estimated its reserve for future guarantee fund assessments for Jackson, included within other liabilities to be £9 million, £18 million and £15 million at 31 December 2007, 31 December 2008 and 31 December 2009 respectively. Similar assessments for the UK businesses were not significant. The Directors believe that the reserve is adequate for all anticipated payments for known insolvencies.

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, Jackson has unfunded commitments of £181 million, £400 million and £339 million related to its investments in limited partnerships and £104 million, £24 million and £89 million related to commercial mortgage loans. These commitments were entered into in the normal course of business and the directors do not expect a material adverse impact on the operations to arise from them.

Jackson owns debt instruments issued by securitisation trusts managed by PPM America. At 31 December 2009, the support provided by certain forebearance agreements Jackson entered into with the counterparty to certain of these trusts could potentially expose Jackson to maximum losses of US$750 million if circumstances allowed the forbearance period to cease. Jackson believes that, so long as the forbearance period continues, the risk of loss under the agreements is remote.

The Prudential Group has provided other guarantees and commitments to third-parties entered into in the normal course of business but the Prudential does not consider that the amounts involved are significant.

H15: Other liabilities

	2007	2008	2009
	£m	£m	£m
Creditors arising from direct insurance and reinsurance operations	538	552	615
Interest payable	76	139	83
Other items	177	199	179
Total	791	890	877

I: OTHER NOTES

I1: Sale of legacy agency book and agency force in Taiwan to China Life Insurance of Taiwan

On 20 February 2009, Prudential announced that it had entered into an agreement to sell the assets and liabilities of its agency distribution business and its agency force in Taiwan to China Life Insurance Company Ltd of Taiwan for the nominal sum of NT$1 subject to regulatory approval. In addition, Prudential would invest £45 million to purchase a 9.99% stake in China Life through a share placement. The business transferred represented 94% of Prudential's in-force liabilities in Taiwan and included Prudential's legacy interest rate guaranteed products with IFRS basis gross assets at 31 December 2008 of £4.5 billion. After taking account of IFRS shareholders' equity of the business at 31 December 2008, provisions for restructuring costs, and other costs the Prudential Group's IFRS shareholders' equity at 31 December 2008 was expected to decrease by approximately £595 million.

Prudential retains its interest in life insurance business in Taiwan through its retained bank distribution partnerships and its direct investment of 9.99% in China Life.

The sale was completed, following regulatory approval, on 19 June 2009. The trading results shown below are for the period 1 January to 19 June 2009.

The carrying value of the IFRS equity of the business, as applied in the calculation of the loss on sale, reflects the application of 'grandfathered' US GAAP under IFRS 4 of insurance assets and liabilities. US GAAP does not, and is not designed to, include the cost of holding economic capital to support the legacy interest rate guaranteed products as recognised under Prudential's supplementary reporting basis under European Embedded Value principles. The IFRS loss on sale reflects this missing element of the economic value. The effects on the IFRS income statement and equity attributable to shareholders is shown below.

The loss on sale and trading results of the Taiwan agency business for the period of ownership comprise:

	2007	2008	2009
	£m	£m	£m
Loss on sale:			
As estimated and announced on 20 February 2009:			
Proceeds	—	—	—
Net asset value attributable to equity holders of Prudential and provision for restructuring costs	—	—	(551)
Goodwill written off	—	—	(44)
	—	—	(595)
Trading losses to completion, net of tax, as shown below	—	—	44
Minority interests and other adjustments	—	—	(8)
Loss on sale of the Taiwan agency business, gross and net of tax (as shown in income statement)	—	—	(559)
Trading results before tax (including short-term fluctuations in investment returns)	(37)	1	(62)
Related tax	(23)	(4)	18
Total	(60)	(3)	(44)
Loss on sale and trading results of the Taiwan agency business:			
—Gross of tax	(37)	1	(621)
—Tax	(23)	(4)	18
—Net of tax	(60)	(3)	(603)
Attributable to:			
Equity holders of Prudential	(60)	(3)	(598)
Minority interests	—	—	(5)
Loss on sale and results of the Taiwan agency business, net of tax	(60)	(3)	(603)

The loss on disposal in 2009 of £559 million includes cumulative foreign exchange gains of £9 million recycled through the profit and loss account as required by IAS 21. The impact on shareholders' funds of the disposal (including trading losses up to the date of disposal) is £607 million. The difference of £12 million from the estimate of £595 million reflects a number of minor adjustments.

Cash and cash equivalents included in the net assets disposed of were £388 million and restructuring and other costs incurred in cash in the year were £64 million. In addition, Prudential invested £45 million in China Life as described above. Accordingly, the cash outflow for the Prudential Group arising from the sale of the Taiwan agency business, as shown in the summary consolidated statement of cash flows, was £497 million.

In order to facilitate comparisons of the Prudential Group's retained businesses, the presentation of the segmental analysis of IFRS loss before shareholder tax (as shown in note B1) has been adjusted to show separately the result for the sold Taiwan agency business, as explained below.

	2007			2008		
	As previously published	Adjustment	Adjusted	As previously published	Adjustment	Adjusted
	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	1,201	(49)	1,152	1,347	(64)	1,283
Short-term fluctuations in investment returns	(137)	86	(51)	(1,783)	62	(1,721)
Shareholders' share of actuarial gains and losses on defined benefit pension schemes	(1)	—	(1)	(14)	1	(13)
Results of sold Taiwan agency business	Included above	(37)	(37)	Included above	1	1
Profit/(loss) before tax	1,063	—	1,063	(450)	—	(450)

I2: Staff and pension plans

a Staff and employment costs

The average number of staff employed by the Group during the year were:

	2007	2008	2009
Business operations:			
UK operations	7,732	6,231	4,516
US operations	3,123	3,298	3,371
Asian operations	16,807	20,154	19,502
Venture fund investment subsidiaries of the PAC with-profit fund	21,184	—	—
Total for continuing operations	48,846	29,683	27,389
Discontinued banking operations	770	—	—
Total	49,616	29,683	27,389

The costs of employment were:

	2007	2008	2009
	£m	£m	£m
Business operations:			
Wages and salaries	819	791	878
Social security costs	62	54	61
Other pension costs (see below)	96	78	95
Pension actuarial and other (gains) losses charged to income statement	2	(10)	138
Venture fund investment subsidiaries of the PAC with-profits fund (see below)	423	—	—
Total for continuing operations	1,402	913	1,172
Discontinued banking operations	21	—	—
Total	1,423	913	1,172

For the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, other pension costs comprises £68 million, £47 million and £57 million relating to defined benefit schemes and £28 million, £31 million, and £38 million relating to defined contribution schemes of continuing operations. For the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of the defined contribution scheme costs, £19 million, £21 million and £27 million related to overseas defined contribution schemes. For 2007, 2008 and 2009 respectively, the £68 million,

£47 million and £57 million comprises a charge of £41 million, £29 million and £29 million relating to PSPS and a charge of £27 million, £18 million and £28 million for other schemes.

Consistent with the derecognition of Prudential's interest in the underlying IAS 19 surplus of PSPS as described in note (b)(i)1 below, £41 million, £29 million and £29 million, for 2007, 2008 and 2009 respectively, for PSPS represents the cash cost of contributions for ongoing service of active members and the unwind of discount on the opening provision for deficit funding for PSPS. The charge of £27 million, £18 million and £28 million, for 2007, 2008 and 2009 respectively, for other schemes comprises a £17 million, £7 million and £19 million, charge on an economic basis, reflecting the total assets of the schemes, and a further £10 million, £11 million and £9 million charge to adjust for amounts invested in Prudential insurance policies to arrive at the IAS 19 basis charge.

For 2007, 2008 and 2009 respectively, the loss of £2 million, gain of £10 million and loss of £138 million for actuarial and other gains comprises a loss of £7 million, a loss of £21 million and a loss of £155 million for actuarial and other losses on an economic basis and an actuarial gain of £5 million, gain of £31 million, and a gain of £17 million to adjust for amounts invested in Prudential insurance policies. The derivation of these amounts is shown in note (b)(i)7 below.

b Pension plans

i Defined benefit plans

1 Summary

The Prudential Group's business operations operate a number of pension schemes. The specific features of these plans vary in accordance with the regulations of the country in which the employees are located, although they are, in general, funded wholly by the Prudential Group and based either on a cash balance formula or on years of service and salary earned in the last year or years of employment. The largest defined benefit scheme is the principal UK scheme, namely the Prudential Staff Pension Scheme ("PSPS"), with 87%, 87% and 86% (2007, 2008 and 2009 respectively) of the underlying scheme liabilities of the Group defined benefit schemes accounted for within PSPS.

The Prudential Group also operates two smaller defined benefit schemes for UK employees in respect of Scottish Amicable Life and M&G. For all three schemes the projected unit method was used for the most recent full actuarial valuations. There is also a small defined benefit scheme in Taiwan but as part of the sale of the Taiwan agency business completed in June 2009, the Prudential Group settled the majority of the obligations under the scheme as a significant number of employees transferred out.

Defined benefit schemes in the UK are required to be subject to full actuarial valuation every three years in order to assess the appropriate level of funding for schemes in relation to their commitments. These valuations include assessments of the likely rate of return on the assets held within the separate trustee administered funds. PSPS was last actuarially valued as at 5 April 2008. This valuation demonstrated the scheme to be 106% funded by reference to the Scheme Solvency Target that forms the basis of the scheme's statutory funding objective. Accordingly, the total contributions to be made by the Prudential Group into the scheme were reduced from the previous arrangement of £70-£75 million per annum to £50 million per annum effective from 1 July 2009. As the scheme was in a surplus position at the valuation date, no formal deficit funding plan was required. However, recognising that there had been significant deterioration in the value of the scheme assets since 5 April 2008 to the date of the finalisation of the valuation, contributions to the scheme for additional funding of £25 million per annum, as well as the £25 million per annum employer's contributions for ongoing service of current employees, was agreed with the Trustees subject to a reassessment when the next valuation is completed. The additional funding is akin to deficit funding. Deficit funding for PSPS is apportioned in the ratio of 70/30 between the PAC life fund and shareholder-backed operations following detailed consideration in 2005 of the sourcing of previous contributions. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity. In 2007, 2008 and 2009 respectively, total contributions for the year including expenses and augmentations were £82 million, £79 million and £67 million.

The valuation of the Scottish Amicable Pension Scheme as at 31 March 2008 demonstrated the scheme to be 91% funded, with a shortfall of actuarially determined liabilities of 9%, representing a deficit of £38 million. Based on this valuation, deficit funding amounts designed to eliminate the actuarial deficit over a seven year period were made from July 2009 of £7.3 million per annum. The IAS19 deficit of the Scottish Amicable Pension Scheme of £54 million, £44 million and £139 million, for 2007, 2008 and 2009 respectively, has been allocated 50% to the PAC with-profits fund and 50% to the PAC shareholders fund.

Subsequent to the year end, the valuation of the M&G Pension Scheme as at 31 December 2008 was finalised in January 2010. The valuation demonstrated the scheme to be 76% funded, with a shortfall of actuarially determined assets to liabilities of £51 million. Based on this valuation, deficit funding amounts designed to eliminate the actuarial deficit over a five year period will be made from January 2010 of £14.1 million per annum for the first two years and £9.3 million per annum for the subsequent three years. The IAS 19 deficit of M&G pension scheme on an economic basis of £17 million, £23 million and £36 million at 31 December 2007, 2008 and 2009 respectively, is wholly attributable to shareholders.

Under the IAS 19 valuation basis, the Prudential Group adopted IFRIC 14, "IAS 19 — The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" in 2008 (and effective for year ended 31 December 2007). Under IFRIC 14, on an economic basis the Prudential Group has not recognised the underlying PSPS surplus of £528 million, £728 million and £513 million, for 2007, 2008 and 2009 respectively, gross of deferred tax due to the Prudential Group not having an unconditional right of refund to any surplus in the scheme. Additionally, under IFRIC 14, the Prudential Group has also recognised a liability for committed deficit funding obligation in PSPS. Although the contributions would increase the surplus in the scheme, the corresponding asset will not be recognised in the Prudential Group accounts. At 31 December 2007 and 31 December 2008 the Prudential Group had recognised a liability for deficit funding for PSPS of £55 million and £65 million gross of deferred tax respectively based on the previous deficit funding commitment to 5 April 2010. At 31 December 2009, based on the new funding arrangement as described above, the Prudential Group has recognised a liability for deficit funding to 30 June 2012 for PSPS of £75 million gross of deferred tax. The asset and liabilities of PSPS are unaffected by the impact of the application of IFRIC 14. PSPS is managed on an economic basis for the longer-term benefit of its current and deferred pensioners and active members. The surplus in PSPS is available to absorb future adverse asset value movements and, if required, strengthening in mortality assumptions.

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, after the effect of the application of IFRIC 14, the shareholders' share of the pension liability for PSPS deficit funding obligation and the deficits of the defined benefit pension schemes amounted to a £63 million, £61 million and £92 million liability net of related tax relief. These amounts are determined after including amounts invested by the M&G scheme in Prudential policies as explained later in this note.

On the economic basis (including investments of the M&G scheme in Prudential policies as assets), for 2007, 2008 and 2009 respectively, a £35 million, £26 million and £32 million pre-tax shareholder charge to operating results based on longer-term returns arises. In addition, outside the operating result but included in total profits is a pre-tax shareholder loss of £1 million, £14 million and £74 million for shareholders' share of actuarial and other gains and losses for 2007, 2008 and 2009 respectively.

In addition for 2007, 2008 and 2009 respectively, also on the economic basis, the PAC with-profits sub-fund was charged £23 million, £10 million and £16 million for its share of the pension charge of PSPS and Scottish Amicable Life and charged with £6 million, £7 million and £81 million for its share of net actuarial and other losses on the scheme assets and liabilities. As shareholder profits for the PAC with-profits sub-fund reflects the surplus for distribution, these amounts are effectively absorbed by an increased charge in the income statement for the transfer to the liability for unallocated surplus.

At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, after the effect of the application of IFRIC 14, the total share of the liability for deficit funding on PSPS and the deficit on the smaller Scottish Amicable Scheme attributable to the PAC with-profits fund amounted to a liability of £88 million, £60 million and £110 million net of related tax relief.

2 Corporate governance

The rules of the Prudential Group's largest pension arrangement, the defined benefit section of PSPS, a final salary scheme, specify that, in exercising its investment powers, the Trustee's objective is to achieve the best overall investment return consistent with the security of the assets of the scheme. In doing this, consideration is given to the nature and duration of the scheme's liabilities. The Trustee sets the benchmark for the asset mix, following analysis of the liabilities by the Scheme's Actuary and, having taken advice from the Investment Managers, then selects benchmark indices for each asset type in order to measure investment performance against a benchmark return.

The Trustee reviews strategy, the asset mix benchmark and the Investment Managers' objectives every three years, to coincide with the Actuarial Valuation, or earlier if the Scheme Actuary recommends. Interim reviews are conducted annually based on changing economic circumstances and financial market levels.

The Trustee sets the general investment policy and specifies any restrictions on types of investment and the degrees of divergence permitted from the benchmark, but delegates the responsibility for selection and realisation of specific investments to the Investment Managers. In carrying out this responsibility, the Investment Managers are required by the Pensions Act 1995 to have regard to the need for diversification and suitability of investments. Subject to a number of restrictions contained within the relevant asset management agreements, the Investment Managers are authorised to invest in any class of investment asset. However, the Investment Managers will not invest in any new class of investment asset without prior consultation with the Trustee.

The Trustee consults the Principal Employer, the Prudential Assurance Company, on these investment principles, but the ultimate responsibility for the investment of the assets of the scheme lies with the Trustee.

The investment policies and strategies for the other two UK defined benefit schemes, the M&G Group Pension Scheme and the Scottish Amicable Staff Pension Scheme, which are both final salary schemes, follow similar principles, but have different target allocations reflecting the particular requirements of the schemes.

3 Assumptions

The actuarial assumptions used in determining benefit obligations and the net periodic benefit costs for the years ended 31 December were as follows:

	2007	2008	2009
	%	%	%
Discount rate*	5.9	6.1	5.8
Rate of increase in salaries	5.3	5.0	5.7
Rate of inflation	3.3	3.0	3.7
Rate of increase of pensions in payment for inflation:			
Guaranteed (maximum 5%)	3.3	3.0	3.7
Guaranteed (maximum 2.5%)†	2.5	2.5	2.5
Discretionary†	2.5	2.5	2.5
Expected returns on plan assets	5.9	6.2	4.5

* The discount rate has been determined by reference to an 'AA' corporate bond index adjusted, where applicable, to allow for the difference in duration between the index and the pension liabilities.

† The rates of 2.5% shown are those for PSPS. Assumed rates of increase of pensions in payment for inflation for all other schemes are 3.3%, 3.0% and 3.7% in 2007, 2008 and 2009 respectively.

The calculations are based on current actuarially calculated mortality estimates with a specific allowance made for future improvements in mortality, which is broadly based on adjusted versions of the medium cohort projections prepared by the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries. In 2007, the mortality assumptions were strengthened by including a floor to the medium cohort improvements.

The tables used for PSPS immediate annuities in payment at 31 December 2007 and 31 December 2008 were:

Male: 100% PMA 92 with CMIR17 improvements to the valuation date and medium cohort improvements subject to a floor of 1.75% up to the age of 90, decreasing linearly to zero by age of 120; and

Female: 100% PFA 92 with CMIR17 improvements to the valuation date and 75% medium cohort improvements subject to a floor of 1% up to the age of 90, decreasing linearly to zero by age of 120.

The tables used for PSPS immediate annuities in payment at 31 December 2009 were:

Male: 108.6% PNMA 00 with medium cohort improvements subject to a floor of 1.75% up to the age of 90, decreasing linearly to zero by age of 120; and

Female: 103.4% PNFA 00 with 75% medium cohort improvements subject to a floor of 1% up to the age of 90 and decreasing linearly to zero by age of 120.

The assumed life expectancies on retirement at age 60, based on the mortality table used was:

	2007 years		2008 years		2009 years	
	Male	Female	Male	Female	Male	Female
Retiring today	26.2	28.3	26.4	28.4	27.4	28.6
Retiring in 15 years' time	28.7	29.3	28.9	29.8	30.1	30.8

The mean term of the current PSPS liabilities is around 18 years.

Using external actuarial advice provided by the scheme actuaries being Towers Watson (previously known as Watson Wyatt) for the valuation of PSPS and by Aon Limited for the M&G scheme, and Xafinity for the Scottish Amicable Scheme, the most recent full valuations have been updated to 31 December 2009, applying the principles prescribed by IAS 19.

4 Summary financial position

The Prudential Group liability in respect of defined benefit pension schemes is as follows:

	2007	2008	2009
	£m	£m	£m
Economic position:			
Deficit, gross of deferred tax, based on scheme assets held, including investments in Prudential insurance policies:			
Attributable to the PAC with-profits fund (i.e. absorbed by the liability for unallocated surplus)	(98)	(67)	(122)
Attributable to shareholder-backed operations (i.e. to shareholders' equity)	(85)	(82)	(128)
Economic deficit — as explained in note 5 below	(183)	(149)	(250)
Excludes investments in Prudential insurance policies (offset on consolidation in the Group financial information against insurance liabilities)	(172)	(157)	(187)
Deficit under IAS 19 included in provisions in the statement of financial position — as explained in note 7 below	(355)	(306)	(437)

The following disclosures explain the economic position and IAS 19 basis of accounting after eliminating investment in Prudential insurance policies on consolidation.

5 Prudential Group economic financial position

The following tables illustrate the movement on the financial position of the Prudential Group's defined benefit pension schemes on an economic basis. The underlying position reflects the assets including the investments in Prudential policies that are offset against liabilities to policyholders on the Prudential Group consolidation and the liabilities of the schemes. The instruments in Prudential policies comprise £140 million, £103 million and £101 million at 31 December 2007, 2008 and 2009, respectively for PSPS and £172 million, £157 million and £187 million at 31 December 2007, 2008 and 2009, respectively for the M&G scheme.

Separately, the economic financial position also includes the effect of the application of IFRIC 14, whereby for PSPS, where there are additional constraints in the trust deed to prevent the company access, the surplus is not recognised and a liability to additional funding (as described earlier) is established.

Estimated pension scheme deficit — economic basis

Movements on the pension scheme deficit (determined on the 'economic basis') are as follows, with the effect of the application of IFRIC 14 being shown separately:

	2007					
		(Charge) credit to income statement				
	Surplus (deficit) in scheme at 1 January 2007	Operating results (based on longer-term investment returns) (note b)	Actuarial and other gains and losses (note c)	Results of sold Taiwan agency business	Contributions paid	Surplus (deficit) in scheme at 31 Dec 2007 (note a)
	£m					
All schemes						
Underlying position (without the effect of IFRIC 14)						
Surplus (deficit)	65	(14)	295	—	101	447
Less: amount attributable to PAC with-profits fund	(73)	(9)	(205)	—	(51)	(338)
Shareholders' share:						
Gross of tax surplus (deficit)	(8)	(23)	90	—	50	109
Related tax	—	6	(25)	—	(14)	(33)
Net of shareholders' tax	(8)	(17)	65	—	36	76
Effect of IFRIC 14						
Surplus (deficit)	(284)	(44)	(302)	—	—	(630)
Less: amount attributable to PAC with-profits fund	193	32	211	—	—	436
Shareholders' share:						
Gross of tax (deficit) surplus	(91)	(12)	(91)	—	—	(194)
Related tax	27	2	26	—	—	55
Net of shareholders' tax	(64)	(10)	(65)	—	—	(139)
With the effect of IFRIC 14						
Surplus (deficit)	(219)	(58)	(7)	—	101	(183)
Less: amount attributable to PAC with-profits fund	120	23	6	—	(51)	98
Shareholders' share:						
Gross of tax (deficit) surplus	(99)	(35)	(1)	—	50	(85)
Related tax	27	8	1	—	(14)	22
Net of shareholders' tax	(72)	(27)	—	—	36	(63)

	2008						
		(Charge) credit to income statement					
	Surplus (deficit) in scheme at 1 January 2008	Operating results (based on longer-term investment returns) (note b)	Actuarial and other gains and losses (note c)	Results of sold Taiwan agency business	Contributions paid	Exchange	Surplus (deficit) in scheme at 31 Dec 2008 (note a)
	£m						
All schemes Underlying position (without the effect of IFRIC 14)							
Surplus (deficit)	447	46	61	(1)	95	(4)	644
Less: amount attributable to PAC with-profits fund	(338)	(48)	(49)	—	(48)	—	(483)
Shareholders' share:							
Gross of tax surplus (deficit)	109	(2)	12	(1)	47	(4)	161
Related tax	(33)	1	(2)	—	(13)	—	(47)
Net of shareholders' tax	76	(1)	10	(1)	34	(4)	114
Effect of IFRIC 14							
Surplus (deficit)	(630)	(82)	(81)	—	—	—	(793)
Less: amount attributable to PAC with-profits fund	436	58	56	—	—	—	550
Shareholders' share:							
Gross of tax (deficit) surplus	(194)	(24)	(25)	—	—	—	(243)
Related tax	55	6	7	—	—	—	68
Net of shareholders' tax	(139)	(18)	(18)	—	—	—	(175)
With the effect of IFRIC 14							
Surplus (deficit)	(183)	(36)	(20)	(1)	95	(4)	(149)
Less: amount attributable to PAC with-profits fund	98	10	7	—	(48)	—	67
Shareholders' share:							
Gross of tax (deficit) surplus	(85)	(26)	(13)	(1)	47	(4)	(82)
Related tax	22	7	5	—	(13)	—	21
Net of shareholders' tax	(63)	(19)	(8)	(1)	34	(4)	(61)

	2009					
		(Charge) credit to income statement				
	Surplus (deficit) in scheme at 1 January 2009	Operating results (based on longer-term investment returns) (note b)	Actuarial and other gains and losses (note c)	Contributions paid	Disposal of Taiwan agency business	Surplus (deficit) in scheme at 31 Dec 2009 (note a)
			£m			
All schemes Underlying position (without the effect of IFRIC 14)						
Surplus (deficit)	644	(71)	(337)	85	17	338
Less: amount attributable to PAC with-profits fund	(483)	33	207	(42)	—	(285)
Shareholders' share:						
Gross of tax surplus (deficit)	161	(38)	(130)	43	17	53
Related tax	(47)	11	36	(11)	(4)	(15)
Net of shareholders' tax	114	(27)	(94)	32	13	38
Effect of IFRIC 14						
Surplus (deficit)	(793)	23	182	—	—	(588)
Less: amount attributable to PAC with-profits fund	550	(17)	(126)	—	—	407
Shareholders' share:						
Gross of tax (deficit) surplus	(243)	6	56	—	—	(181)
Related tax	68	(2)	(15)	—	—	51
Net of shareholders' tax	(175)	4	41	—	—	(130)
With the effect of IFRIC 14						
Surplus (deficit)	(149)	(48)	(155)	85	17	(250)
Less: amount attributable to PAC with-profits fund	67	16	81	(42)	—	122
Shareholders' share:						
Gross of tax (deficit) surplus	(82)	(32)	(74)	43	17	(128)
Related tax	21	9	21	(11)	(4)	36
Net of shareholders' tax	(61)	(23)	(53)	32	13	(92)

(a) On the 'economic basis', after including the underlying assets represented by the investments in Prudential insurance policies as scheme assets, the underlying statements of financial position of the schemes at 31 December were:

	2007				2008				2009			
	PSPS	Other schemes note iii	Total	%	PSPS	Other schemes note iii	Total	%	PSPS	Other schemes note iii	Total	%
		£m				£m				£m		
Equities	1,278	265	1,543	28	823	213	1,036	19	830	266	1,096	20
Bonds	1,134	249	1,383	25	2,430	277	2,707	51	3,406	280	3,686	67
Properties	545	54	599	11	283	18	301	6	272	15	287	5
Cash-like investments(note i)	1,932	5	1,937	36	1,267	6	1,273	24	441	2	443	8
Total value of assets	4,889	573	5,462	100	4,803	514	5,317	100	4,949	563	5,512	100
Present value of benefit obligations	(4,361)	(654)	(5,015)		(4,075)	(598)	(4,673)		(4,436)	(738)	(5,174)	
	528	(81)	447		728	(84)	644		513	(175)	338	
Effect of the application of IFRIC 14 for pension schemes:												
Derecognition of PSPS surplus	(528)	—	(528)		(728)	—	(728)		(513)	—	(513)	
Set up obligation for deficit funding for PSPS	(102)	—	(102)		(65)	—	(65)		(75)	—	(75)	
Pre-tax deficit(note ii)	(102)	(81)	(183)		(65)	(84)	(149)		(75)	(175)	(250)	

Notes

i The PSPS has entered into a derivatives based strategy to match the duration and inflation profile of its liabilities. This involved a reallocation from other investments to cash-like investments with an interest and inflation swap overlay. In broad terms, the scheme is committed to making a series of payments related to LIBOR on a nominal amount and in return the scheme receives a series of fixed and inflation-linked payments which match a proportion of its liabilities. As at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the nominal value of the interest-rate swaps amounted to £1.2 billion, £1.2 billion, and £1.1 billion and inflation-linked swaps amounted to £0.7 billion, £0.3 billion and £1.9 billion respectively.

ii The resulting scheme deficit arising from the excess of liabilities over assets at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of £183 million, £149 million and £250 million comprised a deficit of £98 million, £67 million and £122 million attributable to the PAC with-profits fund and deficit of £85 million, £82 million and £128 million attributable to shareholder operations.

iii In addition to PSPS, there are two smaller schemes in the UK, the Scottish Amicable Life Pension Scheme, and the M&G Pension Scheme, with a combined deficit at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of £71 million, £67 million and £175 million, gross of tax. There is also a small scheme in Taiwan, which at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, had a deficit of £10 million, £17 million and nil, gross of tax. As part of the sale of the Taiwan agency business in June 2009 the Group has settled the majority of the obligations under the Taiwan scheme relating to the employees who were transferred out.

The movements in the deficit on the 'economic basis' between scheme assets and liabilities were:

	2007	2008	2009
	£m	£m	£m
Current service cost	(19)	(19)	(11)
Curtailment credit	—	14	—
Other finance income	2	(2)	(8)
Cash costs and unwind of discount on opening provision for deficit funding for PSPS	(41)	(29)	(29)
Contributions	101	95	85
Actuarial and other gains and losses	(7)	(20)	(155)
Movement due to the sold Taiwan agency business and exchange translation difference	—	(5)	17
Net decrease in deficit	36	34	(101)

(b) The components of the (charge) credit to operating results (gross of allocation of the share attributable to the PAC with-profits fund) are as follows:

	2007	2008	2009
	£m	£m	£m
Service cost	(58)	(45)	(34)
Curtailment credit	—	44	—
Finance (expense) income:			
Interest on pension scheme liabilities	(265)	(289)	(277)
Expected return on assets	309	336	240
Total (charge) credit without the effect IFRIC 14	(14)	46	(71)
Effect of IFRIC 14 for pension schemes	(44)	(82)	23
Total (charge) credit after the effect of IFRIC 14	(58)	(36)	(48)

The net charge to operating profit (gross of the share attributable to the PAC with-profits fund) of £58 million, £36 million and £48 million, for 2007, 2008 and 2009 respectively, is made up of a charge relating to PSPS of £41 million, £29 million and £29 million and a charge in respect of other schemes of £17 million, £7 million and £19 million, for 2007, 2008, and 2009 respectively. This net charge represents:

	2007	2008	2009
	£m	£m	£m
Underlying IAS 19 charge for other pension schemes	(17)	(7)	(19)
Cash costs for PSPS	(34)	(25)	(25)
Unwind of discount on opening provision for deficit funding for PSPS	(7)	(4)	(4)
	(58)	(36)	(48)

Consistent with the derecognition of Prudential's interest in the underlying IAS 19 surplus of PSPS, the charge to operating profit on longer-term investment returns for PSPS reflects the cash cost of contributions for ongoing service of active members. In addition, the charge to the operating results also includes a charge for the unwind of discount on the opening provision for deficit funding for PSPS.

(c) The components of the (charge) credit for actuarial and other gains and losses (gross of allocation of the share attributable to the PAC with-profits fund but excluding the charge relating to the sold Taiwan agency business) are as follows:

	2007	2008	2009
	£m	£m	£m
Actual less expected return on assets	(8)	(356)	108
(Losses) gains on changes of assumptions for plan liabilities	317	272	(521)
Experience (gains) losses on liabilities	(14)	145	76
Total charge without the effect of IFRIC 14	295	61	(337)
Effect of IFRIC 14 for pension schemes	(302)	(81)	182
Actuarial and other gains and losses after the effect of IFRIC 14	(7)	(20)	(155)

The net charge for actuarial and other gains and losses is recorded within the income statement but, within the segmental analysis of profit, the shareholders' share of actuarial and other gains and losses (i.e. net of allocation of the share to the PAC with-profits funds) is excluded from operating profit based on longer-term investment returns.

The 2009 actuarial losses of £337 million primarily reflects the effects of increases in inflation rates and decrease in risk discount rates partially offset by the excess of market returns over long-term assumptions and experience gains on liabilities.

The 2008 actuarial gains of £61 million reflected gains on changes of assumptions of £272 million due to the effect of an increase in the risk discount rate combined with the effect of decreases in inflation rates and experience gains of £145 million which were partially offset by the shortfall of market returns over long term assumptions of £356 million. The 2007 gains on changes of assumptions for liabilities of £317 million reflected gains due to changes in economic assumptions of £509 million which more than offset the actuarial losses of £192 million from the effect of strengthened mortality assumptions for the UK pension schemes.

Consistent with the derecognition of Prudential's interest in the underlying IAS 19 surplus of PSPS, the actuarial gains and losses do not include those of PSPS. In addition, as a result of applying of IFRIC 14, the Prudential Group has recognised a provision for deficit funding in respect of PSPS. The change in 2009 in relation to this provision recognised above as other gains and losses on defined benefit pension schemes was £nil, £13 million and £48 million, for 2007, 2008 and 2009 respectively.

6 *Movement in IAS 19 basis financial position*

The change in the present value of the benefit obligation and the change in fair value of the assets for the total of the PSPS, Scottish Amicable Life, M&G and Taiwan schemes over the period were as follows:

	2007					
		Other schemes				
	PSPS Provision for deficit funding	IAS 19 basis: change in fair value of plan assets	Investments in Prudential insurance policies	Economic basis: total assets	IAS 19 basis: change in present value of benefit obligations	Total Economic basis: net obligations
	£m					
Fair value of plan assets, beginning of year	—	366	161	527	—	527
Present value of benefit obligation, beginning of year	—	—	—	—	(603)	(603)
Provision for deficit funding for PSPS	(143)	—	—	—	—	(143)
	(143)	366	161	527	(603)	(219)
Service cost — current charge only	—	—	—	—	(19)	(19)
Interest cost	—	—	—	—	(31)	(31)
Expected return on plan assets	—	23	10	33	—	33
Employee contributions	—	—	1	1	(1)	—
Employer contributions	82	10	9	19	—	101
Actuarial gains (losses)	—	9	(5)	4	(11)	(7)
Benefit payments	—	(7)	(4)	(11)	11	—
Cash costs and unwind of discount on the opening provision for deficit funding for PSPS	(41)	—	—	—	—	(41)
Movement in the provision for deficit funding for PSPS	—	—	—	—	—	—
Fair value of plan assets, end of year	—	401	172	573	—	573
Present value of benefit obligation, end of year	—	—	—	—	(654)	(654)
Provision for deficit funding of PSPS	(102)	—	—	—	—	(102)
Economic basis deficit	—	—	—	—	—	(183)

	2008					
		Other schemes				
	PSPS Provision for deficit funding	IAS 19 basis: change in fair value of plan assets	Investments in Prudential insurance policies	Economic basis: total assets	IAS 19 basis: change in present value of benefit obligations	Total Economic basis: net obligations
	£m					
Fair value of plan assets, beginning of year	—	401	172	573	—	573
Present value of benefit obligation, beginning of year	—	—	—	—	(654)	(654)
Provision for deficit funding for PSPS	(102)	—	—	—	—	(102)
	(102)	401	172	573	(654)	(183)
Service cost — current charge only	—	—	—	—	(19)	(19)
Curtailment credit	—	—	—	—	14	14
Interest cost	—	—	—	—	(39)	(39)
Expected return on plan assets	—	26	11	37	—	37
Employee contributions	—	—	1	1	(1)	—
Employer contributions	79	7	9	16	—	95
Actuarial gains (losses)	—	(67)	(31)	(98)	90	(8)
Benefit payments	—	(10)	(5)	(15)	15	—
Cash costs and unwind of discount on the opening provision for deficit funding for PSPS	(29)	—	—	—	—	(29)
Movement in the provision for deficit funding for PSPS	(13)	—	—	—	—	(13)
Exchange translation difference	—	—	—	—	(4)	(4)
Fair value of plan assets, end of year	—	357	157	514	—	514
Present value of benefit obligation, end of year	—	—	—	—	(598)	(598)
Provision for deficit funding of PSPS	(65)	—	—	—	—	(65)
Economic basis deficit	—	—	—	—	—	(149)

	2009					
		Other schemes				
	PSPS Provision for deficit funding	IAS 19 basis: change in fair value of plan assets	Investments in Prudential insurance policies	Economic basis: total assets	IAS 19 basis: change in present value of benefit obligations	Total Economic basis: net obligations
	£m					
Fair value of plan assets, beginning of year	—	357	157	514	—	514
Present value of benefit obligation, beginning of year	—	—	—	—	(598)	(598)
Provision for deficit funding for PSPS	(65)	—	—	—	—	(65)
Service cost — current charge only	—	—	—	—	(11)	(11)
	(65)	357	157	514	(598)	(149)
Interest cost	—	—	—	—	(35)	(35)
Expected return on plan assets	—	18	9	27	—	27
Employee contributions	—	—	1	1	(1)	—
Employer contributions	67	9	9	18	—	85
Actuarial gains (losses)	—	6	17	23	(130)	(107)
Benefit payments	—	(11)	(6)	(17)	17	—
Cash costs and unwind of discount on the opening provision for deficit funding for PSPS	(29)	—	—	—	—	(29)
Movement in the provision for deficit funding for PSPS	(48)	—	—	—	—	(48)
Disposal of Taiwan agency business, including exchange translation differences	—	(3)	—	(3)	20	17
Fair value of plan assets, end of year	—	376	187	563	—	563
Present value of benefit obligation, end of year	—	—	—	—	(738)	(738)
Provision for deficit funding of PSPS	(75)	—	—	—	—	(75)
Economic basis deficit	—	—	—	—	—	(250)

7 IAS 19 basis financial position as consolidated

The IAS 19 basis pensions deficit can be summarised as follows:

	2005	2006	2007	2008	2009
	£m	£m	£m	£m	£m
Fair value of plan assets, end of year	4,622	4,988	5,150	5,057	5,224
Present value of funded benefit obligation	(5,228)	(5,023)	(4,826)	(4,493)	(4,951)
Funded status	(606)	(35)	324	564	273
Present value of unfunded obligations (M&G scheme)*	(190)	(187)	(189)	(180)	(223)
	(796)	(222)	135	384	50
Effect of the application of IFRIC 14 for pension schemes;					
Derecognition of PSPS' surplus	—	(141)	(528)	(728)	(513)
Set up obligation for deficit funding for PSPS	—	(143)	(102)	(65)	(75)
Adjustment in respect of investment of PSPS in Prudential policies	—	126	140	103	101
Deficit recognised in the statement of financial position	(796)	(380)	(355)	(306)	(437)

* The M&G pension scheme assets are invested in Prudential insurance policies. For IFRS accounting purposes, the M&G scheme is in effect unfunded. Please see above for more details.

	2007	2008	2009
	£m	£m	£m
Components of net periodic pension cost			
Current service cost	(58)	(45)	(34)
Curtailment credit	—	44	—
Interest cost	(265)	(289)	(277)
Expected return on assets — economic basis	309	336	240
Less: expected return on investments of scheme assets in Prudential insurance policies	(20)	(22)	(16)
Expected return on assets — IAS 19 basis(†)	289	314	224
	(34)	24	(87)
Effect of the application of IFRIC 14	(34)	(71)	30
Pension cost (as referred to in note(I2a))	(68)	(47)	(57)
Actuarial gains and losses — economic basis	295	60	(337)
Less: actuarial losses on investments of scheme assets in Prudential insurance policies	1	79	8
	296	139	(329)
Effect of the application of IFRIC 14	(298)	(129)	191
Actuarial gains and losses — IAS 19 basis* (as referred to in note(I2a))	(2)	10	(138)
Net periodic pension cost (included within acquisition and other operating expenditure in the income statement)	(70)	(37)	(195)

* Consistent with the derecognition of the Prudential interest in the underlying IAS 19 surplus of PSPS, the effect on the net periodic pension cost for PSPS was to replace the usual IAS 19 pension charges and credits with the cash cost of contribution for ongoing services of active members and also not to report the actuarial gains and losses.

† In determining the expected return on scheme assets for 2007, 2008 and 2009 respectively, the 5.9%, 6.1% and 4.5% rate shown below has been applied to the opening assets.

The long-term expected rate of return has been taken to be the weighted average (by market value) of the long-term expected rates of return on each major asset class shown below:

	2005		2006		2007		2008		2009	
	£m	%	£m	%	£m	%	£m	%	£m	%
Scheme assets (IAS 19 basis before effect of IFRIC 14)										
Equity	2,376	51	1,432	29	1,332	26	875	17	917	18
Bonds	1,593	35	2,185	44	1,299	25	2,619	52	3,587	69
Properties	575	12	621	12	583	11	290	6	278	5
Cash-like investments	78	2	750	15	1,936	38	1,273	25	442	8
Total	4,622	100	4,988	100	5,150	100	5,057	100	5,224	100

	2007	2008	2009	Prospectively for 2010
	%	%	%	%
Long-term expected rate of return				
Equity	7.5	7.5	6.8	8.5
Bonds	4.8	5.4	4.8	5.3
Properties	6.8	6.75	6.05	6.75
Cash	5.0	5.5	2.0	4.75
Weighted average long-term expected rate of return	5.9	6.1	4.5	5.9

The expected rates of return have been determined by reference to long-term expectations, the carrying value of the assets and equity and other market conditions at the statement of financial position date.

The actual return on scheme assets was a gain £282 million, a loss of £20 million and a gain of £348 million on an IAS 19 basis, for 2007, 2008 and 2009 respectively.

None of the scheme assets included shares in Prudential or property occupied by the Prudential Group.

	2005	2006	2007	2008	2009
	£m	£m	£m	£m	£m
Fair value of scheme assets, end of year (IAS 19 basis)	4,622	4,988	5,150	5,057	5,224
Present value of the benefit obligation, end of year	(5,418)	(5,210)	(5,015)	(4,673)	(5,174)
Underlying scheme assets in surplus (deficit) of benefit obligation, before the effect of the application of IFRIC 14	(796)	(222)	135	384	50
Experience adjustments on scheme liabilities	1	18	(14)	145	76
Percentage of scheme liabilities at 31 December	(0.02)%	(0.35)%	0.28%	3.10%	1.47%
Experience adjustments on scheme assets (IAS 19 basis)	527	140	(7)	(277)	100
Percentage of scheme assets at 31 December	11.42%	2.81%	(0.14)%	(5.48)%	1.91%

The experience adjustments on scheme liabilities in 2008 of a gain of £145 million related mainly to the 'true up' reflecting improvements in data consequent upon the 2008 triennial valuation of PSPS.

Total employer contributions expected to be paid into the Prudential Group defined benefit schemes for the year ending 31 December 2010 £88 million.

8 Sensitivity of the pension scheme liabilities of the PSPS, Scottish Amicable Life and M&G pension schemes to key variables

The table below shows the sensitivity of the underlying PSPS, Scottish Amicable Life and M&G pension scheme liabilities at 31 December 2007 of £4,361 million, £454 million and £189 million respectively, at 31 December 2008 of £4,075 million, £398 million and £180 million respectively and 31 December 2009 of £4,436 million, £515 million and £223 million respectively to changes in discount rates and inflation rates.

2007

Assumption	Change in assumption	Impact on scheme liabilities on IAS 19 basis	
Discount rate	Decrease by 0.2% from 5.9% to 5.7%	Increase in scheme liabilities by:	
		PSPS	3.5%
		Scottish Amicable Life	5.3%
		M&G	4.8%
Discount rate	Increase by 0.2% from 5.9% to 6.1%	Decrease in scheme liabilities by:	
		PSPS	3.4%
		Scottish Amicable Life	5.1%
		M&G	4.5%
Rate of inflation	Decrease by 0.2% from 3.3% to 3.1% with consequent reduction in salary increases	Decrease in scheme liabilities by:	
		PSPS	1.3%
		Scottish Amicable Life	5.0%
		M&G	4.4%

2008

Assumption	Change in assumption	Impact on scheme liabilities on IAS 19 basis	
Discount rate	Decrease by 0.2% from 6.1% to 5.9%	Increase in scheme liabilities by:	
		PSPS	3.3%
		Scottish Amicable Life	4.9%
		M&G	4.5%
Discount rate	Increase by 0.2% from 6.1% to 6.3%	Decrease in scheme liabilities by:	
		PSPS	3.1%
		Scottish Amicable Life	4.6%
		M&G	4.2%
Rate of inflation	Decrease by 0.2% from 3.0% to 2.8% with consequent reduction in salary increases	Decrease in scheme liabilities by:	
		PSPS	0.8%
		Scottish Amicable Life	4.5%
		M&G	3.8%

2009

Assumption	Change in assumption	Impact on scheme liabilities on IAS 19 basis	
Discount rate	Decrease by 0.2% from 5.8% to 5.6%	Increase in scheme liabilities by:	
		PSPS	3.5%
		Scottish Amicable Life	5.2%
		M&G	4.9%
Discount rate	Increase by 0.2% from 5.8% to 6.0%	Decrease in scheme liabilities by:	
		PSPS	3.2%
		Scottish Amicable Life	4.8%
		M&G	4.9%
Rate of inflation	Decrease by 0.2% from 3.7% to 3.5% with consequent reduction in salary increases	Decrease in scheme liabilities by:	
		PSPS	0.9%
		Scottish Amicable Life	4.9%
		M&G	4.5%

The sensitivity of the underlying pension scheme liabilities to changes in discount rates and inflation rates as shown above does not directly equate to an impact on the profit or loss attributable to shareholders or shareholders' equity due to the effect of the application of IFRIC 14 on PSPS and the allocation of a share of the interest in financial position of the PSPS and Scottish Amicable Schemes to the PAC with-profits fund as described in note (b)(i)(1) above.

For PSPS, the underlying surplus of the scheme of £528 million, £728 million, and £513 million, as at 31 December 2007, 31 December 2008 and 31 December 2009 respectively, has not been recognised under IFRIC 14. Any change in the underlying scheme liabilities to the extent that it is not sufficient to alter PSPS into a liability in excess of the deficit funding provision, will not have an impact on the Prudential Group's results and financial position.

In the event that a change in the PSPS scheme liabilities results in a deficit position for the scheme which is recognisable, the deficit recognised affects the Prudential Group's results and financial position only to the extent of the amounts attributable to shareholder operations. The amounts attributable to the PAC with-profits fund are absorbed by the liability for unallocated surplus and have no direct effect on the profit or loss attributable to shareholders or shareholders' equity. This applies similarly to the Scottish Amicable Scheme, whose deficit has been allocated 50% to the PAC with-profits fund and 50% to the PAC shareholders fund.

9 Transfer value of PSPS scheme

At 31 December 2009, it is estimated that the assets of the scheme are broadly sufficient to cover the liabilities of PSPS on a 'buyout' basis including an allowance for expenses. The 'buyout' basis refers to a basis that might apply in the circumstance of a transfer to another appropriate financial institution. In making this assessment it has been assumed that a more conservative investment strategy applies together with a more prudent allowance for future mortality improvements and no allowance for discretionary pension increases.

ii Other pension plans

The Prudential Group operates various defined contribution pension schemes including schemes in Jackson and Asia. As noted earlier, the cost of the Prudential Group's contributions for continuing operations to these schemes in 2007, 2008 and 2009 respectively, was £28 million, £31 million and £38 million.

I3: Share-based payments

The Prudential Group maintains a number of main share award and share option plans relating to Prudential Shares, which are described below.

The Group Performance Share Plan (GPSP) is the incentive plan in which all executive directors and other senior executives within the Prudential Group can participate. This scheme was established as a replacement for the Restricted Share Plan (RSP) under which no further awards could be made after March 2006. Awards are granted either in the form of a nil cost option, conditional right over shares, or such other form that shall confer to the participant an equivalent economic benefit, with a vesting period of three years. The performance measure for the awards is that Prudential's Total Shareholder Return (TSR) outperforms an index comprising of peer companies. Vesting of the awards between each performance point is on a straight line sliding scale basis. Participants are entitled to the value of reinvested dividends that would have accrued on the shares that vest. Shares are currently purchased in the open market by a trust for the benefit of qualifying employees. Beginning 2010, newly issued shares will be used in settling the awards that vest and are released.

The RSP was, until March 2006, the Group's long-term incentive plan for executive directors and other senior executives designed to provide rewards linked to shareholder return. Each year participants were granted a conditional option to receive a number of shares. There was a deferment period of three years at the end of which the award vested to an extent that depended on the performance of the Group's shares including notional reinvested dividends and on the Group's underlying financial performance. After vesting, the option may be exercised at zero cost at any time, subject to closed period rules, in the balance of a 10-year period. Shares are purchased in the open market by a trust for the benefit of qualifying employees.

The Business Unit Performance Plan ("BUPP") is an incentive plan created to provide a common framework under which awards would be made to senior employees in the UK, Jackson and Asia including the Chief Executive Officers. Awards made under this plan in 2007, 2008 and 2009 are based on growth in Shareholder Capital Value on the European Embedded Value (EEV) basis with performance measured over three years. Upon vesting of awards made up to 2008, half of the awards are released as shares and the other half released in cash. From 2009 all awards made will be settled in shares after vesting. Participants are entitled to receive the value of reinvested dividends over the performance period for those shares that vest. The growth parameters for the awards are relevant to each region and vesting of the awards between each performance point is on a straight line sliding scale basis.

UK-based employees and executive directors are eligible to participate in the Prudential HM Revenue & Customs (HMRC) approved UK Savings Related Share Option Scheme (SAYE scheme), Republic of Ireland based employees can participate in the equivalent Irish SAYE scheme and the Asia-based executive director can participate in the equivalent International SAYE scheme. The schemes allow employees to save towards the exercise of options over Prudential plc shares, at an option price set at the beginning of the savings period at a discount of up to 20% to the market price. In 2009, the rules governing the SAYE schemes were amended so that savings contracts for seven years were discontinued and employees may save up to £250 per month for three or five years. On maturity at the end of the set term, participants may exercise their options within six months of the end of the savings period and purchase Prudential plc shares. If an option is not exercised within six months, participants are entitled to a refund of their cash contributions plus interest if applicable under the rules. Shares are issued to satisfy options that are exercised. No options may be granted under the schemes if the grant would cause the number of shares which have been issued, or which remain issuable pursuant to options granted in the preceding 10 years under the scheme and other share option schemes operated by Prudential, or which have been issued under any other share incentive scheme of Prudential, to exceed 10% of its ordinary share capital at the proposed date of grant.

UK-based executive directors are also eligible to participate in Prudential HMRC approved Share Incentive Plans which allows all employees based in the UK insurance business and the Group Head Office to purchase shares of Prudential plc (partnership shares) on a monthly basis out of gross salary. For every four partnership shares bought, an additional matching share is awarded, purchased on the open market. Dividend shares accumulate while the employee participates in the plan. Partnership shares may be withdrawn from the scheme at any time. If the employee withdraws from the plan within five years, the matching shares are forfeit and if within three years, dividend shares are forfeit.

Jackson operates a performance-related share award which, subject to the prior approval of the Jackson Remuneration Committee, may grant share awards to eligible Jackson employees in the form of a contingent right to receive shares or a conditional allocation of shares. These share awards have vesting periods of four years and are at nil cost to the employee. Award holders do not have any right to dividends or voting rights attaching to the shares. The shares are held in the employee share trust in the form of American Depository Receipts which are tradable on the New York Stock Exchange.

The Prudential Corporation Asia Long-Term Incentive Plan (PCA LTIP) is an incentive plan created in 2008 for senior employees and senior executives based in Asia to replace the Asia Business Unit Performance Plan (BUPP). Awards under the new PCA LTIP will vest after three years subject to the employee being in employment at the time of vesting without any performance conditions. Awards are discretionary and on a year by year basis determined by Prudential Corporation Asia's full year financial results and the employee's contribution to the business in each case for the year prior to the award being made. All awards will be in Prudential shares except for countries where share awards are not feasible due to securities and/or tax reasons, where awards will be replaced by the cash value of the shares that would otherwise have been transferred.

Certain senior executives have annual incentive plans with awards paid partly in cash and partly in deferred shares. The portion of any award made in the form of awards of shares is deferred for three years, with the release of shares subject to close periods. The shares are held in the employee share trust and shares equivalent to dividends otherwise payable will accumulate for the benefit of award holders during the deferral period up to the release date.

In addition, there are other share awards including the Prudential Corporation Asia Deferred Bonus Plan (PCADBP), Prudential Capital Deferred Bonus Plan (PruCap DBP) and other arrangements. There are no performance conditions attaching to these deferred bonus plans and an award vests in full subject to the individual being employed by Prudential at the end of the vesting period. The other arrangements relate to various awards that have been made without performance conditions to individual employees, typically in order to facilitate recruitment of senior employees where awards from their previous employers may be forfeited on leaving.

Movements in share options outstanding under the Prudential Group's share-based compensation plans relating to Prudential plc shares during 2007, 2008 and 2009 were as follows:

Options outstanding (including conditional options)	2007 Number of options	2007 Weighted average exercise price	2008 Number of options	2008 Weighted average exercise price	2009 Number of options	2009 Weighted average exercise price
	millions	£	millions	£	millions	£
Beginning of year:	16.5	2.47	14.5	2.57	12.7	2.44
Granted	4.0	2.69	6.9	3.28	14.0	2.28
Exercised	(1.9)	3.42	(3.5)	2.73	(1.7)	1.05
Forfeited	(1.4)	1.37	(1.5)	0.69	(0.8)	2.48
Expired	(2.7)	2.13	(3.7)	4.94	(5.3)	3.77
End of year	14.5	2.57	12.7	2.44	18.9	2.07
Options immediately exercisable, end of year	0.2	3.35	0.6	2.29	0.3	4.16

The weighted average share price of Prudential plc for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 was £7.15, £5.46 and £4.17 respectively.

Movements in share awards outstanding under the Prudential Group's share-based compensation plans relating to Prudential plc shares at 31 December 2007, 31 December 2008 and 31 December 2009 were as follows:

Awards outstanding	2007 Number of awards	2008 Number of awards	2009 Number of awards
	millions	millions	millions
Beginning of year:	6.6	8.0	8.6
Granted	3.8	3.5	7.9
Exercised	(1.3)	(1.7)	(2.2)
Forfeited	(1.1)	(0.9)	(0.8)
Expired	—	(0.3)	(1.0)
End of year	8.0	8.6	12.5

The following table provides a summary of the range of exercise prices for Prudential plc options (including conditional options) outstanding at 31 December 2007.

Range of exercise prices	Outstanding: Number outstanding	Outstanding: Weighted average remaining contractual life	Outstanding: Weighted average exercise prices	Exercisable: Number exercisable	Exercisable: Weighted average exercise prices
	millions	years	£	millions	£
Between £0 and £1	5.5	8.6	—	—	—
Between £1 and £2	—	—	—	—	—
Between £2 and £3	2.7	1.3	2.66	—	—
Between £3 and £4	1.2	1.7	3.62	0.2	3.37
Between £4 and £5	2.9	2.7	4.62	—	—
Between £5 and £6	2.2	3.5	5.62	—	—
Between £6 and £7	—	0.9	6.55	—	6.95
Between £7 and £8	—	—	—	—	—
	14.5	4.7	2.57	0.2	3.35

The following table provides a summary of the range of exercise prices for Prudential plc options (including conditional options) outstanding at 31 December 2008.

Range of exercise prices	Outstanding: Number outstanding	Outstanding: Weighted average remaining contractual life	Outstanding: Weighted average exercise prices	Exercisable: Number exercisable	Exercisable: Weighted average exercise prices
	millions	years	£	millions	£
Between £0 and £1	5.9	8.3	—	0.3	—
Between £1 and £2	—	—	—	—	—
Between £2 and £3	0.3	1.7	2.66	0.0	2.66
Between £3 and £4	0.5	1.4	3.56	0.0	3.65
Between £4 and £5	4.6	3.3	4.45	0.3	4.07
Between £5 and £6	1.4	2.8	5.59	—	—
Between £6 and £7	0.0	0.4	6.17	0.0	6.17
Between £7 and £8	—	—	—	—	—
	12.7	5.5	2.44	0.6	2.29

The following table provides a summary of the range of exercise prices for Prudential plc options (including conditional options) outstanding at 31 December 2009.

Range of exercise prices	Outstanding: Number outstanding	Outstanding: Weighted average remaining contractual life	Outstanding: Weighted average exercise prices	Exercisable: Number exercisable	Exercisable: Weighted average exercise prices
	millions	years	£	millions	£
Between £0 and £1	6.7	8.6	—	0.0	—
Between £1 and £2	—	—	—	—	—
Between £2 and £3	10.0	3.6	2.88	—	—
Between £3 and £4	0.1	1.0	3.62	0.1	3.43
Between £4 and £5	1.5	3.0	4.37	0.2	4.73
Between £5 and £6	0.6	1.9	5.60	0.0	5.65
Between £6 and £7	—	—	—	—	—
Between £7 and £8	—	—	—	—	—
	18.9	5.2	2.07	0.3	4.16

The years shown above for weighted average remaining contractual life include the time period from end of vesting period to expiration of contract.

The weighted average fair values of Prudential plc options and awards granted during the period are as follows:

2007			2008			2009		
Weighted average fair value			Weighted average fair value			Weighted average fair value		
RSP and GPSP	Other options	Awards	GPSP	Other options	Awards	RSP and GPSP	Other options	Awards
	£			£			£	
4.78	2.55	7.33	4.16	2.14	5.69	3.52	1.55	4.67

The fair value amounts relating to all options including conditional nil cost options above were determined using the Black-Scholes and the Monte Carlo option-pricing models using the following assumptions:

	2007		2008		2009	
	GPSP	Other options	GPSP	Other options	GPSP	Other Options
Dividend yield (%)	2.32	2.32	3.60	3.60	4.41	4.41
Expected volatility (%)	28.90	27.17	30.87	34.67	56.21	60.55
Risk-free interest rate (%)	5.46	5.25	4.23	4.46	1.92	2.15
Expected option life (years)	3.00	3.48	3.00	3.74	3.00	3.67
Weighted average exercise price (£)	—	5.62	—	4.74	—	2.96
Weighted average share price (£)	7.52	7.47	6.63	6.16	4.83	3.82

Under IFRS, compensation costs for all share-based compensation plans are determined using the Black-Scholes model and the Monte Carlo model. Share options and awards are valued using the share price at the date of grant. The compensation costs for all awards and options are recognised in net income over the plans' respective vesting periods. The Prudential Group uses the Black-Scholes model to value all options and awards other than the GPSP, for which the Prudential Group uses a Monte Carlo model in order to allow for the impact of the TSR performance conditions. These models are used to calculate fair values for share options and awards at the grant date based on the quoted market price of the stock at the measurement date, the amount, if any, that the employees are required to pay, the dividend yield, expected volatility, risk-free interest rates and exercise prices.

The expected volatility is measured as the standard deviation of expected share price returns based on statistical analysis of daily share prices over a period up to the grant date equal to the expected life of options. Risk-free interest rates are UK gilt rates with projections for three, five and seven year terms to match corresponding vesting periods. Dividend yield is determined as the average yield over the year of grant and expected dividends are not incorporated into the measurement of fair value. For the GPSP, volatility and correlation between Prudential and an index constructed from a simple average of the TSR growth of 11 companies is required. For grants in 2007, an average index volatility and correlation of 18% and 72% respectively, were used. For grants in 2008, an average index volatility and correlation of 26% and 82% respectively, were used. For grants in 2009 an average index volatility and correlation of 40% and 83%, respectively, were used. Changes to the subjective input assumptions could materially affect the fair value estimate.

When options are granted or awards made to employees, an estimate is made of what percentage is more than likely to vest, be forfeited, lapse or cancelled based on historical information. Based on these estimates, compensation expense to be accrued at that date is calculated and amortised over the vesting period. For early exercises of options or release of awards due to redundancy, death or resignation, the compensation expense is immediately recognised and for forfeitures due to employees leaving the Prudential Group, any previously recognised expense is reversed. However, if an employee loses their award because of the Prudential Group's failure to meet the performance criteria, previously recognised expense is not reversed.

During 2007, 2008 and 2009, the Prudential Group granted share options to certain non-employee independent financial advisors. Those options were measured using the Black-Scholes option pricing model with assumptions consistent with those of other share options. These transactions were measured using an option model because the Prudential Group does not receive a separate and measurable benefit from those non-employees in exchange for the options granted. As such, the fair value of the options themselves is more readily determinable than the services received in return.

c Total share-based payment expense

Total expense recognised in the consolidated financial information related to share-based compensation is as follows:

	2007	2008	2009
	£m	£m	£m
Share-based compensation expense	28	23	37
Amount accounted for as equity-settled	19	27	29
Carrying value at 31 December of liabilities arising from share-based payment transactions	18	12	13
Intrinsic value of above liabilities for which rights had vested at 31 December	4	4	7

I4: Key management and directors' remuneration

a Key management remuneration

Key management principally constitutes the directors of Prudential plc as they have authority and responsibility for planning, directing and controlling the activities of the Prudential Group.

Total key management remuneration amounts to £15,670,000, £18,122,000 and £20,989,000, for 2007, 2008 and 2009 respectively. This comprises salaries and short-term benefits of £9,496,000, £10,425,000 and £11,570,000, for 2007, 2008 and 2009 respectively, post-employment benefits of £967,000, £1,003,000 and £1,132,000, for 2007, 2008 and 2009 respectively, leaving benefits of £nil, £507,000 and £915,000, for 2007, 2008 and 2009 respectively, and share-based payments of £5,207,000, £6,187,000 and £7,372,000, for 2007, 2008 and 2009 respectively.

Post-employment benefits comprise the change in the transfer value of the accrued benefit relating to directors' defined benefit pension schemes in the year and the total contributions made to directors' other pension arrangements.

The share-based payments charge is the sum of £3,456,000, £4,624,000 and £5,270,000, for 2007, 2008 and 2009 respectively, which is determined in accordance with IFRS 2, 'Share-Based Payments' (see note I3) and £1,751,000, £1,563,000 and £2,102,000, for 2007, 2008 and 2009 respectively, of deferred share awards.

b Directors' remuneration

	2007 £000					
	Salary/ Fees	**Bonus**	**Benefits***	**Cash supplements for pension purposes†**	**Total Emoluments 2007**	**Value of anticipated releases from LTIPs in respect of performance periods ending 31 December 2007§**
Chairman						
Sir David Clementi	508	—	41	127	676	—
Executive directors						
Philip Broadley	567	590	56	153	1,366	814
Clark Manning(notes i,ii)	500	1,724	16	—	2,240	2,933
Michael McLintock(note iii)	320	1,780	48	—	2,148	1,280
Mark Norbom (until 14 December 2006)(note iv)	—	—	—	—	—	—
Nick Prettejohn(note v)	615	615	54	80	1,364	—
Barry Stowe(notes vi, vii)	500	500	140	125	1,265	—
Mark Tucker(note viii)	907	1,134	59	227	2,327	1,588
Total executive directors	3,409	6,343	373	585	10,710	6,615
Non-executive directors						
Sir Winfried Bischoff (from 2 August 2007)	25	—	—	—	25	—
Keki Dadiseth(note ix)	81	—	—	—	81	—
Michael Garrett	66	—	—	—	66	—
Ann Godbehere (from 2 August 2007)	29	—	—	—	29	—
Bridget Macaskill	79	—	—	—	79	—
Roberto Mendoza (until 17 May 2007)	24	—	—	—	24	—
Kathleen O'Donovan	98	—	—	—	98	—
James Ross	98	—	—	—	98	—
Lord Turnbull	73	—	—	—	73	—
Total non-executive directors	573	—	—	—	573	—
Overall total	4,490	6,343	414	712	11,959	6,615

* Benefits include, where provided, cash allowances for cars, the use of a car and driver, medical insurance, security arrangements, expatriate benefits.

† Pension supplements that are paid in cash as per pension policy are included in the table. The pension policy and pension arrangements for current executive directors are set out subsequently.

§ Value of anticipated LTIP releases is the total of cash paid plus, for shares released, the value of the released shares based on the share price at 31 December 2007. All executive directors participate in long-term incentive plans and the details of share releases from awards with a performance period ending 31 December 2007 are provided in the footnotes to the table on share awards. Executive directors' participation in all-employee plans are set out subsequently.

Notes

(i) In 2007 it was assumed that for Clark Manning a deferred share award from the 2007 annual bonus valued at $200,000 would be made. This is included in the 2007 bonus figure.

(ii) Clark Manning's bonus figure excludes a contribution of £6,745, from a profit sharing plan, which has been made into a 401K retirement plan. This is included in the table on pension contributions in the section 'Directors' pensions and life assurances'.

(iii) Michael McLintock's 2007 annual incentive contains a deferral element. As a result of a review of remuneration structures of Michael McLintock, an additional award was made under the current LTIP in 2007. Also, in 2007 it was assumed that a deferred share award from the 2007 annual bonus valued at £640,000 would be made. This is included in the 2007 bonus figure.

(iv) Mark Norbom's directorship with Prudential plc ended on 14 December 2006 but he remained in employment until 31 January 2007. In connection with the termination of his employment he received a payment of £291,000 and nine successive monthly payments of £55,792. He also received private medical and life cover, school fees and club memberships until 31 October 2007 and housing benefits until 5 May 2007.

(v) In 2007 it was assumed that for Nick Prettejohn a deferred share award from the 2007 annual bonus valued at £307,625 would be made. This is included in the 2007 bonus figure.

(vi) In 2007 it was assumed that for Barry Stowe a deferred share award from the 2007 annual bonus valued at £250,000 would be made. This is included in the 2007 bonus figure.

(vii) Barry Stowe's benefits include those relating to his expatriate status including costs of £88,288 related to housing.

(viii) In 2007 it was assumed that for Mark Tucker a deferred share award from the 2007 annual bonus valued at £453,600 would be made. This is included in the 2007 bonus figure.

(ix) Keki Dadiseth was paid allowances totalling £9,400 in 2007 in respect of his accommodation expenses in London whilst on Prudential business, in lieu of reimbursing hotel costs as is the usual practice for directors who are not resident in the UK.

(x) In aggregate total fees paid to Directors amounted to £573,000 in 2007.

	2008 £000					
	Salary/ Fees	Bonus	Benefits*	Cash supplements for pension purposes †	Total Emoluments 2008	Value of anticipated releases from LTIPs in respect of performance periods ending 31 December 2008§
Chairman						
Sir David Clementi(note i)	538	—	43	134	715	—
Executive directors						
Philip Broadley (until 15 May 2008)(note ii)	236	118	22	64	440	655
Clark Manning(note iii)	567	1,177	24	—	1,768	929
Michael McLintock(note iv)	320	1,780	54	—	2,154	881
Nick Prettejohn(note v)	650	650	59	85	1,444	577
Barry Stowe(notes vi, vii)	550	337	182	138	1,207	—
Tidjane Thiam (from 25 March 2008)(notes viii, ix, x)	505	650	59	30	1,244	—
Mark Tucker	975	942	66	244	2,227	1,297
Total executive directors	3,803	5,654	466	561	10,484	4,339
Non-executive directors						
Sir Winfried Bischoff (from 2 August 2007)	63	—	—	—	63	—
Keki Dadiseth(note xi)	73	—	—	—	73	—
Michael Garrett	73	—	—	—	73	—
Ann Godbehere	81	—	—	—	81	—
Bridget Macaskill	86	—	—	—	86	—
Harvey McGrath (from 1 September 2008)(note xii)	167	—	—	—	167	—
Kathleen O'Donovan	108	—	—	—	108	—
James Ross	101	—	—	—	101	—
Lord Turnbull	81	—	—	—	81	—
Total non-executive directors	833	—	—	—	833	—
Overall total	5,174	5,654	509	695	12,032	4,339

* Benefits include, where provided, cash allowances for cars, the use of a car and driver, medical insurance, security arrangements, expatriate benefits.

† Pension supplements that are paid in cash are included in the table. The pension policy and pension arrangements for current executive directors are set out subsequently.

§ Value of anticipated LTIP releases is the total of cash paid plus, for shares released, the value of the released shares based on the share price at 31 December 2008. All executive directors participate in long-term incentive plans and the details of share releases from awards with a performance period ending 31 December 2008 are provided in the footnotes to the table on share awards. Executive directors' participation in all-employee plans are set out subsequently.

Notes

(i) Sir David Clementi was Chairman until 31 December 2008 and remained an employee until 31 January 2009.

(ii) Philip Broadley resigned in 2007. In view of his flexibility in agreeing a leaving date after the 2008 Annual General Meeting and for his agreement to act as a consultant for six months post his date of leaving, he was provided with the following:

- a total payment of £507,105 paid in two tranches in June and December 2008;
- medical insurance and life assurance cover for six months after his leaving date; and
- treatment as a 'good leaver' in respect of his outstanding share awards. The deferred share awards under his 2006 and 2007 annual incentive plans were released on his leaving. His outstanding long-term incentive awards will vest according to the rules of the plans in the same way as other recipients of awards, but pro-rated where appropriate for the time worked during the performance period.

All of these payments after June 2008 were subject to his continuing to be available for consultancy for six months after his leaving date and subject to his compliance with non-solicitation and confidentiality conditions.

(iii) Clark Manning's bonus figure excludes a contribution of US$13,800 from a profit sharing plan, which has been made into a 401K retirement plan. This is included in the table on pension contributions on in the section 'Directors' pensions and life assurances'.

(iv) In 2008 it was assumed that for Michael McLintock a deferred share award from the 2008 annual bonus valued at £640,000 would be made. This is included in the 2008 bonus figure.

(v) In 2008 it was assumed that for Nick Prettejohn a deferred share award from the 2008 annual bonus valued at £325,000 would be made. This is included in the 2008 bonus figure.

(vi) In 2008 it was assumed that for Barry Stowe a deferred share award from the 2008 annual bonus valued at £62,013 would be made. This is included in the 2008 bonus figure.

(vii) Barry Stowe's benefits primarily relate to his expatriate status including costs of £91,829 related to housing, £34,113 for children's education and £21,165 for home leave.

(viii) On appointment, Tidjane Thiam was provided with a guarantee that his 2008 bonus would not be less than 100% of salary.

(ix) In 2008 it was assumed that for Tidjane Thiam a deferred share award from the 2008 annual bonus valued at £325,000 would be made. This is included in the 2008 bonus figure.

(x) In addition to the 2008 bonus disclosed in the table above, Tidjane Thiam received a payment of £650,631 to compensate for the loss of 2007 bonus and in lieu of 2005 awards which were due to vest in March 2008.

(xi) Keki Dadiseth was paid allowances totalling £12,063 in 2008 in respect of his accommodation expenses in London whilst on the Company's business, in lieu of reimbursing hotel costs as is the usual practice for directors who are not resident in the UK.

(xii) Harvey McGrath joined Prudential on 1 September 2008 and became Chairman on 1 January 2009

(xiii) In aggregate, total fees paid to Directors amounted to £833,000 in 2008

	Salary/ fees	Bonus	Benefits*	Cash supplements for pension purposes	Other cash payments	Total Emoluments 2009	Value of anticipated releases from LTIPs in respect of performance periods ending 31 Dec 2009§
	2009 £000						
Chairman							
Harvey McGrath	500	—	42	—	—	542	—
Executive directors							
Rob Devey (from 16 November 2009)(note i)	69	600	138	1	—	808	—
Clark Manning(note ii)	696	2,028	29	—	—	2,753	1,223
Michael McLintock(note iii)	320	1,750	53	6	—	2,129	2,572
Nic Nicandrou (from 28 October 2009)(note iv)	98	550	5	1	—	654	—
Nick Prettejohn(note v)	488	505	40	63	607	1,703	763
Barry Stowe(note vi)	646	618	262	162	—	1,688	1,098
Tidjane Thiam(note vii)	763	1,056	49	87	—	1,955	—
Mark Tucker(note viii)	731	841	99	183	308	2,162	1,731
Total executive directors	3,811	7,948	675	503	915	13,852	7,387
Non-executive directors							
Sir Winfried Bischoff(note ix)	47	—	—	—	—	47	—
Keki Dadiseth(note x)	86	—	—	—	—	86	—
Michael Garrett	77	—	—	—	—	77	—
Ann Godbehere	94	—	—	—	—	94	—
Bridget Macaskill	89	—	—	—	—	89	—
Kathleen O'Donovan	109	—	—	—	—	109	—
James Ross	107	—	—	—	—	107	—
Lord Turnbull	87	—	—	—	—	87	—
Total non-executive directors	696	—	—	—	—	696	—
Overall total	5,007	7,948	717	503	915	15,090	7,387

* Benefits include where provided the use of a car and driver, medical insurance, security arrangements and expatriate benefits.

† Pension supplements that are paid in cash are included in the table. The policy on pensions is described in the section on 'Pensions and long-term savings policy'. The pension and long-term savings arrangements for current executive directors are described in the section on "Directors' pensions and life assurance".

§ Value of anticipated LTIP releases is the total of cash paid plus, for shares released, the value of the released shares based on the share price at 31 December 2009. All executive directors participate in long-term incentive plans and the details of share releases from awards with a performance period ending 31 December 2009 are provided in the footnote to the tables on share awards.

2009 figures include deferred share awards made from 2009 annual incentive plans which are detailed in the section "Other share awards".

(i) As part of Rob Devey's appointment terms, it was agreed that any bonus award for Rob would be assessed as if he had been in employment for the whole of 2009. A deferred share award from the 2009 annual bonus valued at £240,000 has been made to Rob. This is included in the 2009 bonus figure. Actual costs reimbursed to Rob as part of his relocation arrangements are included in the benefits figure. It should be noted that Rob elected not to receive his cash supplement for pension purposes in full during 2009. It is anticipated that the Company will make a request to the Trustees of the Alternative Retirement Benefit Scheme during 2010 to accept a contribution for an amount equivalent to this supplement.

(ii) Clark Manning's bonus figure excludes a contribution of $14,700 from a profit sharing plan which has been made into a 401K retirement plan. This is included in the table on pension contributions. A deferred share award from the 2009 annual bonus valued at $476,250 has been made to Clark. This is included in the 2009 bonus figure.

(iii) For Michael McLintock a deferred share award from the 2009 annual bonus valued at £625,000 was made. This is included in the 2009 bonus figure.

(iv) As part of Nic Nicandrou's appointment terms, it was agreed that any bonus award for Nic would be assessed as if Nic had been in employment for the whole of 2009. A deferred share award from the 2009 annual bonus valued at £220,000 was made to Nic. This is included in the 2009 bonus figure. Nic has not yet been reimbursed for any relocation expenses. It should be noted that Nic elected not to receive his cash supplement for pension purposes in full during 2009. It is anticipated that the Company will make a request to the Trustees of the Long Term Savings Plan during 2010 to accept a contribution for an amount equivalent to this supplement.

(v) Nick Prettejohn's 2009 annual bonus payment has been prorated for length of service during the year and is based on performance outcomes achieved at the end of 2009. This bonus was fully paid in cash in March 2010. The figure in the 'Other cash payments' column reflects a termination payment that was agreed as part of his leaving arrangements which was paid in instalments on 13 October 2009 and 11 January 2010.

(vi) For Barry Stowe a deferred share award from the 2009 annual bonus valued at HK$2,248,852 has been made. This is included in the 2009 bonus figure. Barry's benefits primarily relate to his expatriate status including costs of £148,051 for housing, £41,528 for children's education and £32,607 for home leave.

(vii) Tidjane Thiam's 2009 annual bonus outcome was determined taking into account the period of time he was remunerated as Chief Financial Officer and Group Chief Executive. For Tidjane, a deferred share award from the 2009 annual bonus valued at £528,137 has been made. This is included in the 2009 bonus figure.

(viii) As part of Mark Tucker's remuneration arrangements following his resignation from Prudential, it was agreed that his 2009 annual bonus payment would be prorated based on length of service during the year and paid at a target level of performance. The figure in the 'Other cash payments' column reflects a termination payment that was agreed as part of his leaving arrangements and paid on 11 January 2010.

(ix) Sir Winfried Bischoff left Prudential on 15 September 2009.

(x) Keki Dadiseth was paid allowances totalling £5,398 in 2009 in respect of his accommodation expenses in London whilst on the Company's business as is the usual practice for directors who are not resident in the UK.

(xi) In aggregate, total fees paid to Directors amounted to £696,000 in 2009.

Executive directors' non-executive director earnings

Executive directors who are released to serve as non-executive directors of other external companies retain the earnings resulting from such duties.

In 2007, Michael McLintock earned £48,542 from an external company. Other directors served as non-executive directors on the boards of companies in the educational and cultural sectors without receiving a fee for those services.

In 2008, Tidjane Thiam earned 27,000 euros and Michael McLintock earned £38,333 from external companies. Other directors served as non-executive directors on the boards of companies in the educational and cultural sectors without receiving a fee for those services.

In 2009, Tidjane Thiam earned 15,000 euros and Michael McLintock earned £42,500 from external companies. Tidjane Thiam no longer has any paid external non-executive directorships. Some directors also served as non-executive directors on the boards of companies in the educational and cultural sectors without receiving a fee for those services.

Directors' outstanding long-term incentive awards

Plan name	Year of initial award	Conditional share awards outstanding at 1 Jan 2007 (Number of shares)	Conditional awards in 2007 (Number of shares)	Market price at date of original award (pence)	Releases or rights (options) granted upon vesting in 2007 (Number of shares)	Conditional share awards outstanding at 31 Dec 2007 (Number of shares)	Conditional awards in 2008 (Number of shares)	Market price at date of original award (pence)	Releases or rights (options) granted upon vesting in 2008 (Number of Shares)	Rights exercised in 2008	Conditional share awards outstanding at 31 Dec 2008 (Number of shares)	Conditional awards in 2009 (Number of shares)	Market price at date of original award (pence)	Scrip dividend equivalents on vested shares (Number of shares released)	Rights exercised in 2009	Rights lapsed in 2009	Conditional share awards outstanding at 31 Dec 2009 (Number of shares)	Date of end of performance period
Philip Broadley																		
Restricted Share Plan	2004	210,713	—	—	—	—(1)	—	—	—	—	—	—	—	—	—	—	—	31 Dec 06
Restricted Share Plan	2005	182,983	—	—	—	182,983(2)	—	683.00	114,365	114,365	—(2)	—	—	—	—	—	—	31 Dec 07
Group Performance Share Plan	2006	170,127	—	—	—	170,127(3)	—	—	—	—	170,127(6)	—	—	—	—	—	—	31 Dec 08
Group Performance Share Plan	2007	—	147,559	745.00	—	147,559(4)	—	—	—	—	147,559	—	—	—	—	—	—	31 Dec 09
		563,823	147,559	—	—	500,669	—		114,365	114,365	317,686	—	—	—	—	—	—	
Rob Devey																		
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	120,898	639	—	—	—	120,898	31 Dec 11
Business Unit Performance Plan (share element)	2009	—	—	—	—	—	—	—	—	—	—	120,897	639	—	—	—	120,897	31 Dec 11
		—	—	—	—	—	—	—	—	—	—	241,795	—	—	—	—	241,795	
Clark Manning																		
Restricted Share Plan	2004	196,174	—	—	—	—(1)	—	—	—	—	—	—	—	—	—	—	—	31 Dec 06
Restricted Share Plan	2005	163,352	—	—	—	163,352(2)	—	683.00	102,095	102,095	—(2)	—	—	—	—	—	—	31 Dec 07
Group Performance Share Plan	2006	241,415	—	—	—	241,415(3)	—	—	—	—	241,415(6)	—	—	18,259	223,067	18,348	—	31 Dec 08
Business Unit Performance Plan (share element)	2006	120,707	—	—	—	120,707	—	—	—	—	120,707(7)	—	—	—	—	120,707	—	31 Dec 08
Group Performance Share Plan	2007	—	191,140	745.00	—	191,140(4)	—	—	—	—	191,140	—	—	—	—	—	191,140	31 Dec 09
Business Unit Performance Plan (share element)	2007	—	95,570	745.00	—	95,570	—	—	—	—	95,570	—	—	—	—	—	95,570	31 Dec 09
Group Performance Share Plan	2008	—	—	—	—	—	182,262	674.50	—	—	182,262	—	—	—	—	—	182,262	31 Dec 10
Business Unit Performance Plan (share element)	2008	—	—	—	—	—	91,131	674.50	—	—	91,131	—	—	—	—	—	91,131	31 Dec 10
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	468,476	455.5	—	—	—	468,476	31 Dec 11
Business Unit Performance Plan (share element)	2009	—	—	—	—	—	—	—	—	—	—	468,476	455.5	—	—	—	468,476	31 Dec 11
		721,648	286,710	—	—	812,184	273,393	—	102,095	102,095	922,225	936,952	—	18,259	223,067	139,055	1,497,055	
Nic Nicandrou																		
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	316,328	639	—	—	—	316,328	31 Dec 11
		—	—	—	—	—	—	—	—	—	—	316,328	—	—	—	—	316,328	
Michael McLintock																		
Restricted Share Plan	2004	67,429	—	—	—	—(1)	—	—	—	—	—	—	—	—	—	—	—	31 Dec 06
Restricted Share Plan	2005	58,555	—	—	—	58,555(2)	—	—	36,597	36,597	—(2)	—	—	—	—	—	—	31 Dec 07
Group Performance Share Plan	2006	64,199	—	—	—	64,199(3)	—	—	—	—	64,199(6)	—	—	4,852	59,319	4,880	—	31 Dec 08
Group Performance Share Plan	2007	—	52,040	745.00	—	52,040(4)	—	—	—	—	52,040	—	—	—	—	—	52,040	31 Dec 09
Group Performance Share Plan	2008	—	—	—	—	—	48,330	674.50	—	—	48,330	—	—	—	—	—	48,330	31 Dec 10
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	92,022	455.5	—	—	—	92,022	31 Dec 11
		190,183	52,040	—	—	174,794	48,330		36,597	36,597	164,569	92,022	—	4,852	59,319	4,880	192,392	

Plan name	Year of initial award	Conditional share awards outstanding at 1 Jan 2007 (Number of shares)	Conditional awards in 2007 (Number of shares)	Market price at date of original award (pence)	Releases or rights (options) granted upon vesting in 2007 (Number of shares)	Conditional share awards outstanding at 31 Dec 2007 (Number of shares)	Conditional awards in 2008 (Number of shares)	Market price at date of original award (pence)	Releases or rights (options) granted upon vesting in 2008 (Number of Shares)	Rights exercised in 2008	Conditional share awards outstanding at 31 Dec 2008 (Number of shares)	Conditional awards in 2009 (Number of shares)	Market price at date of original award (pence)	Scrip dividend equivalents on vested shares (Number of shares released)	Rights exercised in 2009	Rights lapsed in 2009	Conditional share awards outstanding at 31 Dec 2009 (Number of shares)	Date of end of performance period
Mark Norbom																		
Restricted Share Plan	2004	200,177	—	—	—	—[1]	—	—	—	—	—	—	—	—	—	—	—	31 Dec 06
Restricted Share Plan	2005	182,983	—	—	—	—[5]	—	—	—	—	—	—	—	—	—	—	—	31 Dec 07
Group Performance Share Plan	2006	144,648	—	—	—	—[5]	—	—	—	—	—	—	—	—	—	—	—	31 Dec 08
Business Unit Performance Plan (share element)	2006	72,324	—	—	—	—[5]	—	—	—	—	—	—	—	—	—	—	—	31 Dec 08
		600,132	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	
Nick Prettejohn																		
Group Performance Share Plan	2006	149,964	—	—	—	149,964[3]	—	—	—	—	149,964[6]	—	—	11,341	138,566	11,398	—	31 Dec 08
Business Unit Performance Plan (share element)	2006	74,982	—	—	—	74,982	—	—	—	—	74,982[7]	—	—	—	—	74,982	—	31 Dec 08
Group Performance Share Plan	2007	—	130,071	745.00	—	130,071[4]	—	—	—	—	130,071	—	—	—	—	—	130,071	31 Dec 09
Business Unit Performance Plan (share element)	2007	—	65,035	745.00	—	65,035	—	—	—	—	65,035	—	—	—	—	—	65,035	31 Dec 09
Group Performance Share Plan	2008	—	—	—	—		127,622	674.50	—	—	127,622	—	—	—	—	—	127,622	31 Dec 10
Business Unit Performance Plan (share element)	2008	—	—	—	—		63,811	674.50	—	—	63,811	—	—	—	—	—	63,811	31 Dec 10
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	242,997	455.5	—	—	—	242,997	31 Dec 11
Business Unit Performance Plan (share element)	2009	—	—	—	—	—	—	—	—	—	—	242,997	455.5	—	—	—	242,997	31 Dec 11
		224,946	195,106	—	—	420,052	191,433	—	—	—	611,485	485,994	—	11,341	138,566	86,380	872,533	
Barry Stowe																		
Group Performance Share Plan	2007	—	105,706	745.00	—	105,706[4]	—	—	—	—	105,706	—	—	—	—	—	105,706	31 Dec 09
Business Unit Performance Plan (share element)	2007	—	52,853	745.00	—	52,853	—	—	—	—	52,853	—	—	—	—	—	52,853	31 Dec 09
Group Performance Share Plan	2008	—	—	—	—	—	107,988	—	—	—	107,988	—	—	—	—	—	107,988	31 Dec 10
Business Unit Performance Plan (share element)	2008	—	—	—	—	—	53,994	—	—	—	53,994	—	—	—	—	—	53,994	31 Dec 10
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	196,596	455.5	—	—	—	196,596	31 Dec 11
Business Unit Performance Plan (share element)	2009	—	—	—	—	—	—	—	—	—	—	196,596	455.5	—	—	—	196,596	31 Dec 11
		—	158,559	—	—	158,559	161,982	—	—	—	320,541	393,192	—	—	—	—	713,733	
Tidjane Thiam																		
Group Performance Share Plan	2008	—	—	—	—	—	314,147	674.50	—	—	314,147[8]	—	—	—	—	—	314,147	31 Dec 10
Group Performance Share Plan	2009	—	—	—	—	—	—	—	—	—	—	299,074	455.5	—	—	—	299,074	31 Dec 11
		—	—	—	—	—	314,147	—	—	—	314,147	299,074	—	—	—	—	613,221	
Mark Tucker																		
Restricted Share Plan	2005	356,817	—	—	—	356,817[2]	—	683.00	223,011	—	223,011[2]	—	—	—	—	—	223,011	31 Dec 07
Group Performance Share Plan	2006	337,044	—	—	—	337,044[3]	—	—	—	—	337,044[6]	—	—	25,493	311,428	25,616	—	31 Dec 08
Group Performance Share Plan	2007	—	295,067	745.00	—	295,067[4]	—	—	—	—	295,067	—	—	—	—	—	295,067	31 Dec 09
Group Performance Share Plan	2008	—	—	—	—	—	294,512	674.50	—	—	294,512	—	—	—	—	—	294,512	31 Dec 10
		693,861	295,067	—	—	988,928	294,512	—	223,011	—	1,149,634	—	—	25,493	311,428	25,616	812,590	

Cash rights granted under the Business Unit Performance Plan

Plan name	Year of initial award	Conditional awards outstanding at 1 Jan 2007	Conditional awards in 2007	Payments made in 2007	Conditional awards outstanding at 31 Dec 2007	Conditional awards in 2008	Payments made in 2008	Conditional awards outstanding at 31 Dec 2008	Conditional awards in 2009	Cash rights lapsed in 2009	Conditional awards outstanding at 31 Dec 2009	Date of end of performance period
		£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	
Clark Manning												
Business Unit Performance Plan (Cash element)	2006	577	—	—	577	—	—	577[7]	—	577	—	31 Dec 08
Business Unit Performance Plan (Cash element)	2007	—	624	—	624	—	—	624	—	—	624	31 Dec 09
Business Unit Performance Plan (Cash element)	2008	—	—	—	—	652	—	652	—	—	652	31 Dec 10
Mark Norbom												
Business Unit Performance Plan (Cash element)	2006	361	—	—	—[5]	—	—	—	—	—	—	31 Dec 08
Nick Prettejohn												
Business Unit Performance Plan (Cash element)	2006	374	—	—	374	—	—	374[7]	—	374	—	31 Dec 08
Business Unit Performance Plan (Cash element)	2007	—	400	—	400	—	—	400	—	—	400	31 Dec 09
Business Unit Performance Plan (Cash element)	2008	—	—	—	—	423	—	423	—	—	423	31 Dec 10
Barry Stowe												
Business Unit Performance Plan (Cash element)	2007	—	325	—	325	—	—	325	—	—	325	31 Dec 09
Business Unit Performance Plan (Cash element)	2008	—	—	—	—	358	—	358	—	—	358	31 Dec 10

Notes

2007

Performance levels under current awards at 31 December 2007:

Note	Plan	Award Year	Performance Levels
1	Restricted Share Plan	2004	The ranking of the Company's TSR was ranked at 56th percentile at the end of the three-year performance period ending on 31 December 2006 and as a result the 2004 awards lapsed.
2	Restricted Share Plan	2005	The ranking of the Company's TSR at the end of the three-year performance period ending on 31 December 2007 was 30th out of the remaining 85 companies in the FTSE 100 (35th percentile) and as a result it is anticipated that options over 62.5% of the maximum number of shares in each award was made in 2008 would result in nil cost options over 114,365 shares for Philip Broadley, 102,095 shares for Clark Manning, 36,597 shares for Michael McLintock and 223,011 shares for Mark Tucker.
3	Group Performance Share Plan	2006	At 31 December 2007 Prudential's TSR performance was 121.4% of the TSR performance of the index. At this performance level, 100% of the maximum award would vest.
4	Group Performance Share Plan	2007	At 31 December 2007 Prudential's TSR performance was 113.1% of the TSR performance of the index. At this performance level, 84% of the maximum award would vest.
5	Mark Norbom		The 2005 RSP, 2006 GPSP and the 2006 BUPP awards for Mark Norbom lapsed on the termination of his employment.

2008

Performance levels under current awards at 31 December 2008:

Note	Plan	Award Year	Performance Levels
6	Group Performance Share Plan	2006	At 31 December 2008 Prudential's TSR performance was 117% of the TSR performance of the index. As a result, it is anticipated that awards over 92.4% of the maximum number of shares will be earned, resulting in 311,428 shares for Mark Tucker, 157,197 shares for Philip Broadley, 223,067 shares for Clark Manning, 59,319 shares for Michael McLintock, and 138,566 shares for Nick Prettejohn.
7	Business Unit Performance Share Plans.	2006	At 31 December 2008 Shareholder Capital Value performance under the 2006 BUPPs was as follows:
8	Tidjane Thiam		For 2008 as part of the terms of appointment, a double award under the Group Performance Share Plan of 320% of salary was made to Tidjane Thiam.

Note 7 (2006 BUPPs):

	% growth SCV	Anticipated payout
Jackson	6.1	nil
UK	1.2	nil

2009

Performance levels under current awards at 31 December 2009:

Note	Plan	Award Year	Performance Levels
9	Group Performance Share Plan	2007	At 31 December 2009 Prudential's TSR performance was 143.72% of the TSR performance of the index. Hence it is anticipated that awards granted under this scheme in 2007 will vest in full. This results in 270,478 shares for Mark Tucker; 191,140 shares for Clark Manning; 52,040 shares for Michael McLintock; 119,231 shares for Nick Prettejohn and 105,706 shares for Barry Stowe. In accordance with the plan rules, the anticipated number of shares released for Mark Tucker and Nick Prettejohn as a result of their resignation from Prudential will be prorated accordingly.
10	Business Unit Performance Share Plans	2007	At 31 December 2009, Shareholder Capital Value performance under the 2007 BUPPs was as follows:

	% compound in growth in SCV	No. of shares released from 2007 BUPP share award	Anticipated value of 2007 BUPP cash award release
Jackson	4.1%	nil	nil
UK	0.3%	nil	nil
Asia	20.6%	33,615	£206,700

Note	Plan	Award Year	Performance Levels
11	Group Performance Share Plan and Business Unit Performance Share Plans	2009	2009 awards made under the Group Performance Share Plan and the Business Unit Performance Share Plans have a performance period from 1 January 2009 to 31 December 2011. In determining the 2009 conditional share awards the shares were valued at the average share price for the 30 days immediately following the announcement of Prudential's 2008 results, and the price used to determine the number of shares was 347.74 pence. The awards for Clark Manning and Barry Stowe were made in ADRs (one ADR is equivalent to approximately two Prudential plc shares or $10.31). The figures in the table are represented in terms of Prudential shares.

(i) Restricted Share Plan awards

For RSP awards in 2005, no rights were granted if Prudential's TSR performance as ranked against the comparator group (those companies remaining out of the FTSE 100 at the beginning of the performance period) was at the 50th percentile or below. The maximum grant is made only if the TSR ranking of the Company is 20th percentile or above. Between these points, the size of the grant made is calculated on a straight line sliding scale. In normal circumstances, directors may take up their right to receive shares at any time during the following seven years

Rights which were exercised from options granted from 2005 Restricted Share Plan awards during 2008 are set out in the following table:

	Year of option grant	RSP rights outstanding at 1 Jan 2008	Rights granted during 2008 (Number of shares)	Rights exercised during 2008 (Number of shares)	Rights outstanding at 31 Dec 2008 (pence)	Price paid for the award	Exercise price (pence)	Market price on date of exercise (pence)	Earliest exercise date	Latest exercise date exercise
Philip Broadley . . .	2008	—	114,365	114,365	—	—	nil	539.5	17 April 2008	04 April 2015
Clark Manning . . .	2008	—	102,095	102,095	—	—	nil	647.5	17 April 2008	04 April 2015
Michael McLintock	2008	—	36,597	36,597	—	—	nil	377.0	17 April 2008	04 April 2015

(ii) Awards

The awards made under the Group Performance Share Plan and the Business Unit Performance Plan in respect of 2007 have a performance period from 1 January 2007 to 31 December 2009.

In determining the 2007 conditional share awards the shares were valued at their average share price during the preceding calendar year, and the price used to determine the number of shares was 614.91 pence.

The 2008 awards made under the Group Performance Share Plan and the Business Unit Performance Plan in respect of 2008 have a performance period from 1 January 2008 to 31 December 2010.

In determining the 2008 conditional share awards the shares were valued at the average share price for the 30 days immediately following the announcement of Prudential's 2007 results, and the price used to determine the number of shares was 662.11 pence.

2009 awards made under the Group Performance Share Plan and the Business Unit Performance have a performance period from 1 January to 31 December 2011.

In determining the 2009 conditional share awards the shares were valued at the average share price for the 30 days immediately following the announcement of Prudential's 2008 results, and the price used to determine the number of shares was 347.74 pence.

(iii) Group Performance Share Plan (Group PSP) — all executive directors

Awards under the Group Performance Share Plan are based on Prudential's Total Shareholder Return compared with the TSR performance of its competitors.

Business specific cash based long term incentive plans

Plan name	Year of initial award	Face Value of conditional awards outstanding at 1 Jan 2007	Conditionally awarded in 2007	Payments made in 2007	Face value of conditional awards outstanding at 31 Dec 2007	Conditionally awarded in 2008	Payments made in 2008	Face value of conditional awards outstanding at 31 Dec 2008	Conditionally awarded in 2009	Payments made in 2009	Face value of conditional awards outstanding at 31 Dec 2009	Date of end of performance period
		£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	
Clark Manning												
Business Cash LTIP	2004	1,295	—	2,013	**—**	—	—	**—**	—	—	**—**	31 Dec 06
Business Cash LTIP	2005	1,295	—	—	**1,295**	—	2,385	**—**	—	—	**—**	31 Dec 07
Michael McLintock												
Phantom M&G options	2000	184	—	403	**—**	—	—	**—**	—	—	**—**	31 Dec 02
Phantom M&G options	2001	368	—	—	**368**	—	846	**—**	—	—	**—**	31 Dec 03
Phantom M&G options	2002	368	—	—	**368**	—	1,306	**—**	—	—	**—**	31 Dec 04
Phantom M&G options	2003	368	—	—	**368**	—	850	**—**	—	—	**—**	31 Dec 05
Phantom M&G options	2004	368	—	—	**368**	—	780	**—**	—	—	**—**	31 Dec 06
Phantom M&G shares	2004	225	—	583	**—**	—	—	**—**	—	—	**—**	31 Dec 06
Phantom M&G options	2005	368	—	—	**368**	—	—	**368**	—	394	**—**	31 Dec 07
Phantom M&G shares	2005	225	—	—	**225**	—	527	**—**	—	—	**—**	31 Dec 07
Phantom M&G options	2006	368	—	—	**368**	—	—	**368**	—	254	**—**	31 Dec 08
Phantom M&G shares	2006	225	—	—	**225**	—	—	**225**	—	380	**—**	31 Dec 08
Phantom M&G shares	2007	—	1,333	—	**1,333**	—	—	**1,333**	—	—	**1,333**	31 Dec 09
M&G Executive LTIP	2008	—	—	—	**—**	1,141	—	**1,141**	—	—	**1,141**	31 Dec 10
M&G Executive LTIP	2009	—	—	—	**—**	—	—	**—**	1,830	—	**1,830**	31 Dec 11
Mark Norbom												
Business Cash LTIP	2004	713		413	**—**	—	—	**—**	—	—	**—**	31 Dec 06
Business Cash LTIP	2005	750			**—**	—	—	**—**	—	—	**—**	31 Dec 07
Total cash payments				**3,412**			**6,694**			**1,028**		

2007

Clark Manning

In 2004 and 2005 Clark Manning participated in a cash-based long-term plan that rewards the growth in appraisal value of Jackson. The award payout equals an initial award value adjusted by the change in the Prudential plc share price over the performance period. In order for any award to be made under the 2005 plan, the growth rate over the performance period must be greater or equal to 8% compound growth per annum. At this level of performance, the initial award value is US$864,240. If the on-target performance level of 11.5% per annum compound is achieved the initial award value is doubled. If the annual growth rate is at least 17.5%, the payout increases to a maximum of three times the initial award value. For performance between these points, payouts are on a straight line sliding scale.

For the 2004 award the results led to a payment of US$4,028,896. The face values of the awards for Clark Manning are converted at the average exchange rate for 2007 which was US$2.0015 = £1. For the 2005 Business Cash LTIP, the compound annual growth rate in appraisal value was 22.8% and as a result a payment of US$4,416,308 was made.

Michael McLintock

Michael McLintock's 2004, 2005 and 2006 cash long-term incentive awards were under the M&G Chief Executive Long-Term Incentive Plan that provides a cash reward through phantom M&G share awards and options. For these awards, the phantom share price at the beginning of the performance period was £1. The change in the phantom share price equals the change in M&G profit, modified up or down by the investment performance of M&G, over the performance period. For each year the face value of the share award was £225,000 and the phantom option award had a face value of £367,800. Provided the phantom share options have value, they may be exercised in part or in full during annual exercise periods (three to seven years from the start of the performance period).

For the 2004 award the phantom share price at the end of the performance period was £2.59. This resulted in a payment from the phantom share award of £582,750 and a phantom option award of 367,800 units. Michael McLintock did not exercise any of these options. For the 2005 award, the phantom share price at the end of the performance period was £2.34. This will result in a payment of £526,500 from the share element of the award.

Under the rules of Michael McLintock's 2000 phantom option award, a payment of £402,741 was made at the end of the seven-year exercise period. Following consultations with shareholders an award with a face value of £1,333,000 was made in 2007 under the share element of the M&G Chief Executive Long-Term Incentive Plan.

Mark Norbom

Mark Norbom's awards under the Business Cash LTIP for 2004 vested as a result of Asia's performance and a payment of £412,751 was made in 2007. On the termination of his employment his award under the 2005 Business Cash LTIP lapsed.

2008

Clark Manning

In 2005 Clark Manning participated in a cash-based long-term plan that rewards the growth in appraisal value of Jackson. The award payout equals an initial award value adjusted by the change in the Prudential plc share price over the performance period. In order for any award to be made under the 2005 plan, the growth rate over the performance period must be greater or equal to 8% compound growth per annum. At this level of performance, the initial award value is US$864,240. If the on-target performance level of 11.5% per annum compound is achieved the initial award value is doubled. If the annual growth rate is at least 17.5%, the payout increases to a maximum of three times the initial award value. For performance between these points, payouts are on a straight line sliding scale.

For the 2005 award the results led to a payment of US$4,416,308. The face values of the awards for Clark Manning have been converted at the average exchange rate for 2008 which was US$1.8518 = £1.

Michael McLintock

Michael McLintock's 2005 and 2006 cash long-term incentive awards were under the M&G Chief Executive Long-Term Incentive Plan that provides a cash reward through phantom M&G share awards and options. For these awards, the phantom share price at the beginning of the performance period was £1. The change in the phantom share price equals the change in M&G profit, modified up or down by the investment performance of M&G, over the performance period. For each year the face value of the share award was £225,000 and the phantom option award had a face value of £367,800. Provided the phantom share options have value, they may be exercised in part or in full during annual exercise periods after three to seven years from the start of the performance period.

For the 2005 award the phantom share price at the end of the performance period was £2.34. This resulted in a payment from the phantom share award of £526,500 and a phantom option award of 367,800 units. Michael McLintock did not exercise any of these options. For the 2006 award, the phantom share price at the end of the performance period was £1.69. This will result in a payment of £380,250 from the share element of the award.

Under the rules of Michael McLintock's 2001 phantom option award, a payment of £845,940 was made at the end of the seven year exercise period. An award under the share element of the M&G Chief Executive Long-Term Incentive Plan with a face value of £1,333,000 was made in 2007. Following consultations with shareholders an award with a face value of £1,141,176 was made in 2008 under the M&G Executive Long-Term Incentive Plan, approved by shareholders at the AGM in 2008.

2009

Michael McLintock

For the 2005 phantom option award of 367,800 units, the option price at the end of the performance period was £1.07. This resulted in a payment of £393,546 to Michael McLintock. For the 2006 award, the phantom share price at the end of the performance period was £1.69 and the phantom option price was £0.69. This resulted in a payment from the phantom share award of £380,250 and the phantom option award of £253,782.

The 2008 Directors' Remuneration Report stated that an award of 2,282,353 phantom shares of £1 with an anticipated value of £1,940,000 was made in 2009. Following a re-evaluation of the per unit expected value calculation, the number of units required to deliver this anticipated value has been reduced to 1,830,189. The anticipated value of this award remains unchanged.

Other Share Awards

The table below sets out the share awards that have been made to executive directors under their appointment terms and those deferred from annual incentive plan payouts. The values of the deferred share awards are included in the bonus and total figures in the Directors' remuneration table presented previously. The number of shares is calculated using the average share price over the three business days commencing on the day of the announcement of the Prudential Group's annual financial results for the relevant year.

2007

For the awards from the 2006 annual incentives, made in 2007, the average share price was 681.50 pence.

	Year of initial grant	Conditional share awards outstanding at 1 Jan 2007 (Number of shares)	Conditionally awarded in 2007 (Number of shares)	Scrip dividends accumulated (Number of shares)	Shares released in 2007 (Number of shares)	Conditional Share awards outstanding at 31 Dec 2007 (Number of shares)	Date of end of restricted period	Shares released in 2007 (Number of shares)	Date of release	Market price at original date of award (pence)	Market price at date of vesting or release (pence)
Philip Broadley											
Deferred 2003 annual bonus award	2004	6,387	—	—	6,387	—	31 Dec 06	6,387	15 Mar 07	502	675
Deferred 2005 annual bonus award[note 1]	2006	31,954	—	789	—	32,743[1,2]	31 Dec 08	—	—	—	—
Deferred 2006 annual bonus award[note 1]	2007	—	31,100	768	—	31,686[1,2]	31 Dec 09	—	—	—	—
Clark Manning											
Deferred 2006 annual bonus award[note 1]	2007	—	9,100	224	—	9,324[1,3]	31 Dec 09	—	—	—	—
Michael McLintock											
Deferred 2003 annual bonus award	2004	57,121	—	—	57,121	—	31 Dec 06	57,121	15 Mar 07	502	675
Deferred 2004 annual bonus award	2005	93,750	—	2,317	96,067	—	31 Dec 07	96,067	31 Dec 07	475	712
Deferred 2005 annual bonus award[note 1]	2006	84,779	—	2,095	—	86,874[1]	31 Dec 08	—	—	—	—
Deferred 2006 annual bonus award[note 1]	2007	—	81,438	2,012	—	83,450[1,4]	31 Dec 09	—	—	—	—
Mark Norbom											
Awards under appointment terms[note 7]	2004	89,353	—	—	89,353	—[7]	01 Jan 07	89,353	02 Feb 07	439	705.5
		31,596	—	—	—	—[7]	01 Jan 08	—	—	—	—
		15,339	—	—	—	—[7]	01 Jan 09	—	—	—	—
		414,826	—	—	87,403	—[7]	20 Feb 13	87,403	28 Feb 07	439	673.5
Deferred 2004 annual bonus award[note 1]	2005	33,965	—	—	33,965	—[7]	31 Dec 07	33,965	08 Feb 07	475	715
Deferred 2005 annual bonus award[note 1]	2006	18,306	—	—	18,306	—[7]	31 Dec 08	18,306	08 Feb 07	715.5	715
Nick Prettejohn											
Awards under appointment terms[note 8]	2006	16,000	—	—	16,000	—	31 Oct 07	16,000	31 Oct 07	627.5	712
		5,500	—	—	—	5,500	31 Oct 08	—	—	—	—
Deferred 2006 annual bonus award[note 1]	2007	—	11,837	291	—	12,128[1,5]	31 Dec 09	—	—	—	—
Barry Stowe											
Awards under appointment terms[note 9]	2006	7,088	—	—	7,088	—	01 May 07	7,088	01 May 07	702	746
		7,088	—	—	—	7,088	01 May 08	—	—	—	—
		7,088	—	—	—	7,088	01 May 09	—	—	—	—
		28,706	—	—	—	28,706	01 Sept 09	—	—	—	—
		7,088	—	—	—	7,088	01 Jan 10	—	—	—	—
		2,110	—	—	—	2,110	01 May 10	—	—	—	—
Mark Tucker											
Deferred 2005 annual bonus award[note 1]	2006	37,206	—	919	—	38,125[1]	31 Dec 08	—	—	—	—
Deferred 2006 annual bonus award[note 1]	2007	—	72,302	1,786	—	74,088[1,6]	31 Dec 09	—	—	—	—

Notes

(1) Under the annual bonus plans, the element of bonus for performance above specified levels are made in the form of a share award deferred for three years.

(2) In 2007, a deferred share award from his 2006 annual bonus valued at £211,947 was made to Philip Broadley. This was included in the 2006 total Directors' remuneration. Under the terms agreed on his leaving the Company, the outstanding deferred awards to Philip Broadley were released after his termination date.

(3) In 2007, a deferred share award from his 2006 annual bonus valued at US$121,360 was made to Clark Manning. This was included in the 2006 Directors' remuneration. The exchange rate used was US$1.8430 = £1.

(4) In 2007, a deferred share award from his 2006 annual bonus valued at £555,000 was made to Michael McLintock. This was included in the 2006 Directors' remuneration.

(5) In 2007, a deferred share award from his 2006 annual bonus valued at £80,673 was made to Nick Prettejohn. This was included in the 2006 Directors' remuneration.

(6) In 2007, a deferred share award from his 2006 annual bonus valued at £492,744 was made to Mark Tucker. This was included in the 2006 Directors' remuneration.

(7) Mark Norbom's deferred shares under the 2004 Annual Incentive Plan (33,965 shares) and 2005 Annual Incentive Plan (18,306 shares) were released to him in February 2007. In addition, the 89,353 employer replacement shares which vested on 1 January 2007 were released and the Remuneration Committee exercised its discretion to allow a further 87,403 shares out of his awards under the appointment terms to vest, representing the proportion of the performance period which Mark Norbom had worked in respect of his pension replacement shares. Awards over 374,358 shares granted under the terms of Mark Norbom's appointment lapsed.

(8) In order to secure the appointment of Nick Prettejohn, he was awarded rights to Prudential plc shares that vest as set out in the table. In normal circumstances, releases are conditional on Nick Prettejohn being employed by Prudential at the date of vesting. If there is a change of control of Prudential he may be entitled to retain any unvested awards.

(9) In order to secure the appointment of Barry Stowe and to compensate him for the loss of substantial amounts of outstanding long-term remuneration, he was awarded rights to Prudential plc American Depositary Receipts, that vest as set out in the table. The figures in the table are the equivalent number of Prudential plc shares (one American Depositary Receipt equals two Prudential plc shares). In normal circumstances, releases are conditional on Barry Stowe being employed by Prudential at the date of vesting. If there is a change of control of Prudential he may be entitled to retain any unvested awards.

In order to compensate for the loss of share options, Barry Stowe was also awarded 1,255 Prudential plc ADRs in 2007.

2008

For the awards from the 2007 annual incentives, made in 2008, the average share price was 618.50 pence.

	Year of initial grant	Conditional share awards outstanding at 1 Jan 2008 (Number of shares)	Conditionally awarded in 2008 (Number of shares)	Scrip dividends accumulated (Number of shares)	Shares released in 2008 (Number of shares)	Conditional share awards outstanding at 31 Dec 2008 (Number of shares)	Date of end of restricted period	Shares released in 2008 (Number of shares)	Date of release	Market price at original date of award (pence)	Market price at date of vesting or release (pence)
Philip Broadley											
Deferred 2005 annual bonus award[note 1]	2006	32,743	—	606	33,349	—[1,2]	31 Dec 08	33,349	21 Aug 08	715.5	506.5
Deferred 2006 annual bonus award[note 1]	2007	31,868	—	590	32,452	—[1,2]	31 Dec 09	32,458	21 Aug 08	723	506.5
Clark Manning											
Deferred 2006 annual bonus award[note 1]	2007	9,324	—	276	—	9,600[1,3]	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award[note 1]	2008	—	16,514	489	—	17,003[1]	31 Dec 10	—	—	—	—
Michael McLintock											
Deferred 2005 annual bonus award[note 1]	2006	86,874	—	2,580	89,454	—[1]	31 Dec 08	89,454	31 Dec 08	715.5	416.5
Deferred 2006 annual bonus award[note 1]	2007	83,450	—	2,479	—	85,929[1,4]	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award[note 1]	2008	—	103,811	3,084	—	106,895	31 Dec 10	—	—	—	—
Nick Prettejohn											
Awards under appointment terms[note 8]	2006	5,500	—	—	5,500	—	31 Oct 08	5,500	31 Oct 08	627.5	315
Deferred 2006 annual bonus award[note 1]	2007	12,128	—	359	—	12,487	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award[note 1]	2008	—	49,898	1,482	—	51,380[1,5]	31 Dec 10	—	—	—	—
Barry Stowe											
Awards under appointment terms[note 9]	2006	7,088	—	—	7,088	—	01 May 08	7,088	01 May 08	702	697
		7,088	—	—	—	7,088	01 May 09	—	—	—	—
		28,706	—	—	—	28,706	01 Sep 09	—	—	—	—
		7,088	—	—	—	7,088	01 Jan 10	—	—	—	—
		2,110	—	—	—	2,110	01 May 10	—	—	—	—
Deferred 2007 annual bonus award[note 1]	2008	—	40,551	1,204	—	41,755[1,6]	31 Dec 10	—	—	—	—
Tidjane Thiam											
Awards under appointment terms[note 10]	2008	—	16,336	—	—	16,336	31 Mar 09	—	—	—	—
		—	41,148	—	—	41,148	31 Mar 09	—	—	—	—
		—	48,362	—	—	48,362	31 Mar 10	—	—	—	—
		—	41,135	—	—	41,135	31 Mar 10	—	—	—	—
		—	49,131	—	—	49,131	31 Mar 11	—	—	—	—
Mark Tucker											
Deferred 2005 annual bonus award	2006	38,125	—	1,132	39,257	—[1]	31 Dec 08	39,257	31 Dec 08	715.5	416.5
Deferred 2006 annual bonus award[note 1]	2007	74,088	—	2,200	—	76,288[1,7]	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award[note 1]	2008	—	73,576	2,185	—	75,761[1,7]	31 Dec 10	—	—	—	—

Notes

(1) Under the annual bonus plans, the element of bonus for performance above specified levels are made in the form of a share award deferred for three years. The value of the 2007 deferred share award is included in the total 2007 figure in the Directors' remuneration summary table.

(2) Under the terms agreed on his leaving Prudential, the outstanding deferred awards to Philip Broadley have been released to him.

(3) In 2008, a deferred share award from his 2007 annual bonus valued at US$200,000 was made to Clark Manning. This is included in the 2007 total in the Directors' remuneration summary table. The exchange rate used was US$2.0015 = £1.

(4) In 2008, a deferred share award from his 2007 annual bonus valued at £640,000 was made to Michael McLintock. This is included in the 2007 total in the Directors' remuneration summary table.

(5) In 2008, a deferred share award from his 2007 annual bonus valued at £307,625 was made to Nick Prettejohn. This is included in the 2007 total in the Directors' remuneration summary table.

(6) In 2008, a deferred share award from his 2007 annual bonus valued at £250,000 was made to Barry Stowe. This is included in the 2007 total in the Directors' remuneration summary table.

(7) In 2008, a deferred share award from his 2007 annual bonus valued at £453,600 was made to Mark Tucker. This is included in the 2007 total in the Directors' remuneration summary table.

(8) In order to secure the appointment of Nick Prettejohn, he was awarded rights to Prudential plc shares that vest as set out in the table. In normal circumstances, releases are conditional on Nick Prettejohn being employed by Prudential at the date of vesting. If there is a change of control of Prudential he may be entitled to retain any unvested awards.

(9) In order to secure the appointment of Barry Stowe and to compensate him for the loss of substantial amounts of outstanding long-term remuneration, he was awarded rights to Prudential plc American Depositary Receipts, which vest as set out in the table. The figures in the table are the equivalent number of Prudential plc shares (one American Depositary Receipt equals two Prudential plc shares). In normal circumstances, releases are conditional on Barry Stowe being employed by Prudential at the date of vesting. If there is a change of control of Prudential he may be entitled to retain any unvested awards.

(10) In order to secure the appointment of Tidjane Thiam, the following awards were made

- to compensate for the loss of 2007 bonus an award of 49,131 shares with a value of £325,000 vesting on 31 March 2011; and
- In order to compensate for the loss of outstanding deferred share awards under annual incentive plans and long-term awards with his previous employer he was granted restricted share awards, in lieu of his 2006 and 2007 awards, without performance measures which will vest in March 2009 and 2010, respectively. These awards were valued taking the relative share prices of his previous employer on the day prior to his last working day and Prudential on his first working day.

2009

For the awards from the 2008 annual incentives, made in 2009, the average share price was 308.63 pence.

	Year of initial grant	Conditional share awards outstanding at 1 Jan 2009 (Number of shares)	Conditionally awarded in 2009 (Number of shares)	Scrip dividends accumulated (Number of shares)	Shares released in 2009 (Number of shares)	Conditional share awards outstanding at 31 Dec 2009 (Number of shares)	Date of end of restricted period	Shares released in 2009 (Number Of shares)	Date of release	Market price at original date of award (pence)	Market price at date of vesting or release (pence)
Rob Devey(note 2)											
Awards under appointment terms	2009	—	50,575	—	—	50,575	31 Mar 12	—	—	—	—
Clark Manning											
Deferred 2006 annual bonus award	2007	9,600	—	464	—	10,064	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award	2008	17,003	—	822	—	17,825	31 Dec 10	—	—	—	—
Michael McLintock											
Deferred 2006 annual bonus award	2007	85,929	—	4,161	—	90,090	31 Dec 09	—	—	—	—
Deferred 2007 annual bonus award	2008	106,895	—	5,176	—	112,071	31 Dec 10	—	—	—	—
Deferred 2008 annual bonus award	2009	—	207,368	10,042	—	217,410	31 Dec 11	—	—	—	—
Nick Prettejohn(note 3)											
Deferred 2006 annual bonus award	2007	12,487	—	604	13,091	—	31 Dec 09	13,091	1 Oct 09	723	592
Deferred 2007 annual bonus award	2008	51,380	—	2,488	53,868	—	31 Dec 10	53,868	1 Oct 09	635	592
Deferred 2008 annual bonus award(note 1)	2009	—	105,304	5,099	110,403	—	31 Dec 11	110,403	1 Oct 09	349.5	592
Nic Nicandrou(note 4)											
Awards under appointment terms	2009	—	10,616	—	—	10,616	31 Mar 10	—	—	—	—
		—	5,889	—	—	5,889	31 Mar 10	—	—	—	—
		—	13,898	—	—	13,898	31 Mar 11	—	—	—	—
		—	16,059	—	—	16,059	31 Mar 11	—	—	—	—
		—	68,191	—	—	68,191	31 Mar 12	—	—	—	—
Barry Stowe											
Awards under appointment terms	2006	7,088	—	—	7,088	—	1 May 09	7,088	15 May 09	702	437
		28,706	—	—	28,706	—	1 Sep 09	28,706	1 Sep 09	702	525.5
		7,088	—	—	—	7,088	1 Jan 10	—	—	—	—
		2,110	—	—	—	2,110	1 May 10	—	—	—	—
Deferred 2007 annual bonus award	2008	41,755	—	2,022	—	43,777	31 Dec 10	—	—	—	—
Deferred 2008 annual bonus award(note 1)	2009	—	20,092	972	—	21,064	31 Dec 11	—	—	—	—
Tidjane Thiam											
Awards under appointment terms	2008	16,336	—	—	16,336	—	31 Mar 09	16,336	31 Mar 09	662	337
		41,148	—	—	41,148	—	31 Mar 09	41,148	31 Mar 09	662	337
		48,362	—	—	—	48,362	31 Mar 10	—	—	—	—
		41,135	—	—	—	41,135	31 Mar 10	—	—	—	—
		49,131	—	—	—	49,131	31 Mar 11	—	—	—	—
Deferred 2008 annual bonus award(note 1)	2009	—	105,304	5,099	—	110,403	31 Dec 11	—	—	—	—
Mark Tucker(note 5)											
Deferred 2006 annual bonus award	2007	76,288	—	3,694	79,982	—	31 Dec 09	79,982	1 Oct 09	723	592
Deferred 2007 annual bonus award	2008	75,761	—	3,669	79,430	—	31 Dec 10	79,430	1 Oct 09	635	592

Notes:

(1) Under the annual bonus plans, the element of bonus for performance above specified levels are made in the form of a share award deferred for three years. The value of the 2008 deferred share award is included in the total 2008 figure in the Directors' remuneration summary table.

(2) In order to secure the appointment of Rob Devey and to compensate him for the loss of outstanding long-term remuneration, Rob was awarded rights to Prudential shares as set out in the table.

(3) Under the terms agreed on his leaving Prudential, the outstanding deferred awards to Nick Prettlejohn have been released to him.

(4) In order to secure the appointment of Nic Nicandrou and to compensate him for the loss of outstanding long-term remuneration, Nic was awarded rights to Prudential shares as set out in the table.

(5) Under the terms agreed on his leaving Prudential, the outstanding deferred awards to Mark Tucker have been released to him.

Outstanding share options

Options outstanding under the Savings-Related Share Option (SAYE) scheme are set out below. The SAYE is open to all UK and certain overseas employees. Options under this scheme up to HMRC limits are granted at a 20% discount and cannot normally be exercised until a minimum of three years has elapsed. No payment has been made for the grant of any options. The price to be paid for exercise of these options is shown in the table below. No variations to any outstanding options have been made.

2007

	Year of initial grant	Option outstanding at 1 Jan 2007	Exercised in 2007	Market price on exercise date (pence)	Options forfeit in 2007	Options granted in 2007	Options outstanding at 31 Dec 2007	Market price at 31 Dec 2007 (pence)	Original exercise price (pence)	Exercise price adjusted for 2004 Rights issue (pence)	Earliest exercise date	Latest exercise date
Philip Broadley	2000	2,716	2,716	763.5	—	—	—	—	364	346	01 Jun 07	30 Nov 07
Michael McLintock	2003	6,153	—	—	—	—	6,153	712	280	266	01 Jun 08	30 Nov 08
Nick Prettejohn	2006	661	—	—	—	—	661	712	565	n/a	01 Jun 09	30 Nov 09
Mark Tucker	2005	2,297	—	—	—	—	2,297	712	407	n/a	01 Dec 08	31 May 09

Notes:

(1) Gains of £11,339 were made by directors in 2007 on the exercise of share options.

(2) No price was paid for the award of any option.

(3) The highest and lowest share prices during 2007 were 811 pence and 618 pence respectively.

2008

	Year of initial grant	Option outstanding at 1 Jan 2008	Exercised in 2008	Market price on exercise date (pence)	Options forfeit in 2008	Options granted in 2008	Options outstanding at 31 Dec 2008	Market price at 31 Dec 2008 (pence)	Original exercise price (pence)	Exercise price adjusted for 2004 Rights issue (pence)	Earliest exercise date	Latest exercise date
Michael McLintock	2003	6,153	6,153	517.5	—	—	—	416.5	280	266	01 Jun 08	30 Nov 08
Nick Prettejohn	2006	661	—	—	—	—	661	416.5	565	n/a	01 Jun 09	30 Nov 09
Tidjane Thiam	2008	—	—	—	—	1,705	1,705	416.5	551	n/a	01 Jun 11	30 Nov 11
Mark Tucker	2005	2,297	—	—	—	—	2,297	416.5	407	n/a	01 Dec 08	31 May 09

Notes:

(1) Gains of £15,420 were made by directors in 2008 on the exercise of share options.

(2) No price was paid for the award of any option.

(3) The highest and lowest share prices during 2008 were 726 pence and 245 pence respectively.

2009

	Year of initial grant	Option outstanding at 1 Jan 2009	Exercised in 2009	Market Price on Exercise date (pence)	Options forfeit in 2009	Options granted in 2009	Options outstanding at 31 Dec 2009	Market price at 31 Dec 2009 (pence)	Original exercise price (pence)	Exercise price adjusted for 2004 Rights issue (pence)	Earliest exercise date	Latest exercise date
Nick Prettejohn	2006	661	—	—	661	—	—	—	565	n/a	01 Jun 09	30 Nov 09
Tidjane Thiam	2008	1,705	—	—	—	—	1,705	640	551	n/a	01 Jun 11	30 Nov 11
Mark Tucker	2005	2,297	—	—	2,297	—	—	—	407	n/a	01 Dec 08	31 May 09

Notes

(1) Gains of £nil were made by directors in 2009 on the exercise of share options.

(2) No price was paid for the award of any option.

(3) The highest and lowest share prices during 2009 were 650.5 pence and 207 pence respectively.

Dilution

For 2007, 2008 and 2009 Prudential met its obligations under its share plans by funding an employee trust which acquires shares on the open market either at the time of grant or by maintaining sufficient shares in the trust to meet the requirements as awards vest. Shares relating to options granted under all-employee share plans are satisfied by new issue shares. The combined dilution from all outstanding options at 31 December 2007, 31 December 2008 and 31 December 2009 was 0.1%, 0.02% and 0.2% respectively of the total share capital at the time. From 2010 onwards shares released from Prudential's GPSP and BUPP will be fulfilled by using new issue shares as the primary vehicle to satisfy these arrangements rather than purchasing shares in the open market.

Directors' pensions and life assurance

In 2007, 2008 and 2009 the Chief Executive of Jackson employed in the US was eligible to participate in Jackson's Defined Contribution Retirement Plan, a qualified 401K retirement plan, on the same basis as all other US based employees, into which contributions of 6% of basic salary up to a maximum of US$13,500, US$13,500 and US$14,700, were made in 2007, 2008 and 2009 respectively. He is also eligible to participate in the profit sharing element of Jackson's IRS-approved Defined Contribution Retirement Plan. The plan is an all-employee plan that provides eligible participants with annual profit sharing, depending on the financial results of Jackson for the plan year, with a maximum of 6% of salary capped at US$13,200 in 2007, US$9,200 in 2008 and US$14,700 in 2009.

The Chief Executive of Asia is eligible to receive a 25% cash salary supplement for pension purposes. UK executive directors are offered a choice of a combination of HMRC approved pension schemes and/or cash supplementary payments. If an executive director opts to join one of the HMRC approved pension plans, participation is on the same basis as other employees who joined at the same date as the executive director in question. For defined benefit schemes, the policy is to retain a notional scheme earnings cap, set at £112,800 and £117,600 and £123,600 for the 2007/08, 2008/09 and 2009/10 tax years respectively. No employees with employment offers after 30 June 2003 are eligible for membership of any defined benefit schemes.

For UK executive directors hired after 30 June 2003 Prudential's policy is to provide a supplement of 25% of salary. This includes, where relevant, any Company contributions to the staff defined contribution pension plan, which UK executive directors may choose to join. This plan has no salary cap.

Prudential's current practice in respect of pension arrangements for the current executive directors is set out below. Philip Broadley participated in a non-contributory scheme that provided a pension of 1/60th of Final Pensionable Earnings for each year of service on retirement at age 60.

Philip Broadley was entitled to supplements based on the portion of his basic salary not covered for pension benefits under a HMRC approved scheme. He was also provided with life assurance cover of four times salary.

Michael McLintock participates in a contributory scheme that provides a target pension of 2/3rds of Final Pensionable Earnings on retirement at age 60 for an employee with 30 years or more potential service, for which his contribution is 4% of basic salary. In both cases Final Pensionable Earnings are capped by a notional scheme earnings cap which replicates the HMRC earnings cap in force before A-Day (6 April 2006).

Michael McLintock is entitled to supplements based on the portion of his basic salary not covered for pension benefits under a HMRC approved scheme. He is also provided with life assurance cover of four times salary.

Rob Devey, Nic Nicandrou and Tidjane Thiam are entitled to a total salary supplement of 25% of basic salary. They were all members of the staff defined contribution pension plan as at 31 December 2009, which provides death in service benefits including life assurance of four times salary. The company contributions to the pension plan are included in the supplement.

Clark Manning participates in a US tax-qualified defined contribution plan (a 401K plan). He also provided with life assurance cover of two times salary.

Barry Stowe is paid a salary supplement of 25% of his salary. He is also provided with life assurance cover of four times salary.

Where supplements for pension purposes are paid in cash, the amounts are included in the Directors' remuneration table summary.

Details of directors' pension entitlements under HMRC approved defined benefit schemes and supplements that are in the form of contributions to pension arrangements paid by Prudential are set out in the following table.

2007

				Additional pension earned during year ended 31 Dec 2007		Transfer value of accrued benefit at 31 Dec (note 3)			
	Age at 31 Dec 2007	Years of pensionable service at 31 Dec 2007	Accrued benefit at 31 Dec 2007	Ignoring inflation on pension earned to 31 Dec 2006 (note 1)	Allowing for inflation on pension earned to 31 Dec 2006 (note 2)	2007 B	2006 A	Amounts of (B-A) less contributions made by directors during 2007	Contributions to pension and life assurance arrangements (note 4)
			£000	£000	£000	£000	£000	£000	£000
Sir David Clementi	58	—	—	—	—	—	—	—	15
Philip Broadley	46	7	14	2	2	135	111	24	—
Clark Manning	49	—	—	—	—	—	—	—	15
Michael McLintock	46	15	38	3	4	435	397	25	91
Nick Prettejohn	47	—	—	—	—	—	—	—	74
Barry Stowe	50	—	—	—	—	—	—	—	—
Mark Tucker	50	—	—	—	—	—	—	—	11

Notes:

(1) As required by Stock Exchange Listing rules.

(2) As required by the Companies Act remuneration regulations.

(3) The transfer value equivalent has been calculated in accordance with Actuarial Guidance Note GN11.

(4) Supplements in the form of cash are included in the Directors' Remuneration summary table.

2008

				Additional pension earned during year ended 31 Dec 2008		Transfer value of accrued benefit at 31 Dec (note 3)			
	Age at 31 Dec 2008	Years of pensionable service at 31 Dec 2008	Accrued benefit at 31 Dec 2008	Ignoring inflation on pension earned to 31 Dec 2007 (note 1)	Allowing for inflation on pension earned to 31 Dec 2007 (note 2)	2008 B	2007 A	Amounts of (B-A) less contributions made by directors during 2008	Contributions to pension and life assurance arrangements (note 4)
			£000	£000	£000	£000	£000	£000	£000
Sir David Clementi	59	—	—	—	—	—	—	—	18
Philip Broadley(*)	47	8	16	2	2	147	135	12	—
Clark Manning	50	—	—	—	—	—	—	—	14
Michael McLintock	47	16	43	4	4	426	435	(22)	94
Nick Prettejohn	48	—	—	—	—	—	—	—	78
Barry Stowe	51	—	—	—	—	—	—	—	4
Tidjane Thiam	46	—	—	—	—	—	—	—	96
Mark Tucker	51	—	—	—	—	—	—	—	14

* **Philip Broadley left on 31 May 2008 and all transfer information provided is for that date.**

Notes

1 As required by Stock Exchange Listing rules.

2 As required by the Companies Act remuneration regulations.

3 The transfer value equivalent has been calculated in accordance with Actuarial Guidance Note GN11.

4 Supplements in the form of cash are included in the Directors' remuneration summary table.

2009

				Additional pension earned during year ended 31 Dec 2009		Transfer value of accrued benefit at 31 Dec (note 3)			
	Age at 31 Dec 2009	Years of pensionable service at 31 Dec 2009	Accrued benefit at 31 Dec 2009	Ignoring inflation on pension earned to 31 Dec 2008 (note 1)	Allowing for inflation on pension earned to 31 Dec 2008 (note 2)	2009 B	2008 A	Amounts of (B-A) less contributions made by directors during 2009	Contributions to pension and life assurance arrangements (note 4)
			£000	£000	£000	£000	£000	£000	£000
Rob Devey	41	—	—	—	—	—	—	—	0
Clark Manning	51	—	—	—	—	—	—	—	21
Michael McLintock	48	17	47	5	5	755	426	329[(5)]	89
Nic Nicandrou	44	—	—	—	—	—	—	—	0
Nick Prettejohn	49	—	—	—	—	—	—	—	59
Barry Stowe	52	—	—	—	—	—	—	—	2
Tidjane Thiam	47	—	—	—	—	—	—	—	113
Mark Tucker	52	—	—	—	—	—	—	—	16

Notes:

(1) As required by Stock Exchange Listing rules.

(2) As required by the Companies Act remuneration regulations.

(3) The transfer value equivalent has been calculated in accordance with Actuarial Guidance Note GN11.

(4) Supplements in the form of cash are included in the Directors' remuneration table.

(5) A number of factors operating together have resulted in the increase in transfer value over the year. This includes increases due to changes in market conditions from inflation rates rising and interest rates falling, an extra year of service accruing, an increase in the HMRC earnings cap and Michael drawing one year closer to retirement.

No enhancements to the retirement benefits paid to or receivable by directors or former directors other than the discretionary pension increases awarded to all pensioners have been made during the years 2007, 2008 or 2009.

Total contributions to directors' pension arrangements including cash supplements for pension purposes were £1,163,687 for 2007, £1,027,267 for 2008 and £876,466 for 2009 of which £166,557 for 2007, £268,668 for 2008 and £298,586 for 2009 related to money purchase schemes.

c *Five highest paid individuals*

Of the five individuals with the highest emoluments, two for 2009 (2008: two; 2007: one) are Directors whose emoluments are disclosed in note I4. The aggregate of the emoluments in respect of the other three for 2009 (2008: three; 2007: four) are as follows:

	2007	2008	2009
	£m	£m	£m
Basic salaries, allowances and benefits in kind	1	1	1
Pension contributions*	—	—	—
Bonuses paid or receivable	19	10	12
Share based and other cash payments	4	2	4
Total	24	13	17

* Pension contributions payable in the period were less than £100,000 in each period.

Their emoluments were within the following bands:

	2007	2008	2009
£2,600,001 — £2,700,000	—	1	—
£3,300,001 — £3,400,000	1	—	—
£3,800,001 — £3,900,000	1	—	—
£4,700,001 — £4,800,000	—	1	—
£4,900,001 — £5,000,000	1	—	—
£5,200,001 — £5,300,000	—	—	1
£5,400,001 — £5,500,000	—	—	1
£6,000,001 — £6,100,000	—	1	—
£6,600,001 — £6,700,000	—	—	1
£12,600,001 — £12,700,000	1	—	—

I5: Fees payable to auditor (including expenses)

	2007	2008	2009
	£m	£m	£m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	1.8	1.6	1.8
Fees payable to the Company's auditor and its associates for other services:			
Audit of subsidiaries and associates pursuant to legislation	4.4	5.0	5.5
Other services supplied pursuant to legislation	2.9	2.4	2.7
Other services relating to taxation	0.4	0.6	0.6
Valuation and actuarial services	0.7	0.7	0.1
Services relating to corporate finance transactions	0.2	—	0.7
All other services	1.0	0.5	1.0
Total	11.4	10.8	12.4

In addition, there were fees incurred of £0.2 million, £0.2 million and £0.2 million, for 2007, 2008 and 2009 respectively, for the audit of pension schemes.

The Audit Committee regularly monitors the non-audit services provided to the Group by its auditor and has developed a formal Auditor Independence Policy which sets out the types of services that the auditor may provide, consistent with the guidance in Sir Robert Smith's report 'Audit Committees — Combined Code Guidance' and with the provisions of the US Sarbanes-Oxley Act.

The Audit Committee annually reviews the auditor's objectivity and independence.

I6: Related party transactions

Transactions between Prudential and its subsidiaries are eliminated on consolidation.

In addition, Prudential has transactions and outstanding balances with certain unit trusts, OEICs, collateralised debt obligations and similar entities which are not consolidated and where a group company acts as manager. These entities are regarded as related parties for the purposes of IAS 24. The balances are included in the Prudential Group's statement of financial position at fair value or amortised cost in accordance with their IAS 39 classifications. The transactions are included in the income statement and include amounts paid on issue of shares or units, amounts received on cancellation of shares or units and paid in respect of the periodic charge and administration fee. Further details of the aggregate assets, liabilities, revenues, profits or losses and reporting dates of entities considered to be associates under IFRS are disclosed in note H8.

Executive officers and directors of Prudential may from time to time purchase insurance, asset management or annuity products marketed by group companies in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with other persons.

Apart from the transactions with directors referred to below, no director had interests in shares, transactions or arrangements that require disclosure, other than those given in note I4. Key management and directors' remuneration is disclosed in note I4.

In 2007, 2008 and 2009, other transactions with directors were not deemed significant both by virtue of their size and in the context of the directors' financial positions. As indicated above, all of these transactions are on terms broadly equivalent to those that prevail in arm's length transactions.

I7: Subsidiary undertakings

i Principal subsidiaries

The principal subsidiary undertakings of Prudential at 31 December 2007, all wholly owned except PCA Life Assurance Company Limited and audited by KPMG Audit Plc and/or its member firms, were:

	Main activity	Country of incorporation
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Annuities Limited*	Insurance	England and Wales
Prudential Retirement Income Limited ("PRIL")*	Insurance	Scotland
M&G Investment Management Limited*	Asset management	England and Wales
Jackson National Life Insurance Company*	Insurance	US
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore
PCA Life Assurance Company Limited* (99% owned)	Insurance	Taiwan

* Owned by a subsidiary undertaking of Prudential.

Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for PRIL which operates mainly in England and Wales.

The principal subsidiary undertakings of Prudential at 31 December 2008, all wholly owned except PCA Life Assurance Company Limited and audited by KPMG Audit Plc and/or its member firms, were:

	Main activity	Country of incorporation
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Annuities Limited*	Insurance	England and Wales
Prudential Retirement Income Limited ("PRIL")*	Insurance	Scotland
M&G Investment Management Limited*	Asset management	England and Wales
Jackson National Life Insurance Company*	Insurance	US
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore
PCA Life Assurance Company Limited* (99% owned)	Insurance	Taiwan

* Owned by a subsidiary undertaking of Prudential.

Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for PRIL which operates mainly in England and Wales.

The principal subsidiary undertakings of Prudential at 31 December 2009, all wholly owned and audited by KPMG Audit Plc and/or its member firms, were:

	Main activity	Country of incorporation
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Annuities Limited*	Insurance	England and Wales
Prudential Retirement Income Limited ("PRIL")*	Insurance	Scotland
M&G Investment Management Limited*	Asset management	England and Wales
Jackson National Life Insurance Company*	Insurance	US
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore

* Owned by a subsidiary undertaking of Prudential.

Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for PRIL which operates mainly in England and Wales.

ii Dividend restrictions and minimum capital requirements

Certain Prudential Group subsidiaries are subject to restrictions on the amount of funds they may transfer in the form of cash dividends or otherwise to the parent company. UK insurance companies are required to maintain solvency margins which must be supported by capital reserves and other resources, including unrealised gains on investments. Jackson can pay dividends on its capital stock only out of earned surplus unless prior regulatory approval is obtained. Furthermore, without the prior regulatory approval, dividends cannot be distributed if all dividends made within the preceding 12 months exceed the greater of Jackson's statutory net gain from operations or 10% of Jackson's statutory surplus for the prior year. In 2010, the maximum amount of dividends that can be paid by Jackson without prior regulatory approval is US$454 million (£281 million) (in 2009: US$290 million (£202 million)) and (in 2008: US$490 million (£246 million)). The Prudential Group's Asian subsidiaries, mainly the Singapore and Malaysia businesses, may remit dividends to the Prudential Group, in general, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations.

The Prudential Group capital position statement for life assurance businesses is set out in note D5, showing the available capital reflecting the excess of regulatory basis over liabilities for each fund or group of companies determined by reprove to the local regulation of the subsidiaries. In addition, disclosure is also provided in note D5 of the local capital requirements of each of the funds or group of companies.

iii Acquisition and disposal of subsidiaries

2007

On 1 May 2007, Prudential completed the sale of Egg Banking plc to Citibank Overseas Investment Corporation, a subsidiary of Citigroup Inc.

On 9 November 2007, Prudential completed the sale of PPM Capital, its direct private equity business.

The PAC with-profits fund acquired a number of venture capital holdings through PPM Capital and M&G. Prior to November 2007, the Group was deemed to have a controlling interest in these venture capital holdings, in aggregate with, if applicable, other holdings held by, for example, the Prudential Staff Pension Scheme. In November 2007, the Group disposed of PPM Capital following which the Group no longer had a controlling interest in venture fund investment subsidiaries that it managed and consequently ceased to consolidate these investments from that date. The Group continues to consolidate, where applicable, the venture capital holdings managed by M&G.

The acquisitions made in 2007 were as follows:

- 71% of the voting equity interest of Orizon AG, an employment hiring agency, which was managed by PPM Capital; and
- 78% of the voting equity interest of Red Funnel, a ferry company, which was managed by M&G.

These acquisitions are considered individually immaterial and therefore all information relating to the acquisitions has been presented in aggregate in this note.

The results of the acquisitions have been included in the consolidated financial information of the Prudential Group and contributed a loss of £8.3 million to earnings within the income statement.

The table below identifies the net assets of these acquisitions and minor business purchases by existing venture holdings and reconciles the net assets to the consideration paid:

	2007 Fair Value on acquisition
	£m
Cash and cash equivalents	20
Other current assets	26
Property, plant and equipment	38
Intangible assets other than goodwill	1
Other non-current assets	3
Less liabilities, including current liabilities and borrowings	(304)
Net assets acquired	(216)
Goodwill	313
Cash consideration	97

Aggregate goodwill of £313 million was recognised for the excess of the cost over the Group's interest in the net fair value of the entities' assets, liabilities, and contingent liabilities acquired.

Following the disposal of PPM Capital, SUSPA, TJ Hughes, Sterigenics, Muller & Weygandt, TMF Group, JOST, Histoire D'or, Azzuri Communications, Paramount plc and Orizon AG ceased to be consolidated as subsidiary undertakings and goodwill and other intangible assets, net of amortisation, relating to these investments were derecognised accordingly.

2008

There were no acquisitions or disposals of subsidiaries during the year. There were no new acquisitions or disposals of venture capital investments in 2008. However, during the year, the holding in the voting equity interest of Red Funnel increased from 78% to 90%.

2009

During 2009, the holding in the voting equity interest of Red Funnel, owned by the PAC with-profits fund managed by M&G, increased from 90% to 100%.

I8: Commitments

i Operating leases

The Prudential Group leases various offices to conduct its business. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

	2007	2008	2009
	£m	£m	£m
Future minimum lease payments for non-cancellable operating leases fall due during the following periods:			
Not later than 1 year	38	86	63
Later than 1 year and not later than 5 years	126	199	178
Later than 5 years	111	140	104

The total minimum future sublease rentals to be received on non-cancellable operating leases for land and buildings for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, was £0.4 million, £0.2 million, and £nil.

Minimum lease rental payments for the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, of £50 million, £84 million and £105 million are included in the consolidated income statement.

ii Capital commitments

The Prudential Group has provided, from time to time, certain guarantees and commitments to third-parties including funding the purchase or development of land and buildings and other related matters. At 31 December 2007, 31 December 2008 and 31 December 2009 respectively, the aggregate amount of contractual obligations to purchase and develop investment properties amounted to £64 million, £1 million, and £nil.

I9: Discontinued operations

Discontinued banking operations in 2007 related entirely to UK banking operations following the sale on 1 May 2007 of Egg Banking plc to Citi. Consideration paid to Prudential was, net of expenses, £527 million cash. Cash and cash equivalents disposed of in 2007 were £1,065 million. Accordingly, the cash outflow for the Prudential Group in 2007 arising from the disposal of Egg, as shown in the consolidated cash flow statement, was £538 million.

The profit included in the 2007 income statement in respect of discontinued banking operations for the period of ownership was as follows:

	2007
	£m
Interest income	261
Interest expense	(148)
Net interest income	113
Fee and commission income	41
Fee and commission expense	(8)
Operating income	146
General administrative expenses	(56)
Impairment losses on loans and cash advances to customers	(149)
Other operating expenses	(9)
Operating loss based on longer-term investment returns	(68)
Profit on sale of Egg Banking plc	290
Profit before tax	222
Tax on operating loss based on longer-term investment returns	19
Tax on profit on sale of Egg Banking plc	—
Tax attributable to shareholders' profits	19
Profit for the year	241

The interest income on financial assets not at fair value through profit and loss for the period of ownership in 2007 was £241 million. The interest expense on financial liabilities not at fair value through profit and loss for the period of ownership in 2007 was £148 million.

Fee and commission income in 2007 includes £27 million relating to financial instruments held at amortised cost. These fees primarily related to balance transfer fees and late payment fees. Fee and commission expense in 2007 includes fee expenses relating to financial liabilities held at amortised cost of £4 million which related to treasury fees. Of the loss for the period of ownership in 2007, no loss was attributable to minority interests in Egg.

In 2009, a charge of £14 million, which is net of nil tax, reflects completion of adjustments for a previously disposed business.

I10: Cash flows

Structural borrowings of shareholder-financed operations comprise core debt of the parent company and Jackson surplus notes. Core debt excludes borrowings to support short-term fixed income securities programmes, non-recourse borrowings of investment subsidiaries of shareholder-financed operations and other borrowings of shareholder-financed operations. Cash flows in respect of these borrowings are included within cash flows from operating activities.

Cash flows relating to discontinued operations in 2007, as detailed in note I9, are inflows of £157 million for the period of ownership in 2007. All of these related to cash flows from operating activities.

Structural borrowings of with-profits operations relate solely to the £100 million 8.5% undated subordinated guaranteed bonds which contribute to the solvency base of SAIF. Cash flows in respect of other borrowings of with-profits funds, which principally relate to consolidated investment funds are also included within cash flows from operating activities.

I11: Post balance sheet events

i Acquisition of UOB Life Assurance Limited

On 6 January 2010 the Prudential Group announced the acquisition from United Overseas Bank (UOB) of its 100% interest in UOB Life Assurance Limited in Singapore for total cash consideration of SGD428 million (£192 million) subject to a post-completion adjustment to reflect the net asset value as at the completion date. This acquisition accompanied the announcement of a long-term strategic partnership with UOB. Through this partnership the Prudential Group's life insurance products will be distributed through UOB Group's 414 bank branches across Singapore, Indonesia and Thailand.

The Prudential Group continues to complete its compilation of the acquisition balance and further details will be provided in the Prudential Group's 2010 half year results announcement.

ii Japanese insurance subsidiary's closure to new business

On 15 January 2010 the Prudential Group's Japanese insurance subsidiary announced its intention to suspend underwriting new policyholder contracts in Japan after 15 February 2010. The company reinforced its commitment to servicing its existing policyholder base, which comprised over 170,000 contracts as at 30 September 2009. This decision will be reviewed on an on-going basis in the light of changes to the business environment.

This decision does not affect the Prudential Group's asset management operations in Japan, which rank amongst the largest foreign asset managers in Japan.

iii Agreement to acquire AIA Group Limited

On 1 March 2010, Prudential announced that it had reached agreement with American International Group Inc. ("AIG"), on terms for the combination of Prudential and AIA Group Limited ("AIA"), a wholly-owned subsidiary of AIG (the "Transaction"). The AIA Group is a leading life insurance organisation in the Asia Pacific region which provides individuals and businesses with products and services for their insurance, protection, savings, investment and retirement needs in 15 geographical markets in the region. The combined group will be the leading life insurer in Hong Kong, Singapore, Malaysia, Indonesia, Vietnam, Thailand and the Philippines with the leading foreign life insurance business in China and India, a significantly enhanced presence in the high growth South East Asian life markets and strong operations in the US and UK.

The Transaction will be effected through the acquisition of both Prudential (by a scheme of arrangement, the "Scheme") and AIA by a new company ("New Prudential"). The new company will assume the name Prudential plc, be headquartered and incorporated in the UK, and traded on the main market of the London Stock Exchange with ADRs traded on the New York Stock Exchange. The existing Board of Prudential will become the Board of New Prudential.

AIG will receive total consideration of US$35.5 billion, comprising US$25.0 billion in cash (subject to reduction in an amount equal to the aggregated nominal value of any subordinated notes for which AIA Aurora subscribes under the Subordinated Note Commitment Letter) and US$10.5 billion in New Prudential shares and other securities, which will be increased by an amount equal to the aggregate nominal amount of any subordinated notes for which AIA Aurora subscribes under the Subordinated Note Commitment Letter. The cash component of the consideration will be financed through an underwritten rights issue, raising US$20.0 billion (net of costs fees and expenses) and through issuance of up to US$5.0 billion senior and subordinated notes (net of costs fees and expenses). These issues have been agreed to be underwritten by certain banks. Subsequently, Prudential has entered into the Hybrid Capital Facility pursuant to which the Joint Lead Arrangers will, at the request of Prudential subscribe for Lower Tier 2 capital notes and/or Upper Tier 2 capital notes and/or advance Lower Tier 2 capitals and/or advance Upper Tier 2 capital loans in an aggregate principal value of up to US$5.4 billion to be issued by or advanced to Prudential. In addition to the Hybrid Capital Facility, Prudential has also entered into the Subordinated Note Commitment Letter under which, to the extent that the Joint Lead Arrangers are unable to procure subscriptions in full for the Bond Offerings for an aggregate amount equal to US$5.4 billion, AIA Aurora has agreed to subscribe for subordinated debt securities in an aggregate amount equal to the lesser of: (i) US$1.875 billion; and (ii) the amount required to make the aggregate amount of subordinated debt securities subscribed for under the Bond Offerings, the Hybrid Capital Facility and pursuant to the Subordinated Note Commitment Letter equal to US$5.4 billion. The effectiveness of the Subordinated Note Commitment Letter is conditional on the consent of the Joint Lead Arrangers being obtained.

The Rights Issue and the Scheme will be subject to shareholder approval at the General Meeting. The Transaction is also subject to certain regulatory and anti-trust approvals including various regulatory approvals required on a change of control of Prudential as a result of the Scheme.

On 8 March 2010 Prudential confirmed that the Prudential Group had entered into foreign exchange hedging arrangements in respect of its requirement to convert the pounds sterling proceeds of the rights issue into US dollars, which is the currency in which Prudential must pay the cash element of the consideration.

iv Change to the Prudential Group's holding in PruHealth and PruProtect

On 11 May 2010, Discovery Holdings of South Africa announced that it has entered into an agreement to acquire the entire share capital of Standard Life Healthcare, a wholly-owned subsidiary of the Standard Life Group, for £138 million. Discovery will fund the purchase of the Standard Life Healthcare transaction, and intends to contribute Standard Life Healthcare to PruHealth as a capital investment. Once completed, Discovery intend to increase their shareholding in both PruHealth and PruProtect from the current level of 50 per cent, to 75 per cent. Prudential will have a 25 per cent shareholding in both companies within the joint venture, including Standard Life Healthcare. The transaction is subject to obtaining the necessary regulatory approvals from the Financial Services Authority (UK) and the South African Reserve Bank. The effective date of the transaction is expected to be 31 July 2010.