Registered No: 15454

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Annual Report and Financial Statements for the Year Ended 31 December 2018

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Incorporated and registered in England and Wales. Registered no. 15454

Registered office: Laurence Pountney Hill, London EC4R 0HH

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Directors

Mr P Spencer - Chairman
Mr C P Adamson
Mr R Bennison
Ms C J Bousfield
Ms J Dawson
Mr M Evans (Appointed 17 October 2018)
Mr M T FitzPatrick
Mr J W Foley
Dr I Owen (Appointed 18 April 2018)

Company Secretary

Ms J A Owens

Auditor

KPMG LLP, London

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2018

Principal activity

The principal activity of The Prudential Assurance Company Limited (the Company) in the course of 2018 was transacting long-term insurance business in the United Kingdom. This activity is expected to continue in 2019. Throughout 2018 the Company also owned insurance subsidiary undertakings including Prudential Pensions Limited (PPL), Prudential International Assurance plc (PIA) and a branch in Poland. These transacted insurance business in the United Kingdom and overseas.

The Company is part of M&GPrudential, the UK and European savings and investments business of Prudential plc. In March 2018 Prudential plc announced its intention to demerge M&GPrudential from Prudential plc, resulting in two separately-listed companies, with different investment characteristics and opportunities. In preparation for the demerger the legal ownership of the Company's Hong Kong insurance subsidiaries was transferred from the Company to Prudential Corporation Asia Limited ('PCAL') on 19 December 2018.

The Company is a wholly owned subsidiary undertaking of another company registered in England and Wales and therefore group financial statements and a group business review are not prepared. Accordingly, the financial statements and the following business review present information about the Company as an individual undertaking and are not consolidated.

Business review

The Company's brand benefits from a heritage that stretches back over 170 years and a franchise that is based on long-term thinking, longevity experience, market-leading multi asset investment capability and financial strength. Such attributes continue to be highly sought after by customers and their financial advisers as they plan for retirement and other long term savings needs.

The fundamentals underpinning the UK's retirement market are changing. Risk and responsibility for retirement provision continues to transfer away from the state and employers to individuals. The new flexible arrangements introduced by Pensions Freedom in 2015 allow individuals to take control over their own pensions but have introduced significant additional complexity. The burden of mitigating investment risk, longevity risk and inflation risk in respect of retirement income increasingly falls directly onto them.

2018 was a year of market volatility and political uncertainty, with the FTSE 100 index, for instance, showing a 12.5% fall across the year. Consumer demand for savings and investment products specifically designed to mitigate risk and reduce volatility has remained strong.

The with-profits fund is invested across a broad range of assets and aims to provide steady returns to customers. It is the largest fund of its kind in the UK and its financial strength has enabled the Company to add approximately £20.6bn to policy values in the last 10 years. Over the same period the fund has delivered a cumulative investment return of 129.5%, compared with the FTSE All-Share (total return) index return of 121.4%. Due to global market volatility investment returns for the with-profits fund fell by 2.8 per cent before tax in 2018, compared with the FTSE All-Share which fell by 9.5%.

There are significant new opportunities for the Company as the demand for risk-managed investments to fund retirement rises. Increased life expectancy in retirement puts further demands on long-term product performance.

The Prudential Retirement Account is an online account-based plan, that allows customers to benefit from an income in retirement and facilitate access to their fund as they save. This solution continued to be in high demand, with assets now at £12bn (2017: £7.2bn). Launched in 2016, the Prudential Retirement Account is one of the products which allows customers to invest in PruFund, a customer proposition managed by Prudential Portfolio Management Group, the Company's award-winning and market leading multi-asset management team.

PruFund aims to grow savers' money over the medium to long term whilst protecting them from the ups and downs of direct stock market investment. There has been strong and sustained demand with £12bn invested in PruFund alone in 2018 and total customer assets under management increasing by 19% to £43bn (2017: £36bn).

The Company continues to focus on deepening its already strong relationships with independent financial advisers. An important part of the Company's service offering is the ongoing hands-on support from its regional sales units, technical helpline and business development and consultancy team. The Company also distributes products via other group companies. Prudential Financial Planning Limited provides restricted advice services and Prudential Distribution Limited intermediates non-advised sales.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2018 (continued)

Throughout 2018, M&GPrudential continued to invest in making it easier for all customers of the Prudential brand to do business with us. The MyPru online servicing portal, which allows customers to enjoy ease and convenience of accessing policies online, and dramatically reducing the time it takes to withdraw money from bonds are just two of the ways that a digitisation of the business is making customers' lives easier. As part of M&GPrudential, the Company has the opportunity to offer its customers a wider set of solutions as their needs evolve.

The Company sees significant opportunities for continued growth, including from the synergies available from the combination of the asset management business of M&G with Prudential's life insurance business.

In support of this, M&GPrudential announced a major investment programme in the new combined business's infrastructure to improve customer service, accelerate product development, and widen customer choice. A substantial investment has been made in a business modernisation programme which is now well underway and already showing service benefits for customers. In January 2018, we announced a new partnership with Tata Consultancy Services ('TCS') to transfer, consolidate and upgrade the customer administration systems for our traditional insurance business. This involved the transfer of 2,500 people, including 650 Prudential colleagues.

Each day, the Company moves closer to its model of a simpler, lower-cost, digital organisation. The impact on customer outcomes is already evident. Examples include: a new digital service for investment bond customers that has reduced cash withdrawal waiting times by almost 80 per cent; changes to the Company's bereavements processes which are saving our customers 200,000 days of their time each year; and delivery of simplified annual benefit statements for more than one million Prudential customers. Our transformation also comes with clear efficiency gains, which will benefit our shareholders, and our with-profits policyholders.

The Company's roll-out of business in Poland continued in 2018 with sales (APE), as defined on page 4, increasing by 20 per cent in local currency terms. Prudential Poland now has 843 tied agents operating from 22 branches and access to a large network of multi-agent consultants.

Strategic Direction

In March 2018 Prudential plc announced its intention to demerge M&GPrudential from Prudential plc, resulting in two separately-listed companies, with different investment characteristics and opportunities. M&GPrudential is one of the leading retirement and savings businesses in the UK and Europe. M&GPrudential as a standalone group will continue to drive its transformation into a more capital-efficient and customer-focused business, targeting growing customer demand for comprehensive financial solutions. As part of the proposed demerger, the Company agreed in March 2018 to the partial sale of its shareholder annuity portfolio, resulting in an overall increase in Solvency II capital surplus of £0.9bn during 2018 and a UK GAAP loss of £0.5bn as discussed below. Under the terms of the agreement the portfolio has initially been reinsured to Rothesay Life and most of the portfolio will subsequently be transferred in accordance with Part VII of the Financial Services and Markets Act 2000. As with other changes to the business, the Company's priority is to ensure these customers are treated fairly. The capital benefit of the transaction will be retained within the Company to support the demerger process.

Early in 2018 an M&GPrudential Group Company signed an agreement with TCS, a global leader in IT, business process and digital services, to enhance its service for UK savings and investment customers as described above. Over four million life and pensions contracts have moved to Diligenta, the FCA-regulated subsidiary of TCS.

On 26 November 2018 the Company's legal ownership was transferred from its previous parent company Prudential plc to a new holding company, M&G Prudential Limited. M&G Prudential Limited is a subsidiary of Prudential plc. The ultimate parent of the Company therefore remains Prudential plc, a public limited company, limited by shares, incorporated and registered in England and Wales and the parent company of the Prudential group ('the Prudential Group' or 'the Group').

On 14 December 2018, the beneficial interests in the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were sold to Prudential Corporation Asia Limited, with the legal ownership transferring on 19 December 2018. See note 31 for further details.

M&GPrudential has been reviewing its operations across Europe since the UK voted to leave the European Union. In January 2019, in accordance with Part VII of the Financial Services and Markets Act 2000, the Company transferred all of its long term European business (excluding the UK) into PIA, a subsidiary of the Company which is based in the Republic of Ireland. The with-profits element of the business is reinsured back into the Company

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2018 (continued)

ensuring continuation of the economic substance of the previous situation. The shareholder-backed business has not been reinsured back to the Company following the Part VII transfer.

Key performance indicators and measurement

Key Performance Indicators	**2018** **£m**	**2017** **£m**
New business profit	9	9
Core operating profit	528	571
Non-core operating profit:		
Effect of longevity reinsurance transactions	—	31
Other management actions to improve solvency	58	245
Changes in longevity assumption basis	441	204
FCA Thematic Review of Annuities Sales Practices	166	(225)
Provision for Guaranteed Minimum Pensions	(55)	—
Total operating profit before restructuring and other similar expenditure	1,147	835
Restructuring and other similar expenditure	(58)	(38)
Total operating profit note (i)	1,089	797
Non-operating (loss) profit:		
Partial sale of annuity portfolio	(508)	—
Revaluation of Hong Kong subsidiaries	599	1,586
Other non-operating profit items	172	209
Total Non-operating profit items	263	1,795
Profit on ordinary activities before tax	1,352	2,592
Shareholders' funds	6,877	15,611
APE sales note (ii)	1,500	1,473
Estimated Solvency II capital surplus:		
Policyholders' capital surplus	5,458	4,803
Shareholders' capital surplus	3,691	6,115

Notes

(i) Operating profit is the underlying operating result based on longer term investment returns and excludes non-operating items such as the revaluation and disposal of the Company's subsidiaries and dividends received from them. Operating profit based on longer-term investment returns gives a more relevant measure of the performance of the business than UK GAAP profits. The UK GAAP measure of profit includes short-term fluctuations in investment performance which can distort the results year on year and are largely beyond management control.

(ii) Annual premium equivalent (APE) sales comprise regular premium sales plus one-tenth of single premium insurance sales. APE is a more useful performance measure than gross premiums written as it contains only new business, whereas gross premiums written includes premiums from contracts that started in previous years and are therefore less relevant to the Company's current performance. Additionally, APE contains only one tenth of single premiums, to allow for the fact that such inflows are less significant than regular premium business which may be expected to continue for a period of time.

Operating Profit

Operating profit is the underlying operating result based on longer term investment returns and excludes non-operating items such as the revaluation and disposal of the Company's subsidiaries and dividends received from them. Core refers to the underlying profit of the insurance business excluding the effect of, for example, management actions to improve solvency and material assumption changes.

The operating profit from core in-force business of £528m (2017: £571m) is comprised of the £320m (2017: £288m) shareholder transfer from the with-profits fund and £208m (2017: £283m) from the shareholder fund.

The with-profits shareholder transfer is £32m higher than 2017 due to growth of the with-profits funds under management. The decrease in profits on shareholder-backed business of £75m is principally because the partial sale of the shareholder annuity portfolio means there is a smaller portfolio remaining on which profits may be earned.

Non-core operating profit for 2017 include £31m in respect of longevity reinsurance transactions which were not repeated in 2018. Other management actions include the effect of repositioning the fixed income portfolio to improve the trade-off between yield and credit risk.

Other management actions in 2017 included the impact of repositioning the fixed income portfolio to improve the trade off between yield and credit risk. Following significant trading in 2017, there was reduced opportunity for this activity in 2018.

Changes in longevity assumption basis of £441m reflect changes to annuitant mortality assumptions to reflect current mortality, as well as the adoption of the Continuous Mortality Investigation (CMI) 2016 model. For 2017, the £204m benefit largely arose from the adoption of the CMI 2015 model.

The 2018 non-core operating profit increase is primarily due to the increase of £391m in relation to the Thematic Review of Annuities Sales Practices (TRASP). A charge of £225m was made in 2017 in relation to TRASP, whereas income of £166m in relation to insurance recoveries has been recognised for 2018.The Company has agreed with the Financial Conduct Authority (FCA) to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. The review is examining whether customers were given sufficient information about their potential eligibility to purchase an enhanced annuity, either from Prudential or another pension provider. A gross provision of £400m, before costs incurred, was established at 31 December 2017 to cover the costs of undertaking the review and any related redress and following a reassessment, no change has been made in 2018. The majority of the provision will be utilised in 2019. The ultimate amount that will be expended by the Company on the review will remain uncertain until the project is completed. Additionally, in 2018, the Company agreed with its professional indemnity insurers that they will meet £166m of claims costs, which will be paid as the Company incurs costs/redress. This income has been recognised in operating profit and on the balance sheet within 'Other debtors' at 31 December 2018.

From April 1987, pension schemes were able to "contract out" of the State Earnings Related Pension Scheme, enabling companies and members to pay lower National Insurance Contributions, but their schemes had to provide a minimum level of benefit, the Guaranteed Minimum Pension ('GMP'). Recent court cases have confirmed that there is a requirement for GMPs to be equalised between male and female members / policyholders. The Company has included £55m within the long term business provision for the expected costs of equalisation, however there is uncertainty as to the extent to which the judgements apply to schemes other than active defined benefit schemes and therefore the extent to which the Company may be responsible for achieving this across its product lines.

Restructuring and other similar expenditure include restructuring and IFRS17 costs. The increase in costs is due to transformation costs in preparation of the demerger.

Non-operating profit (loss)

In March 2018, M&GPrudential announced the partial sale of the Company's shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, the Company reinsured £12bn of liabilities (valued as at 31 December 2017) to Rothesay Life. The loss arising from the transaction was £508m. The loss arising from the partial sale of the annuity portfolio has been treated as a non-operating item as it relates to a disposal of a material business.

On 14 December 2018, the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were sold to Prudential Corporation Asia Limited. This resulted in a revaluation gain of £599m prior to the transfer, which represents the estimated fair value of the business at the date of sale of £9,450m less the opening amount at 1 January 2018 of £8,851m. In 2017 the Hong Kong subsidiaries contributed a revaluation gain of £1,586m. Revaluation gains for shareholder subsidiaries are short term fluctuations in investment return and are therefore treated as a non-operating item.

Other non-operating items of £172m for 2018 consist of £183m of dividends received, £6m of short term fluctuations in investment returns and a revaluation loss of £17m on shareholder subsidiaries. The 2017 amount of £209m consisted of £88m of dividends received, £41m short term fluctuations and a revaluation gain on shareholder subsidiaries of £80m.

Profit on ordinary activities before tax

The results of the Company for the year as set out on pages 23 to 24 show a profit on ordinary activities before tax of £1,352m (2017: £2,592m profit), £1,240m lower than in 2017 as described above.

Shareholders' Funds

The shareholders' funds of the Company total £6,877m (2017: £15,611m). The decrease of £8,734m consists of the profit after tax of £1,229m offset by distributions of £9,963m. The distributions include a deemed distribution of £9,417m representing the difference between the fair value of the Hong Kong subsidiaries of £9,450m at the date of sale and the consideration received of £33m. In addition interim cash dividends of £546m were paid in the year.

Annual Premium Equivalent ('APE') Sales

Sales on an APE basis (Regular Premiums plus 1/10th Single Premiums) were £1,500m, 2 per cent higher than 2017 sales of £1,473m.

Ongoing demand for the Company's PruFund multi-asset funds remains strong as customers continue to be attracted by its performance track record, the benefits of a smoothed return in managing market volatility and its ability to reduce customer investment risk in the current market conditions. In total across all products, PruFund APE sales of £1,221m increased by 3 per cent from 2017, and total assets under management have increased 19 per cent since the start of the year to £43bn. The Prudential Retirement Account product has generated £238m (2017: £185m) of PruFund APE within Income Drawdown, an increase of 29 per cent and £508m (2017: £487m) of PruFund APE within Individual Pensions, an increase of 4 per cent.

Reflecting increased demand for the Company's wider range of investment propositions post-pension reforms, total income drawdown APE sales have increased by 15 per cent to £256m (2017: £222m). Total individual pensions APE sales were £603m (2017: £607m). The PruFund range of investment funds within an ISA wrapper generated APE sales of £141m (2017: £133m).

The Company's strong sales performance demonstrates its success in diversifying its product portfolio in response to the expanding market for flexible retirement income and pensions products. Offshore bonds APE sales of £86m (2017: £78m) increased by 10 per cent compared to 2017 and onshore bonds APE sales were £255m (2017: £258m) decreased by 1 per cent.

These strong performances were partly offset by a 11 per cent reduction in corporate pensions APE sales to £124m (2017: £140m) following a strategic decision to partially withdraw from the unit-linked corporate pensions market.

In Poland, the Company's life business continues to grow steadily. The business continues in its development of new distribution channels and enhancement of existing channels. Brand awareness is improving, demonstrating the Company's ability to effectively enter new markets.

Available Capital

The Company is subject to the Solvency II capital regime. This was developed by the European Union ('EU') in order to harmonise the various regimes previously applied across EU member states. Both policyholder and shareholder Solvency II surplus are on a recalculated transitional measure basis as at 31 December 2018 following approval from the Prudential Regulation Authority (PRA).

The high quality and recurring nature of the Company's operating capital generation and its disciplined approach to managing balance sheet risk provide meaningful protection against significant adverse market-driven effects on this metric. The Company's shareholder Solvency II capital surplus was estimated at £3.7bn at 31 December 2018 (2017: £6.1bn), equivalent to a coverage ratio of 172 per cent (2017: 178 per cent). There was a £4.1bn reduction in surplus from the transfer of the Hong Kong subsidiaries. Excluding the impact of this transfer, the Shareholder estimated solvency surplus has strengthened by £1.7bn.

While the surplus position of the Company's with-profits funds remain strong on a Solvency II basis, it is ring-fenced from the shareholder balance sheet and is therefore excluded from the Company's estimated shareholder

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2018 (continued)

Solvency II surplus results. The Company's estimated with-profits funds Solvency II surplus at 31 December 2018 was £5.5bn (2017: £4.8bn), equivalent to a coverage ratio of 231 per cent (2017: 201 per cent).

The Company's available capital position is covered further in note 29.

Principal Risks & uncertainties

As a provider of savings and retirement solutions, the Company's business involves the managed acceptance of risk. The Company is subject to the Group's internal control and risk management processes as detailed in the Group Governance Manual (GGM) and Group Risk Framework (GRF). The control procedures and systems established within the Group are designed to manage, rather than eliminate, the risk of failure to meet business objectives. As such they can only provide reasonable, rather than absolute, assurance against misstatement or loss, and focus on optimising the levels of risk and reward within a clearly defined risk appetite, with the aim of achieving the business objectives.

The GRF requires all business units and functions within the Group, including the Company, to establish processes for identifying, evaluating and managing key risks. The risk management framework for the Company is approved by the Board and operates based on the concept of three lines of defence: risk management, risk oversight and independent assurance.

The Company's results and financial condition are exposed to both financial and non-financial risks from its core activities and from those of a number of subsidiary companies. The key risk factors, mentioned below, should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

As at the date of approval of the Report and Accounts, the Company's Financial Strength is rated Aa3 by Moody's (stable outlook), A+ by Standard & Poor's (stable outlook) and AA- by Fitch (stable outlook).

Financial and Insurance risk

The Company is exposed to financial and insurance risk through its financial assets, financial liabilities, and policyholder liabilities. The financial risk factors affecting the Company include market risk, credit risk, insurance risk and liquidity risk. Further information on the financial and insurance risk management objectives and policies of the Company and the exposure of the Company to the related risk factors is given in note 28 (C) - (F).

A significant part of the Company's profit is related to bonuses for policyholders declared on its with-profits products, which are broadly based on historic and current rates of return on equity, property and fixed income securities, as well as the Company's expectations of future investment returns. Any adverse impact on the current and longer-term future asset returns may impact the current and future levels of with-profits bonuses and is therefore likely to impact the Company's profitability. Unlike traditional with-profits products, no regular or final bonuses are declared for PruFund contracts. Policyholder return is determined by an Expected Growth Rate (EGR) which is declared each quarter. The shareholder transfer only crystallises at the point when a claim is paid to the policyholder and is 1/9th of the difference between the policyholder payout and the premium(s) paid.

(a) Market risk

Market Risk is the risk of loss, or of adverse changes in the financial situation resulting, directly and indirectly, from fluctuations in the prices of financial instruments. Market risk includes but is not limited to interest rate risk, inflation risk, equity risk, currency risk, property risk, basis risk and other assets / alternative investments risk.

The key areas of the business impacted by market risk is the non-profit annuity business, assets held by the with-profits fund and the equity release mortgage book See note 28 (C) for further details.

(b) Credit risk

Credit risk is the risk of loss for the Company's business, or of adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties and debtors in the form of defaults, or other significant credit event (e.g. downgrades or spread widening).

The Company is exposed to significant levels of credit risk. The credit risk arises mainly from the corporate bond holdings in the non-profit annuity and with-profits business. See note 28 (D) for further details.

The Company, in the normal course of business enters into a variety of transactions with counterparties, including cash deposit, reinsurance and derivative transactions. Failure of any of these counterparties to discharge their obligations, or where adequate collateral is not in place (in case of reinsurance counterparties), could have an adverse impact on the Company's results.

(c) Insurance Risk

Insurance risk is the risk of loss for the Company's business, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend or volatility of a number of insurance risk drivers.

Insurance risk arises mainly from the annuity business in the form of longevity risk. The other insurance risks run by the Company are expense risk, persistency risk and mortality/morbidity risk. See note 28 (E) for further details.

- Longevity risk: This is the risk that the Company's (current and deferred) annuity customers live longer than expected in the Company's current pricing and reserving assumptions, and as a result future reserving and capital assumptions are changed. In addition, overall amounts in payment made to customers may be greater than anticipated due to longer life expectancy.

- Expense risk: This is the risk of actual expenses exceeding the assumptions in pricing and reserving bases and is relevant to all lines of business. If actual expenses are significantly different than assumed on pricing and reserving basis, the Company's operating results could be adversely affected.

- Persistency risk: This is the risk that customer retention levels are different from the Company's expectations, which is relevant to all non-annuity business. This risk can materialise if more or (for some lines of business) fewer customers opt for early termination of its products than anticipated. The Company's persistency assumptions reflect the recent past experience for each relevant line of business and expected trends in future persistency rates. If the actual levels of future persistency are significantly different than assumed in reserving and capital calculations, the Company's operating results could be adversely affected.

- Mortality and morbidity risks: These relate to assumptions around the expected number of deaths or illnesses used in pricing and calculating reserves. These are relevant for those lines of business where the customer pay-out is dependent on a death or illness.

(d) Liquidity risk

Liquidity risk is the risk that the Company may be unable to meet payment of obligations in a timely manner at a reasonable cost or the risk of unexpected increases in the cost of funding the portfolio at appropriate maturities or rates.

Liquidity risk arises mainly as a result of unplanned policyholder withdrawals and collateral requirements in its with-profit business:

- surrenders and processing delays in its unit-linked business;
- ineffective asset/liability matching for an annuity business, leading to a mismatch between actual and expected annuity payments; and
- cash outflows from the shareholder business, e.g. due to tax. See Note 28 (F) for further details.

Non-financial risk

The Company is exposed to business environment, strategic, reputational, conduct, operational and group risk.

(a) Business environment risk

Business environment risk is the risk of exposures to forces in the external environment that could significantly change the fundamentals that drive the business's overall objectives and strategy.

Key dimensions to business environment risk pertaining to the Company are regulatory, political, macroeconomic, technology and market competition.

- Regulatory: Changes in UK government policy, legislation (including tax), regulation or regulatory interpretation applying to insurance companies may adversely affect the Company's product range, distribution channels, capital requirements and, consequently, reported results and financing requirements. Regulators in other jurisdictions in which the Company operates may also introduce changes in the regulatory framework for long-term savings and retirement arrangements and investments, including to selling practices and solvency requirements.

- Political: Global political risks have been on the rise and look set to remain heightened. Domestically, the withdrawal of the UK from the EU introduces significant uncertainties for both the UK and the EU, affecting consumer and market confidence, and potentially increasing market volatility and the risk of a downturn in economic activity.

- Macroeconomic: Macroeconomics refers to the behaviour of the aggregate economy, focusing on factors such as economic growth, inflation, productivity and unemployment. The UK macroeconomic environment is expected to become more challenging, and may adversely impact consumer behaviour.

- Technology: The Company has a high dependency on technology to operate effectively with the maintenance, integrity and resilience of the IT infrastructure and applications paramount to meeting business and customer needs. The Company's current reliance on a large number of legacy systems spread over a complex supply chain and increasing utilisation of outsourcing/Cloud deployments creates an enhanced risk of breaches and IT issues. Additionally, the rising cyber threat and importance of customer data security requires increased focus on cyber and data privacy controls to mitigate the risks posed by a larger digital footprint and increasingly sophisticated attacks.

- Competition: The UK Financial Services market is highly competitive with several factors affecting the Company's ability to sell its products and maintain its profitability. Key considerations include; price and yields offered; financial strength and ratings; investment performance and historic bonus levels; brand strength and name recognition; developing demographic trends and customers' appetite or need for certain savings products.

(b) Strategic risk

Strategic risk is the risk of ineffective, inefficient, or inadequate senior management processes for the development and implementation of business strategy in relation to the business environment and the Company's capabilities.

The merger of M&G with Prudential UK and demerger from Prudential plc, along with the transformation strategy, will deliver capital-light, digitally-enabled, customer-focused solutions. This presents a significant opportunity to leverage scale, financial strength and complementary product and distribution capabilities but does carry risk for the Company in terms of overall availability of funding, resources and the wider impacts of an extensive change agenda.

(c) Reputational risk

Reputational risk is the risk of loss resulting from failure to proactively monitor stakeholder perceptions and effectively respond to events which may impact the Company's reputation.

A number of external events during 2018 provided a reminder of the potential for reputational damage, and the merger, demerger and transformation activities increase exposure to reputation risk for the Company. The anticipated Product Administration System (IT) migrations and increasing use of outsourcing and Cloud-based technologies pose a material threat to the Company's reputation if mishandled, due to the level of customer data potentially impacted and the visibility externally. Reputational risk considerations are also an important part of the Company's management of Environmental, Social and Governance issues.

(d) Conduct risk

Conduct risk is the risk that arises from the approach taken to customer relationships throughout the business model and is the risk that the Company's behaviours and decision making are inappropriate, leading to unfair or poor outcomes for customers.

Customer needs are central to all decisions the Company makes regarding the provision of financial products and services. The Company aims to uphold a reputation built over 170 years, for acting responsibly and with integrity in supporting customers whilst respecting the laws and regulations, as well as meeting internationally accepted standards of responsible business conduct.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2018 (continued)

(e) Operational risk

Operational risk is the risk of loss (or unintended gain or profit) arising from inadequate or failed internal processes, personnel and systems, or from external events. This includes employee error, system failures, fraud, the risk of a cyber-attack or some other event which disrupts business processes.

The Company's primary exposure to operational risk arises from business processes (e.g. customer administration, sales), people capabilities, operation of systems and financial reporting activity. The transformational changes to products, systems and outsourcers will all change the operational risk profile of the business, heightening it in the short-term but reducing it over the longer term. Additional exposure is anticipated as M&GPrudential demerges from Prudential plc.

The Company relies on a number of outsourcing partners to provide several business operations, including: back office, customer-facing operations, IT support functions and investment operations. This creates reliance upon the operational performance and long-term sustainability of these outsourcing partners, and failure to adequately oversee the outsourcing partner, or the failure of an outsourcing partner (or its key IT and operational systems and processes) could result in significant disruption to business operations and customers.

The transformational changes to products, systems and outsourcers will change the operational risk profile of the business, heightening it in the short-term but reducing it over the longer term due to significant investment in improving the control environment. Additional exposure is anticipated as M&G Prudential demerges from Prudential plc.

(f) Group risk

Group risk is the risk associated with being part of a group, particularly as a result of contagion. Being a member of a group can provide significant advantages for the Company in terms of diversification of risk, financial strength, technical expertise and management experience. It can also give rise to risks; for example, if a guarantee of financial support given by the parent were removed, or from particular transactions arising from an impaired parent or affiliate within the group. The independent capitalisation of the Company as well as the risk management processes and internal control mechanisms within the Company ensure group risk is appropriately managed. This is particularly important given the planned demerger.

On behalf of the Board of directors.

JAOwens

J A Owens
Company Secretary

20 March 2019

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2018

Incorporated and registered in England and Wales. Registered no. 15454

The directors present their report and the audited financial statements of the Company for the year ended 31 December 2018.

Likely developments, business strategies and prospects

Likely future developments in the business of the Company are discussed in the strategic report in accordance with section 414C of the Companies Act 2006 (the Act).

Ultimate parent company

On 26 November 2018 the Company's legal ownership was transferred from its previous parent company Prudential plc to a new holding company, M&G Prudential Limited. M&G Prudential Limited is a subsidiary of Prudential plc. The ultimate parent of the Company therefore remains Prudential plc.

Subsidiary, associate undertakings and branches

Particulars of the Company's subsidiary undertakings at 31 December 2018 are shown in note 30. During 2018, the Company transacted business through a branch outside the United Kingdom in Poland, prior to the Part VII transfer of its business on 1 January 2019, as discussed in the 'Post balance sheet events' section below. On 14 December 2018, the beneficial interest in the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were sold to Prudential Corporation Asia Limited, with the legal ownership transferring on 19 December 2018.

With-profits governance

The Company produces an annual with-profits report, which is available on request and our website at www.pru.co.uk, setting out how it has complied with its Principles and Practices of Financial Management (PPFM).

The Board has established a With-Profits Committee (WPC), made up of five members (each of whom is external and independent of the Company). The WPC provides the Board with an independent assessment of the way in which the Company manages its with-profits business, its compliance with the PPFM, and how the Company balances the rights and interests of policyholders and shareholders in relation to its with-profits funds. The WPC has the right, if it wishes, to make a statement to with-profits policyholders in addition to the Company's report described above.

The Company has a With-Profits Actuary who has the specific duty to advise the Board on the application of discretion in relation to with-profits business; and a Chief Actuary who provides the Board with certain actuarial advice, and fulfils various statutory duties under the new regulatory reporting regime introduced on 1 January 2016. Both of these are Financial Conduct Authority and Prudential Regulation Authority approved roles.

The Company has an Independent Governance Committee (IGC), formed as part of the Government's initiative to improve outcomes for pension scheme members. As a large pension scheme provider, the Company is required to set up and support an IGC, whose findings are reported to the Board and the Financial Conduct Authority. The IGC acts solely in the interests of scheme members, and to assess, raise concerns and report on the value for money of the Company's contract-based defined contribution workplace pension schemes on an ongoing basis, ensuring compliance with regulatory and legislative requirements.

Corporate responsibility

The Company is a wholly owned subsidiary within the Prudential Group and Corporate Responsibility (CR) is integral to the way the Group does business.

The Group, of which the Company is a part, has developed a Group Governance Framework which is underpinned by a Group Governance Manual and associated processes. This encompasses all key policies and procedures for example, the Group Code of Business Conduct.

As a business that provides savings, income, investment and protection products and services, social value is created through the day-to-day operations. The Group provides customers with ways to help manage uncertainty and build a more secure future. In seeking to match the long-term liabilities the Group has towards its customers with similarly long-term financial assets, it provides capital that finances businesses, builds infrastructure and fosters growth in both developed and developing markets.

The Group's sustainable approach to business is reinforced by the Group-wide CR strategy. While the Group believes that CR is best managed on the ground by those closest to the customer and local stakeholders, the Group approach is underpinned by four global CR themes:

- Serving its customers: The Group aims to provide fair and transparent products that meets the customers' needs;
- Valuing its people: The Group aspires to retain and develop highly engaged employees;
- Supporting local communities: The Group seeks to make a positive contribution to its communities through long-term partnerships with charitable organisations that make a real difference; and
- Protecting the environment: The Group takes responsibility for the environment in which it operates.

These themes demonstrate the Group's CR commitments and principles to its stakeholders and provide clarity to its businesses, including the Company, on where they should focus their CR efforts and resources in the context of their individual markets.

The Prudential plc Board discusses the Group's performance in the areas of social and environmental management at least once a year and also reviews and approves the Group's corporate responsibility report and strategy on an annual basis.

Post balance sheet events

M&GPrudential has been reviewing its operations across Europe since the UK voted to leave the European Union. In January 2019, in accordance with Part VII of the Financial Services and Markets Act 2000, the Company transferred all of its long term European business (excluding the UK) into PIA, a subsidiary of the Company which is based in the Republic of Ireland. The with-profits element of the business is reinsured back into the Company ensuring continuation of the economic substance of the previous situation. The shareholder business has not been reinsured back to the Company following the Part VII transfer.

Financial Performance

The state of affairs of the Company at 31 December 2018 is shown in the balance sheet on pages 26 and 27. The profit and loss account appears on pages 23 and 24.

Financial instruments

The Company is exposed to financial risk through its financial assets, financial liabilities, and policyholder liabilities. The financial risk factors affecting the Company include market risk, credit risk and liquidity risk. Information on the financial risk management objectives and policies of the Company and the exposure of the Company to the financial risk factors is given in note 28. Further information on the use of derivatives by the Company is provided in note 28 (G).

Share Capital

There have been no changes in the Company's share capital during 2018 as shown in note 21.

Dividends

Total dividends for 2018 were £9,963m.

An interim dividend of £282m was declared on 20 May 2018. A second interim dividend of £231m was declared on 22 November 2018. An additional interim dividend of £33m was paid in December following receipt of the proceeds from the sale of Hong Kong subsidiaries at the same amount.

In addition, the difference between the fair value of the Hong Kong subsidiaries at the date of sale of £9,450m and the consideration received of £33m represents a deemed distribution. An amount of £9,417m is therefore included within dividends within the financial statements.

The directors have not recommended a final dividend on the ordinary shares for 2018.

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2018 (continued)

In 2017 there was an interim dividend of £238m and a second interim dividend of £200m. The directors did not recommended a final dividend on the ordinary shares for 2017.

Directors

The present directors are shown on page 1. Dr I Owen was appointed on 18 April 2018 and Mr M Evans was appointed on 17 October 2018. There have been no further changes.

Disclosure to the auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

Auditor

KPMG LLP were reappointed as auditor of the Company by the members at last year's Annual General Meeting on 24 April 2017. It is the intention that KPMG LLP be reappointed under the deemed appointment rules of section 487 of the Companies Act 2006.

Directors' and officers' protection

Prudential plc has arranged appropriate insurance cover in respect of legal action against directors and senior managers of companies within the Prudential Group. In addition, the Articles of Association of the Company provide for the directors, officers and employees of the Company to be indemnified in respect of liabilities incurred as a result of their office. Prudential plc also provides protections for directors and senior managers of companies within the Group against personal financial exposure they may incur in their capacity. These include qualifying third party indemnity provisions (as defined by the relevant Companies Act) for the benefit of directors of Prudential plc, including, where applicable, in their capacity as a director of the Company and other companies within the Group. These indemnities were in force during 2018 and remain in force.

On behalf of the Board of directors.

JAOwens

J A Owens
Secretary
20 March 2019

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE STRATEGIC REPORT, DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of its profit or loss for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

KPMG

Independent auditor's report

to the members of The Prudential Assurance Company Limited

1. **Our opinion is unmodified**

We have audited the financial statements of The Prudential Assurance Company Limited ("the Company") for the year ended 31 December 2018 which comprise the profit and loss account, statement of comprehensive income, statement of changes in equity, balance sheet and the related notes, including the accounting policies in note 1.

In our opinion the financial statements:

— give a true and fair view of the state of Company's affairs as at 31 December 2018 and of its profit for the year then ended;

— have been properly prepared in accordance with UK accounting standards, including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland;* and

— have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were appointed as auditor by the shareholders in October 1999. The period of total uninterrupted engagement is for the 20 financial years ended 31 December 2018.

We have fulfilled our ethical responsibilities under, and we remain independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview		
Materiality: financial statements as a whole	£85m (2017: £186m) 1.2% (2017: 1.2%) of net assets	
Risks of material misstatement		**vs 2017**
Event driven NEW	The impact of uncertainties due to the UK exiting the European Union on our audit	▲
Recurring risks	Valuation of technical provisions	◀▶
	Valuation of investments	◀▶

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
The impact of uncertainties due to the UK exiting the European Union on our audit Refer to page 9 (Strategic report) and page 70 (financial disclosures)	**Unprecedented levels of uncertainty** All audits assess and challenge the reasonableness of estimates, in particular as described in the valuation of technical provisions and valuation of investments, and related disclosures and the appropriateness of the going concern basis of preparation of the financial statements (see below). All of these depend on assessments of the future economic environment and the company's future prospects and performance. Brexit is one of the most significant economic events for the UK and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown.	We developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included: — **Our Brexit knowledge –** We considered the directors' assessment of Brexit-related sources of risk for the company's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks. — **Sensitivity analysis –** When addressing the valuation of policyholder liabilities and valuation of investments, we compared the directors' analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty and, where forecast cash flows are required to be discounted, considered adjustments to discount rates for the level of remaining uncertainty. — **Assessing transparency** – As well as assessing individual disclosures as part of our procedures on valuation of policyholder liabilities and valuation of investments, we considered all of the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks. **Our results** — As reported under valuation of policyholder liabilities and valuation of investments, we found the resulting estimates and related disclosures of these matters and disclosures in relation to going concern to be acceptable. However, no audit should be expected to predict the unknowable factors or all possible future implications for a company and this is particularly the case in relation to Brexit.

2. Key audit matters: including our assessment of risks of material misstatement (continued)

	The risk	Our response
Valuation of technical provisions (2018: £132,770 million, 2017: £135,221 million) The risk is unchanged compared to the prior year. Refer to page 29 (accounting policy) and page 53 (financial disclosures).	**Subjective valuation:** The Company has significant technical provisions representing 72 percent (2017: 68 percent) of the Company's total liabilities. This is an area that involves significant judgement over uncertain future outcomes, mainly the ultimate total settlement value of long term policyholder liabilities. The valuation of the policyholder liabilities in relation to the annuity business requires significant judgment in the selection of key assumptions covering both operating assumptions and economic assumptions. The key operating assumptions are mortality, which is determined by reference to the Company's own experience and expected levels of future mortality, and the expected level of future expenses, which is based on the expected future costs for administering the underlying policies. The key economic assumption is credit risk that is based on the Company's view of expected future investment defaults. The effect of these matters is that, as part of our risk assessment, we determined that the valuation of technical provisions has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. **Calculation error and data capture** Management uses complex actuarial models to calculate policyholder liabilities. There is the risk that the modelling does not appropriately reflect the model specifications and / or the product features due to incorrect or incomplete data input into the model and / or unauthorised or erroneous changes to the models.	We used our own actuarial specialists to assist us in performing our procedures in this area. Our procedures included: — **Control design and operation:** We used our own IT specialists to assist us in performing our procedures in this area which included testing of the design, implementation and operating effectiveness of key controls over the valuation process including additional testing in relation to model evaluation as a result of identified weaknesses in the general IT control environment. Controls testing in respect of the valuation process included assessment and approval of the methods and assumptions adopted over the calculation of policyholder liabilities as well as appropriate access and change management controls over the actuarial models. — **Methodology choice:** We have assessed the methodology for selecting assumptions and calculating the policyholder liabilities. This included: — Assessing the methodology adopted for selecting assumptions by applying our industry knowledge and experience and comparing the methodology used against industry standard actuarial practice; — Evaluating the analysis of the movements in policyholder liabilities during the year, including consideration of whether the movements were in line with the methodology and assumptions adopted; and — Comparing changes in methodology to our expectations derived from market experience. — **Historical comparison:** — Evaluating the evidence used to prepare the mortality experience investigation by reference to actual mortality experience of the policyholders in order to assess whether this supported the year-end assumptions adopted. — Assessing whether the expense assumptions reflect the expected future costs of administering the underlying policies by analysing current year unit costs, considering the expected future level of expense inflation and assessing the appropriateness of the likely impact of planned management actions on future costs.

2. Key audit matters: including our assessment of risks of material misstatement (continued)

The risk	Our response
	— **Benchmarking assumptions and sector experience:** — Comparing mortality experience to industry data on current mortality and expectations of future mortality improvements. — Evaluating the credit risk methodology and assumptions by reference to industry practice and our expectation derived from market experience. — Using the results of our industry benchmarking of assumptions and actuarial market practice to inform our challenge of the assumptions in relation to the mortality, credit risk and expense assumptions. — **Model evaluation:** — Evaluating the appropriateness of the calibration of the Continuous Mortality Investigation ('CMI') model (the CMI Bureau releases industry wide mortality tables), adopted based on the analysis of the characteristics of the policyholder population and actual mortality experience. — Using our own valuation models to perform an independent recalculation of a sample of policyholder liabilities to ensure that the models have been calibrated in line with the Company's specifications. — **Assessing transparency**: Considering whether the Company's disclosures in relation to the assumptions used in the calculation of policyholder liabilities are compliant with the relevant accounting requirements and appropriately represent the sensitivities of these assumptions to alternative scenarios and inputs. **Our results** — We found valuation of technical provisions to be acceptable (2017 result: acceptable).

2. Key audit matters: including our assessment of risks of material misstatement (continued)

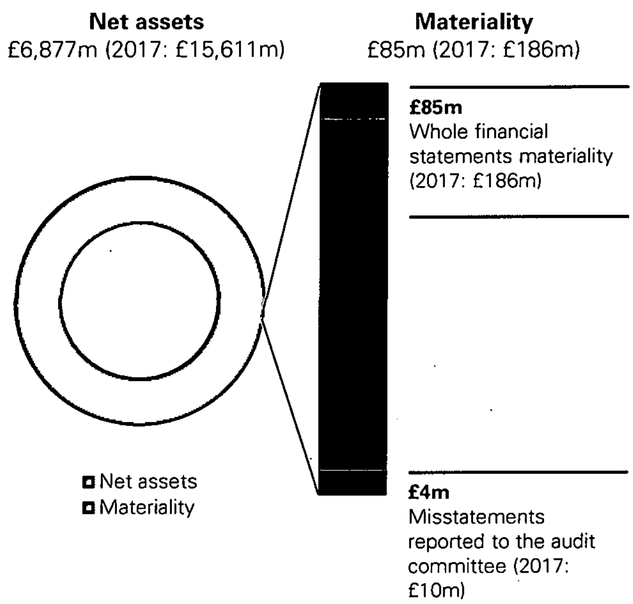
	The risk	Our response
Valuation of investments (2018: £160,527 million, 2017: £184,680 million, comprising investments of £145,981 million (2017: £166,377 million) and assets held to cover linked liabilities of £14,546 million (2017:£18,303 million)) The risk is unchanged compared to the prior year. Refer to page 31 (accounting policy) and page 49 (financial disclosures).	**Subjective valuation:** The areas that involved significant audit effort and judgement were the valuation of illiquid positions within the financial investments portfolio representing 14 per cent (2017: 9 per cent) of the total investment assets. These included private placement loans, unlisted Net Asset Value ('NAV') funds and equity release mortgages. For these positions a reliable third party price was not readily available and therefore the application of expert judgement in the valuations adopted is required. The effect of these matters is that, as part of our risk assessment, we determined that the valuation of these illiquid positions has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount.	We used our own actuarial and valuation specialists to assist us in performing our procedures in this area Our procedures included: — **Methodology choice:** We assessed the appropriateness of the pricing, methodologies with reference to relevant account standards and Company's own valuation guidelines as well as industry practice. — **Control design and operation:** Testing of the design, implementation and operating effectiveness of key controls over the valuation process for the investments, including review and approval of the estimates and assumptions used for the valuation and key authorisation and data input controls. — **Independent re-performance:** Remodelling the valuation of the assets and comparing the output to management's valuations. — **Benchmarking of assumptions and sector experience:** Validating the key inputs and assumptions used for the valuation and comparing these to our own market and industry benchmarks. — **Tests of detail:** — Independently obtaining the most recent NAV statements, investment manager and administrator control reports to assess the appropriateness of the fair value of the unlisted funds. — Performing a retrospective test over the NAV valuations for each fund to assess if the fund valuations reported in the audited financial statements in the prior year were materially consistent with the most recent NAV valuation statements available at the time. — **Assessing transparency:** Assessing whether the Company's disclosures in relation to the valuation of investments are compliant with the relevant accounting requirements and appropriately present the sensitivities in the valuations based on alternative outcomes. **Our results** — We found valuation of investments to be acceptable (2017 result: acceptable).

3. Our application of materiality and an overview of the scope of our audit

Materiality for the financial statements as a whole was set at £85m (2017: £186m), determined with reference to a benchmark of net assets (of which it represents 1.2%(2017: 1.2%) We consider net assets to be the most appropriate benchmark as we consider this to be the metric that is most relevant to the users of the financial statements.

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £4 million (2017: £10 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Our audit of the company was undertaken to the materiality level specified above and was all performed at the Company's offices in the UK (London, Reading and Craigforth) and India (Mumbai).



4. We have nothing to report on going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease its operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Company will continue in operation.

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Company's business model and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period. The risks that we considered most likely to adversely affect the Company's available financial resources over this period were

— Adverse impacts arising from fluctuations or negative trends in the economic environment which affect the valuations of the Company's investments, wider credit spreads and defaults and valuation of policyholder liabilities due to the impact of these market movements; and

— Adverse policyholder lapse or claims experience.

As these were risks that could potentially cast significant doubt on the Company's ability to continue as a going concern, we considered sensitivities over the level of available financial resources indicated by the Company's financial forecasts taking account of reasonably possible (but not unrealistic) adverse effects that could arise from these risks individually and collectively and evaluated the achievability of the actions the Directors consider they would take to improve the position should the risks materialise. We also considered less predictable but realistic second order impacts, such as failure of counterparties who have transactions with the Company (such as banks and reinsurers) to meet commitments that could give rise to a negative impact on the Company's financial position, increased illiquidity which also adds to uncertainty over the accessibility of financial resources and may reduce capital resources as valuations decline and the impact of Brexit on the economic environment and the resulting impact on the Company's capital resources.

Based on this work, we are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least a year from the date of approval of the financial statements.

We have nothing to report in these respects, and we did not identify going concern as a key audit matter

5. We have nothing to report on the strategic report and the directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

— we have not identified material misstatements in those reports;

— in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. **We have nothing to report on the other matters on which we are required to report by exception**

Under the Companies Act 2006, we are required to report to you if, in our opinion:

— adequate accounting records have not been kept by the Company, or returns adequate for our audit have not been received from branches not visited by us; or

— the financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. **Respective responsibilities**

Directors' responsibilities

As explained more fully in their statement set out on page 14, the Directors are responsible for the preparation of the financial statements including being satisfied that they give a true and fair view. They are also responsible for: such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience, and through discussion with the directors and other management (as required by auditing standards), and from inspection of the company's regulatory and legal correspondence and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably. Firstly, the company is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits legislation and taxation legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the company is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of company's licence to operate. We identified the area of regulatory capital as that most likely to have such an effect recognising the financial and regulated nature of the company's activities Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors (and other management) and inspection of regulatory and legal correspondence, if any. These limited procedures did not identify actual or suspected non-compliance.

Owing to inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

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

Daniel Cazeaux (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
Canary Wharf
London
E14 5GL
20 March 2019

Profit and Loss Account for the year ended 31 December 2018

Long-term Business Technical Account		2018 £m	2017 £m	Note
Gross premiums written		**13,002**	13,077	2
Outward reinsurance premiums		**(13,117)**	(1,030)	
Earned premiums, net of reinsurance		**(115)**	12,047	
Investment income		**10,993**	11,028	3
Unrealised (losses) gains on investments		**(14,141)**	1,300	
Claims paid				
	Gross amount	**(12,163)**	(12,019)	
	Reinsurers' share	**1,435**	1,085	
Claims paid, net of reinsurance		**(10,728)**	(10,934)	
Change in provision for claims				
	Gross amount	**(34)**	(29)	
Claims incurred, net of reinsurance		**(10,762)**	(10,963)	
Change in long-term business provision				
	Gross amount	**2,417**	(9,283)	
	Reinsurers' share	**9,074**	318	
		11,491	(8,965)	
Change in technical provision for linked liabilities		**3,721**	(54)	
Change in other technical provisions, net of reinsurance		**15,212**	(9,019)	
Net operating expenses		**(949)**	(1,011)	5
Investment expenses and charges		**(343)**	(408)	6
Tax attributable to the long-term business		**379**	(670)	7
Transfer from (to) the fund for future appropriations		**137**	(1,569)	
Balance on the long-term business technical account		**411**	735	

The accounting policies on pages 28 to 34 along with the accompanying notes on pages 35 to 86 form an integral part of the financial statements.

Profit and Loss Account for the year ended 31 December 2018 (continued)

Non-Technical Account

	2018 £m	2017 £m	Note
Balance on the long-term business technical account	**411**	735	
Tax credit attributable to the balance on the long-term business technical account	**74**	180	7
Balance on the long-term business technical account before tax	**485**	915	
Investment income	**9,691**	15	3
Unrealised (losses) gains on investments	**(8,823)**	1,659	
Other income	**19**	17	
Other charges	**(20)**	(14)	
Total profit on other activities	**867**	1,677	
Profit on ordinary activities before tax	**1,352**	2,592	
Tax on profit on ordinary activities	**(123)**	(166)	7
Profit for the financial year	**1,229**	2,426	

The accounting policies on pages 28 to 34 along with the accompanying notes on pages 35 to 86 form an integral part of the financial statements.

Note: General Business Technical Account

The Company no longer underwrites new non-life insurance contracts directly and its run-off obligations have been reinsured (as explained further in note 2b). As such the non-life business is no longer material enough to require the presentation of a technical underwriting account and instead the relevant information is presented in note 2b.

Statement of Comprehensive Income for the year ended 31 December 2018

	2018 £m	2017 £m	Note
Profit for the financial year	**1,229**	2,426	
Other comprehensive income:			
Revaluation of group-occupied property	**6**	2	
Actuarial gains on defined benefit pension schemes	**46**	94	9
Deferred tax (charge)	**(8)**	(16)	
Transfer (to) from the fund for future appropriations	**(44)**	(80)	
Total other comprehensive income for the financial year, net of income tax	**—**	—	
Total comprehensive income for the financial year	**1,229**	2,426	

The accounting policies on pages 28 to 34 along with the accompanying notes on pages 35 to 86 form an integral part of the financial statements.

Statement of changes in equity for the year ended 31 December 2018

	Share Capital	Other reserves (*)	Profit and loss account	Total
	£m	£m	£m	£m
Balance at 1 January 2017	330	536	12,757	13,623
Profit for the financial year	—	—	2,426	2,426
Other comprehensive income for the financial year	—	—	—	—
Total comprehensive income for the financial year	—	—	2,426	2,426
Dividends	—	—	(438)	(438)
Total distribution to owners, recognised directly in equity	—	—	(438)	(438)
Balance as at 31 December 2017	**330**	**536**	**14,745**	**15,611**
Balance as at 1 January 2018	330	536	14,745	15,611
Profit for the financial year	—	—	1,229	1,229
Total comprehensive income for the financial year	—	—	1,229	1,229
Dividends	—	—	(9,963)	(9,963)
Total distribution to owners, recognised directly in equity	—	—	(9,963)	(9,963)
Balance as at 31 December 2018	**330**	**536**	**6,011**	**6,877**

(*) Other reserves are capital reserves relating to the acquisition of Scottish Amicable Life Assurance Society in 1997.

Balance sheet as at 31 December 2018

Assets	**2018**	2017	Note
	£m	£m	
Intangible assets			
Computer software	**6**	8	12
	6	8	
Investments			
Land and buildings	**9,064**	8,837	13
Investments in group undertakings and participating interests	**5,155**	13,267	14
Other financial investments	**131,762**	144,273	15
	145,981	166,377	
Assets held to cover linked liabilities	**14,546**	18,303	16
Reinsurers' share of technical provisions			17
Long-term business provision	**10,978**	1,904	
Claims outstanding	**142**	144	
Technical provisions for linked liabilities	**7,135**	5,772	
	18,255	7,820	
Debtors			
Debtors arising out of direct insurance operations			
Policyholders	**20**	21	
Intermediaries	**1**	1	
Debtors arising out of reinsurance operations	**11**	9	
Other debtors	**1,487**	1,326	18
	1,519	1,357	
Other assets			
Cash at bank and in hand	**2,080**	3,365	19
Finance lease assets	**33**	33	13
	2,113	3,398	
Prepayments and accrued income			
Accrued interest and rent	**744**	871	
Deferred acquisition costs: long-term business	**40**	45	
Accrued external dividends receivable	**68**	63	
Other prepayments and accrued income	**142**	179	
	994	1,158	
Total assets (excluding pension asset)	**183,414**	198,421	
Pension asset	**130**	110	9
Total assets (including pension asset)	**183,544**	198,531	

Balance sheet as at 31 December 2018 (continued)

Liabilities	**2018**	2017	Note
	£m	£m	
Capital and reserves			
Share capital	**330**	330	21
Other reserves	**536**	536	
Profit and loss account	**6,011**	14,745	
Shareholders' funds – equity interests	**6,877**	15,611	2
Fund for future appropriations	**13,487**	13,581	
Technical provisions			
Long-term business provision	**132,084**	134,566	26
Claims outstanding	**674**	641	8
Unearned revenue provision	**12**	14	
Total technical provisions	**132,770**	135,221	
Technical provisions for linked liabilities	**21,681**	24,075	
Provisions for other risks and charges			
Deferred taxation	**711**	1,334	7
Obligations under finance leases	**17**	18	13
Other	**401**	408	22
	1,129	1,760	
Deposits received from reinsurers	**1,172**	1,260	
Creditors			
Creditors arising out of direct insurance operations	**64**	89	
Creditors arising out of reinsurance operations	**78**	36	
Other borrowings not owed to credit institutions	**89**	123	
Other creditors including taxation and social security	**6,043**	6,635	23
	6,274	6,883	
Accruals and deferred income	**154**	140	
Total liabilities	**183,544**	198,531	

The accounting policies on pages 28 to 34 along with the accompanying notes on pages 35 to 86 form an integral part of the financial statements.

The accounts on pages 23 to 86 were approved by the Board of directors on 20 March 2019 and were signed on its behalf by:

C J Bousfield
Director
20 March 2019

Notes on the financial statements

1. Accounting policies

A. Company Information

The Prudential Assurance Company Limited (the Company) is a private limited company, incorporated and registered in England and Wales.

The address of its registered office is Laurence Pountney Hill, London EC4R 0HH.

B. Basis of Preparation

The financial statements are prepared in accordance with Part 15 of the Companies Act 2006 (the Act) and Schedule 3 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the Regulations). The financial statements are prepared in accordance with Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (FRS 102) and Financial Reporting Standard 103, "Insurance Contracts" (FRS 103), and have been prepared under the historical cost accounting rules, modified to include the revaluation of investments.

As the Company is a wholly owned subsidiary undertaking of another company registered in England and Wales, group financial statements are not prepared. Accordingly, the financial statements present information about the Company as an individual undertaking and are not consolidated.

The Company's ultimate parent, Prudential plc, includes the Company in its consolidated financial statements. Details of where to obtain copies of the consolidated accounts are disclosed in note 24. In these financial statements, the Company is considered to be a qualifying entity under FRS 102 and has applied the exemptions available in respect of the following disclosures:

- Reconciliation of the number of shares outstanding from the beginning to end of the period;
- Cashflow Statement and related notes;
- Key Management Personnel Compensation; and
- Related party transactions with wholly owned subsidiary undertakings of the Prudential Group.

As the consolidated financial statements of Prudential plc include the equivalent disclosures, the Company has also taken the exemptions available under FRS 102 in respect of certain disclosures required by FRS 102.26 *Share Based Payments* (FRS 102.26).

The financial statements are prepared in pounds sterling (£) which is the functional currency of the Company and rounded to the nearest million (£m).

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

The preparation of the financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The tables below set out the areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements.

Critical accounting judgements	**Accounting policy/note reference**
Classification of insurance and investment contracts	C

Critical accounting estimates	**Accounting policy/note reference**
Measurement of long-term business provision	C and 26
Determination of fair value of financial investments	F and 28
Measurement of pension scheme	J and 9

Notes on the financial statements (continued)

1 Accounting Policies (continued)

The directors have a reasonable expectation that the Company will be able to continue in operational existence for the foreseeable future and thus continue to adopt the going concern basis of accounting in preparing the financial statements. This conclusion has been based upon the following:

- The Company is a subsidiary within the Prudential Group and it and its ultimate parent company are continuing to trade profitably and there are no plans for liquidation. Prudential plc and the Company have put in place intra-group arrangements to formalise circumstances in which capital support would be made available by Prudential plc. While it is considered unlikely that such support will be required, the arrangements are intended to provide additional comfort to the Company and its policyholders.

- The Company has a satisfactory capital surplus, generates positive cashflows and has very low debt-financing. It is supported by its inherited estate, which is surplus capital available on top of what is necessary to cover policyholders' reasonable expectations, and which has not yet been allocated to policyholders or shareholders. Consideration has also been given to the Company's performance, the market in which it operates, its strategy and risks and uncertainties, as set out in the Strategic Report on pages 2 to 10. The management of financial risk is set out in note 28, including the Company's exposure to credit risk and liquidity risk which it carefully manages through cashflow forecasting and fund management.

In assessing the going concern of the Company, the directors have assessed the Company's current and projected solvency position under Solvency II, and consider the Company to have an appropriate capital surplus in line with the Company's risk appetite.

C. Long-term Business

i. *Classification of insurance and investment contracts*

The measurement basis of long-term business contract liabilities is dependent upon the classification of the contracts under FRS 103 as either insurance contracts (if the level of insurance risk is significant), or investment contracts (if the risk is insignificant). A further distinction is made between investment contracts with and without discretionary participation features. Discretionary participation features (DPF) represent the contractual right to receive additional profit-sharing benefits as a supplement to guaranteed benefits. The Company's insurance contracts and investment contracts with DPF are primarily with-profits and other protection type or annuity policies. The investment contract without DPF classification applies primarily to certain unit-linked and similar contracts written by the Company.

Insurance contracts and investment contracts with DPF are accounted for under FRS 103. Investment contracts without DPF are accounted for as financial liabilities under FRS 102.11 *Basic Financial Instruments* and, where relevant, the provisions of FRS 102.23 *Revenue* in respect of the attaching investment management features of the contracts.

The provisions for investment contracts without DPF are included in Technical Provisions for Linked Liabilities in the balance sheet.

ii. *Technical account treatment*

Premiums and annuity considerations for conventional with-profit policies and other protection type life insurance and annuity policies are accounted for when due. For unit-linked business and unitised with-profit policies, premiums are accounted for when the liabilities arising from the premiums are recognised. Premiums exclude any taxes or duties based on premiums. Pensions annuity contracts that vest during the year are included in claims incurred and premium income at the annuity purchase price.

Claims paid include maturities, annuities, surrenders and death claims. Maturity claims are accounted for on the policy maturity date. Annuity claims are accounted for when the annuity becomes due for payment. Surrenders are accounted for when paid and death claims when notified.

Under FRS 102.11, the accounting treatment for investment contracts without DPF reflects the deposit nature of the arrangement with premiums and claims reflected as deposits and withdrawals taken directly to the balance

Notes on the financial statements (continued)

1 Accounting Policies (continued)

sheet as a movement on the investors' liability with the long-term technical account reflecting fee income, expenses and taxation on these contracts.

The costs of acquiring new non-profit insurance contracts, principally commission and directly attributable costs associated with policy issue and underwriting, which are not matched by policy charges are capitalised and amortised against margins in future revenues on the related insurance contracts for non-profit business to the extent that the amounts are recoverable out of margins.

Under FRS 102, for investment contracts without DPF, only the incremental, directly attributable acquisition costs relating to the securing of the investment management element of the contracts can be capitalised and amortised in line with related revenue. If these contracts involve up-front charges, this income is also deferred and amortised through the technical account in line with contractual service provision.

Bonus additions made to policies are included in the change in the long-term business provision or, where the policy is no longer in force, in claims incurred. Shareholder profits arising from traditional with-profits business are simply 1/9th of the annual and final bonus distributions. Under FRS 103, shareholders' transfers are recognised only on declaration. Unlike traditional with-profits products, no regular or final bonuses are declared for PruFund contracts. Policyholder return is determined by an Expected Growth Rate (EGR) which is declared each quarter. The shareholder transfer only crystallises at the point when a claim is paid to the policyholder and is 1/9th of the difference between the policyholder payout and the premium(s) paid.

The fund for future appropriations (FFA) comprises amounts arising in relation to participating policies and other non-linked policies, the allocation of which to policyholders or to shareholders has not been determined at the balance sheet date.

For non-profit and investment linked business, the profits are a modified form of cash flow profits on the basis of income less outgoings less movement in reserves. The accounting modifications are deferred acquisition costs and deferred income as appropriate, as described above.

iii. *Measurement of long-term business provisions*

The assumptions used to calculate the long-term business provisions are described in note 26.

The Company applies FRS 103, which requires with-profits funds to use the realistic value of liabilities as the basis for the estimated value of the liabilities to be included in the financial statements.

Realistic reserves are established using best estimate assumptions, and taking into account the firm's regulatory duty to treat its customers fairly.

The realistic value of liabilities is calculated as:
(i) a with-profits benefits reserve (WPBR) plus
(ii) future policy related liabilities (FPRL) plus
(iii) the realistic current liabilities of the fund

The WPBR is the main component of the product related liability, and is mainly determined using a retrospective asset share calculation.

Asset shares are calculated by rolling up the premiums paid (net of expenses and charges), using the actual investment returns earned on the with-profits fund. The assumptions used within the asset share calculations are consistent with those that are used to determine policyholders' bonuses. A number of adjustments are made to reflect future expected policyholder benefits and other outgoings.

For certain classes of business a prospective bonus reserve valuation is performed instead, valuing future claims and expenses using the expected future bonus rates.

The FPRL includes a market consistent valuation of the costs of guarantees, options and smoothing. This is determined using stochastic modelling. The FPRL also includes other liabilities such as tax on shareholder transfers and enhancements to policy benefits arising from the distribution of surplus from non-profit business written within the with-profits fund. For the Scottish Amicable Insurance Fund (SAIF), the realistic liability calculation

Notes on the financial statements (continued)

1 Accounting Policies (continued)

requires that all of the surplus within the fund is distributed to policyholders and therefore the FPRL is increased up to the point where the fund has no working capital.

D. General Business

The Company no longer underwrites general business directly and its run-off obligations have been reinsured externally. Claims incurred comprise the settlement and handling costs of paid claims arising from events occurring in the year and adjustments to prior years' claims provisions. Outstanding claims comprise claims incurred up to but not paid at the end of the accounting period whether reported or not.

Transactions in respect of general business operations in run-off are presented in note 2b.

E. Reinsurance

In the normal course of business the Company 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 balance sheet representing payments due from or premiums due to reinsurers and the reinsurers' share of technical provisions. The measurement of reinsurers' share of technical provisions is consistent with the measurement of the underlying direct insurance contracts.

F. Investments

Investment income and realised and unrealised gains or losses in respect of long-term business are included in the long-term business technical account. Other investment income and realised and unrealised gains or losses are included in the non-technical account.

Realised gains or losses are determined as the difference between net proceeds on disposal and the purchase price. Movements in unrealised gains or losses comprise the change in the value of investments held at the balance sheet date and the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals.

Investments in group undertakings and participating interests are carried at fair value through profit and loss. The Company's long-term business investments are taken to the technical account while the shareholder investments are taken to the non-technical account.

The Company has chosen to account for its financial instruments in accordance with FRS 102.11.2(b) which applies the recognition and measurement provisions of IAS 39 (as adopted for use in the EU) with the disclosure requirements of FRS 102.11 and FRS 102.12 *Other Financial Instruments* (FRS 102.12). Upon initial recognition financial investments are recognised at fair value. Subsequently, the Company is permitted, subject to specific criteria, to designate its investments as either 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. The Company holds financial investments on the following bases:

(i) Financial investments at fair value through profit and loss - this comprises assets designated by management as fair value through profit and loss on inception and derivatives. These investments are valued at fair value with all changes thereon being recognised in the profit and loss account. An analysis of net gains/losses is disclosed separately in note 3 and note 15. The Company uses bid prices to value its quoted financial investments. Actively traded investments without quoted prices are valued using external broker bid prices. If there is no active established market for an investment, the Company applies an appropriate valuation technique such as discounted cashflow analysis. Further information on valuation techniques is provided in note 28(A).

(ii) Loans and receivables - these comprise 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 secured by mortgages, deposits, loans to policyholders and other unsecured loans and receivables. These investments are carried at amortised cost using the effective interest method and are subject to impairment reviews. The Company measures the amount of the impairment loss by comparing the amortised cost with the present value of its estimated future cashflows discounted at the original effective interest rate. If, in subsequent periods, an impaired loan or receivable recovers in value (in part or in full),

Notes on the financial statements (continued)

1 Accounting Policies (continued)

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).

Certain mortgage loans of the Company have been designated at fair value through profit and loss as this loan portfolio is managed and evaluated on a fair value basis and these are included within loans in the balance sheet.

The Company policy on derecognition of financial assets is to only derecognise when it is deemed that substantially all the risks and rewards of ownership have been transferred.

Basic financial assets, including deposits with ceding undertakings, debtors arising out of direct insurance or reinsurance operations, other debtors and cash are initially recognised at transaction price plus attributable transaction costs. Subsequent to initial recognition they are measured at amortised cost using the effective interest method and subject to impairment reviews where appropriate.

The Company uses derivatives for the purpose of efficient portfolio management or the reduction in investment risk. In so doing, the Company obtains cost effective and efficient exposure to various markets to manage exposure to interest rate, currency, credit and other business risks. Derivatives are carried at fair value with movements in fair value being recorded in the long term technical account or non-technical account. The Company has opted not to apply hedge accounting to derivatives.

Properties are carried at fair value, with changes in fair value included in the profit and loss account in accordance with FRS 102.16 *Investment Property* (FRS 102.16). Properties are valued annually, by a number of different professional external valuers using the Royal Institution of Chartered Surveyors valuation standards. No depreciation is provided on investment properties as the directors consider that to depreciate them would not give a true and fair view.

In accordance with the provisions of Schedule 3 of the regulations, there is a requirement to show the net book value of properties on a historical cost basis in a note to the accounts. For this purpose properties are depreciated over forty years. Leasehold properties are depreciated over forty years, or if the lease is less than forty years, over the length of the lease.

Leases of investment property where the Company 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. Finance leases are subsequently measured at fair value.

Group-occupied properties are carried at fair value in the balance sheet and are valued annually, by a number of different external valuers using the Royal Institution of Chartered Surveyors valuation standards. An increase in fair value is recognised in other comprehensive income, except to the extent that it is the reversal of a previous valuation decrease which was recognised in profit or loss. A decrease in fair value is recognised immediately in profit or loss, except to the extent that it reverses a previous revaluation surplus recognised in other comprehensive income.

G. Financial Liabilities

Financial liabilities are designated as either fair value through profit and loss, amortised cost or investment contracts with DPF accounted for under FRS 103.

The Company holds financial liabilities on the following bases:

(i) Financial liabilities at fair value through profit and loss - these comprise derivatives, investment contracts without DPF and certain creditors. Derivative liabilities and certain creditors are valued at fair value with all changes thereon being recognised in the profit and loss account. An analysis of net gains/losses is disclosed separately in note 3 and note 15. The accounting policy for investment contracts without DPF is described in section C above.

(ii) Financial liabilities that are not valued at fair value through profit and loss and are not investment contracts with DPF are mainly creditors shown at settlement value.

Notes on the financial statements (continued)

1 Accounting Policies (continued)

(iii) Investment contracts with DPF. The accounting policy is covered in section C above.

The Company's policy on derecognition of financial liabilities is to derecognise only when the obligation specified in the contract is discharged, cancelled or has expired.

H. Tax

Tax on the profit or loss for the year comprises current and deferred tax. The UK HM Revenue & Customs rules for taxing long-term business are significantly different to those applying to non-insurance companies and the different classes of business written by the Company are themselves subject to distinct rules.

Current tax is the expected tax payable on all taxable profits arising in the current year, using tax rates enacted or substantively enacted at the balance sheet date, plus any adjustment to tax payable in respect of previous years. Taxable profits have been calculated using accounting profit or loss as a starting point.

Deferred tax is provided on timing differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rate that is expected to apply to the reversal of the related difference, using tax rates enacted or substantively enacted at the balance sheet date.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that it is probable that they will be recovered against the reversal of deferred tax liabilities or other future taxable profits.

Except where otherwise required by accounting standards, full provision for deferred tax without discounting is made for all timing differences which have arisen but not reversed at the balance sheet date.

I. Foreign Currency

Monetary foreign currency assets and liabilities are translated at the year end exchange rates and foreign currency transactions are translated into the functional currency using the spot exchange rates at the dates of the transactions. The trading results of the Polish branch are translated at average exchange rates for the year. Exchange difference are included in the profit and loss account.

J. Pension Costs

The Company applies the requirements of FRS 102.28 *Employee Benefits* (FRS 102.28). The Prudential Group operates a number of defined benefit pension schemes and a portion of these defined benefit pension schemes' surplus or deficit is attributed to the Company. Further details are disclosed in note 9.

The assets and liabilities of the defined benefit pension schemes of the Prudential Group are subject to a full triennial actuarial valuation using the projected unit method. Estimated future cashflows are 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 their present value. The Prudential Staff Pension Scheme (PSPS) is the largest defined benefit scheme and accounts for 82% of the underlying scheme liabilities of the Prudential Group's defined benefit schemes. There is also a smaller defined benefit scheme, Scottish Amicable Staff Pension Scheme (SASPS). The difference between the fair value of the scheme assets and the actuarial value of the scheme liabilities is a surplus or deficit on the scheme. The Company's share of pension surplus is recognised to the extent that the Company is able to recover a surplus either through reduced contributions in the future or through refunds from the scheme.

The aggregate of the actuarially determined service cost of the currently employed personnel, gains and losses on settlements and curtailments, and the interest on the net defined benefit liability/asset are recognised in the profit and loss account.

The actuarial gains and losses which arise from changes in assumptions, the return on plan assets greater or less than the discount rate, and experience gains and losses on liabilities are recognised in the statement of comprehensive income. Actuarial gains and losses also include adjustment for unrecognised pension surplus.

Notes on the financial statements (continued)

1 Accounting Policies (continued)

K. Intangible Assets

Intangible assets are carried at cost less amortisation and any accumulated impairment losses.

Intangible assets also include computer software amortised over three years with the exception of a policy administration system used by the Polish branch which is amortised over eight years.

L. Dividend Policy

Interim and final dividends are recognised in the period in which they are declared to the extent that they are unconditional on any future events. Dividends declared after the balance sheet date in respect of the prior reporting period are treated as a non-adjusting event. Dividend income is recognised when the right to receive payment is established.

M. Share-based Payments

The Company offers share award and option plans for certain key employees and a Save As You Earn (SAYE) plan for all UK employees. The Company has both equity-settled plans and cash-settled plans.

Share options and awards of the parent company's equity instruments, for which the parent company (Prudential plc) has the obligation to settle, are valued using the share price at the date of grant and are accounted for as equity-settled i.e. recognised in equity as a capital contribution from Prudential plc. Share options and awards for which the Company has the obligation to settle are valued using the share price at the balance sheet date and are accounted for as cash-settled i.e. as an obligation to transfer the equity instruments of Prudential plc. The compensation costs for all awards and options are recognised in net income over the plans' respective vesting periods.

The majority of employees in the UK are employed by Prudential Distribution Limited, a service company within the Prudential Group. Therefore the share-based payment cost for the Company is immaterial. Further details of the main share award and share option plans are disclosed in the accounts of Prudential Distribution Limited.

N. Cash at bank and in hand

The Company applies the definitions of cash and cash equivalents as defined in FRS 102.7 *Statement of cashflows* (FRS 102.7) for amounts disclosed under cash at bank and in hand. This consists 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 day's maturity from the date of acquisition.

O. Provisions and contingencies

Appropriate provision is made in the financial statements where the Company either has an obligation, or it is probable that it has an obligation, arising from past events and a reliable estimate of the obligation can be made. Consistent with FRS 102.21 *Provisions and Contingencies* (FRS 102.21) no provisions are made for contingent liabilities, but they are disclosed in note 27.

Notes on the financial statements (continued)

2. Segmental Analysis

(a) Long-term business

Premiums and profit

	Gross premiums written		Balance on the technical account before tax	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
United Kingdom	**12,088**	12,252	**490**	921
Poland	**29**	18	**(3)**	(5)
Europe	**885**	807	**(2)**	(1)
	13,002	13,077	**485**	915

New business

	Regular premiums		Single premiums	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
United Kingdom	**162**	173	**12,369**	12,097
Poland	**15**	12	**—**	—
Europe	**—**	—	**875**	788
	177	185	**13,244**	12,885

New business amounts include business accounted for as investment contracts, as well as insurance contracts business included within gross premiums written in the income statement.

Analysis of premium income	**2018** **£m**	2017 £m
Direct	**12,117**	12,270
Reinsurance accepted	**885**	807
	13,002	13,077
Individual business	**11,341**	11,389
Group contracts	**776**	881
	12,117	12,270
Regular premiums	**757**	775
Single premiums	**11,360**	11,495
	12,117	12,270
Participating contracts	**10,741**	10,450
Non-participating contracts	**282**	291
Linked long-term contracts (excluding investment contracts without discretionary participation features)	**1,094**	1,529
	12,117	12,270
United Kingdom	**12,088**	12,252
Poland	**29**	18
	12,117	12,270

Notes on the financial statements (continued)

The geographical analyses of long-term premiums are based on the territory of the operating unit assuming the risk. Premiums by territory of risk are not materially different.

Net reinsurance income

Net reinsurance expense in respect of long-term business for the year ended 31 December 2018 was £1,245m (2017: £713m income).

(b) General business

Analysis of technical account	Gross Claims Incurred		Reinsurance Balance	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Other (*)	**1**	8	**(1)**	(8)
	1	8	**(1)**	(8)

* Other business is primarily employers' liability and public liability insurance.

The general insurance business consists of operations in run-off comprising UK personal and commercial lines. All the business is fully reinsured externally and as such there is no profit or loss arising.

(c) Shareholders' funds

Shareholders' funds relate to the following countries:

	Shareholders' Funds	
	2018	2017
	£m	£m
United Kingdom	**6,889**	15,620
Poland	**(12)**	(9)
Total	**6,877**	15,611

Notes on the financial statements (continued)

3. Investment income

	Long-term business		Non-technical account	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Income from:				
Group undertakings	**122**	84	**185**	89
Other investments				
Land and buildings	**466**	496	**—**	—
Other investments	**4,663**	5,150	**111**	35
	5,251	5,730	**296**	124
Gains on loans and receivables	**9**	16	**—**	1
Gains on the realisation of investments at fair value through profit and loss other than derivatives	**5,918**	4,436	**9,452**	8
(Losses) gains on the realisation of derivatives – see note 28	**(351)**	875	**(59)**	(127)
(Decrease) Increase in the value of subsidiaries	**(19)**	—	**2**	9
Exchange gains (losses)	**144**	(73)	**—**	—
Fees for policy administration and asset management services arising from unit-linked investment contracts	**41**	44	**—**	—
	10,993	11,028	**9,691**	15

All income is from assets measured at fair value with the exception of interest income on loans and receivables which was £89m for the year ended 31 December 2018 (2017: £66m).

All gains above are from assets measured at fair value with the exception of gains on loans and receivables.

4. Bonuses

Bonuses added during the year are included in the change in the long-term business provision or, where the policy is no longer in force, in claims incurred. The total cost of bonuses was £2,737m (2017: £2,507m) analysed between the with-profits sub-fund and defined charge participating sub-fund of £2,409m (2017: £2,153m) and the Scottish Amicable Insurance Fund of £328m (2017: £354m).

5. Net operating expenses

	Long-term business	
	2018	2017
	£m	£m
Acquisition costs	**183**	218
Change in deferred acquisition costs	**5**	7
Administrative expenses*	**760**	769
Amortisation of computer software & licence and distribution rights (note 12)	**1**	17
	949	1,011

* Included in administrative expenses is a charge of £Nil (2017: charge of £225m) to cover the costs of undertaking the FCA Thematic Review and any potential redress (covered further in note 22).

Notes on the financial statements (continued)

Acquisition costs include receipt of commission in respect of long-term direct insurance business of £11m (2017: payments of £15m). Administrative expenses include commissions in respect of long-term direct insurance business of £37m (2017: £43m). Administrative expenses are principally recharged from Prudential Distribution Limited, a service company within the Prudential Group.

No foreign exchange differences have been credited (charged) to administrative expenses.

Operating leases

The Company leases office space in London and Reading under non-cancellable operating leases. The London lease has run since 2002 and is due to expire in 2022; the Reading lease has run since 2013 and is due to expire in 2030, however there is a break option on that lease in 2025.

Total future minimum lease payments under non-cancellable operating leases are payable in the following periods:

	2018	2017
	£m	£m
Less than 1 year	**3**	4
1 to 5 years	**13**	13
Over 5 years	**4**	6
Total	**20**	23

The total operating lease expense in 2018 was £4m (2017: £4m).

6. Investment expenses and charges

	Long-term business	
	2018	2017
	£m	£m
Investment management expenses	**330**	389
Interest on bank borrowings	**13**	19
	343	408

7. Tax

The UK Government made substantial changes to the rules relating to the taxation of life insurance companies, effective from 1 January 2013. A deferred tax liability was recognised for the adjustment that arose on transition to the new regime. This adjustment is required to be spread and taxed over a 10 year period.

The Company is the lead litigant in a group action against HM Revenue and Customs (HMRC) concerning the correct historic tax treatment applying to dividends received from overseas portfolio investments of its with-profits funds. In February 2018 the Supreme Court heard HMRC's appeal against the earlier Court of Appeal decision in the company's favour. The decision of the Supreme Court released in July 2018 upheld the main point in dispute in the company's favour but reversed the decisions of the lower courts on some practical points of how to apply that principle.

The Company has so far recognised a policyholder tax credit of £150m in respect of its claim against HMRC (2017: £150m). £38m of this amount has been paid by HMRC to the Company and the balance is held as an amount of tax due from HMRC. The Company and HM Revenue & Customs ("HMRC") are working through the mechanics of implementing the Supreme Court decision and expects to receive full and final repayment from HMRC in 2019.The Company will be entitled to interest on the tax repaid. At the balance sheet date, the Company has received from HMRC and recognised £40m (2017: £40m) in respect of the interest that may be due.

Under the terms of the agreement governing the domestication of the Company's Hong Kong branch in 2014, its Hong Kong subsidiary was entitled to a proportionate share of any tax and interest ultimately paid to the Company. At the balance sheet date the Company is holding a provision of £12m (2017: £12m) in respect of this liability which is included within current tax payable (See note 23).

a) Tax charged (credited)

	Long-term funds		Shareholders' Profits	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Current Tax				
UK corporation tax	**183**	475	**30**	(45)
Double tax relief	**—**	(6)	**—**	—
Overseas tax	**72**	71	**—**	—
Adjustments in respect of prior year	**2**	(7)	**14**	—
Total current tax	**257**	533	**44**	(45)
Deferred tax				
Origination and reversal of timing differences	**(631)**	168	**—**	—
Total deferred tax	**(631)**	168	**—**	—
Shareholders' attributable tax in respect of the long-term business				
Current	**—**	—	**109**	216
Deferred	**—**	—	**(35)**	(36)
Total shareholders' attributable tax	**—**	—	**74**	180
Tax allocated to non-technical account	**(5)**	(31)	**5**	31
Tax charge on profit on ordinary activities	**(379)**	670	**123**	166

b) Factors affecting tax charge for the period

	2018	2017
	£m	£m
Profit on ordinary activities before tax	**1,352**	2,592
Profit on ordinary activities multiplied by effective rate of corporation tax in the UK of 19 per cent (2017: effective rate of 19.25 per cent)	**257**	499
Permanent differences	**10**	1
Adjustment to current tax in respect of previous periods	**—**	1
Non-taxable income	**(34)**	(16)
Revaluation of subsidiaries	**(110)**	(319)
Total tax charge for the period	**123**	166

c) Balance Sheet

	Attributable to Long-term funds		Attributable to Shareholders' funds	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Provision for Deferred Tax				
Accelerated capital allowances	**18**	18	—	—
Short term timing differences	**(1)**	(1)	—	—
Unrealised gains	**607**	1,211	—	—
Deferred acquisition costs	**(61)**	(73)	—	—
Life transitional arrangements	**126**	160	—	—
Pension asset	**22**	19	—	—
Undiscounted provision for deferred tax liability	**711**	1,334	—	—
Deferred tax liability (deferred tax asset) at start of the period	**1,334**	1,150	—	(1)
Deferred tax (credit) charged in technical/non-technical account for the period	**(631)**	168	—	1
Deferred tax charge from statement of comprehensive income	**8**	16	—	—
Adjustment in respect of prior year		—	—	—
Deferred tax liability at end of the period	**711**	1,334	—	—

Deferred tax is provided at the rate applicable when the temporary differences are expected to reverse. The net reversal of the deferred tax balance expected to occur in the next twelve months is uncertain as this will relate mainly to the valuation of unrealised gains which cannot be reliably estimated.

8. Incurred but not reported provision

A gross and ceded IBNR (Incurred but not Reported) provision of £110m (2017: £110m) has been maintained for the general insurance business operations in run off, primarily for industrial disease exposure, and is included within claims outstanding. This liability is reinsured externally and there is a corresponding asset held in reinsurance receivables.

9. Information on staff and pension costs

The average number of persons employed by the Company during the year was:

	2018	2017
United Kingdom	**5**	9
Poland	**267**	249
	272	258

During 2018, the employment contracts of the remaining UK employees of the Company were transferred to another company within the Prudential Group.

The majority of employees in the UK are employed by Prudential Distribution Limited, a service company within the Prudential Group.

	2018	2017
	£m	£m
Wages and salaries	**5**	5
Social security and pension costs	**1**	1
	6	6

Defined Benefit Pension Schemes

The majority of staff employed by the Prudential Group in the UK are members of the Prudential Group's pension schemes. The largest scheme is the Prudential Staff Pension Scheme (PSPS). This scheme is primarily (based on total numbers in the scheme), a defined benefit scheme. This scheme was closed to new employees on 31 July 2003. Employees after this date are enrolled in the defined contribution section of the scheme. At 31 December 2018, the underlying PSPS liabilities account for 82% (2017: 82%) of the aggregate liabilities of the Prudential Group's defined benefit schemes. There is also a smaller defined benefit scheme, Scottish Amicable Staff Pension Scheme (SASPS).

Both schemes are group pension schemes, whereby the costs associated with them are shared across different entities under common control.

The Company is the principal employer of PSPS. The contributions into both schemes are payable at the minimum level of contributions required under the scheme rules. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity.

The surplus in PSPS and the deficit in SASPS are apportioned in accordance with FRS 102.28 Employee benefits, by way of stated policy:

- 70% of the surplus in PSPS is allocated to the with-profits fund of the Company and 30% is allocated to Prudential plc, the immediate parent company.
- 40% of the deficit and related costs of SASPS is allocated to the with-profits fund of the Company and 60% is allocated to Prudential Financial Services Limited, a fellow subsidiary undertaking.

For both schemes, the projected unit method was used for the most recent full actuarial valuations. Defined benefit schemes are subject to full actuarial valuation every three years to assess the appropriate level of funding for schemes having regard to their commitments. These valuations include assessments of the likely rate of return on the assets held within the separate trustee administered funds.

The last completed actuarial valuation of PSPS was as at 5 April 2017 and was finalised during 2018. This valuation demonstrated the scheme to be 105 per cent funded by reference to the Scheme Solvency Target that forms the basis of the scheme's funding objective. There was a small change to the ongoing contributions into the scheme, which are payable at the minimum level required under the scheme rules. Excluding expenses, the contributions are now payable at approximately £5m per annum (2017: £6m) for ongoing service of active members of the scheme. No deficit or other funding is required. Deficit funding for PSPS, where applicable, is apportioned in the ratio of 70/30 between the PAC with-profits fund and Prudential plc based on the sourcing of previous contributions. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity.

The last completed actuarial valuation of the SASPS was as at 31 March 2017 and was finalised in 2017. This valuation demonstrated the scheme to be 75 per cent funded. Based on this valuation, it was agreed with the Trustees that the level of deficit funding is £26m per annum from 1 April 2017 to 31 March 2027, subject to review at subsequent valuations.

In January 2019, following consultation, the Company reached agreement that salary increases for defined benefit scheme members who earn in excess of £35,000 will no longer be pensionable after 30 September 2019. Pension benefits will still relate to how many years they have been active scheme members, as they do now, as long as they remain working for the Company. The impact of this is not reflected in the 2018 results.

Corporate Governance

The Company's UK pension schemes are regulated by 'The Pension Regulator' in accordance with the Pension Act 1995. Trustees have been appointed for each pension scheme and they have the ultimate responsibility to ensure that the scheme is managed in accordance with the Trust Deed & Rules. The Trustees are required by the Pension Regulator to be well conversant with the Trust Deed & Rules and to act in accordance with these Rules.

The Rules of 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.

Ultimate responsibility for the investment of the assets of the scheme lies with the Trustee.

The investment policies and strategies for the SASPS which is also a final salary scheme, follow similar principles, but have different target allocations reflecting the particular requirements of the scheme.

The key assumptions adopted for the valuations in PSPS and SASPS were:

	2018	2017
	%	%
Price inflation:		
Retail Price Index (RPI)	**3.3**	3.1
Consumer Price Index (CPI)	**2.3**	2.1
Rate of increase in salaries	**3.3**	3.1
Rate of increase of pensions in payment:		
PSPS		
Guaranteed - LPI (Max 5%)	**2.5**	2.5
Guaranteed - LPI (Max 2.5%)	**2.5**	2.5
Discretionary	**2.5**	2.5
SASPS	**3.3**	3.1
Rate used to discount scheme liabilities	**2.8**	2.5

The calculations are based on current actuarially calculated mortality estimates with a specific allowance made for future improvements in mortality. The specific allowance made is in line with a custom calibration used for 2018 to reflect the 2015 mortality model from the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries (CMI). For the PSPS immediate annuities in payment, in 2018 a long-term improvement rate of 1.75 per cent per annum and 1.5 per cent per annum were applied for males and females, respectively.

The most recent full valuations have been updated to 31 December 2018 applying the principles prescribed by FRS 102.28.

Notes on the financial statements (continued)

The combined assets and liabilities of PSPS and SASPS were:

	31 December 2018		31 December 2017	
	£m	**%**	£m	%
Equities	**212**	**3**	379	5
Bonds	**7,138**	**90**	7,299	88
Properties	**207**	**3**	200	2
Other assets	**324**	**4**	418	5
Total value of assets	**7,881**	**100**	8,296	100
Present value of underlying scheme liabilities	**7,052**		7,713	
Underlying surplus in the schemes	**829**		584	

Of which the following amounts have been attributed to the Company:

	2018	2017
	£m	£m
Attributable to the Company's with-profits fund	**130**	110

None of the scheme assets included shares in or property occupied by the Company.

The total actual return on scheme assets for both PSPS and SASPS is a loss of £1m (2017: net gain of £292m) of which a loss of £4m (2017: net gain of £185m) relates to the amounts attributable to the Company's with-profits fund offset by a gain of £3m in the shareholder fund.

The surplus in the Prudential Staff Pension Scheme recognised in the balance sheet of the Company represents the amount which is recoverable through reduced future contributions that is attributable to the Company and is net of the apportionment to Prudential plc.

Underlying scheme assets and liabilities of PSPS and SASPS

The change in the present value of scheme liabilities and the change in the fair value of the scheme assets of PSPS and SASPS are as follows:

2018 £m	Assets	Liabilities	Net surplus	Effect of FRS 102 for derecognition of surplus	Total surplus (deficit)	PAC share of surplus (deficit)
Net surplus (deficit) at start of year	8,296	(7,712)	584	(485)	99	110
Current service cost	—	(36)	(36)	—	(36)	(15)
Past service cost**	—	(48)	(48)	—	(48)	(29)
Net interest on net defined benefit	201	(188)	13	(12)	2	3
Administration expenses	(8)	—	(8)	—	(8)	(5)
Benefit payments	(461)	461	—	—	—	—
Company contributions*	47	—	47	—	47	20
Actuarial gains and losses	(194)	471	277	(179)	98	46
Net surplus (deficit) at end of year	7,881	(7,052)	829	(676)	154	130
PSPS net surplus (deficit) at end of year	7,075	(6,167)	908	(676)	233	162
SASPS net surplus (deficit) at end of year	806	(885)	(79)	—	(79)	(32)

* The contributions include deficit funding, ongoing service contributions and expenses.

Notes on the financial statements (continued)

**In October 2018, the High Court ruled that pension schemes are required to equalise benefits for the effect of guaranteed minimum pensions (GMPs). GMPs are a minimum benefit that schemes that were contracted-out on a salary-related basis between 1978 and 1997 are required to provide. In light of this Court ruling, at 31 December 2018, the Group has recognised an estimated allowance for GMP equalisation within valuation of £31m for PSPS and £17m for SASPS. A portion of these costs are allocated to the Company in line with the apportionments described on page 41.

2017 £m	**Assets**	**Liabilities**	**Net surplus**	**Effect of FRS 102 for derecognition of surplus**	**Total surplus (deficit)**	**PAC share of surplus (deficit)**
Net surplus (deficit) at start of year	8,428	(7,947)	481	(558)	(77)	17
Current service cost	—	(37)	(37)	—	(37)	(15)
Net interest on net defined benefit	213	(201)	12	(14)	(2)	—
Administration expenses	(8)	—	(8)	—	(8)	(5)
Benefit payments	(467)	467	—	—	—	—
Company contributions*	44	—	44	—	44	19
Actuarial gains and losses	86	6	92	87	179	94
Net surplus (deficit) at end of year	**8,296**	**(7,712)**	**584**	**(485)**	**99**	**110**
PSPS net surplus (deficit) at end of year	**7,474**	**(6,752)**	**722**	**(485)**	**237**	**166**
SASPS net surplus (deficit) at end of year	**822**	**(960)**	**(138)**	**—**	**(138)**	**(56)**

* The contributions include deficit funding, ongoing service contributions and expenses.

Per FRS 102.28.22, a surplus is only recognised to the extent that the Company is able to access the surplus either through an unconditional right of refund to the surplus or through reduced future contributions relating to ongoing service, which have been substantively enacted or contractually agreed. The Company does not have an unconditional right of refund to any surplus of the scheme. The PSPS pension asset represents the present value of the economic benefit to the Company from the difference between future ongoing contributions to the scheme and estimated accrued cost of service.

The Company accounts for both PSPS and SASPS in accordance with FRS 102.28. The valuation information presented in accordance with FRS 102.28 equates to that which would be presented in accordance with IAS 19 *Employee benefits*, the equivalent IFRS standard applicable to the Group.

Pension charge and actuarial gains (losses) of PSPS and SASPS

The pension credit and actuarial gains (losses) relating to PSPS attributable to the Company's with-profits fund are related to the surplus recognised on the balance sheet of the Company.

The amounts attributable to the Company's with-profits fund for both PSPS and SASPS are absorbed by the transfer to or from the FFA and therefore have no direct effect on shareholders' profit or shareholders' funds. In 2018, there was a pension credit of £46m (2017: credit of £20m).

In 2018, the actuarial gains included a credit of £178m (2017: credit of £55m) for the adjustment to the unrecognised portion of the PSPS surplus which has not been applied against the pension charge. The actuarial gain of £46m (2017: actuarial gain of £94m) is included in the statement of comprehensive income and reflected in the transfer to or from the FFA.

Total employer contributions expected to be paid into PSPS and SASPS for the year ending 31 December 2018 amounts to £47m, reflecting the annual accrual cost, deficit funding (SASPS only), and expenses.

The table below shows the sensitivity of the underlying PSPS and SASPS liabilities at 31 December 2018 of £6,167m (2017: £6,752m) and £885m (2017: £960m) to changes in discount rates, inflation rates and mortality rate assumptions.

Notes on the financial statements (continued)

Assumption	Change in assumption	Impact on PSPS and SASPS scheme liabilities on FRS102.28 basis
2018		
Discount rate	Decrease by 0.2% from 2.8% to 2.6%	Increase scheme liabilities by: PSPS 3.5% SASPS 5.1%
Discount rate	Increase by 0.2% from 2.8% to 3.0%	Decrease scheme liabilities by: PSPS 3.3% SASPS 4.7%
Rate of inflation	RPI: Decrease by 0.2% from 3.3% to 3.5% CPI: Decrease by 0.2% from 2.5% to 2.7% with consequent reduction in salary increases	Decrease scheme liabilities by: PSPS 0.6% SASPS 3.8%
Mortality rate	Increase life expectancy by 1 year	Increase scheme liabilities by: PSPS 3.9% SASPS 3.7%

Assumption	Change in assumption	Impact on PSPS and SASPS scheme liabilities on FRS102.28 basis
2017		
Discount rate	Decrease by 0.2% from 2.5% to 2.3%	Increase scheme liabilities by: PSPS 3.5% SASPS 5.3%
Discount rate	Increase by 0.2% from 2.5% to 2.7%	Decrease scheme liabilities by: PSPS 3.3% SASPS 5.0%
Rate of inflation	RPI: Decrease by 0.2% from 3.1% to 3.3% CPI: Decrease by 0.2% from 2.1% to 2.3% with consequent reduction in salary increases	Decrease scheme liabilities by: PSPS 0.6% SASPS 4.0%
Mortality rate	Increase life expectancy by 1 year	Increase scheme liabilities by: PSPS 4.0% SASPS 3.6%

The amounts attributable to the Company's with-profits fund for both PSPS and SASPS are absorbed by the transfer to or from the FFA and therefore have no direct effect on shareholders' profit or shareholders' funds.

10. Directors' emoluments

	2018	2017
	£	£
Aggregate emoluments	**2,140,520**	3,790,104
Excess retirement benefits:		
Current directors	**143,500**	241,843
Past directors	—	—
	2,284,020	4,031,947
Highest Paid Director:		
Aggregate emoluments and amounts receivable (excluding shares) under long term incentive schemes	**910,090**	1,839,398

Emoluments are reported for directors who are deemed to work for the Company i.e. provide qualifying services in accordance with Schedule 5 of the Regulations. No Company contributions were made to a defined contribution pension scheme in 2018 or in 2017 on behalf of any director. No directors (2017: No) exercised share options during the year. No directors (2017: one) were entitled to shares under Prudential's main long-term incentive scheme and three director (2017: three) was entitled to retirement funds under defined benefit schemes.

The highest paid director in 2018 (and 2017) received shares under long-term incentive schemes but exercised share options in 2017 only.

Notes on the financial statements (continued)

During the year a significant proportion of two executive Directors' salaries have been apportioned to the new holding company set up in preparation for the demerger and are not included in the amounts above.

11. Auditor's remuneration

During the year the Company obtained the following services from KPMG LLP (KPMG) at costs as detailed below:

	2018	2017
	£000's	£000's
Fees payable to the Company's auditor for the audit of the Company's annual accounts	**2,465**	2,169
Fees payable to the Company's auditor and its associates for other services:		
Audit-related assurance services	**674**	616
Audit of the Company's subsidiaries, pursuant to legislation	**161**	165
Other assurance services	**50**	50
Total fees payable	**3,350**	3,000

12. Intangible assets

	2018		2017		
	Computer Software	**Total**	Licence	Computer Software	Total
	£m	**£m**	£m	£m	£m
Cost:					
At 1 January 2018	**12**	**12**	174	7	181
Exchange differences	**(1)**	**(1)**	—	1	1
Additions	**—**	**—**	—	4	4
Disposals	**—**	**—**	(174)	—	(174)
At 31 December 2018	**11**	**11**	—	12	12
Amortisation:					
At 1 January 2018	**4**	**4**	159	2	161
Recognised in the long-term business technical account	**1**	**1**	15	2	17
Disposals	**—**	**—**	(174)	—	(174)
At 31 December 2018	**5**	**5**	—	4	4
Net book value at 31 December 2018	**6**	**6**	—	8	8

In the prior year, intangible assets included a licence, which represented the value of an agreement with a fellow subsidiary company for the use of certain Scottish Amicable assets. This was amortised over a period of 20 years to 30 September 2017, on a basis consistent with the revenue stream from the agreement. This was derecognised from 1 October 2017 and was treated as a disposal. No gains or losses were recognised from this disposal.

There have been no impairments during the year (2017: £nil).

Notes on the financial statements (continued)

13. Land and buildings

	2018	2017
	£m	£m
Current value		
Freeholds	5,105	4,579
Leaseholds with a term of over 50 years	3,275	3,625
Leaseholds with a term of less than 50 years	684	633
	9,064	8,837
Cost	6,039	5,789

If the revalued land and buildings were stated on the historical cost basis, the amounts would be:

	2018	2017
	£m	£m
At cost	6,039	5,789
Aggregate depreciation	(3,606)	(3,455)
Net book value based on historical cost	2,433	2,334

(a) Group-occupied property

	2018	2017
	£m	£m
Balance at 1 January	138	136
Revaluations	6	2
Disposals	—	—
Balance at 31 December	144	138

(b) Investment property

	2018	2017
	£m	£m
Balance at 1 January	8,699	8,488
Additions		
Resulting from acquisitions	268	268
Resulting from expenditure capitalised	83	17
Disposals	(105)	(439)
Net gain from fair value adjustments	2	376
Other changes	(27)	(11)
Balance at 31 December	8,920	8,699

The 2018 profit and loss account includes rental income from investment properties of £466m (2017: £496m).

Leasehold properties included above are reported as finance lease assets. A reconciliation between the total of future minimum lease payments at the balance sheet date, and their present value is shown below:

Notes on the financial statements (continued)

	2018 £m			2017 £m		
	Future minimum payments	**Future finance charges**	**PV of future minimum payments**	Future minimum payments	Future finance charges	PV of future minimum payments
Less than 1 year	**1**	**—**	**1**	1	—	1
1 to 5 years	**4**	**(1)**	**3**	4	(1)	3
Over 5 years	**122**	**(108)**	**13**	123	(109)	14
Total	**127**	**(109)**	**17**	128	(110)	18

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 of £1m (2017: £1m) has been recognised as income with an expense charge of £8m (2017: £6m). There are no restrictions on the realisability of investment property or the remittance of income and proceeds of disposal. The contractual obligations to purchase or develop investment properties at 31 December 2018 were £375m (2017: £104m).

The Company's policy is to let investment properties to tenants through operating leases. Minimum future rentals to be received on non-cancellable operating leases of the Company's freehold investment properties are receivable in the following periods:

	2018 £m	2017 £m
Less than 1 year	**239**	239
1 to 5 years	**885**	845
Over 5 years	**1,981**	2,026
Total	**3,105**	3,110

(c) Finance lease asset

A reconciliation between the total of future minimum lease payments recoverable by the Company at the balance sheet date, and their present value is shown below:

	2018 £m			2017 £m		
	Future minimum receivables	**Future finance credits**	**PV of future minimum receivables**	Future minimum receivables	Future finance credits	PV of future minimum receivables
Less than 1 year	**2**	**—**	**2**	2	—	2
1 to 5 years	**9**	**(2)**	**7**	9	(2)	7
Over 5 years	**371**	**(347)**	**24**	371	(347)	24
Total	**382**	**(349)**	**33**	382	(349)	33

Notes on the financial statements (continued)

14. Investments in group undertakings and participating interests

	Cost		Current value	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Long-term fund investments	**1,566**	1,308	**2,921**	2,416
Shareholder investments				
Prudential Holborn Life Limited	**59**	59	**95**	112
Prudential Pensions Limited	**6**	6	**17**	17
Prudential Lifetime Mortgages Limited	**66**	66	**73**	73
Prudential International Assurance plc	**194**	194	**293**	293
Prudential Retirement Income Limited	**877**	877	**100**	100
Prudential General Insurance Hong Kong Limited	**—**	17	**—**	46
Prudential Hong Kong Limited	**—**	17	**—**	8,805
Total Shareholder investments	**1,203**	1,236	**578**	9,446
Total	**2,768**	2,544	**3,499**	11,862
Interest in joint ventures and associate long-term fund investments	**372**	191	**671**	463
Debt securities issued by, and loans to group undertakings – long term funds	**985**	942	**985**	942
Total	**4,125**	3,677	**5,155**	13,267

On 14 December 2018, the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were sold to Prudential Corporation Asia Limited. See note 31 for further details.

Refer to note 30 for further information on the related undertakings of the Company.

15. Other financial investments

	Cost		Carrying value	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Fair value through profit and loss				
Shares and other variable yield securities and units in unit trusts	**41,249**	38,492	**48,192**	52,745
Debt securities and other fixed income securities	**60,265**	65,753	**63,999**	73,453
Derivative assets	**870**	818	**2,283**	2,661
Participation in investment pools	**4,215**	2,937	**5,046**	3,705
Loans secured by mortgages	**2,429**	2,527	**2,439**	2,675
Amortised cost				
Loans to policyholders secured by insurance policies	**3**	4	**3**	4
Other loans	**887**	862	**871**	815
Deposits with credit institutions	**8,929**	8,215	**8,929**	8,215
	118,847	119,608	**131,762**	144,273

The change in carrying value of other financial investments included in the Profit and Loss account was a gain of £12,293m (2017: £530m gain) analysed between a gain of £12,497m (2017: £643m gain) included in the Long-term business technical account and a £204m loss (2017: £113m loss) included in the Non-technical account.

Notes on the financial statements (continued)

The change in carrying value of £12,293m (2017: £530m gain) included a gain of £7,316m (2017: £3,016m gain) in respect of equity securities, gain of £3,924m (2017: £1,987m loss) in respect of debt securities, a gain of £981m (2017: £13m gain) in respect of derivatives and a gain of £72m (2017: £512m loss) in respect of other financial instruments.

	Carrying value	
	2018	2017
Amounts included in the above relating to listed investments:	**£m**	£m
Shares and other variable yield securities and units in unit trusts	**43,912**	49,162
Debt securities and other fixed income securities	**56,061**	65,852
	99,973	115,014

The table below analyses the derivative positions of the Company:

	2018 £m		2017 £m	
	Fair value assets	Fair value liabilities	Fair value assets	Fair value liabilities
Derivative financial instruments held to manage interest rate and currency profile:				
Interest rate swaps	**1,828**	**337**	2,054	398
Cross currency swaps	**2**	**484**	36	379
Currency exchange forward contracts	**104**	**771**	268	99
Bond futures	**46**	**44**	12	7
Credit default swaps	**34**	**1**	29	—
Inflation swaps	**210**	**295**	192	302
Derivative financial instruments held to manage market risk and efficient investment management:				
Equity options	**50**	**220**	51	374
Equity futures	**9**	**20**	17	34
Equity warrants	**—**	**—**	2	—
Total	**2,283**	**2,172**	2,661	1,593

The nature of the derivative financial instruments used by the Company in 2018, are similar to those used in 2017. These include the partial equity hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, which was set up in 2013. This arrangement was extended each year since 2015. This is currently a liability of £220m (2017: liability of £374m).

The use of derivatives is disclosed in note 28G.

Treatment of equity release mortgages transfer

On 1 January 2016 an equity release mortgage portfolio owned by the Company was restructured to meet the Solvency II matching adjustment requirements. The beneficial interest in the equity release mortgage portfolio was sold to Prudential Equity Release Mortgages Limited (PERM) in an arm's-length transaction. The consideration for the purchase was the issue of loan notes to Prudential Retirement Income Limited (PRIL), which were subsequently transferred to the Company, at the fair value of the mortgage book.

Under UK Generally Accepted Accounting Practice the asset does not qualify for de-recognition from the financial statements of the Company at the reporting date, as the Company retains all the risks and rewards of ownership and has substantially the same rights to the use of the asset as before the arrangement. Consequently, the mortgage portfolio is still recognised in the financial statements of the Company and not within PERM.

The effect of the above is that the assets and liabilities created by the restructure are recognised within the Company's financial statements, and are not recognised in the financial statements of PERM.

The fair value of this equity release mortgage portfolio at 31 December 2018 was £1,210m (2017: £1,319m).

16. Assets held to cover linked liabilities

	Cost		Carrying value	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Assets held to cover linked liabilities	**11,683**	13,293	**14,546**	18,303

17. Reinsurers' share of technical provisions

In March 2018, M&GPrudential announced the partial sale of the Company's shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, the Company reinsured £12bn of liabilities (valued as at 31 December 2017) to Rothesay Life. This is expected to be followed by a Part VII transfer of most of the portfolio by 30 June 2019. The liabilities relating to M&GPrudential's total UK shareholder annuity portfolio as at 31 December 2018 were £30bn, of which £11.6bn is reinsured by Rothesay Life. The profit and loss impact of the transaction was a loss of £508m.

Aside from the reinsurance agreement with Rothesay Life discussed above, no new longevity reinsurance transactions were undertaken during 2018 (2017: a longevity reinsurance transaction covering £0.5bn of annuity liabilities contributed £31m to profit).

At 31 December 2018, longevity reinsurance covered £6.3bn of annuity liabilities equivalent to 21% of total annuity liabilities. In addition a further 23% is reinsured by Rothesay Life.

Included in income and expense in the profit and loss account is £10,435m reflecting the movement in the reinsurers' share of technical provision to £18,255m at 31 December 2018 from £7,820m at 31 December 2017.

18. Other debtors

	2018	2017
	£m	£m
Amounts owed by ultimate parent company	**534**	528
Amounts owed by fellow subsidiaries	**153**	140
Amounts owed by subsidiary companies, associate and joint ventures	**224**	135
Tax recoverable	**212**	296
Other	**364**	227
	1,487	1,326

During 2018 a Settlement and Release agreement was signed with the Group's insurers, confirming that they will reimburse Prudential for £166m of costs arising from the Company's review in connection with the Thematic Review of Annuity Sales Practices. Remaining amounts receivable of £146m have been recognised within Other debtors in the 'other' category above.

Other debtors include £5m (2017: £1m) due after more than one year.

Notes on the financial statements (continued)

19. Bank current accounts

Under the terms of the Company's arrangements with the Prudential Group's main UK banker, the bank has a right of set-off between credit balances (other than those of long term business funds) and all overdrawn balances of those Group undertakings with similar arrangements.

20. Assets attributable to the long term business fund

Of the total amount of assets shown in the balance sheet on page 26, £182,423m (2017: £188,653m) is attributable to the long-term business fund.

21. Share capital

The Company's issued ordinary share capital is £329,517,064 comprising 1,318,068,254 ordinary shares of 25p each fully paid. There were no changes in the ordinary share capital of the Company during the year.

22. Other Provisions

	2018	2017
	£m	£m
At 1 January	**408**	217
Charged to income statement:		
Additional provisions	**38**	225
Unused amounts released	**—**	(3)
Used during the year	**(45)**	(31)
Total at 31 December	**401**	408

Regulatory Provisions - FCA Thematic Review of non-advised Annuity Sales Practises

The amounts above include a provision for review of past annuity sales after utilisation during the year of £324 million (2017: £369m). The Company has agreed with the Financial Conduct Authority (FCA) to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. The review is examining whether customers were given sufficient information about their potential eligibility to purchase an enhanced annuity, either from Prudential or another pension provider. A gross provision of £400m, before costs incurred, was established at 31 December 2017 to cover the costs of undertaking the review and any related redress and following a reassessment, no change has been made in 2018. The majority of the provision will be utilised in 2019. The ultimate amount that will be expended by the Company on the review will remain uncertain until the project is completed. If the population subject to redress increased or decreased by 10%, then the provision would be expected to increase or decrease by circa 7% accordingly. Additionally, in 2018, the Company agreed with its professional indemnity insurers that they will meet £166m of claims costs, which will be paid as the Company incurs costs/redress. This income has been recognised in operating profit and on the balance sheet within 'Other debtors' at 31 December 2018.

Notes on the financial statements (continued)

23. Other creditors including tax and social security

	2018	2017
	£m	£m
Amounts owed to fellow subsidiaries and ultimate holding company	151	183
Amounts owed to subsidiary companies, associate and joint ventures	645	723
Tax	251	282
Derivative liability (see note 15)	2,172	1,593
Other creditors	2,824	3,854
	6,043	6,635

24. Ultimate parent company

On 26 November 2018 the Company's legal ownership was transferred from its previous parent company Prudential plc to a new holding company M&G Prudential Limited. M&G Prudential Limited is a subsidiary of Prudential plc. The ultimate parent of the Company therefore remains Prudential plc. Copies of these accounts can be obtained from the Company Secretary, Laurence Poutney Hill, London, EC4R 0HH.

25. Related party transactions

The Company has taken advantage of the exemption under FRS 102.33 *Related Party Disclosures* (FRS 102.33) paragraph 1A from disclosing transactions with other wholly-owned subsidiary undertakings of the Prudential Group.

26. Long-term business provision

The Company's long-term products consist of life insurance, investment, pensions and pension annuities. In common with other UK long-term insurance companies, the Company's products are structured as either with-profits (or participating) products, or non-participating products including annuities in payment and unit-linked products. Depending upon the structure, the level of shareholders' interest in the value of policies and the related profit or loss varies.

With-profits policies are supported by the with-profits sub-fund (WPSF) and can be single or regular premium. The return to shareholders on virtually all with-profits products is in the form of a statutory transfer to the Company's shareholders' funds which is analogous to a dividend from the Company's long-term fund and is dependent upon the level of bonuses credited or declared on policies in that year. There are two types of bonuses for traditional with-profits products – "annual" and "final". Annual bonuses are declared once a year, and are determined as a prudent proportion of the long-term expected future investment return on the underlying assets. Once credited, annual bonuses are guaranteed in accordance with the terms of the particular product. In contrast, "final" bonuses are only guaranteed until the next bonus declaration, and are primarily determined on the actual investment return achieved, smoothed over the life of the policy. With-profits policyholders currently receive 90 per cent of the distribution from the WPSF as bonus additions to their policies and shareholders receive 10 per cent as a statutory transfer.

Unlike traditional with-profits products, no regular or final bonuses are declared for PruFund contracts. Policyholder return is determined by an Expected Growth Rate (EGR) which is declared each quarter. The shareholder transfer only crystallises at the point when a claim is paid to the policyholder and is equal to one ninth of the difference between the policyholder payout and the premium(s) paid.

The Scottish Amicable Insurance Fund (SAIF) is a closed sub-fund that contains the bulk of the business originally written by the Scottish Amicable Life Assurance Society and acquired by the Company on 30 September 1997. Under the terms agreed at the time of the purchase, the SAIF inherited estate will be distributed to with-profits policyholders as an addition to the with-profits benefits arising in SAIF. The SAIF policyholders therefore receive 100 per cent of the distribution from the sub-fund as bonus additions to their policies.

Notes on the financial statements (continued)

The defined charge participating sub-fund (DCPSF) forms part of the Company's long-term fund and comprises the accumulated investment content of premiums paid in respect of the defined charge participating with-profits business issued in France, the defined charge participating with-profits business reassured into the Company from both Prudential International Assurance plc and Canada Life (Europe) Assurance Ltd and the with-profits annuity business transferred to the Company from the Equitable Life Assurance Society on 31 December 2007. All profits in this fund accrue to policyholders in the DCPSF.

There is a substantial volume of non-participating business in the with-profits sub-fund; profits from this business accrue to the with-profits sub-fund.

The Company also writes non-participating business, the profit on which accrues solely to shareholders.

i. Analysis of movements in insurance liabilities including FFA

	Technical Provisions		
	Technical Provisions £m	Linked liabilities £m	Total £m
At 1 January 2017			
Comprising			
Technical provisions	126,016	23,928	149,944
Fund for future appropriations	11,933	—	11,933
	137,949	23,928	161,877
Premiums	12,853	267	13,120
Surrenders	(4,526)	(639)	(5,165)
Maturities/Deaths	(6,013)	(1,011)	(7,024)
Shareholders' transfers post tax	(233)	—	(233)
Switches	(192)	192	—
Investment-related items and other movements	9,000	1,338	10,338
Foreign exchange translation differences	113	—	113
Assumption changes	(149)	—	(149)
As at 31 December 2017/1 January 2018	**148,802**	**24,075**	**172,877**
Comprising			
Technical provisions	135,221	24,075	159,296
Fund for future appropriations	13,581	—	13,581
	148,802	24,075	172,877
Premiums	12,793	241	13,035
Surrenders	(4,769)	(593)	(5,362)
Maturities/Deaths	(5,447)	(1,609)	(7,056)
Shareholders' transfers post tax	(259)	—	(259)
Switches	(165)	165	—
Investment-related items and other movements	(4,210)	(601)	(4,811)
Foreign exchange translation differences	218	3	221
Assumption changes	(706)	—	(706)
As at 31 December 2018	**146,257**	**21,681**	**167,939**
Comprising			
Technical provisions	132,770	21,681	154,451
Fund for future appropriations	13,487	—	13,487
	146,257	**21,681**	**167,938**

Notes on the financial statements (continued)

The impact does not represent premiums, claims and investment movements as reported in the income statement. For example premiums shown above will exclude any deductions for fees/charges. Claims represent the policyholder liabilities provision released, rather than the claim amount paid to the policyholder.

Durations of long-term business contracts on a discounted basis:

With the exception of most unitised with-profit bonds and other whole of life contracts the majority of the contracts of the Company have a contract term. However, in effect, the maturity term of contracts reflects the earlier of death, maturity, or lapse of the contract. In addition, with-profit contracts include projected future bonuses based on current investment values. The actual amounts payable will vary with future investment performance of SAIF and the WPSF. Instead the Company uses cash flow projections of expected benefit payments. The following table shows the maturity profile of the cash flows used for insurance contracts i.e. those containing significant insurance risk, and investment contracts, which do not contain significant insurance risk:

2018	With-profits business			Policyholder Annuities	Shareholder Annuities	Other		
	Insurance contracts %	Investment contracts %	Total %	Insurance contracts %	Insurance contracts %	Insurance contracts %	Investment contracts %	Total %
0-5 years	35	37	36	34	27	45	31	36
5-10 years	23	27	26	25	23	25	24	24
10-15 years	16	17	17	17	19	14	18	17
15-20 years	11	9	10	11	14	8	13	11
20-25 years	7	4	5	6	9	4	7	6
Over 25 years	8	6	6	7	8	4	7	6

2017	With-profits business			Policyholder Annuities	Shareholder Annuities	Other		
	Insurance contracts %	Investment contracts %	Total %	Insurance contracts %	Insurance contracts %	Insurance contracts %	Investment contracts %	Total %
0-5 years	33	37	36	31	26	42	30	34
5-10 years	23	27	25	24	23	26	22	23
10-15 years	16	17	17	17	18	15	18	17
15-20 years	11	10	10	11	13	9	14	12
20-25 years	7	4	5	7	9	4	8	7
Over 25 years	10	5	7	10	11	4	8	7

Notes:

(i) The cash flow projections of expected benefit payments used in the maturity profile table above are from 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 unit-linked and similar contracts.

(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.

ii. Determining insurance liabilities

The principal valuation methods and bases adopted for the main relevant classes of business which are not reinsured are as follows:

Business in With-Profits Sub-Fund, SAIF and Defined Charge Participating Sub-Fund

The overarching principle in assumption setting is that realistic provisions are established using best estimate assumptions, taking into account the firm's regulatory duty to treat its customers fairly.

Assumptions are required in three areas, namely:

Notes on the financial statements (continued)

(i) Retrospective assumptions,
(ii) Prospective assumptions, and
(iii) Stochastic modelling assumptions relating to the economic asset model and management actions.

Retrospective assumptions

Retrospective assumptions are required for the accumulation of past asset shares up to the valuation date. These assumptions are determined by reference to actual past experience primarily in relation to investment returns, expenses and miscellaneous surplus. The assumptions include past expense write-offs and enhancements to asset shares, and are as used when calculating asset shares for the purpose of bonus setting.

The 2018 year end Investment Return for asset shares is:

Return	With-Profits Sub Fund Main Asset Share Fund	High Reversionary Bonus fund (held within the With-Profits Sub-Fund)	PruFund Cautious Fund (held within the With-Profits Sub-Fund)	SAIF
Gross return	-2.79%	-2.46%	-2.21%	-2.81%
Net return	-2.25%	-1.99%	-1.80%	-2.26%

The High Reversionary Bonus and PruFund Cautious funds are contained within the with-profits sub-fund. Compared with the assets backing the main asset share fund, the High Reversionary Bonus and PruFund Cautious funds are both allocated a higher proportion of fixed interest securities and a lower proportion of equities.

Prospective assumptions

Prospective assumptions are required for the adjustments to asset shares where a prospective calculation gives a higher result and for the stochastic modelling of the cost of guarantees, options and smoothing.

For asset share adjustments, the economic assumptions used represent the best estimate assumptions allowing for prevailing market conditions at the valuation date.

Expense assumptions have been revised to reflect the Company's most recent experience, and expected expenditure over the business planning period.

The table below shows the mortality bases used for the valuation at 31 December 2018:

Product	Mortality Table (M/F)	Age Rating Years (M/F)	Multiplier % (M/F)
Prudence Bond	AMC00/AFC00	-1 / -1	90 / 90
PSA / PIB	AMC00/AFC00	-0.5 / -0.5	75 / 75
Personal Pensions	AMC00/AFC00	-1 / -1	80 / 80
Ordinary Branch assurances	AMC00/AFC00	-0.5 / -0.5	85 / 85
Industrial Branch	PAC 78 WL (Internal Table)	0 / 0	55 / 55
With-Profit Deferred Annuities	PMA92c2004 (1d) / Female not used	0 / 0	37.5/ not used
SAIF Conventional With-Profits	AMC00/AFC00	1 / 1	55 / 55 Life & 35 / 35 Pensions
SAIF/Ex-SAL Accumulating With-Profits Life	AMC00/AFC00	1 / 1	45 / 45 Life & 40 / 40 Pensions

For mortality and persistency, the assumptions for asset share adjustments are the best estimate European Embedded Value assumptions. The persistency assumptions used to value the cost of options and guarantees are reduced by a 10% margin to make an allowance for the impact of policyholders' group actions in extreme market scenarios.

Notes on the financial statements (continued)

Stochastic asset model economic calibration and management actions

The cost of options, guarantees and smoothing are assessed on a market consistent basis, so that the reserves held are equal to the theoretical cost of hedging the guarantees in the market. In the absence of a deep, liquid market these costs are assessed using a "market consistent" model, with a market consistent calibration.
In order to value the Company's guarantees and options, the stochastic asset/liability model projects the with-profits liabilities forward over the next 40 years for 5,000 separate economic scenarios.

Separate asset models are used for the risk free rate (assumed to be the UK swap rate), UK equities, overseas equities, corporate bonds, property and real interest rates. Where appropriate securities or derivatives are traded, it has been demonstrated that the model is able to closely reproduce these prices. Where this is not the case (for example for property and corporate bonds) expert judgement has been applied. Allowance has also been made for the correlation of investment returns between different asset classes.

The cost of guarantees, options and smoothing is very sensitive to the bonus, market value reduction and investment policies that the Company will employ under varying investment conditions. The stochastic modelling incorporates several management actions to protect the fund in adverse investment scenarios. These management actions are consistent with the PPFM and the obligation to treat customers fairly.

Other non-linked business

Provisions are predominantly calculated by the net premium valuation method. Discount rates are derived based on gilt yields of a duration consistent with that of the underlying business as these yields are representative of the returns that will be earned on the investments backing these liabilities, and also allow for inflation growth.

Mortality assumptions for annuity business are set in light of recent population and internal experience, with an allowance for expected future mortality improvements. Given the long-term nature of annuity business, longevity remains a significant assumption in determining policyholder liabilities. The assumptions used reference recent population mortality data, with specific risk factors applied on a per policy basis to reflect the features of the Company's portfolio.

The recent declining mortality improvements observed in population data were considered as part of the judgement exercised in setting the 2018 mortality basis. New mortality projection models are released regularly by the Continuous Mortality Investigation (CMI). The CMI 2016 model was used to produce the 2018 results and the CMI 2015 model was used to produce the 2017 results. The default calibration of CMI 2016 was adopted to reflect the Company's view of future mortality improvements based on a range of possible outcomes, with an appropriate margin for prudence. The mortality improvement assumptions used are the default calibration of CMI 2016 with a long term rate of 1.75% for males and 1.50% for females plus 0.5% constant increase to per annum improvement rates.

Notes on the financial statements (continued)

The following discount rates were used for annuity business:

	Interest Rate %
UK (excluding Scottish Amicable Insurance Fund)	
Ex-PAL Annuities (Fixed) - pre 1/1/2019	2.72
Ex-PAL Annuities (Fixed) - post 1/1/2019	2.74
Ex-PAL Annuities (Linked) - pre 1/1/2019	2.52
Ex-PAL Annuities (Linked) - post 1/1/2019	2.54
NPSF Annuities (Fixed) - pre 1/1/2019	2.95
NPSF Annuities (Fixed) - post 1/1/2019	2.96
NPSF Annuities (Linked) - pre 1/1/2019	2.88
NPSF Annuities (Linked) - post 1/1/2019	2.89
Other Shareholder Annuities (Fixed) - pre 1/1/2019	2.95
Other Shareholder Annuities (Fixed) - post 1/1/2019	2.96
Other WPSF Annuities (Fixed)	2.75
Other WPSF Annuities (Linked)	4.61

The following discount and mortality bases were used for term assurances:

	Interest Rate %	Actuarial Mortality Table Reference*
UK (excluding Scottish Amicable Insurance Fund)		
Term assurances - life business	1.04	80% to 85% AMC00/AFC00+1
Term assurances - pensions business	1.30	65% AMC00/AFC00+1
Scottish Amicable Insurance Fund		
Term assurances - life business	n/a	n/a
Term assurances – pensions business	1.87	65% AMC00/AFC00+1

*For assurances, provision for AIDS is made either by increasing the underlying mortality rates or by holding an explicit additional provision. In both cases, the adjustment is one-third of the "R6A" tables.

Linked business in the Shareholder Fund and Scottish Amicable Insurance Fund

The provision for mortality, morbidity and expenses is calculated using a discounted cashflow method on the following bases:

Discount Rate	1.30% Gross
Fund Growth	4.88% Gross
Mortality	AMC00/ AFC00 Ultimate+1 age adj 70%-100% depending upon product type
Administration Expenses	£71 to £148 depending on product type
Expense Inflation	Shareholder: 3.88%. SAIF: 4.88% for retained expenses, 3.38% for third party expenses

Notes on the financial statements (continued)

Linked business in the With-Profit Sub-Fund

The provision for mortality, morbidity and expenses is calculated using a discounted cashflow method on the following bases:

Discount Rate	1.30% Gross
Fund Growth	4.88% Gross
Mortality	AMC00/ AFC00 Ultimate+1 age adj 75%-100% depending upon product type
Administration Expenses	£70 to £99 depending on product type
Expense Inflation	4.88% for retained expenses, 3.38% for third party expenses for SAA

Other long-term business provisions

Additional provisions have been established, the most significant being for the potential costs and expenses of compensating the Company's pension policyholders under the Financial Services Authority (FSA), the UK insurance regulator at the time, review of pension opt-outs and transfer cases, for the potential costs of compensating endowment mortgage policyholders and for the potential cost of meeting annuity rate guarantees at vesting. Refer to note 27.

iii. Effect of changes in assumptions used to measure with-profits assets and liabilities

For the with-profits sub-fund, the aggregate effect of assumption changes in 2018 was a net charge to the FFA of £394m (2017: net charge of £58m), relating to changes in mortality, expense, persistency and tax assumptions, where appropriate in the two periods.

27. Commitments, Contingencies and Related Obligations

Pension Mis-selling Review

The pensions review by the Financial Services Authority (FSA), the UK insurance regulator at the time, of past sales of personal pension policies required all UK life insurance companies to review their cases of potential mis-selling and record a provision for the estimated costs.

Whilst the Company believed it met the requirements of the FSA (the UK insurance regulator at the time) to issue offers of redress to all impacted customers by 30 June 2002, there is a population of customers who, whilst an attempt was made at the time, to invite them to participate in the review, may not have received their invitation. These customers are being re-engaged to ensure that they have the opportunity to take part in the review.

The provision at 31 December 2018 has been increased to reflect two legislative changes - the FCA FG17/9: 'Guidance for firms on how to calculate redress for unsuitable defined benefit pension transfers' and the recent court judgement in respect of the equalisation of Guaranteed Minimum Pensions (GMPs). It is also based on the best estimate assumptions and market conditions.

At 31 December 2018, the pension mis-selling amount included within the long-term business provision was £777m (2017: £505m). The table below summarises the change for the year ended 31 December 2018.

	Year Ended 31 December 2018 £m	Year Ended 31 December 2017 £m
Balance at start of the period	**505**	505
Changes to actuarial assumptions and method of calculation	**357**	47
Redress paid to policyholders	**(85)**	(46)
Payment of administrative costs	**—**	(1)
Balance at end of the period	**777**	505

The pension mis-selling amount above at 31 December 2018 of £777m is stochastically determined on a discounted basis.

Amounts in respect of the costs associated with the review have been included in the change in long-term business provisions in the Company's long-term technical account and the transfer to or from the FFA has been determined accordingly.

The directors believe that, based on current information, the amount, together with future investment return on the assets backing it, will be adequate to cover the costs of pension mis-selling including administration costs. The amount represents the best estimate of probable costs and expenses.

The costs associated with the pension mis-selling review have been met from the inherited estate. Accordingly, these costs have not been charged to the asset shares used in the determination of policyholder bonus rates. Hence policyholders' payout values have been unaffected by pension mis-selling.

In 1998, the Company 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.

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, retail price index 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. Hence removal of the assurance for new business has had no impact on policyholder returns.

Pensions Equalisation Review

The European Court of Justice ruled in 1990 that pension schemes should equalise retirement ages for males and females (Barber vs Guardian Royal Exchange). This affects certain defined benefit pension schemes previously administered by Scottish Amicable Life Assurance Society and wound up schemes formerly administered by the Company, where the Company issued the buy-out policy to members. Investigations are ongoing to determine the extent to which the Company was responsible or liable for any errors in members' benefit calculations and whether compensation or redress may be payable, and from which fund. Accordingly, an amount is held within the long term business provision of £99m in respect of shareholder-backed business and £13m in respect of SAIF, as at 31 December 2018 excluding any utilisation to date (2017: £92m and £21m respectively).

Guaranteed Minimum Pensions

From April 1987, pension schemes were able to "contract out" of the State Earnings Related Pension Scheme, enabling companies and members to pay lower National Insurance Contributions, but their schemes had to provide a minimum level of benefit, the Guaranteed Minimum Pension ('GMP'). Recent court cases have confirmed that there is a requirement for GMPs to be equalised between male and female members / policyholders. The Company has included an amount within the long term business provision for the expected costs of equalisation, however there is uncertainty as to the extent to which the judgements apply to schemes other than active defined benefit schemes and therefore the extent to which the Company may be responsible for achieving this across its product lines.

Notes on the financial statements (continued)

Mortgage Endowment Products Review

Historically, in common with several other UK insurance companies, the Company 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, would equal or exceed the mortgage debt. The FSA (the UK regulator at the time) was concerned that the maturity value of some of these products would be less than the mortgage debt because of a decrease in expected future investment returns since these products were sold. The FSA 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. This programme remains in place following the change in the regulatory regime.

The Company 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) and transferred into the Scottish Amicable Insurance Fund (SAIF). Technical provisions of £0.6m (2017: £0.6m) in the shareholder fund and £1.4m (2017: £7.5m) in SAIF were held at 31 December 2018 to cover potential compensation in respect of mortgage endowment product mis-selling claims. As SAIF is a separate ring-fenced fund, wholly attributable to the policyholders of the fund, this provision has no impact on shareholders.

In addition, the Company's main with-profits fund paid compensation of £0.1m in respect of mortgage endowment products mis-selling claims in the year ended 31 December 2018 (2017: £0.9m) and held a technical provision of £4.0m at 31 December 2018 (2017: £9.3m) in respect of further compensation. In line with the time limit prescribed by the FSA and the Association of British Insurers, impacted customers have three years to lodge a mis-selling complaint from the date they receive their first "red" letter indicating that there is a high risk their mortgage endowment may not achieve its projected final value.

Guaranteed Annuities

The Company used to sell guaranteed annuity products in the UK and held a technical provision of £49m at 31 December 2018 (2017: £53m) within the main with-profits fund to honour guarantees on these products.

The Company's main exposure to guaranteed annuities in the UK is through the SAIF and a technical provision of £361m was held in SAIF at 31 December 2018 (2017: £503m) to honour the guarantees.

Guarantees and Commitments

Since 2012 the Company has agreed to guarantee the funding obligation at the date of the last triennial valuation that Prudential Distribution Limited (PDL), a service company within the Prudential Group and principal employer, and other participating employers have to the Scottish Amicable Staff Pension Scheme. The funding obligation arises from the deficit in this pension scheme as at 31 March 2018 (£215m). Payment under the guarantee would be exercised should PDL fail to meet its funding obligation. The guarantee expires on 31 March 2027.

The Company has undrawn commitments of £4.0bn (2017: £3.2bn) to private equity and infrastructure funds in which the Company is already an investor. These funds will be drawn down at the fund managers' discretion over a 3 to 5 year period.

The Company also provides, from time to time, other guarantees and commitments to other companies within the Group and third parties entered into in the normal course of business but the directors do not consider that the amounts involved are significant.

Support of Long-term Business Funds by Shareholders' Funds

As a proprietary insurance company, the Company 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 Company'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 Scottish Amicable Life Assurance Society, a mutual society, was transferred to the Company. In effecting the transfer, a separate sub-fund SAIF, was established within the Company'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 the 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 change in the SAIF technical provisions (no FFA is shown for SAIF in 2018 because technical provisions are set to equal assets). Shareholders have no interest in the profits of SAIF but are entitled to the investment management fees paid on this business.

SAIF with-profits policies contain minimum levels of guaranteed benefit to policyholders. In addition, as mentioned earlier in this note, certain pensions products have guaranteed annuity rates at retirement. Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations of the policyholders of SAIF, the Company's shareholder fund would be liable to cover any such deficiency in the first instance.

The Polish branch became operational in March 2013. The Company's inherited estate is contributing to the costs of establishing the branch, and receives repayment through income from charges levied on the business. There is an obligation of the Company's shareholder funds to ensure the inherited estate will be repaid in full with interest and an amount is included in the longer term business provision for the estimated cost to the shareholder of any shortfall at end of the term of the agreement.

Litigation

The Company is, and in the future may be, subject to legal actions and disputes in the ordinary course of its business. Current litigation includes a claim for £157m in respect of which the Company is one of a number of defendants. The claim relates to a financial restructuring carried out by a borrower in one of the Company's investments. The Company received judgement in its favour in November 2017, which the borrower has subsequently appealed.

While the outcome of this and other matters cannot be predicted with certainty, the directors believe that the ultimate outcome of such litigation will not have a material adverse effect on the Company's financial condition and results. This is considered a contingent liability.

Intra-group Capital Support Arrangements

Prudential plc and the Company have put in place intra-group arrangements to formalise circumstances in which capital support would be made available by Prudential plc (including in the scenarios referred to in Pension Mis-selling Review above). While it is considered unlikely that such support will be required, the arrangements are intended to provide additional comfort to the Company and its policyholders.

In 2016 the Company put in place an arrangement to formalise circumstances in which capital support would be made available to its subsidiary Prudential Pensions Limited (PPL). The drawdown of support would be triggered by a breach of pre-specified solvency conditions in PPL (105% of Solvency Capital Requirement or 105% of Economic Capital Requirement).

There is an obligation of the Company's shareholder funds to support Prudential Financial Planning Ltd, another group company, which became operational in 2013. Part of the acquisition costs incurred in the early years of operation are to be spread over five years to reflect the period over which the benefit, in terms of sales, would arise. Where the initial funding was provided by the Company's with-profits fund, it is subject to support from the shareholder funds that in the event of a closure during this period, the amortisation will be reversed and the shareholder will reimburse the consequent estate drain.

Notes on the financial statements (continued)

28. Financial assets and liabilities

A. Financial instruments - designation and fair values

All financial assets of the Company are designated as either fair value through profit and loss or loans and receivables. Financial liabilities are designated as either fair value through profit and loss, amortised cost or investment contracts with discretionary participation features accounted for under FRS 103 as described in the Accounting Policies section.

2018	Fair value through profit and loss £m	Loans and receivables £m	Total carrying value £m	Fair value £m
Financial Assets				
Deposits with credit institutions	—	8,929	8,929	8,929
Equity securities and portfolio holdings in unit trusts	48,192	—	48,192	48,192
Debt securities and other fixed income securities (note i)	63,999	—	63,999	63,999
Loans (note ii)	1,478	1,836	3,314	3,383
Participation in investment pools	5,046	—	5,046	5,046
Derivative assets	2,283	—	2,283	2,283
Assets held to cover linked liabilities	14,546	—	14,546	14,546
Debtors arising out of direct insurance operations	—	21	21	21
Debtors arising out of reinsurance operations	—	11	11	11
Accrued investment income	—	954	954	954
Other debtors	—	1,275	1,275	1,275
Cash at bank and in hand	—	2,080	2,080	2,080
Finance Lease asset (see note 13)	33	—	33	33
Total	**135,577**	**15,106**	**150,683**	**150,752**

	Fair value through profit and loss £m	Amortised cost £m	Investment contracts with DPF £m	Total carrying value £m	Fair value £m
Financial Liabilities					
Finance lease obligations (see note 13)	—	17	—	17	17
Other borrowings not owed to credit institutions (note iii)	—	89	—	89	89
Investment contracts with discretionary participation features (note iv)	—	—	67,018	67,018	—
Investment contracts without discretionary participation features	6,989	—	—	6,989	6,989
Creditors arising out of direct insurance operations	—	64	—	64	64
Creditors arising out of reinsurance operations	—	78	—	78	78
Deposits received from reinsurers	—	1,172	—	1,172	1,172
Other creditors	355	3,265	—	3,620	3,620
Derivative liabilities	2,172	—	—	2,172	2,172
Total (note v)	**9,516**	**4,685**	**67,018**	**81,219**	**14,201**

Notes on the financial statements (continued)

2017	Fair value through profit and loss £m	Loans and receivables £m		Total carrying value £m	Fair value £m
Financial Assets					
Deposits with credit institutions	—	8,215		8,215	8,215
Equity securities and portfolio holdings in unit trusts	52,745	—		52,745	52,745
Debt securities and other fixed income securities (note i)	73,453	—		73,453	73,453
Loans (note ii)	1,620	1,874		3,494	3,585
Participation in investment pools	3,705	—		3,705	3,705
Derivative assets	2,661	—		2,661	2,661
Assets held to cover linked liabilities	18,303	—		18,303	18,303
Debtors arising out of direct insurance operations	—	22		22	22
Debtors arising out of reinsurance operations	—	9		9	9
Accrued investment income	—	1,113		1,113	1,113
Other debtors	—	1,030		1,030	1,030
Cash at bank and in hand	—	3,365		3,365	3,365
Finance Lease asset (see note 13)	33	—		33	33
Total	**152,520**	**15,628**		**168,148**	**168,239**

	Fair value through profit and loss £m	Amortised cost £m	Investment contracts with DPF	Total carrying value £m	Fair value £m
Financial Liabilities					
Finance lease obligations (see note 13)	—	18	—	18	18
Other borrowings not owed to credit institutions (note iii)	—	123	—	123	123
Investment contracts with discretionary participation features (note iv)	—	—	62,323	62,323	—
Investment contracts without discretionary participation features	7,629	—	—	7,629	7,629
Creditors arising out of direct insurance operations	—	89	—	89	89
Creditors arising out of reinsurance operations	—	36	—	36	36
Deposits received from reinsurers	—	1,260	—	1,260	1,260
Other creditors	367	4,393	—	4,760	4,760
Derivative liabilities	1,593	—	—	1,593	1,593
Total (note v)	**9,589**	**5,919**	**62,323**	**77,831**	**15,508**

Notes

(i) As at 31 December 2018, £355m (2017: £302m) of convertible bonds were included in debt securities. There were no convertible bonds included in borrowings.

(ii) Loans and receivables are reported net of allowance for loan losses of £17m (2017: £14m losses).

(iii) As at 31 December 2018, £89m (2017: £123m) of loans repayable, contingent on regulatory surplus emerging, was included in "Other borrowings not owed to credit institutions".

(iv) It is impractical to determine fair value of investment contracts with discretionary participation features due to the lack of a reliable basis to measure such features.

Notes on the financial statements (continued)

(v) For financial liabilities designated as fair value through profit and loss there was no material impact on profit from movements in credit risk during 2018 and 2017.

Determination of fair value

The fair values of the financial assets and liabilities as shown in the table above have been determined on the following bases:

The fair values of the financial instruments which are held at fair value through profit and loss 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 Company'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 disclosed value cannot be realised in immediate settlement of the financial instrument.

The investment properties of the Company are externally valued by professionally qualified external valuers using the Royal Institution of Chartered Surveyors valuation standards. An 'income capitalisation' technique is predominantly applied for these properties. This technique calculates the value through the yield and rental value depending on factors such as the lease length, building quality, covenant and location. The variables used are compared to recent transactions with similar features to those of the Company's investment properties. As the comparisons are not with properties which are virtually identical to Company's investment properties, adjustments are made by the valuers where appropriate to the variables used. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of the properties.

The Company's shareholder investments in entities that undertake insurance business, and also the investment in the entity that undertakes mortgage lending and administration, are valued using embedded values as determined in accordance with the European Embedded Value (EEV) principles. The EEV basis results have been prepared in accordance with the EEV Principles dated April 2016, issued by the European Insurance CFO Forum. Investments in other subsidiaries are valued based on net asset value where the directors consider that net asset value provides a close approximation to fair values.

Other than the loans which have been designated at fair value through profit or loss, the loans and receivables have been shown net of provisions for impairment. The discount rate is updated for the market risk rate of interest where applicable.

The estimated fair value of derivative financial instruments reflects the estimated amount the Company 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.

The fair value of other financial liabilities is determined using discounted cash flows of the amounts expected to be paid.

Notes on the financial statements (continued)

Level 1, 2 and 3 fair value measurement hierarchy of financial instruments

The table below includes financial instruments carried at fair value analysed by level of the FRS 102.34 *Specialist Activities Financial Institutions* (FRS 102.34) paragraph 22 defined fair value hierarchy (and also includes loans carried at amortised cost in the balance sheet but for which the fair value is disclosed in the financial statements). This hierarchy is based on the inputs to the fair value measurement and reflects the lowest level input that is significant to that measurement. The Company's policy is to recognise transfers into and transfers out of levels at the end of each half year except for material transfers which are recognised as of the date of the event or change in circumstances that caused the transfer.

The classification criteria and its application to the Company 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 be considered active. It also includes other financial instruments 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 investment contract liabilities without DPF that are valued using observable inputs.

In addition level 2 includes debt securities that are valued internally using standard market practices. Of the total level 2 debt securities of £60,307m (2017: £68,501m), £9,387m (2017: £9,295m) 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 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, directly held investment properties and investments in property funds which are exposed to bespoke properties or risks and investments which are internally valued or subject to a significant number of unobservable assumptions. It also includes debt securities and equity release mortgage loans 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.

During 2017, the assumptions used within the discounted cash flow model to value equity release mortgage loans were refined to reflect developing market practice, including consideration of the Prudential Regulation Authority's industry-wide review in this area and resulting guidance. This refinement incorporates inputs relevant to determining the discount rate that are not market observable. As a result, the loans were reclassified as Level 3. There was no material difference in the fair value of these loans recognised in 2017 arising from this change in the valuation model.

Significant assumptions for equity release mortgage assets within the valuation of the no-negative-equity guarantee include the expected annual increase in house prices of 3.05% (2017: 3.19%) and the implied house price volatility of 13% (2017: 13%).

Notes on the financial statements (continued)

	31 December 2018			
	Level 1	**Level 2**	**Level 3**	**Total**
	£m	**£m**	**£m**	**£m**
With-profits*				
Investment properties	—	—	7,577	**7,577**
Equity securities and portfolio holdings in unit trusts	44,383	3,635	174	**48,192**
Debt securities	5,636	42,852	246	**48,734**
Loans	—	1,140	288	**1,428**
Other investments (including derivative assets)	55	3,329	3,610	**6,994**
Derivative liabilities	(64)	(1,169)	—	**(1,233)**
Total financial investments, net of derivative liabilities	**50,010**	**49,787**	**11,895**	**111,692**
Percentage of total	**45%**	**44%**	**11%**	**100%**
Unit-linked				
Assets held to cover linked liabilities	6,990	—	—	**6,990**
Total investments net of derivative liabilities	6,990	—	—	**6,990**
Investment contract without discretionary participation features held at fair value	—	(6,989)	—	**(6,989)**
Total	**6,990**	**(6,989)**	**—**	**1**
Percentage of total	**N/A**	**N/A**	**0**	**100%**
Non-linked shareholder-backed**				
Investment properties	—	—	1,660	**1,660**
Equity securities and portfolio holdings in unit trusts	—	—	—	**—**
Debt securities	3,742	17,455	372	**21,569**
Loans	—	472	1,514	**1,986**
Other investments (including derivative assets)	—	555	1	**556**
Derivative liabilities	—	(939)	—	**(939)**
Total financial investments, net of derivative liabilities	**3,742**	**17,543**	**3,547**	**24,832**
Percentage of total	**15%**	**71%**	**14%**	**100%**
Company total				
Investment properties	—	—	9,237	**9,237**
Equity securities and portfolio holdings in unit trusts	44,383	3,635	175	**48,193**
Debt securities	9,378	60,307	617	**70,302**
Loans	—	1,611	1,802	**3,413**
Other investments (including derivative assets)	55	3,883	3,611	**7,549**
Assets held to cover linked liabilities	6,990	—	—	**6,990**
Derivative liabilities	(64)	(2,108)	—	**(2,172)**
Total financial investments, net of derivative liabilities	**60,742**	**67,328**	**15,442**	**143,512**
Investment contract without discretionary participation features held at fair value	—	**(6,989)**	—	**(6,989)**
Total	**60,742**	**60,339**	**15,442**	**136,523**
Percentage of total	**45%**	**44%**	**11%**	**100%**

* With-profits includes assets held to cover index-linked liabilities.

** Non unit-linked shareholder-backed includes assets held to cover index-linked liabilities.

Notes on the financial statements (continued)

	31 December 2017			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
With-profits*				
Investment properties	—	—	7,403	**7,403**
Equity securities and portfolio holdings in unit trusts	49,623	3,079	43	**52,745**
Debt securities	5,670	41,105	234	**47,009**
Loans	—	1,119	397	**1,516**
Other investments (including derivative assets)	29	3,720	2,341	**6,090**
Derivative liabilities	(41)	(517)	—	**(558)**
Total financial investments, net of derivative liabilities	**55,281**	**48,506**	**10,418**	**114,205**
Percentage of total	**48%**	**43%**	**9%**	**100%**
Unit-linked				
Assets held to cover linked liabilities	8,165	—	1	**8,166**
Total financial investments net of derivative liabilities	8,165	—	1	**8,166**
Investment contract without discretionary participation features held at fair value	—	(7,629)	—	**(7,629)**
Total	**8,165**	**(7,629)**	**1**	**537**
Percentage of total	**N/A**	**N/A**	**—%**	**100%**
Non-linked shareholder-backed**				
Investment properties	—	—	1,653	**1,653**
Equity securities and portfolio holdings in unit trusts	—	—	—	**—**
Debt securities	7,521	27,396	306	**35,223**
Loans	—	448	1,657	**2,105**
Other investments (including derivative assets)	—	526	1	**527**
Derivative liabilities	—	(1,036)	—	**(1,036)**
Total financial investments, net of derivative liabilities	**7,521**	**27,334**	**3,617**	**38,472**
Percentage of total	**20%**	**71%**	**9%**	**100%**
Company total				
Investment properties	—	—	9,055	**9,055**
Equity securities and portfolio holdings in unit trusts	49,623	3,079	43	**52,745**
Debt securities	13,191	68,501	540	**82,232**
Loans	—	1,567	2,054	**3,621**
Other investments (including derivative assets)	29	4,246	2,342	**6,617**
Assets held to cover linked liabilities	8,165	—	1	**8,166**
Derivative liabilities	(41)	(1,553)	—	**(1,594)**
Total financial investments, net of derivative liabilities	**70,967**	**75,840**	**14,035**	**160,842**
Investment contract without discretionary participation features held at fair value	—	**(7,629)**	—	**(7,629)**
Total	**70,967**	**68,211**	**14,035**	**153,213**
Percentage of total	**46%**	**45%**	**9%**	**100%**

* With-profits includes assets held to cover index-linked liabilities.
** Non unit-linked shareholder-backed includes assets held to cover index-linked liabilities.

Assets held to cover unit-linked liabilities, shown in the table, only covers those assets which are required to be disclosed under the provisions of FRS 102.34 for the fair value hierarchy. There are a further £989m (2017: £1,045m) of assets which comprise the total assets held to cover unit-linked liabilities, which consist mainly of cash at bank, other debtors and property.

Interest expense

The interest expense on financial liabilities not at fair value through profit and loss was £6m for the year ended 31 December 2018 (2017: £7m).

Notes on the financial statements (continued)

B. Risk Management

The Company's business involves the acceptance and management of risk. The Company has in place a risk management process, which is undertaken in accordance with the GRF.

A number of risk factors affect the Company's operating results and financial condition. The financial risk categories affecting the Company's financial instruments and insurance assets and liabilities are set out below:

Risk Type	Definition
Market risk	The risk of loss for the Company, or of adverse change in the financial situation, resulting directly or indirectly, from fluctuations in the level or volatility of market prices of assets and liabilities.
Credit risk	The risk of loss for the Company or of adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors in the form of default or other significant credit event (e.g. downgrade or spread widening).
Insurance risk	The risk of loss for the Company, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend or volatility of a number of insurance risk drivers. These include adverse longevity, mortality and morbidity experience.
Liquidity risk	The risk of the Company being unable to generate sufficient cash resource to meet financial obligations as they fall due in business as usual and stress scenarios.

The financial assets and liabilities attaching to the Company's life assurance business are, to varying degrees, subject to the risks described above that may have a material effect on the profit or loss and shareholders' funds. They can be categorised as follows:

- With-profits sub-fund business;
- SAIF; and
- Shareholder fund.

With-profits sub-fund business
The shareholder results of the Company's with-profits business are sensitive to market risk only through the indirect effect of investment performance on previously declared policyholder bonuses. Since 2013, the Company has held a partial equity hedge of the shareholder transfers expected to emerge from the with-profits sub-fund in order to mitigate this risk and arrangements were put in place to top up existing hedges in 2018. During 2018, the Company entered into a hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, specifically with regard to the PruFund 2018 new business, as they arise over the period to 2027. The investment assets of the Company's with-profits fund are subject to market risk. Changes in their carrying value, net of the related changes to asset-share liabilities of with-profit contracts, affect the level of unallocated surplus. Therefore, the level of unallocated surplus is particularly sensitive to the level of investment returns on the portion of the assets that represents surplus. However as unallocated surplus is accounted for as a liability, movements in its value do not affect shareholders' profit or shareholders' funds.

The shareholder results of the Company's with-profits fund are currently one-ninth of the cost of bonuses declared to with-profits policyholders. For certain unitised with-profits products, such as the PruFund range of funds, the bonuses represent the policyholders' net return based on the smoothed unit price of the selected investment fund.

Investment performance is a key driver of bonuses declared, and hence the shareholder results. Due to the 'smoothed' basis of bonus declaration, the sensitivity to short-term investment performance is relatively low. However, long-term investment performance may affect future shareholder transfers.

Mortality and other insurance risk are relatively minor factors in the determination of the bonus rates. Adverse persistency experience can affect the level of profitability from with-profits but in any given one year, the shareholders' share of cost of bonus may only be marginally affected. However, altered persistency trends may affect future expected shareholder transfers.

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

Notes on the financial statements (continued)

Shareholder fund
The Company's shareholder fund principally comprises annuity business previously written by Scottish Amicable Life and Prudential Retirement Income Ltd, lifetime mortgage business, unit-linked and other non-participating business. The financial assets covering the liabilities for those types of business are subject to market risk. The liabilities for annuity contracts are subject to market risk arising from changes in the returns of backing assets. The sensitivity of the Company's shareholder fund's annuity business' results (excluding the return assets backing capital) to market risk for movements in the carrying value of liabilities and covering assets is broadly neutral on a net basis, except to the extent of any minor asset/liability duration mismatch and exposure to credit risk.

The liabilities of the unit-linked business change in line with the matching linked assets. Amounts under unit-linked contracts are generally repayable on demand and the Company is responsible for ensuring there is sufficient liquidity within the asset portfolio to enable liabilities to unit-linked policyholders to be met as they fall due. Other liabilities of the Company's shareholder fund are broadly insensitive to market risk.

C. Market Risk

As described in section B market risk is the risk of loss, or adverse change in the financial situation resulting directly or indirectly, from fluctuations in the level or volatility of market prices of assets and liabilities.

Market risk comprises six types of risk, namely:
- Equity: due to fluctuations in equity prices;
- Interest rate: due to changes in market interest rates;
- Inflation: in relation to liability payments linked to inflation indices;
- Property: due to changes in property valuations;
- Currency: due to changes in foreign exchange rates; and
- Other assets / alternative investments: due to fluctuations in any other market prices or alternative investments (other than those detailed above).

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

The split of the Company'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 Company has available. This mix of liabilities allows the Company to invest a substantial portion of its investment funds in equity and property investments that the Company believes produce greater returns over the long term. On the other hand the Company has some liabilities that contain guaranteed returns which generally will be supported by fixed income investments.

The Company continues to invest further into private illiquid assets, increasing the concentration of fixed income investments.

Interest rate risk

The net exposure to interest rate movement for the Company is substantially ameliorated by virtue of the close matching of assets with appropriate duration to the liabilities. However, some exposure remains due to holding more assets than needed to cover the liabilities.

The close matching by the Company of assets of appropriate duration to its shareholder fund's annuity liabilities is based on maintaining economic and regulatory capital. The measurement of liabilities under capital reporting requirements and FRS 103 is not the same, with contingency reserves and some other margins for prudence not included for FRS 103 reporting purposes. As a result FRS 103 shareholders' funds are higher than regulatory capital and more sensitive to interest rate risk.

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The estimated sensitivity of the shareholder-backed business to a movement in interest rates of 1% and 2% as at 31 December 2018 and 2017 are as follows:

	2018				2017			
	Fall of 1%	**Rise of 1%**	**Fall of 2%**	**Rise of 2%**	Fall of 1%	Rise of 1%	Fall of 2%	Rise of 2%
	£m	**£m**	**£m**	**£m**	£m	£m	£m	£m
Carrying value of debt securities and derivatives	**3,317**	**(2,792)**	**7,369**	**(5,193)**	5,805	(4,659)	13,497	(8,541)
Long term business provision	**(2,162)**	**1,801**	**(4,784)**	**3,317**	(4,210)	3,443	(9,426)	6,295
Related tax effects	**(199)**	**171**	**(446)**	**323**	(254)	190	(658)	348
Net sensitivity of profit after tax and shareholders' funds	**956**	**(820)**	**2,139**	**(1,553)**	1,341	(1,026)	3,413	(1,898)

Other Price Risk - Equities and Property

In addition, the shareholder backed portfolio of the Company includes equity securities and 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.

	2018		2017	
	Decrease of 20%	**Decrease of 10%**	Decrease of 20%	Decrease of 10%
	£m	**£m**	£m	£m
Pre-tax profit	**(332)**	**(166)**	(331)	(165)
Related deferred tax effects	**56**	**28**	56	28
Net sensitivity of profit after tax and shareholders' funds	**(276)**	**(138)**	(275)	(137)

A 10% or 20% increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above.

In the equity risk sensitivity analysis shown above the Company has considered the impact of an instantaneous 20 per cent fall in equity markets. The Company believes a fall of greater than 20% would be expected to occur over a greater period of time rather than instantaneously, during which time the Company would be able to put mitigating management actions in place.

Currency Risk

As at 31 December 2018 the Company held 39% and 2% (2017: 35% and 3%) 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 80% (2017: 73%) are held by the with-profit fund, allow the Company to obtain exposure to foreign equity and debt markets.

The financial liabilities, of which 90% (2017: 88%) are held by the with-profit fund, mainly relate to investment contracts with discretionary participation features.

The exchange risks inherent in these exposures are partially mitigated through the use of derivatives, mainly forward currency contracts.

D. Credit risk

The Company's long-term fund holds large amounts of investments that contain credit risk on which a certain level of defaults is expected. These expected losses are considered when the Company determines the crediting rates, deposit rates and premium rates for the products that will be supported by these assets. Certain over-the-counter derivatives contain a credit risk element that is controlled through evaluation of collateral agreements

Notes on the financial statements (continued)

and master netting agreements on interest rate and currency swaps. The Company is also exposed to credit-related losses in the event of non-performance by counterparties.

Debt Securities and Other Fixed Income Securities

The following table summarises by rating the securities held by the Company as at 31 December 2018 and 2017.

	2018 £m						
	AAA	**AA+ to AA-**	**A+ to A-**	**BBB+ to BBB-**	**Below BBB-**	**Other**	**Total**
With-profits	**6,678**	**8,543**	**10,766**	**13,439**	**2,480**	**4,951**	**46,857**
Non-linked shareholder-backed	**2,495**	**4,795**	**3,745**	**1,287**	**134**	**4,686**	**17,142**
Total debt securities and other fixed income securities	**9,173**	**13,338**	**14,511**	**14,726**	**2,614**	**9,637**	**63,999**

	2017 £m						
	AAA	**AA+ to AA-**	**A+ to A-**	**BBB+ to BBB-**	**Below BBB-**	**Other**	**Total**
With-profits	6,336	8,452	10,815	11,951	2,246	5,035	44,835
Non-linked shareholder-backed	4,631	8,756	7,418	2,799	163	4,851	28,618
Total debt securities and other fixed income securities	10,967	17,208	18,233	14,750	2,409	9,886	73,453

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In the table above 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.

Where no external ratings are available internal ratings produced by the Prudential Group's asset management operations, which are prepared on a comparable basis to external ratings, are used where possible. Of the total debt securities held at 31 December 2018 which are not externally rated, £6,345m (2017: £6,577m) were internally rated AAA to A-, £2,554m (2017: £2,573m) were internally rated BBB+ to B- and £738m were internally rated as below B- or unrated (2017: £737m). The majority of the unrated debt security investments were held by the Company's with-profits fund and relate to convertible debt and other investments which are not covered by rating analysts nor have an internal rating attributed to them.

As detailed in section B the primary sensitivity of profit or loss and shareholders' equity of the Company relates to non-linked shareholder-backed business.

Excluded from the table above is £6,309m (2017: £9,042m) of assets backing unit-linked and index-linked contracts which are included within assets held to cover linked liabilities. The policyholders of these contracts bear the credit risk arising from these assets.

The Company's exposure to the Eurozone sovereigns of Portugal, Italy, and Spain is £111m (2017: £173m) with £75m (2017: £81m) in the with-profits fund and £36m (2017: £92m) in the shareholder funds. The Company's exposure to banking operations in these Eurozone countries is £61m (2017: £47m) all within the with-profits fund.

Loans and receivables

In accordance with accounting policy, impairment reviews were performed for loans and receivables. During the year ended 31 December 2018, impairment losses of £7m (2017: £4m) and £nil reversal of impairment losses (2017: £nil) were recognised for loans and receivables.

Of the total loans and receivables held £13m (2017: £8m) are past their due date but have not been impaired. 100% (2017: 100%) of the loans and receivables that are past due but not impaired are less than one year past their due date for 2018. The Company expects full recovery of these loans and receivables.

Reinsurer's share of technical provisions

Of the reinsurer's share of technical provisions at 31 December 2018 of £18,255m (2017: £7,820m), 67% (2017: 18%) of the balance relates to companies outside of the Prudential Group and of this 99% (2017: 94%) of the balances were from reinsurers with S&P's rating of BBB and above.

Securities lending and reverse repurchase agreements

The Company 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 Company's balance sheet; 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 2018, the Company has £8,245m (2017: £8,175m) of lent securities and assets subject to repurchase agreements. The cash and securities collateral held or pledged under such agreements was £8,662m (2017: £8,674m).

At 31 December 2018, the Company had entered into reverse repurchase transactions under which it purchased securities and had taken on the obligation to resell the securities. The fair value of the collateral held in respect of these transactions was £8,481m (2017: £8,292m).

During 2018 and 2017 the Company did not take possession of any other collateral held as security.

Collateral and pledges under derivative transactions

At 31 December 2018, the Company had pledged £989m (2017: £665m) for liabilities and held collateral of £1,373m (2017: £1,957m) in respect of over-the-counter derivative transactions.

These transactions are conducted under terms that are usual and customary to collateralised transactions including, where relevant, standard securities lending and repurchase agreement.

Collateral Pledged and Received for Reinsurance Contracts

The Company has entered into several reinsurance agreements where the Reinsurer has agreed to reinsure the Company in respect of the reinsurance claims in consideration of the Company agreeing to pay to the Reinsurer the reinsurance premium and reinsurance fee. Exposure collateral calculations are performed on each agreement on either a quarterly or annual basis, with relevant collateral then being pledged or held by the Company. The calculations commenced in 2018. As at 31 December 2018, the Company had pledged collateral of £4m, relating to these agreements.

Collateral Pledges for Equity Release mortgages

At 31 December 2018 the Company had pledged collateral of £396m (2017: £367m) consisting of debt securities for the deferred purchase consideration for the mortgages purchased from Santander.

E. Insurance Risk

The Company is exposed to significant levels of insurance risk. Insurance risk arises mainly from the annuity business in the form of longevity risk, which is the risk that the Company's (current and deferred) annuity customers live longer than expected in the Company's current pricing and reserving assumptions, and as a result future reserving and capital assumptions are changed. The Company conducts rigorous research into longevity risk, using data from its annuitant portfolio. As part of its pension annuity pricing and reserving policy, mortality rates are reviewed annually using external data at levels based on the Company's calibration of the Continuous Mortality Investigations (CMI) 2016 mortality projection model as published by the Institute and Faculty of Actuaries. If mortality improvement rates significantly exceed the improvement assumed, the Company's operating results could be adversely affected. Further any major medical breakthrough (for example in the treatment of cancer or

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other life-threatening diseases) that would require the Company to strengthen its longevity assumptions would have an impact on the Company's results.

Mortality and morbidity risks relate to assumptions around the expected number of deaths or illnesses used in pricing and calculating reserves. These are relevant for those lines of business where the customer payoff is dependent on a death or illness. An example is the impact of epidemics or other events that cause a large number of illnesses and/or deaths. Significant influenza epidemics have occurred three times in the last century, but the likelihood, timing, or the severity of future epidemics cannot be predicted. The effectiveness of external parties, including governmental and non-governmental organisations, in combating the spread and severity of any epidemics could have a material impact on the Company's loss experience if such an epidemic were to occur. If the actual mortality or morbidity rates were significantly higher than those assumed in pricing and reserving, then the Company would make a loss on certain lines of business which could be offset by potential gains on other lines of business due to the natural diversification between longevity and mortality risks.

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

- The extent to which changes to the assumed rate of improvements in mortality give rise to changes in the measurement of liabilities;
- changes in renewal expense levels; and
- the variance between actual and expected mortality experience.

A decrease in assumed mortality rates of 1% would decrease pre-tax profits by approximately £37m (2017: £66m). A decrease in credit default assumptions of five basis points would increase pre-tax profit by £99m (2017: £198m). A decrease in renewal expenses (excluding asset management expenses) of 5% would increase pre-tax profits by £21m (2017: £40m). The effect on profits would be approximately symmetrical for changes in assumptions that are directionally opposite to those explained above. The net effect on profit after tax and shareholders' equity from all the changes in assumptions as described above would be an increase of approximately £69m (2017: £143m). This analyses has been determined by varying the relevant assumption as at the reporting date while holding all other assumptions constant.

For unit-linked business, 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.

With-profits sub-fund business
Mortality and other insurance risk are relatively minor factors in the determination of the bonus rates. Adverse persistency experience can affect the level of profitability from with-profits but in any given one year, the shareholders' share of cost of bonus may only be marginally affected. However, altered persistency trends may affect shareholder profits to the extent that likely lead to changes in future shareholder transfers.

F. Liquidity Risk

Liquidity risk is the risk that the Company may be unable to meet payment of obligations in a timely manner at a reasonable cost or the risk of unexpected increases in the cost of funding the portfolio at appropriate maturities or rates. Liquidity management in the Company seeks to ensure that, even under adverse conditions, the Company has access to the funds necessary to cover surrenders, withdrawals and maturing liabilities. Liquidity risk is carefully managed in particular in relation to: bank balances, cashflow forecasting, appropriate fund management (to ensure that assets are not unduly concentrated in less liquid investments) and detailed cash-flow matching for the annuity business. Specific arrangements are also in place to manage liquidity in the linked funds, particularly property funds where the underlying assets are relatively illiquid.

In practice, most of the Company's assets are marketable securities. This, combined with the fact that a large proportion of the liabilities contain discretionary surrender values or surrender charges, reduces the liquidity risk.

Liquidity Analysis

(i) Contractual maturities of financial liabilities

The following tables set out the contractual maturities and repricing dates for applicable classes of financial liabilities, excluding derivative liabilities and investment contracts, which are separately presented. The financial liabilities are included in the column relating to the contractual maturities and repricing dates at the undiscounted

Notes on the financial statements (continued)

cash flows (including contractual interest payments) due to be paid assuming conditions are consistent with those at year end.

2018	**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 un-discounted cashflows**	**Total carrying value**
Financial Liabilities	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Amounts owed to credit institutions	**1**	**1**	**1**	**1**	**1**	**13**	**18**	**18**
Other borrowings not owed to credit institutions	**—**	**89**	**—**	**—**	**—**	**—**	**89**	**89**
	1	**90**	**1**	**1**	**1**	**13**	**107**	**107**

2017	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 un-discounted cashflows	Total carrying value
Financial Liabilities	£m	£m	£m	£m	£m	£m	£m	£m
Amounts owed to credit institutions	1	1	1	1	1	13	18	18
Other borrowings not owed to credit institutions	—	123	—	—	—	—	123	123
	1	**124**	**1**	**1**	**1**	**13**	**141**	**141**

ii) Maturity analysis of derivatives and investment contracts

The following table provides a maturity analysis of derivative assets and liabilities:

2018	**Total carrying value**	**1 year or less**	**After 1 to 3 years**	**After 3 to 5 years**	**After 5 years**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Net derivative position	**111**	**111**	**—**	**—**	**—**	**111**

2017	Total carrying value	1 year or less	After 1 to 3 years	After 3 to 5 years	After 5 years	Total
	£m	£m	£m	£m	£m	£m
Net derivative position	1,068	1,068	—	—	—	1,068

The net derivative positions as shown in the table above comprise the following derivative assets and liabilities:

	2018	2017
	£m	£m
Derivative assets (note 15)	**2,283**	2,661
Derivative liabilities (note 15)	**(2,172)**	(1,593)
Net derivative position	**111**	1,068

The 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 Company has no cash flow hedges.

Notes on the financial statements (continued)

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 the European Embedded Value (EEV) basis results.

	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 un-discounted value	Total carrying value
	£bn	£bn	£bn	£bn	£bn	£bn	£bn	£bn
2018								
Life assurance investment contracts	**8**	**29**	**28**	**20**	**12**	**16**	**113**	**74**
2017								
Life assurance investment contracts	7	27	26	19	12	14	105	70

This table has been prepared on an undiscounted basis and accordingly the amounts shown for life assurance investment contracts differ from those included in the balance sheet. Durations of long-term business contracts, covering both insurance and investment contracts, on a discounted basis are included in note 26.

G. Derivatives and Hedging

The Company uses derivatives for the purpose of efficient portfolio management or the reduction in investment risk. In so doing, the Company obtains cost effective and efficient exposure to various markets and to manage exposure to equity, interest rate, currency, credit and other business risks. The Company also hedges against the equity risk affecting future shareholder transfers from the with profits sub fund. The Company has opted not to apply hedge accounting to derivatives.

The Company uses various interest rate derivative instruments such as interest rate swaps and swaptions to reduce exposure to interest rate volatility.

The Company also uses various currency derivatives in order to limit volatility due to foreign currency exchange rate fluctuations arising on securities denominated in currencies other than sterling.

All over-the-counter derivative transactions are conducted under standardised ISDA (International Swaps and Derivatives Association Inc) master agreements and CSA (Credit Support Annex) in accordance with the regulatory requirements.

The Group has collateral agreements between the individual group entities, of which the Company is one, and relevant counterparties in place under each of these market master agreements. The Company has also entered into cleared derivative positions under the EMIR (European Market Infrastructure Regulation).

The total fair value balances of derivative assets and liabilities are shown in note 15.

There are hedging arrangements in place for the liabilities. In addition to some product/purpose specific arrangements, the main objective of the hedging arrangement is to broadly match a subset of the market consistent liabilities and hence protect the Solvency II position of the with-profits business against adverse market movements. A benchmark of a theoretical replicating portfolio (comprising of equity put options and interest rate exposures) representing the liabilities has been determined, based on characteristics of the with-profits liability. The actual and required hedging positions are monitored on a monthly basis and rebalanced if required.

During 2013 the Company entered into a partial equity hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, which has been extended in 2017 and 2018. The effect in 2018 is an unrealised gain of £201m (2017: unrealised loss of £113m) and a realised loss of £48m (2017: realised loss of £97m) charged to the non-technical account.

During 2018, the Company entered into a hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, specifically with regard to the PruFund 2018 new business, as arise over the period to 2027. The transaction resulted in no gain or loss in the non-technical account in 2018.

Notes on the financial statements (continued)

29. Capital Requirements and Management

The Company's estimated and unaudited shareholder Solvency II Own Funds at 31 December 2018 is £8.8bn, (2017: £15.7bn) after allowing for recalculation of transitional measures as at 31 December 2018. This relates to shareholder-backed business including future with-profits shareholder transfers, but excludes the shareholders' share of the estate in line with Solvency II requirements. Own Funds is the Solvency II measure of assets less liabilities and certain other restrictions.

While the surplus position of the Company with-profits funds remain strong on a Solvency II basis, it is ring-fenced from the shareholder balance sheet and is therefore excluded from the Company's shareholder Solvency II surplus results. The Company's estimated and unaudited with-profits Solvency II Own Funds at 31 December 2018 was £9.6bn (2017: £9.6bn), after allowing for recalculation of transitional measures as at 31 December 2018.

The sale of the Hong Kong subsidiaries resulted in a decrease of £8.8bn in the value of participations, offset by the removal of the Hong Kong ring-fenced funds restriction of £0.9bn and £0.2bn effect on the transitional measure for technical provisions, giving an own funds impact of £7.7bn at the date of transfer. The Solvency Capital Requirement ('SCR') decreased by £2.7bn due to the release of the Hong Kong business standalone SCR, partially offset by a loss of diversification benefit. These changes resulted overall in a decrease in surplus of £5.0bn. These figures include the impact of surplus arising from Hong Kong during 2018 prior to the sale.

The reinsurance of £12bn of the Company's annuity portfolio to Rothesay Life resulted in a decrease of £0.2bn to Own Funds and a decrease of £1.1bn to the SCR, giving an overall increase in surplus of £0.9bn.

The Solvency II Pillar I capital requirements at 31 December 2018 have been calculated using the Company's Internal Capital Model. The method used to calculate the capital has been to:

- (i) identify the major risks to which the business is exposed,
- (ii) specify a probability distribution which defines the full range of outcomes for each risk, including the 99.5% (or 1-in-200) worst outcome that the directors believe could occur over the coming year,
- (iii) specify an appropriate dependency structure between each of the risks,
- (iv) use stochastic modelling to generate up to 100,000 equally likely risk scenarios where each risk is simulated at the same time, having regard to the probability distribution for each risk and the dependency between different risks,
- (v) calculate the change in the available capital over a one year period in each scenario, and
- (vi) set the capital as the change in the available capital in the 99.5th worst scenario.

Shareholder fund

The Company manages its Own Funds to ensure that sufficient Own Funds are available on an ongoing basis to meet regulatory capital requirements. This is achieved by targeting a capital buffer significantly in excess of regulatory capital requirements. This buffer is intended to absorb the impact of stressed market conditions and thus make the regulatory balance sheet resilient to stresses that affect the Company shareholder-backed business, and is calibrated such that following a stress event (at the calibrated likelihood) the business remains able to cover its Solvency II Solvency Capital Requirement (SCR).

Projections are performed over three year time horizons to understand how the Own Funds and capital position is expected to develop and how this might be affected by adverse events taking place. Informed by the results of these projections there are a number of actions available to management to strengthen Own Funds position, including (but not limited to) changes to investment strategy, dividend policy and risk transfer.

Policyholder Fund

The Company manages its Own Funds to ensure that sufficient Own Funds are available on an ongoing basis to meet regulatory capital requirements. The risk appetite is the key tool for determining what level of Own Funds is needed to ensure that regulatory capital requirements continue to be met with a high degree of confidence.

Projections are performed over three year time horizons to understand how the Own Funds and capital position is expected to develop and how this might be affected by adverse events taking place, including assessment against risk appetite. Informed by the results of these projections there are a number of actions available to management to influence the development of the Own Funds position, including (but not limited to) changes to investment strategy, bonus policy, level and type of new business and risk transfer.

Notes on the financial statements (continued)

The Company's estimated Own Funds position for shareholder and policyholder business separately is shown below, along with reconciliations to shareholders' funds and the FFA.

The Company's Solvency II capital requirement has been met during the year.

Reconciliation of the Shareholder Funds and FFA to the estimated Solvency II Own Funds (unaudited)

	2018	2017
	£m	£m
UK with profits funds		
Fund for future appropriations	13,487	13,581
Value of shareholder transfers	(2,394)	(2,731)
Impact of risk margin (net of transitionals)	(1,005)	(726)
Other valuation differences	(451)	(546)
With Profits Ring Fenced Fund - Estimated Solvency II Own Funds	**9,637**	**9,578**
Other long term business		
Shareholders' equity	6,877	15,611
Impact of risk margin (net of transitionals)	(581)	(838)
Add value of shareholder transfers	2,394	3,817
Asset valuation differences	515	(2,549)
Other valuation differences	(459)	(29)
Decrease in value of net deferred tax liabilities (resulting from valuation differences above)	76	133
Restrictions on ring fenced funds	(5,458)	(5,211)
Shareholder business - estimated Solvency II Own Funds	**3,364**	**10,934**
Estimated Company Solvency II Own Funds note(i)	**13,001**	**20,512**

Analysis of movement in own funds (unaudited)

	2018	2017
	£m	£m
Own Funds at 1 January	**20,512**	**18,168**
Transfer of Hong Kong subsidiaries	(6,894)	
Annuity sale impact	(234)	
Own Funds at 1 January restated	**13,384**	
Underlying operating experience	1,358	1,909
Management actions	403	401
Operating experience	1,761	2,310
Non-operating experience (including market movements)	(1,923)	1,224
Other capital movements		
Foreign currency translation impacts	—	(739)
Dividends paid	(330)	(438)
Deferred tax assets/liabilities	109	(13)
Own Funds at 31 December	**13,001**	**20,512**
Change in own funds	**(7,511)**	**2,344**

Notes on the financial statements (continued)

30. Related Undertakings

The related undertakings are prepared in accordance with "The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015".

The following is a list of related undertakings of the Company at 31 December 2018.

(i) Direct subsidiary undertakings

Investment

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Cardinal Distribution Park Management Limited	Ordinary Shares	66%	United Kingdom	1st Floor, Cavendish House, 39 Waterloo Street, Birmingham, B2 5PP, UK
Carraway Guildford General Partner Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Carraway Guildford Limited Partnership	Limited partnership interest	50%	United Kingdom	Lloyds Chambers, 1 Portsoken Street, London, E1 8HZ
Cribbs Causeway JV Limited	Share Capital	50%	United Kingdom	40 Broadway, London SW1H 0BU, UK
Cribbs Mall Nominee (1) Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Edger Investments Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Edinburgh Park (Management) Limited	Private company limited by guarantee	100%	Scotland	Shepherd & Wedderburn, 1 Exchange Crescent, Conference Square, Edinburgh, Scotland, EH3 8UL
Foudry Properties Limited	Ordinary Shares	50%	United Kingdom	Clearwater Court, Vastern Road, Reading RG1 8DB
The Greenpark (Reading) Limited Partnership	Limited Partnership Interest	50%	United Kingdom	5 Laurence Pountney Hill, London, EC4R 0HH
Manchester JV Limited	Ordinary Shares	50%	United Kingdom	40 Broadway, London, England And Wales, United Kingdom, SW1H 0BT
Manchester Nominee (1) Limited	Ordinary Shares	100%	United Kingdom	Governors House, Laurence Pountney Hill, London, EC4R 0HH
Minster Court Estate Management Limited	A Ordinary Shares and B Ordinary Shares	56%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
NAPI REIT, Inc	Ordinary Shares	99%	USA	7 St. Paul Street, Suite 820, Baltimore MD 21202, USA
Optimus Point Management Company Limited	Ordinary Shares	58.1%	United Kingdom	Barrat House Cartwright Way, Forest Business Park, Bardon Hill, Coalville, Leicestershire, LE67 1UF, UK
Pacus (UK) Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
PPMC First Nominees Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Investment (Luxembourg) 2 S.à r.l.	Ordinary shares	100%	Luxembourg	34-38, Avenue de la Liberté, L-1930, Luxembourg
Prudential Loan Investments SCSp	Limited partnership interest	100%	Luxembourg	1, Rue Hildegard von Bingen, L-1282 Luxembourg

Notes on the financial statements (continued)

Prudential Properties Trusty Pty Limited	Unclassified Shares	100%	Australia	Pricewaterouse Coopers, Level 1, Darling Park Tower 2, 201 Sussex Street, Sydney, NSW 2000, Australia
Prudential Property Investments Limited	Ordinary Shares and Redeemable Preference Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 1 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 2 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 3 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prutec Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
PVM Partnerships Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Sealand (No 1) Limited	Ordinary Shares	100%	Jersey	Lime Grove House, Green Street, St Helier, Jersey, JE1 2ST
Sealand (No 2) Limited	Ordinary Shares	100%	Jersey	Lime Grove House, Green Street, St Helier, Jersey, JE1 2ST
Smithfield Limited	Has both £1.00 Ordinary Shares and $1.00 Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Three Snowhill Birmingham SARL	Ordinary Shares	100%	Luxembourg	5, rue Guillaume Kroll, L-1882, Luxembourg
Two Snowhill Birmingham SARL	Ordinary shares	100%	Luxembourg	5, rue Guillaume Kroll, L-1882, Luxembourg
Wessex Gate Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Westwacker Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Insurance

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential International Assurance plc	Ordinary Shares	100%	Ireland	Montague House, Adelaide Road, Dublin 2, D02 K39, Ireland
Prudential Pensions Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Pension

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential Corporate Pensions Trustee Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Notes on the financial statements (continued)

Holding company

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential Holborn Life Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Mortgage lending

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential Lifetime Mortgages Limited	Ordinary & Preference Shares	100%	United Kingdom	Craigforth, Stirling, FK9 4UE, UK

Financing

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Scottish Amicable Finance plc	Ordinary Shares	99.99%	United Kingdom	Craigforth, Stirling, FK9 4UE, UK

Service

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential International Management Services Limited	Ordinary Shares	100%	Ireland	Montague House, Adelaide Road, Dublin 2, D02 K39, Ireland

In liquidation

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential Retirement Income Limited (in liquidation)	Ordinary Shares & Preference Shares	100%	United Kingdom	Mazars LLP, 90 St. Vincent Street, Glasgow, G2 5UB, UK

Dormant

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Scottish Amicable Life Assurance Society	No Share Capital	100%	United Kingdom	Craigforth, Stirling, Scotland, FK9 4UE

(ii) Other subsidiaries, associated undertakings, joint ventures and significant holdings

Investment

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
ANRP II (AIV VI FC), L.P.	Limited Partnership Interest	37%	Cayman Islands	Walkers Corporate Limited, Cayman Corporate Centre, 27 Hospital Road, George Town KY 9008, Cayman Islands
BWAT Retail Nominee (1) Limited	A Ordinary Shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Notes on the financial statements (continued)

BWAT Retail Nominee (2) Limited	A Ordinary Shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Carraway Guildford (Nominee A) Limited	Ordinary Shares	100%	Jersey	IFC 5, St Helier, JE1 1ST, Jersey
Carraway Guildford (Nominee B) Limited	Ordinary Shares	100%	Jersey	IFC 5, St Helier, JE1 1ST, Jersey
Carraway Guildford Investments Unit Trust	Ordinary Shares	100%	Jersey	13 Castle Street, St Helier, Jersey, JE4 5UT
Centaurus Retail LLP	Limited Partnership Interest	50%	United Kingdom	40 Broadway, London, SW1H 0BU, UK
Centre Capital Non-Qualified Investors IV AIV Orion, L.P.	Limited partnership interest	46%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors IV AIV-ELS, L.P.	Limited partnership interest	46%	USA	2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors IV, L.P.	Limited partnership interest	45%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors V AIV-ELS LP	Limited partnership interest	37%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors V LP	Limited partnership interest	33%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
CF Prudential European QIS Fund	Ordinary Shares	98%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
CF Prudential Japanese QIS Fund	Ordinary Shares	98%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
CF Prudential North American QIS Fund	Ordinary Shares	99%	United Kingdom	135 Bishopsgate, London EC2M 3UR, UK
CF Prudential Pacific Markets Trust Fund	Ordinary Shares	98%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
CF Prudential UK Growth QIS Fund	Ordinary Shares	99%	United Kingdom	17 Rochester Row, London, SW1P 1QT, UK
CF UK Growth Qualified Investor Scheme	Ordinary Shares	99%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Cribbs Causeway Merchants Association Ltd	Limited by Guarantee	Membership is fluid, therefore there is no fixed percentage interest	United Kingdom	Management Offices, The Mall at Cribbs Causeway, Bristol BS34 5DG
Eastspring Investments - Asia Pacific Equity Fund	Ordinary Shares	97%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Local Bond Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Smaller Companies Fund	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Total Return Bond Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg

Notes on the financial statements (continued)

Eastspring Investments - Developed and Emerging Asia Equity Fund	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Global Emerging Markets Dynamic Fund	Ordinary shares	93%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - US Equity Income Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Japan Equity Fund	Ordinary shares	90%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments SICAV-FIS Africa Equity FUND	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
European Specialist Investment Funds - M&G Total Return Credit Investment Fund	Ordinary shares	26%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
Folios III Designated Activity Company	Ordinary Shares	60%	Ireland	Fourth Floor, 76 Lower Baggot Street, Dublin 2
Infracapital Partners LP	Limited partnership interest	33%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Infracapital Partners II LP	Limited partnership interest	26%	United Kingdom	Governor's House, Laurence Pountney Hill, London, EC4R 0HH, England
MCF S.r.l.	Ordinary shares	45%	Italy	Via Montenapoleone 29, Milan
M&G Absolute Return Bond Fund Total	Ordinary Shares	42%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Asia Property Fund	A Class Shares	54%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G Corporate Bond Fund	Ordinary shares	31%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Dividend Fund	Ordinary shares	58%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G European Credit Investments Fund	Ordinary Shares	82%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
M&G European High Yield Credit Investments Fund	Ordinary Shares	100%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
M&G European Property Fund SICAV-FIS	Ordinary Shares	50%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G European Secured Property Income Fund	Units	24%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G European Select Fund	Ordinary Shares	42%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Gilt & Fixed Interest Income Fund	Ordinary shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Global Convertibles Fund	Ordinary Shares	59%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G (Lux) European Strategic Value Fund	Ordinary Shares	79%	Luxembourg	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Positive Impact Fund Total	Ordinary Shares	52%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Real Estate Debt Finance VI Designated Activity Company	Ordinary Shares	46%	Ireland	4th Floor, 76 Lower Baggot Street, Dublin 2, D02 Ek81
M&G UK Property Fund	Ordinary Shares	100%	Luxembourg	16, Boulevard Royal, L-2449, Luxembourg

Notes on the financial statements (continued)

M&G UK Residential Property Fund	Limited Partnership Interest	58%	Luxembourg	34-38, avenue de la Liberté, L-1931, Luxembourg
M&G UK Companies Financing Fund II LP	Limited partnership interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Old Kingsway, LP	Limited Partnership Interest	99%	USA	251 Little Falls Drive, Wilmington, DE 19808, USA
PPM America Private Equity Fund III LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund IV LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund V LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund VI LP	Limited Partnership Interest	40%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM Core Plus Fixed Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Credit Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Funds - PPM Floating Rate Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM High Yield Core Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Small Cap Value Fund	Ordinary Shares	95%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Strategic Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
Property Partners (Two Rivers) Limited	Ordinary Shares	50%	United Kingdom	Bow Bells House, 1 Bread Street, London, EC4H 9HH, UK
Prudential Credit Opportunities SCSp	Ordinary shares	100%	Luxembourg	1, rue Hildegard von Bingen, L - 1282, Luxembourg
Prudential Dynamic 10-40 Portfolio	Ordinary Shares	29%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 20 - 55 Portfolio	Ordinary Shares	34%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 40-80 Portfolio	Ordinary Shares	35%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 0-30 Portfolio	Ordinary Shares	25%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 60-100 Portfolio	Ordinary Shares	30%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic Focused 20 - 55 Portfolio	Ordinary Shares	38%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK

Notes on the financial statements (continued)

Prudential Equity Release Mortgages Limited	Ordinary Shares	100%	United Kingdom	Governors House, Laurence Pountney Hill, London, EC4R 0HH
Prudential Greenfield LP	Limited partnership interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential M&G UK Companies Financing Fund LP	Limited partnership interest	34%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Limited Partnership	Limited Partnership Interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Nominee 1 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Nominee 2 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate General Partner Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Loan Investments 1 S.à.r.l.	Ordinary Shares	100%	Luxembourg	1, Rue Hildegard von Bingen, L-1282 Luxembourg
Randolph Street LP	Limited Partnership Interest	100%	USA	2711 Centreville Road, Suite 400, Wilmington, DE 19808, USA
Sectordate Limited	Ordinary Shares	33%	United Kingdom	1st Floor Cavendish House 39 Waterloo Street Birmingham, B2 5PP
Selly Oak Shopping Park Limited Partnership	Limited Partnership Interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
SMLLC L.L.C.	Limited Partnership Interest	100%	USA	251 Little Falls Drive, Wilmington, DE 19808, USA
St Edward Homes Limited	Ordinary Shares	50%	United Kingdom	Berkeley House, 19 Portsmouth Road, Cobham, Surrey KT11 1JG, UK
Silverfleet Capital 2004 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2005 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2006 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2009 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2011-2012 GPLP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital II WPLF	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
The Car Auction Unit Trust	Ordinary shares	50%	Guernsey	Dorey Court, Admiral Park St Peter Port GY1 3BG, Guernsey
The Heights Management Company Limited	Limited by Guarantee	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
The St Edward Homes Partnership	Limited Partnership Interest	50%	United Kingdom	Berkeley House, 19 Portsmouth Road, Cobham, Surrey KT11 1JG

Notes on the financial statements (continued)

The Strand Property Unit Trust	Limited Partnership Interest	50%	Jersey	Liberte house, 19-23 La Motte Street, St Helier, Jersey, JE2 4SY
The Two Rivers Trust	Ordinary shares	50%	Jersey	Liberte house, 19-23 La Motte Street, St Helier, Jersey, JE2 4SY
Wynnefield Private Equity Partners II, LP	Limited Partnership Interest	99%	USA	1209 Orange Street, Wilmington, DE 19801, USA

In liquidation

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Fashion Square ECO LP (in liquidation)	Limited Partnership Interest	50%	USA	1209 Orange Street, Wilmington, DE 19801, USA

Financing

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
Prudential Vietnam Finance Company Limited	Ownership Interest	100%	Vietnam	23rd Floor, Saigon Trade Centre, 37 Ton Duc Thang Street, District 1, Ho Chi Minh City, Vietnam

31. Acquisition and disposal of material subsidiaries and participating interests

On 14 December 2018, the beneficial interest in the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were sold to Prudential Corporation Asia Limited, with the legal ownership transferring on 19 December 2018. The Hong Kong companies offer both participating and non-participating term, whole life endowment and unit-linked policies. These were previously included as investments in group undertakings in the Company's financial statements.

The transfer resulted in a decrease of £9,450m to investments in group undertakings. The difference between the fair value of the Hong Kong subsidiaries of £9,450m at the date of transfer and the consideration received of £33m represents a deemed distribution.

In 2017 Prudential Retirement Income Limited, a wholly owned subsidiary of the Company, was placed into liquidation. The original cost was £199m.

32. Post balance sheet events

M&GPrudential has been reviewing its operations across Europe since the UK voted to leave the European Union. In January 2019, in accordance with Part VII of the Financial Services and Markets Act 2000, the Company transferred all of its long term European business (excluding the UK) into PIA, a subsidiary of the Company which is based in the Republic of Ireland. The with-profits element of the business is reinsured back into the Company ensuring continuation of the economic substance of the previous situation. The shareholder-backed business has not been reinsured back to the Company following the Part VII transfer.