

Registered No: 15454

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

**Annual Report and Financial Statements for the Year Ended
31 December 2015**

**Final
Dated 24 March 2016**

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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THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Directors

Mr P Spencer - Chairman (appointed 1 January 2016)
Mr M Wells - Deputy Chairman (appointed 19 June 2015)
Mr N A Nicandrou
Mr H A Hussain
Mr M J Yardley
Mr T C Thiam (resigned 31 May 2015)
Ms W Au (resigned 31 August 2015)
Ms J Hunt (resigned 2 November 2015)
Mr C Adamson (appointed 8 June 2015)
Mr J Foley (appointed 19 January 2016)

Company Secretary

Ms S D Windridge (resigned 31 May 2015)
Ms J Fountain (appointed 1 June 2015 and resigned 22 January 2016)
Mr G R S Dunlop (appointed 22 January 2016)

Auditor

KPMG LLP, London

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015

Principal activity

The principal activity of the Company in the course of 2015 was transacting long-term insurance business in the United Kingdom. Throughout 2015 the Company also owned several insurance subsidiary undertakings and a branch in Poland that transacted insurance business in the United Kingdom and overseas. These activities will continue in 2016.

The Company itself 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

Market review and strategy

The Company's long-term products consist of life insurance, 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 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 – "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 with-profits sub-fund as bonus additions to their policies and shareholders receive 10 per cent as a statutory transfer.

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.

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, and this business is written in the Company's non-profit sub-fund. The concept of long-term fund as described above for the UK was abolished under the Solvency II regime, which came into effect on 1 January 2016. This was to avoid the long-term fund as a whole being considered a 'ringfenced fund' for Solvency II purposes. The PAC non-profits funds will still fall outside a ring-fenced structure under the new regime.

The UK is the world's fifth largest retail investment market. Wealth is concentrated in the 50+ age group with the younger generation of savers being typically less well-funded. In the Company's target over 50 demographic, the population growth rate is almost double the growth rate of the UK population as a whole and while the introduction of pension freedom reforms in April 2015 has fundamentally changed the way in which individuals can access their savings to help fund their income in retirement, the need to accumulate savings remains unchanged. These far reaching changes, when combined with the Company's unique brand product propositions and distribution capabilities, provide new and significant opportunities for the profitable and capital efficient growth of the business in the UK.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

When compared to 2012 the UK pensions industry today is almost unrecognisable. Three years of unprecedented regulatory change combined with consumer lifestyle changes has resulted in a structural marketplace shift in how customers view retirement. The distinction between customers accumulating funds during working lives and then using them to provide an income in retirement is no longer as clear-cut as it once was. Customers are engaging more frequently with their providers and the demand for financial advice and guidance is increasing. Those companies who are well-known, financially strong and create products and services to match the pension freedom needs and expectations of customers are likely to succeed.

The Company is well placed in this evolving marketplace due to our ability to offer differentiated products to meet customer needs. This is evident in its new business profile relative to a few years ago. Where once bonds and annuities were the dominant components of new business, post pension freedoms the Company is writing more bond, ISA, pension saving and income drawdown business, which has more than offset declining sales of individual annuities.

In addition, the implementation of Solvency II, effective from 1 January 2016, results in an increase in the capital resources requirement that is required to support the writing of longevity risk. As a result of this and based on the range of other opportunities in the long-term savings and retirement market, we expect the Company's participation in the annuity market to be reduced in the future.

For over 167 years the Company has been providing financial security to generations of UK customers through an unwavering focus on long-term value as evidenced by its longevity experience, multi-asset investment capabilities and financial strength. Such attributes are highly sought after today by customers adjusting to pension freedoms and by financial advisers who require a brand they can trust to help secure dependable incomes in retirement for their clients. The Company's inherent brand strengths, in combination with its range of market leading with-profits and retirement income products, continues to resonate strongly with customers and distributors. This is driving significant demand for the Company's differentiated and market leading retirement solutions.

The Company is a leader in its chosen markets, benefiting from a strong investment track record, a financially strong with-profits fund and a recognised reputation for developing innovative products.

Over the long-term the Company's with-profits fund has continued to perform strongly. Over a period spanning nearly twenty years the Company's asset share fund has outperformed the median investment return of its peer group by an average of just over 100 basis points per annum.

The Company's modern with-profits propositions, or PruFund platform, provides the ability to create products tailored for the customers of the pension freedoms world.

In the past year the Company has made two significant enhancements that have broadened access to its proposition: making PruFund available through an ISA wrapper and through a drawdown product.

The Company's competitive strength in these areas combined with its product suite continues to attract new customers seeking protection from the impact of volatile market conditions.

Importantly for customers, the Company's PruFund range provides smoothing in a volatile and uncertain investment environment. The strength of the proposition is reflected in the consistent growth we have experienced, both in terms of the number of customers invested and the assets under management. PruFund comprises a range of different funds, with or without explicit guarantees, and a range of 'risk rated' fund options. The Company meets a wide range of customer needs by providing access to PruFund through a variety of tax or product wrappers, namely - ISAs, bonds, pensions and drawdown.

In Corporate Pensions, the Company continues to focus on securing new members and incremental business from its current portfolio of customers and on additional voluntary contribution plans within the public sector, where it is the market leader providing schemes for 73 of the 101 public sector authorities in the UK.

In the wholesale market, the Company's aim is to continue to participate selectively in bulk and back-book buyouts using its financial strength, superior investment track record, extensive mortality risk assessment experience and servicing capabilities. The Company will continue to maintain a strict focus on value and only participate in capital-efficient transactions that meet its strict return on capital requirements.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

In Poland, the Company's life business continues to grow steadily. The business now has 18 branches across Poland and 597 financial planning consultants. Its success demonstrates our ability to build a new business franchise by transferring our existing product and distribution strengths to a new market.

Performance and measurement

The following table sets out the key performance indicators for the Company. These are considered to be the key metrics for the Company as these are the measures by which the Company's performance, development and position can be measured effectively.

Key Performance Indicators	2015	2014	Change
	£m	£m	%
Operating profit (note i)	453	650	(30)%
Non-operating profit items	1,554	4,142	(62)%
Profit on ordinary activities before tax	2,007	4,792	(58)%
Shareholders' funds	10,493	8,933	17 %
APE sales	918	866	6 %
Available capital on the Prudential Regulation Authority (PRA Solvency I) regulatory bases:			
With-profits, Scottish Amicable Insurance Fund, Defined Charge Participating Sub-fund	7,588	7,159	6 %
Non-profit sub-fund	490	194	153 %

Note (i) Operating profit is the underlying operating result based on longer term investment returns and excludes non-operating items such as the revaluation of, and dividends from, the Company's subsidiaries.

Operating Profit

The operating profit is comprised of profits from the long-term funds of £482m (2014: £668m) and losses of £29m (2014: £18m) from the shareholder funds.

The 2015 long-term business operating results are £482m, £186m lower than in 2014, with a profit of £486m from the UK business, £184m lower than in 2014, and a £4m loss, compared to a £2m loss in 2014, due to new business strain in the Polish branch. In the UK, profits attributable to the with-profits business are £14m higher than in 2014 due to an increase in the terminal bonus rates and an increase in claims. The operating profit attributable to the non-profit sub-fund business is £198m lower than in 2014. This is primarily due to lower profits from the quota share reinsurance with Prudential Retirement Income Limited (PRIL), caused mainly by the increase in quota share from 15% to 20% in 2014 not repeated in 2015 partially offset by an increase in profits caused in part by a change in mortality assumptions. Also in 2014 there was a one-off increase in other in-force profits following ongoing improvements to systems and processes which enabled the reclaim of a historic undercharge to the Scottish Amicable Insurance Fund (SAIF).

The operating loss arising from the shareholders' funds is £29m, an increase of £11m, compared to the loss of £18m in 2014. This was driven by a £7m increase in the loss on the partial equity hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, combined with increased project costs of £11m in 2015. This was partially offset by an increase in GI commission income of £3m.

Non-operating Profit

The main component of the non-operating items is the revaluation of shareholder subsidiaries of £1,316m (2014: £4,127m), the reduction of £2,811m being caused mainly by the revaluation of the Hong Kong subsidiaries to which the Hong Kong branch business transferred in 2014. The corresponding revaluation of Hong Kong in 2015 was £1,217m. This is offset by items giving rise to a positive swing being dividends received from subsidiaries of £278m (2014: Nil), £210m of which were a result of the PEAH restructure (see note 34). The remaining dividends were received from the Hong Kong subsidiaries (£58m) and PPL (£10m).

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

Profit on ordinary activities before tax

The results of the Company for the year as set out on pages 17 to 18 show a profit on ordinary activities before tax of £2,007m (2014: £4,792m), £2,785m lower than in 2014.

Shareholders' Funds

The shareholders' funds of the Company total £10,493m (2014: £8,933m). The increase of £1,560m, after taking account of dividends paid to Prudential plc of £361m is due to profit after tax of £1,921m.

APE Sales

Sales on an APE basis (Regular Premiums plus 1/10th Single Premiums) are £918m, 6 per cent higher than 2014 sales of £866m.

The Company's retail business achieved strong sales growth driven by a growing demand for its savings and retirement products and specifically the distinctive PruFund range, with momentum increasing through the year as additional products and services came online including PruFund ISA, Flexible Income Drawdown and our simplified non-advised drawdown Pension Choices Plan. The Company's capabilities in multi-asset investing, the strength of its brand and diversified distribution, provide a position of strength from which to meet evolving customer needs in a post pensions freedom retirement market.

Sales from other retail products, including individual pensions, income drawdown and offshore bonds, and PruFund ISA increased by 122 per cent. Demand for the Company's PruFund multi-asset funds among its target customer base remains strong as they continue to be attracted by both the performance track record and the benefits of a smoothed return to manage market volatility and reduce risk. The Company's successful launch in February 2015 of the PruFund range of investment funds within an ISA wrapper generated APE sales of £73m with assets under management totalling £674m at the end of December 2015. In total across all products, PruFund APE sales of £574m increased by 82 per cent, with total assets under management having increased 42 per cent since the start of the year to £16.5bn. Offshore bond sales were 21 per cent higher, reflecting the growing popularity of the Company's with-profits fund. Income drawdown sales grew by 191 per cent and individual pensions sales increased by 108 per cent, both driven by the strength of the with-profits PruFund offering, together with customers selecting more flexible retirement income solutions in anticipation of the pension reforms.

Corporate pensions sales were 3 per cent higher than 2014. The Company remains the largest provider of Additional Voluntary Contribution plans within the public sector, where the Company provides schemes for 73 of the 101 public sector authorities in the UK (2014: 72 of the 99 schemes).

Offsetting these favourable movements are lower sales of immediate annuities. Immediate annuity sales were 30 per cent lower resulting from the pension freedoms.

Available Capital

The Company's with-profits fund is supported by a large inherited estate, with the free assets of the with-profits fund valued at approximately £7.6bn at the year-end on a regulatory realistic basis. This provides the working capital required to support the fund and for other purposes as considered appropriate by the Directors. The strength of the with-profits fund offers strong policyholder protection and assists in generating positive returns for both policyholders and shareholders.

The with-profits sub-fund earned a return of 3.6 per cent before tax in 2015 on investments covering policyholder liabilities. 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 £22 billion to policy values in the last 10 years. Over the same period the fund has delivered a cumulative investment return of 80.8 per cent, compared with the FTSE-All Share (total return) index return of 71.8 per cent.

The available capital on a Solvency I basis in the Company's non-profit sub-fund as at 31 December 2015 is £490m (2014: £194m).

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

The concept of long-term fund as described above for the UK was abolished under the Solvency II regime, which came into effect on 1 January 2016. This was to avoid the long-term fund as a whole being considered a 'ringfenced fund' for Solvency II purposes.

From 1 January 2016 available capital will be measured on a Solvency II basis following the European Union's Solvency II Directive coming into effect. At 1 January 2016, the estimated Solvency II own funds of the shareholder business and the with-profits funds was £10.5bn and £7.6bn respectively, giving rise to an estimated Solvency II surplus of £3.3bn for the shareholder business and £3.2bn for the with-profits funds. The difference between the Solvency II surplus and the Solvency I available capital is the risk margin net of the transitional adjustment, and other items including differences in the definition of the risk-free rate and the matching adjustment impact for non-profit annuity liabilities within the with-profits funds.

The Company's available capital position is covered further in note 30 on page 71.

As at the date of signing the accounts, the Company's Financial Strength is rated Aa3 by Moody's (stable outlook), AA by Standard & Poor's (stable outlook) and AA by Fitch (stable outlook).

Risks & uncertainties

As a provider of insurance services, the Company's business is the managed acceptance of risk. The Company is a wholly owned subsidiary of the Prudential Group and is subject to the Group's internal control and risk management processes as detailed in the Group Governance Manual and Group Risk Framework. 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 and not absolute assurance against material misstatement or loss, and focus on optimizing the levels of risk and reward with the aim of achieving the business objectives.

The Group Risk Framework 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 long-term with-profits and non-profits business and from the underlying business within its investments in a number of subsidiary and associate companies, the value of which can be affected by certain risks factors. The key risk factors, mentioned below, should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

Financial risks

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, insurance risk and liquidity risk. Further 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 27 on page 49, note 29 (C) on page 64 and in note 29 (E) on page 67.

The local economic outlook for 2016 is relatively unchanged from the previous period, with modest growth expected over the year. The global outlook is mixed however, with increased uncertainty arising from a slowdown in China and increased volatility across emerging markets. This could adversely affect the Company's business and profitability. Interest rates within the UK and Eurozone remain close to historic lows, whilst the US raised interest rates in 2015 for the first time in nine years. Expectations regarding future interest rate paths are varied, and this reflects the increased uncertainty across the global markets generally.

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 expected future asset returns may impact the current and future levels of with-profits bonuses and is therefore likely to impact the Company's profitability.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

(a) Market risk

Market risk is the risk of loss or adverse change in the financial condition of the Company, resulting directly or indirectly, from fluctuations in the level and/or volatility of market prices of assets and liabilities and changes in interest rates and exchange rates.

Market risk is one of the largest risks for the Company. The key areas of the business impacted by market risk are the non-profit annuity business, the present value of expected future shareholder transfers from the with-profits business, the lifetime mortgage book and currency risk on the value of the business in the Hong Kong subsidiary. The continued uncertainty in international economic and investment climates, combined with a low growth, low return environment, have increased market risk and this could adversely affect the Company's business and profitability, principally through the following:

- Investment impairments or reduced investment returns, as a result of market volatility, could result in direct losses and may also impair the Company's ability to write desired volumes of new business, which would, in turn, have a negative impact on the Company's assets under management and profitability.
- The asset and liability mismatch risk and the risk of insolvency has increased due to historically low interest rates. The Company manages this risk by appropriate matching of its assets and liabilities.

(b) Credit risk

Credit risk is the risk of loss to the Company resulting from fluctuations in the credit standing of issuers of securities, counterparties and debtors in the form of defaults, downgrades or widening of credit spreads.

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. Corporate borrowers continue to experience a challenging business environment and volatile profits and cashflows. This principally impacts credit risk through the following:

- Increased risk of credit losses through defaults and widening of credit spreads on corporate bonds. This is a material risk for the Company, and is managed by careful management of the corporate bond portfolio and having appropriate concentration and credit rating limits in place.
- 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. The Company manages cash counterparty risk by using secured cash placements (such as reverse repos) and having counterparty concentration limits in place for unsecured cash deposits. Reinsurance counterparty risk is managed by diversifying its reinsurance exposures across a number of counterparties, and by having minimum counterparty credit rating limits and maximum concentration limits in place. Derivative counterparty risk is largely mitigated by careful counterparty selection and adequate collateralisation arrangements.

(c) Insurance risk

Insurance risk is the risk of loss or of adverse change in the value of insurance liabilities of the Company, resulting from changes in the level, trend or volatility of a number of insurance risk drivers. These include adverse longevity, mortality, morbidity, persistency and expense experience.

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 annuity pricing and reserving policy, the Company assumes that current rates of mortality continue to improve over time at levels based on the Company's calibration of the Continuous Mortality Investigations (CMI) 2014 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 other life-threatening diseases) that would require the Company to strengthen its longevity assumptions would have an impact on the Company's results.

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

The other insurance risks run by the Company are expense risk, persistency risk and mortality/morbidity risk. These risks are less material than the market, credit and longevity risks.

- Expense risk is the risk of actual expenses exceeding the assumptions in pricing and reserving bases and is relevant to all lines of business. The Company makes assumptions about future expected levels of expenses for each line of business and uses these in pricing and calculating reserves. If the actual expenses exceed these assumptions, the Company's operating results could be adversely impacted. The nature of the contractual arrangement with the Company's principal outsourcer partially mitigates this risk.
- Persistency risk is the risk of actual persistency or customer retention levels being different to the Company's expectations. 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 including any 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. This risk is only relevant to the non-annuity lines of business written by the Company.
- 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.

In common with other industry participants, the profitability of the Company's businesses ultimately depends on a mix of factors including investment performance and asset impairments, mortality and morbidity trends, policy surrender rates, unit cost of administration and new business acquisition expense.

(d) Liquidity risk

Liquidity risk is the risk that the Company, although solvent on a balance sheet basis, does not have sufficient cash resources available to meet its obligations as they fall due, or can secure them only at excessive cost.

Liquidity risk is not a material risk for the Company. This risk is managed through careful management of bank balances, cash-flow 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. As a result all of the Company's insurance funds have substantial volumes of readily realisable assets.

Non-financial risk

The Company is exposed to business environment, strategic, 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.

The Company conducts its business subject to regulation and the associated regulatory risks, and is therefore exposed to changes in laws, and regulations that affect the products and markets in which it operates.

Changes in government policy, legislation (including tax), regulation or regulatory interpretation applying to UK insurance companies may be applied retrospectively, may adversely affect the Company's product range, distribution channels, capital requirements and, consequently, reported results and financing requirements. Regulators in jurisdictions in which the Company operates may change the level of solvency capital required to

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

be held or could introduce possible changes in the regulatory framework for long-term savings and retirement arrangements and investments, or the regulation of selling practices and solvency requirements. In addition, there could be changes to the maximum level of non-domestic ownership by foreign companies in certain jurisdictions. Furthermore, as a result of interventions by governments in response to recent financial and global economic conditions, it is widely expected that there will continue to be a substantial increase in government regulation and supervision of the financial services industry, including the possibility of higher capital requirements, restrictions on certain types of transactions and enhanced supervisory powers.

The material regulatory and legislative change risks currently faced are:

- The European Union's Solvency II Directive came into effect on 1 January 2016. This measure of regulatory capital is more volatile than under the previous Solvency I regime and regulatory policy may evolve under the new regime. The European Commission will review elements of the Solvency II legislation from 2016 onwards including a review of the Long Term Guarantee measures by 1 January 2021.
- The UK Government has committed to holding a "remain/leave" referendum on EU membership which will be held on 23 June 2016. The possible withdrawal of the UK from the EU would have political, legal and economic ramifications for both the UK and the EU, although these are expected to be more pronounced in the UK.
- The International Association of Insurance Supervisors (IAIS) is developing ComFrame which is focused on the supervision of large and complex Internationally Active Insurance Groups (IAIGs). ComFrame will establish a set of common principles and standards designed to assist regulators in addressing risks that arise from insurance groups with operations in multiple jurisdictions. As part of this, work is underway to develop a global Insurance Capital Standard (ICS) that would apply to IAIGs. Once the development of the ICS has been concluded, it is intended to replace the Basic Capital Requirement as the minimum group capital requirement for G-SIIs. Further consultations on the ICS are expected over the coming years, and a version of the ICS is expected to be adopted as part of ComFrame in late 2019.
- The Company is subject to regulation by both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) which gives rise to increased thematic review activity, and additional regulatory demands and the implications from the FCA's competition objective. On 3 March 2016, the FCA published a report setting out its findings from a thematic review covering eleven firms, including the Company. The FCA has issued a statement clarifying that in order to address the findings identified by the thematic review, it will consult on guidance which will provide firms with extra detail on the actions they should be taking in order to treat their closed-book customers fairly in the future. In addition, the FCA will convene an industry-wide discussion with the aim that the industry reaches a voluntary solution to capping or removing exit and/or paid-up charges on relevant products. In addition, the FCA announced in its statement that further work is required to consider whether six of the eleven firms (including the Company) have failed to meet the FCA's standards in relation to disclosure to customers of exit and paid-up charges and, if so, whether remedial and/or disciplinary action is necessary or appropriate in relation to these firms or others across the market. These investigations have commenced and will enable the FCA to establish the reasons for the practices within firms; whether customers have suffered detriment as a result and how widespread any practices are within the six firms. The FCA has stated that no conclusion has been reached as to whether there have been any breaches of regulatory requirements.
- Following the Pension Freedom changes in April 2015, the retirement market in the UK is experiencing a material change that has impacted the Company's chosen markets and product offerings. Further pension reforms have been consulted and may happen in the future.
- Given the outsourced nature of the Company's operating model, there is exposure to changes in the environment that affect the economics of these arrangements. Examples of this would include potential changes to VAT on the outsourcing arrangements and medium term degradation of cost benefits arising from wage and cost inflation.
- In April 2016, under the Scotland Act 2012 the Scottish Parliament will be able to set their own rates of income tax which could impact the Company given it has a significant number of employees and policyholders that would be impacted by any such changes.

The market for UK financial services is highly competitive with several factors affecting the Company's ability to sell its products and its continued profitability, including price and yields offered, financial strength and ratings,

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

range of product lines and product quality, brand strength and name recognition, investment management performance, historic bonus levels, developing demographic trends and customers' appetite for certain savings products.

Changes in methodologies and criteria used by rating agencies could result in downgrades that do not reflect changes in the general economic conditions or the Company's financial condition but could significantly impact its competitive position and hurt its relationships with creditors or trading counterparties.

The Company's principal competitors in the life insurance market include many of the major retail financial services companies including, in particular, Aviva, Legal & General, Lloyds Banking Group and Standard Life. The Company believes competition will intensify in response to consumer demand, technological advances, the impact of consolidation, regulatory actions and other factors. The Company's ability to generate an appropriate return depends significantly upon its capacity to anticipate and respond appropriately to these competitive pressures.

The uncertain economic environment may reduce consumer confidence and their propensity to buy savings products and also adversely impact investment returns, and/or interest rates.

(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 Group's capabilities.

The strategic focus on with-profits and long-term savings and retirement products means the Company is dependent on being able to continue to deliver profitable volumes from these lines of business and that unplanned regulatory or legal changes do not adversely impact customer or advisor behaviour. The concentration leaves the Company's UK business at risk to a significant change in its business model arising from future regulatory developments.

The Company operates a largely outsourced operating model, with heavy dependence on both internal and external organisations. Outsourced activities include investment management, a significant part of the Company's customer-facing functions as well as some IT functions. This places strategic reliance on the performance of these organisations and as such their performance is monitored carefully.

(c) Conduct risk

Conduct risk is the risk of loss arising from the approach taken by firms in their relationship with customers.

The Company puts customer needs at the heart of its business in providing financial products and services to its customers. In so doing, the Company aims to uphold a reputation built over 160 years, for acting responsibly and with integrity in supporting customers whilst respecting the laws and regulations, traditions and cultures within which it operates, as well as meeting internationally accepted standards of responsible business conduct.

Exposure to conduct risk will arise from the impact on consumers from the way the Company manages itself, the products and services provided; the response and management of the financial risks to which customers are exposed, through to the performance of the products they buy from the Company and through intermediaries.

(d) Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events.

The Company is exposed to operational risk in the ordinary course of its business and as a result may be subject to unplanned costs, regulatory fines or legal actions and disputes in relation to contracts or a course of conduct taken. These legal actions and disputes may relate specifically to the Company's businesses and operations or may be issues that are common to companies that operate in the Company's markets. Although the Company believes it has adequately provisioned for the potential costs of litigation and regulatory matters, no assurance can be provided that such reserves are sufficient. Given the large or indeterminate amounts of damages sometimes sought, and the inherent unpredictability of litigation and disputes, it is possible that an adverse outcome could, from time to time, have an adverse effect on results and cash flows.

The Company's activities involve processing a large number of complex transactions across numerous and diverse long term insurance products, that are undertaken both internally and through third parties administrators. As a

STRATEGIC REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

result it is exposed to the risks of data integrity and transaction processing errors, including exposure to computer viruses, attempts at unauthorised access and cyber-security attacks. Further, because of the long-term nature of much of the Company's business, accurate records have to be maintained securely for significant periods. The Company is therefore exposed to data security risk potentially resulting in regulatory breaches, complaints and brand damage.

The Company's systems and processes incorporate controls which are designed to manage and mitigate the operational risks associated with its activities as any weakness in the administration and finance systems and pricing and reserving processes could impact operations or the financial results.

As with any large organisation, the Company is affected by the risk of operational failures due to inadequate practices for the recruitment, development, management or retention of employees and contractors.

(e) 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; 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.

On behalf of the Board of directors.



G R S Dunlop
Company Secretary
24 March 2016

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2015

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

Introduction

None of the information required to be included in the Directors' Report under Schedule 7 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended by The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013) has been set out in the Company's Strategic Report.

Subsidiary and associate undertakings and branches

Particulars of the Company's subsidiary undertakings at 31 December 2015 are shown on page 77 in note 32. At 31 December 2015 the Company had a branch outside the United Kingdom in Poland.

With-profits governance

The Company produces an annual report, which is available on request, 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 an Actuarial Function Holder (Chief Actuary as at 1 January 2016) who will provide the Board with all other actuarial advice. Both of these are Financial Conduct Authority and Prudential Regulation Authority approved roles.

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
- 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 ASSURANCE COMPANY LIMITED

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

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

On 1 January 2016, the Company's subsidiary, Prudential Retirement Income Limited increased the proportion of business reassured under the quota share arrangement with the Company from 20% to 100%. An initial additional reinsurance premium of £23,228m has been deposited back from PRIL to PAC in respect of this increase.

On 1 January 2016 the portfolio of Equity Release Mortgage (ERM) assets held by the Company's shareholder fund was restructured. As part of the restructure the ERM assets were transferred to the Company's subsidiary, Prudential Retirement Income Limited, as part of the settlement of the intra-group loan between the two entities. A loan asset to Prudential plc was also transferred to Prudential Retirement Income Limited as part of the settlement. The full financial impact of this restructure cannot be estimated.

Accounts

The state of affairs of the Company at 31 December 2015 is shown in the balance sheet on pages 21 and 22. The profit and loss account appears on pages 17 and 18.

Share Capital

There have been no changes in the Company's share capital during 2015 as shown on page 46 in note 21.

Dividends

An interim dividend of £361.0m (2014: £409.8m) was declared on 7 December 2015, of which a dividend of £159.4m (2014: £263.5m) on the ordinary shares was paid on 18 December 2015 and the remaining £201.6m (2014: £146.3m) was satisfied by a reduction in the balance outstanding on the loan from the Company to Prudential plc, resulting in the release of £361.0m from the retained profit and reserves of the Company. The directors have not declared a final dividend on the ordinary shares for 2015 (2014: £Nil).

No dividend was paid on the A preference shares in 2015 (2014: £Nil). No dividend was paid on any other preference shares.

Directors

The present directors are shown on page 1. Mr Thiam resigned on 31 May 2015, Ms W Au resigned on 31 August 2015 and Ms J Hunt resigned on 2 November 2015. Mr Adamson was appointed on 8 June 2015, Mr Wells appointed 19 June 2015 and Mr J Foley was appointed on 19 January 2016. A new Independent Chairman, Paul Spencer was also appointed, as at 1 January 2016. There have been no further changes.

Disclosure to 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.

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 29 (E) on page 67. Further information on the use of derivatives by the Company is provided in note 29 (G) on page 70.

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2015 (continued)

Auditor

The directors re-appointed KPMG LLP as auditor of the Company on 19 May 2015. An ordinary resolution of the Company for the re-appointment of KPMG LLP as auditor of the Company will be proposed to the members of the Company in accordance with Section 485(4) 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 as such. 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 2015 and remain in force.

On behalf of the Board of directors.

A handwritten signature in black ink, appearing to read 'G R S Dunlop', with a large initial 'D' and a flourish.

G R S Dunlop
Secretary
24 March 2016

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 FRS102 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 the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and 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; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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 the financial statements comply with the Companies Act 2006. They 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.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE PRUDENTIAL ASSURANCE COMPANY LIMITED

We have audited the financial statements of The Prudential Assurance Company Limited for the year ended 31 December 2015 set out on pages 17 to 81. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

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

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 15, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2015 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared are consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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



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

24 March 2016

Profit and Loss Account for the year ended 31 December 2015

Note	Long-term Business Technical Account	2015	2014
		£m	£m
2	Gross premiums written	7,581	7,209
	Outward reinsurance premiums	(320)	(1,877)
	Earned premiums, net of reinsurance	7,261	5,332
3	Investment income	6,109	7,307
	Unrealised (losses) gains on investments	(2,738)	3,775
	Claims paid		
	Gross amount	(9,366)	(8,822)
	Reinsurers' share	694	665
	Claims paid, net of reinsurance	(8,672)	(8,157)
	Change in provision for claims		
	Gross amount	(81)	61
	Reinsurers' share	—	—
	Claims incurred, net of reinsurance	(8,753)	(8,096)
	Change in long-term business provision		
	Gross amount	146	(8,589)
	Reinsurers' share	(520)	2,388
		(374)	(6,201)
	Change in technical provision for linked liabilities	276	(76)
	Change in other technical provisions, net of reinsurance	(98)	(6,277)
5	Net operating expenses	(690)	(658)
6	Investment expenses and charges	(331)	(304)
33	Other technical charges	—	(1,701)
7	Tax attributable to the long-term business	(149)	(540)
9	Actuarial and other gains (losses) on pension schemes	29	(12)
	Transfer (to) from the fund for future appropriations	(263)	1,655
	Balance on the long-term business technical account	377	481

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Profit and Loss Account for the year ended 31 December 2015 (continued)

Note	<u>Non-Technical Account</u>	<u>2015</u> £m	<u>2014</u> £m
2	Balance on the general business technical account	—	—
	Balance on the long-term business technical account	377	481
7	Tax credit attributable to the balance on the long-term business technical account	90	130
	Balance on the long-term business technical account before tax	<u>467</u>	<u>611</u>
3	Investment income	178	(8)
	Unrealised gains on investments	1,356	4,131
	Other income	28	24
	Other charges	(22)	(27)
	Total profit on other activities	<u>1,540</u>	<u>4,120</u>
34	Profit on disposal of joint venture	—	61
	Profit on ordinary activities before tax	<u>2,007</u>	<u>4,792</u>
7	Tax on profit on ordinary activities	(86)	(135)
	Profit for the financial year	<u>1,921</u>	<u>4,657</u>

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 2015

Note

	<u>2015</u>	<u>2014</u>
	£m	£m
Profit for the financial year	1,921	4,657
Other comprehensive income:		
33 Transfer of accumulated equity in the Hong Kong branch	—	(268)
Revaluation of company-occupied property	21	19
Transfer to the fund for future appropriations	(21)	(19)
Total other comprehensive income /(expense) for the financial year, net of income tax	—	(268)
Total comprehensive income for the financial year	<u>1,921</u>	<u>4,389</u>

Statement of changes in equity for the year ended 31 December 2015

	Share Capital	Revaluation reserve	Other reserves (*)	Profit and loss account	Total
	£m	£m	£m	£m	£m
Balance at 1 January 2014	330	—	536	4,088	4,954
Profit for the financial year	—	—	—	4,657	4,657
Other comprehensive income for the financial year	—	—	—	(268)	(268)
Total comprehensive income for the financial year	—	—	—	4,389	4,389
Dividends	—	—	—	(410)	(410)
Total distribution to owners, recognised directly in equity	—	—	—	(410)	(410)
Balance as at 31 December 2014	330	—	536	8,067	8,933
Balance as at 1 January 2015	330	—	536	8,067	8,933
Profit for the financial year	—	—	—	1,921	1,921
Other comprehensive income for the financial year	—	—	—	—	—
Total comprehensive income for the financial year	—	—	—	1,921	1,921
Dividends	—	—	—	(361)	(361)
Total distribution to owners, recognised directly in equity	—	—	—	(361)	(361)
Balance as at 31 December 2015	330	—	536	9,627	10,493

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

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Balance sheet as at 31 December 2015

Note	<u>Assets</u>	<u>2015</u> £m	<u>2014</u> £m
12	Intangible assets		
	Licence	31	47
	Computer software	3	4
		<u>34</u>	<u>51</u>
	Investments		
13	Land and buildings	8,085	7,753
14	Investments in group undertakings and participating interests	11,485	10,676
15	Other financial investments	95,062	93,258
	Deposits with ceding undertakings	4,584	4,755
		<u>119,216</u>	<u>116,442</u>
16	Assets held to cover linked liabilities	11,861	12,254
17	Reinsurers' share of technical provisions		
	Long-term business provision	9,832	10,323
	Claims outstanding	145	143
	Technical provisions for linked liabilities	4,954	4,999
		<u>14,931</u>	<u>15,465</u>
	Debtors		
	Debtors arising out of direct insurance operations		
	Policyholders	44	37
	Intermediaries	1	1
	Debtors arising out of reinsurance operations	5	56
18	Other debtors	1,127	1,195
		<u>1,177</u>	<u>1,289</u>
	Other assets		
19	Cash at bank and in hand	1,462	1,075
13	Finance lease assets	33	—
		<u>1,495</u>	<u>1,075</u>
	Prepayments and accrued income		
	Accrued interest and rent	645	669
	Deferred acquisition costs (DAC)		
	Long-term business	59	70
	Accrued external dividends receivable	40	38
	Other prepayments and accrued income	178	202
		<u>922</u>	<u>979</u>
	Total assets (excluding pension asset)	<u>149,636</u>	<u>147,555</u>
9	Pension asset	85	19
20	Total assets (including pension asset)	<u>149,721</u>	<u>147,574</u>

Balance sheet as at 31 December 2015 (continued)

Note	<u>Liabilities</u>	<u>2015</u> £m	<u>2014</u> £m
	Capital and reserves		
21	Share capital	330	330
	Other reserves	536	536
22	Profit and loss account	9,627	8,067
2	Shareholders' funds – equity interests	<u>10,493</u>	<u>8,933</u>
	Fund for future appropriations	10,759	10,476
	Technical provisions		
27	Long-term business provision	103,122	103,283
8	Claims outstanding	583	506
	Unearned revenue provision	22	27
	Total technical provisions	<u>103,727</u>	<u>103,816</u>
	Technical provisions for linked liabilities	16,815	17,253
	Provisions for other risks and charges		
7	Deferred taxation	658	719
13	Obligations under finance leases	66	63
	Other	70	49
		<u>794</u>	<u>831</u>
	Deposits received from reinsurers	1,133	1,360
	Creditors		
	Creditors arising out of direct insurance operations	147	76
	Creditors arising out of reinsurance operations	78	75
	Other borrowings not owed to credit institutions	175	70
23	Other creditors including taxation and social security	5,503	4,567
24	Preference shares	1	1
		<u>5,904</u>	<u>4,789</u>
	Accruals and deferred income	96	116
	Total liabilities	<u>149,721</u>	<u>147,574</u>

The accounts on pages 17 to 81 were approved by the Board of directors on 24 March 2016.



H A Hussain
Director
24 March 2016

Notes on the financial statements (continued)

1 Accounting Policies

A. Company Information

The Prudential Assurance Company Limited (the Company) is a private limited company and is 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 25. In these financial statements, the Company is considered to be a qualifying entity and has applied the exemptions available under FRS 102 in respect of the following disclosures:

- Reconciliation of the number of shares outstanding from the beginning to end of the period;
- Cash Flow 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 under FRS 102 available in respect of certain disclosures required by FRS 102.26 *Share Based Payments* (FRS 102.26).

The financial statements are prepared in 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 Company has adopted FRS 102 and FRS 103 in these financial statements. Details of the transition are disclosed in note 31.

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 table below sets 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 estimates and assumptions	Accounting policy/note reference
Classification of insurance and investment contracts	D
Measurement of long-term business provision	D and 27
Determination of fair value of financial investments	G and 29
Measurement of pension scheme	K and 9

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.

The Company is a subsidiary within the Prudential Group and it and its parent company, which is also the 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

Notes on the financial statements (continued)

1 Accounting Policies (continued)

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 is supported by its inherited estate (note 28 on page 55), generates positive cashflows and has very low debt-financing. In addition 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 11, the management of financial risk as set out in note 29, including its exposure to credit risk and liquidity risk which it carefully manages through cash-flow 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, which became effective on 1 January 2016, and considers the Company to have a healthy solvency margin.

C. Change in Accounting Policies

The Company has early adopted "Amendments to FRS 102 - Fair value hierarchy disclosures (March 2016)" in these financial statements. Except for the transition to FRS 102 and FRS 103, there have been no other changes to accounting policies during the financial year.

D. Long-term Business

i. *Classification of insurance and investment contracts*

The measurement basis of liabilities of long-term business contracts 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 discretionary participation features are primarily with-profits and other protection type or annuity policies. The investment contract without discretionary participation features classification applies primarily to certain unit-linked and similar contracts written by the Company. Insurance contracts and investment contracts with discretionary participation features are accounted for under FRS 103. Investment contracts without discretionary participation features are accounted for as financial liabilities under FRS 102.11 *Basic Financial Instruments* (FRS 102.11) and, where relevant the provisions of the FRS 102.23 *Revenue* (FRS 102.23) in respect of the attaching investment management features of the contracts.

The provisions for investment contracts without discretionary participation features 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. 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 discretionary participation features reflects the deposit nature of the arrangement with premiums and claims reflected as deposits and withdrawals taken directly to the balance 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 certain costs associated with policy issue and underwriting, which are not matched by policy charges are capitalised and amortised against

Notes on the financial statements (continued)

1 Accounting Policies (continued)

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 102.11, for the investment contracts without discretionary participation features, only the incremental, directly attributable acquisition costs relating to the securing of 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.

Following the implementation of the Retail Distribution Review (RDR), policies sold on or after 1 January 2013 are no longer be eligible for deferred acquisition costs to be written against them. Therefore, the deferred acquisition costs will begin to run off as the in-force business starts to be weighted more towards post-RDR policies.

Deferred acquisition costs, deferred income reserves and provisions for future expenses commonly called "sterling reserves" are not permitted to be recognised under FRS 102 for investment contracts.

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.

Profits comprise actuarial surpluses allocated to shareholders adjusted, other than for with-profits business, for the deferral of acquisition costs and movements in the shareholders' interest in reserves held within long-term funds. For with-profits business, unappropriated surplus is carried forward in the fund for future appropriations and no allocation is made to the shareholders. There is no deferral of acquisition costs for with-profits business.

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.

iii. *Measurement of long-term business provisions*

The assumptions used to calculate the long-term business provisions are described in note 27.

The Company applies FRS 103, which impacts the basis of reporting for the with-profits business provisions. FRS 103 is underpinned by the PRA's Peak 2 realistic basis of reporting.

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

The PRA 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, less 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 actually 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 including conventional with-profits whole life, industrial branch and many pension contracts (which have capped charges) 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 or previously from the Company's subsidiary, Prudential Annuities Limited (PAL), prior to the Part VII Transfer. For the Scottish Amicable Insurance Fund (SAIF), the PRA realistic liability calculation requires

Notes on the financial statements (continued)

1 Accounting Policies (continued)

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.

The PRA realistic value of liabilities is adjusted in accordance with FRS 103 to remove the present value of shareholder transfers and related tax. Shareholder transfers are recognised as a liability for the purposes of PRA regulatory returns but, for accounting purposes under FRS 103, shareholders' transfers are recognised only on declaration, consistent with the current basis of financial reporting.

Under PRA reporting, the assets include the present value of non-profit business written within the with-profit funds. For financial reporting purposes these items are not recognised. Similarly, that part of these future profits which is included in the PRA FPRL is excluded for financial reporting purposes.

E. General Business

The Company no longer underwrites general business directly and its run-off obligations have been reinsured.

Claims incurred comprise the settlement and handling costs of paid and outstanding 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.

F. 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 premiums due to or payments due from reinsurers and the share of benefits and claims recoverable from reinsurers. The measurement of reinsurance assets is consistent with the measurement of the underlying direct insurance contracts.

G. 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 investment 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.

Based on the fact that the Company previously applied FRS 26 *Financial Instruments: Recognition and Measurement*, 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 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 which are deemed to be held for trading. 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

Notes on the financial statements (continued)

1 Accounting Policies (continued)

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 cash flow technique. Further information on valuation techniques is provided in note 29 (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 and loans to policyholders and other unsecured loans and receivables. These investments are carried at amortised cost using the effective interest method and subject to impairment reviews where appropriate. The Company measures the amount of the impairment loss by comparing the amortised cost with the present value of its estimated future cash flows discounted at the original effective interest rate. 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.

Basic financial assets, including deposits with ceding undertakings, debtors arising out of direct insurance operations/reinsurance operations, other debtors and cash at bank and in hand 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 and 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.

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, paragraph 76 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, there is a requirement to show the net book value on a historical cost basis of properties 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 leases inception at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Company-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. No depreciation is provided on company-occupied property as such depreciation would be immaterial.

H. Financial Liabilities

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.

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 discretionary participation features 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 policies for investment contracts without discretionary participation features are described in section D above.

Notes on the financial statements (continued)

1 Accounting Policies (continued)

- (ii) Financial liabilities that are not valued at fair value through profit and loss and are not investment contracts with discretionary participation features are mainly creditors shown at settlement value.
- (iii) Investment contracts with discretionary participation features. The accounting policy is covered in section D above.

I. 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, and 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.

J. Foreign Currency

Foreign currency revenue transactions are translated at average exchange rates for the year. Monetary foreign currency assets and liabilities are translated at year end exchange rates. Exchange differences are included in the profit and loss account.

K. 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' surpluses or deficits 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 cash flows 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 84% of the underlying scheme liabilities of the Prudential Group's defined benefit schemes. 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 net 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 long-term technical account. Actuarial gains and losses also include adjustment for unrecognised pension surplus.

Notes on the financial statements (continued)

1 Accounting Policies (continued)

L. Intangible Assets

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

Intangible assets include a licence, which represents the value of an agreement with a fellow subsidiary company for the use of certain Scottish Amicable assets, which is being amortised over a period of 20 years to 30 September 2017, on a basis consistent with the revenue stream from the agreement.

Intangible assets also include computer software amortised over three years.

M. 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 in respect of the prior reporting period are treated as a non-adjusting event.

N. Share-based Payments

The Company offers share award and option plans for certain key employees and a 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.

O. Cash at bank and in hand

The Company applies the definitions of cash and cash equivalents as defined in FRS 102.7 *Statement of Cash Flows* (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.

P. 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.

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	
	<u>2015</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>
	£m	£m	£m	£m
United Kingdom	6,866	6,634	471	613
Poland	5	3	(4)	(2)
France	710	572	—	—
	<u>7,581</u>	<u>7,209</u>	<u>467</u>	<u>611</u>

New business

	Regular premiums		Single premiums	
	<u>2015</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>
	£m	£m	£m	£m
United Kingdom	220	211	6,264	5,982
Poland	3	2	—	—
France	—	—	688	546
	<u>223</u>	<u>213</u>	<u>6,952</u>	<u>6,528</u>

Analysis of premium income

	<u>2015</u>	<u>2014</u>
	£m	£m
Gross written premiums:-		
Direct	6,571	4,834
Reinsurance accepted	1,010	2,375
	<u>7,581</u>	<u>7,209</u>
Analysis of gross direct premiums:-		
Individual business	6,006	4,340
Group contracts	565	494
	<u>6,571</u>	<u>4,834</u>
Regular premiums	892	917
Single premiums	5,679	3,917
	<u>6,571</u>	<u>4,834</u>
Participating contracts	3,997	3,514
Non-participating contracts	261	340
Linked long-term contracts (excluding investment contracts without discretionary participation features)	2,313	980
	<u>6,571</u>	<u>4,834</u>
United Kingdom	6,566	4,831
Poland	5	3
France	—	—
	<u>6,571</u>	<u>4,834</u>

Notes on the financial statements (continued)

Net reinsurance income

Net reinsurance income in respect of long-term business for the year ended 31 December 2015 was an expense of £192m (2014: £1,184m income).

(b) General business

<u>Analysis of technical account</u>	Gross Premiums Written		Gross Premiums Earned		Gross Claims Incurred		Gross Operating Expenses		Reinsurance Balance	
	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Other (*)	—	—	—	—	6	11	—	—	(6)	(11)
	—	—	—	—	6	11	—	—	(6)	(11)

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

Following the transfer of the Hong Kong branch this business is no longer reported in the general business technical account of the Company (see note 33). The remaining general business is operations in run-off comprising UK personal and commercial lines of general insurance business. All the business is fully reinsured and as such there is no profit or loss arising. The business reinsured is mostly UK employers' liability and public liability business.

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

(c) Shareholders' funds

Shareholders' funds relate to the following countries:

	Shareholders' Funds	
	2015	2014
	£m	£m
United Kingdom	10,491	8,932
Poland	2	1
Total	10,493	8,933

Notes on the financial statements (continued)

3. Investment income

	Long-term business		Non-technical account	
	2015 £m	2014 £m	2015 £m	2014 £m
Income from:				
Group undertakings	79	1,300	234	(45)
Other investments				
Land and buildings	423	420	—	—
Listed investments	2,884	2,801	—	—
Unlisted investments	233	207	—	—
Other investments	395	322	27	108
	<u>4,014</u>	<u>5,050</u>	<u>261</u>	<u>63</u>
Losses on loans and receivables	(23)	(48)	—	—
Gains on the realisation of investments at fair value through profit and loss other than derivatives	1,732	1,537	—	—
Gains (losses) on the realisation of derivatives – see note 29	170	622	(36)	(34)
Impairment in the value of subsidiaries	—	—	(48)	(38)
Exchange gains	168	100	1	1
Fees for policy administration and asset management services arising from unit-linked investment contracts	48	46	—	—
	<u>6,109</u>	<u>7,307</u>	<u>178</u>	<u>(8)</u>

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 £2,352m (2014: £2,222m) analysed between the with-profits sub-fund and defined charge participating sub-fund of £1,994m (2014: £1,860m) and the Scottish Amicable Insurance Fund of £358m (2014: £362m).

5. Net operating expenses

	Long-term business	
	2015 £m	2014 £m
Acquisition costs	332	287
Change in deferred acquisition costs	11	12
Administrative expenses	330	347
Amortisation of licence and distribution rights (note 12)	17	12
	<u>690</u>	<u>658</u>

Acquisition costs include commissions in respect of long-term direct insurance business of £98m (2014: £88m). Administrative expenses include commissions in respect of long-term direct insurance business of £43m (2014: £39m). Administrative expenses are principally recharged from Prudential Distribution Limited, a service company within the Prudential Group.

Notes on the financial statements (continued)

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

6. Investment expenses and charges

	Long-term business		Non-technical account	
	<u>2015</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>
	£m	£m	£m	£m
Investment management expenses	300	277	—	—
Interest on bank borrowings	31	27	—	—
	<u>331</u>	<u>304</u>	<u>—</u>	<u>—</u>

7. Tax

The reduction in the UK corporation tax rate to 20% from 1 April 2015 has been reflected in the financial statements for the year ended 31 December 2015. In July 2015, the UK Government announced additional reductions in the main rate of corporation tax to 19% from 1 April 2017 and to 18% from 1 April 2020 which are also reflected in the financial statements as the changes were substantively enacted at the balance sheet date. The effect of this change on the deferred tax liabilities at 31 December 2015 is a reduction of £9m. The Chancellor has proposed a further reduction to the UK corporation tax rate to 17% from 1 April 2020, however this is not reflected in the financial statements for the year ended 31 December 2015 as it has not yet been substantively enacted.

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 has been recognised for the adjustment that arises on transition to the new regime. This adjustment is required to be spread and taxed over a 10 year period.

Notes on the financial statements (continued)

a) Tax charged (credited)

	Long-term funds		Shareholders' Profits	
	<u>2015</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>
	£m	£m	£m	£m
Current Tax				
UK corporation tax	152	485	4	(2)
Double tax relief	(3)	(7)	—	—
Overseas tax	38	28	—	—
Adjustments in respect of prior year	17	15	(2)	(5)
Total current tax	<u>204</u>	<u>521</u>	<u>2</u>	<u>(7)</u>
Deferred tax				
Origination and reversal of timing differences	(61)	31	—	—
Effect of changes in tax rate on closing balances	—	—	—	—
Adjustments in respect of prior year	—	—	—	—
Total deferred tax	<u>(61)</u>	<u>31</u>	<u>—</u>	<u>—</u>
Shareholders' attributable tax in respect of the long-term business				
Current	—	—	107	153
Deferred	—	—	(17)	(23)
Total shareholders' attributable tax	<u>—</u>	<u>—</u>	<u>90</u>	<u>130</u>
Tax allocated to non-technical account	6	(12)	(6)	12
Tax charge on profit on ordinary activities	<u>149</u>	<u>540</u>	<u>86</u>	<u>135</u>

b) Factors affecting tax charge for the period

	<u>2015</u>	<u>2014</u>
	£m	£m
Profit on ordinary activities before tax	2,007	4,792
Profit on ordinary activities multiplied by effective rate of corporation tax in the UK of 20.25 per cent (2014: effective rate of 21.50 per cent)	406	1,030
Permanent differences	12	7
Adjustment to current tax in respect of previous periods	(2)	2
Different tax bases of long-term insurance (current tax)	2	1
Effect of short term timing differences	(6)	(3)
Effect of overseas tax	—	—
Non-taxable income	(57)	(2)
Gains not taxable	—	(13)
Revaluation of subsidiaries	(269)	(887)
Total tax charge for the period	<u>86</u>	<u>135</u>

Notes on the financial statements (continued)

c) Balance Sheet

	Attributable to Long-term funds		Attributable to Shareholders' funds	
	2015 £m	2014 £m	2015 £m	2014 £m
Provision for Deferred Tax				
Accelerated capital allowances	18	18	—	—
Short term timing differences	(1)	(1)	(1)	(1)
Unrealised gains	643	703	—	—
Deferred acquisition costs	(91)	(95)	—	—
Life transitional arrangements	75	91	—	—
Pension asset	15	4	—	—
Undiscounted provision for deferred tax liability	<u>659</u>	<u>720</u>	<u>(1)</u>	<u>(1)</u>
Deferred tax liability (deferred tax asset) at start of the period	720	689	(1)	(1)
Deferred tax charged in technical/non-technical account for the period	<u>(61)</u>	<u>31</u>	<u>—</u>	<u>—</u>
Deferred tax liability (deferred tax asset) at end of the period	<u>659</u>	<u>720</u>	<u>(1)</u>	<u>(1)</u>

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 12 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 (2014: £110m) has been maintained for the general insurance business operations in run off, primarily for industrial disease exposure, and is included within claims outstanding.

9. Information on staff and pension costs

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

	2015	2014
United Kingdom	11	12
Poland	104	86
	<u>115</u>	<u>98</u>

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

	2015 £m	2014 £m
Wages and salaries	4	4
Social security and pension costs	—	1
	<u>4</u>	<u>5</u>

Notes on the financial statements (continued)

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 a defined benefit scheme but no employees with employment offers after 31 July 2003 are eligible for membership of the defined benefit section of the Scheme. At 31 December 2015, the underlying PSPS liabilities account for 84% (2014: 84%) 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).

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 2014 and was finalised in 2015. This valuation demonstrated the scheme to be 107 per cent funded by reference to the Scheme Solvency Target that forms the basis of the scheme's funding objective. The contributions into the scheme are payable at the minimum level of contributions required under the scheme rules. Excluding expenses, the contributions are now payable at approximately £6m per annum 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 2014 and was finalised in 2015. This valuation demonstrated the scheme to be 78 per cent funded. Based on this valuation, it was agreed with the Trustees to increase the previous level of deficit funding of £13.1m to £21m per annum from 1 January 2015 to 31 March 2024, subject to review at subsequent valuations.

For SASPS, as at 31 December 2015 40% of the deficit is attributable to the Company's with-profits fund (2014: approximately 50%). The remaining shareholders' share of the deficit of SASPS is borne by Prudential Financial Services Limited, a fellow subsidiary undertaking of the Prudential Group.

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.

The Trustee consults the Principal Employer, the Prudential Assurance Company, on the investment principles, but the ultimate responsibility for the investment of the assets of the scheme lies with the Trustee.

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

Notes on the financial statements (continued)

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:

	2015	2014
	%	%
Price inflation:		
Retail Price Index (RPI)	3.0	3.0
Consumer Price Index (CPI)	2.0	2.0
Rate of increase in salaries	3.0	3.0
Rate of increase of pensions in payments:		
PSPS		
Guaranteed - LPI (Max 5%)	2.5	2.5
Guaranteed - LPI (Max 2.5%)	2.5	2.5
Discretionary	2.5	2.5
SASPS	3.0	3.0
Rate used to discount scheme liabilities	3.8	3.5

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 and was updated in 2014 to reflect the 2012 mortality model from the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries (CMI). For the PSPS immediate annuities in payment, in 2015 and 2014, a long-term improvement rate of 1.75 per cent per annum and 1.25 per cent per annum were applied for males and females, respectively.

The most recent full valuations have been updated to 31 December 2015 applying the principles prescribed by FRS 102.28.

The combined assets and liabilities of PPS and SASPS were:

	31 December 2015		31 December 2014	
	£m	%	£m	%
Equities	537	7	528	7
Bonds	6,278	85	6,584	86
Properties	70	1	93	1
Other assets	511	7	445	6
Total value of assets	7,396	100	7,650	100
Present value of underlying scheme liabilities	6,510		6,954	
Underlying surplus in the schemes	886		696	

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

	2015	2014
	£m	£m
Attributable to the Company's with-profits fund	<u>85</u>	<u>19</u>

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

Notes on the financial statements (continued)

The total actual return on scheme assets for both PSPS and SASPS is a net loss of £1m (2014: net gain of £1,273m) of which a net loss of £0.6m (2014: net gain of £878m) relates to the amounts attributable to the Company's with-profits fund.

The surplus in the Prudential Staff Pension Scheme recognised in the balance sheet of the Company represents the element of 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:

	2015
	£m
Present value of scheme liabilities at beginning of year	6,954
Current service cost	29
Past service cost	(48)
Curtailment	—
Interest cost	237
Employee contributions*	1
Remeasurement: Actuarial losses	(370)
Benefit payments	(293)
Present value of scheme liabilities at end of year	<u>6,510</u>

	2015
	£m
Fair value of scheme assets at beginning of year	7,651
Interest income	258
Employee contributions	1
Employer contributions*	38
Remeasurement: Return on plan assets excluding interest income	(259)
Benefit payments	(293)
Fair value of scheme assets at end of year	<u>7,396</u>

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

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

	2015	2014
	£m	£m
Pension charge		
Operating charge:		
Current service cost	(29)	(23)
Past service cost	48	(4)
	<u>19</u>	<u>(27)</u>
Curtailment	—	2
Net interest on net pension scheme liabilities	21	21
Total pension charge of the schemes	<u>40</u>	<u>(4)</u>
Of which the following amounts have been attributed to the Company:		
With-profits fund	<u>(20)</u>	<u>14</u>

The pension charge relating to PSPS attributable to the Company is related to the surplus recognised on the balance sheet of the Company.

Notes on the financial statements (continued)

The actuarial (losses) gains relating to PSPS attributable to the Company's with-profits fund are related to the surplus recognised on the balance sheet of the Company. In 2015, the actuarial losses attributable to the Company's with-profits fund included a charge of £49m (2014: a charge of £61m) for the adjustment to the unrecognised portion of the PSPS surplus which has not been applied against the pension charge. Since the shareholders' profit in respect of the Company's with-profits fund is a function of the actuarially determined surplus for distribution, the overall profit and loss account result is not directly affected by the level of pension cost or other expenses relating to the with-profits fund. The pension credit of £20m (2014: charge of £14m) and actuarial gains of £29m (2014: actuarial losses of £12m) attributable to the Company's with-profits fund are included in the technical account and reflected in the transfer to or from the fund for future appropriations.

Total employer contributions expected to be paid into PSPS and SASPS for the year ending 31 December 2015 amounts to £38.5m, reflecting the annual accrual cost and deficit funding (SASPS only), and expenses.

The table below shows the sensitivity of the underlying PSPS and SASPS liabilities at 31 December 2015 of £5,758m (2014: £6,157m) and £752m (2014: £797m) to changes in discount rates, inflation rates and mortality rate assumptions.

Assumption	Change in assumption	Impact on PSPS and SASPS scheme liabilities on FRS102.28 basis
2015		
Discount rate	Decrease by 0.2% from 3.8% to 3.6%	Increase scheme liabilities by: PSPS 3.3% SASPS 5.1%
Discount rate	Increase by 0.2% from 3.8% to 4.0%	Decrease scheme liabilities by: PSPS 3.1% SASPS 4.7%
Rate of inflation	RPI: Decrease by 0.2% from 3.0% to 3.2% CPI: Decrease by 0.2% from 2.0% to 2.2% with consequent reduction in salary increases	Decrease scheme liabilities by: PSPS 0.5% SASPS 4.0%
Mortality rate	Increase life expectancy by 1 year	Increase scheme liabilities by: PSPS 3.2% SASPS 2.5%

Assumption	Change in assumption	Impact on PSPS and SASPS scheme liabilities on FRS102.28 basis
2014		
Discount rate	Decrease by 0.2% from 3.5% to 3.3%	Increase scheme liabilities by: PSPS 3.4% SASPS 5.3%
Discount rate	Increase by 0.2% from 3.5% to 3.7%	Decrease scheme liabilities by: PSPS 3.2% SASPS 4.9%
Rate of inflation	RPI: Decrease by 0.2% from 3.0% to 3.2% CPI: Decrease by 0.2% from 2.0% to 2.2% with consequent reduction in salary increases	Decrease scheme liabilities by: PSPS 0.6% SASPS 4.1%
Mortality rate	Increase life expectancy by 1 year	Increase scheme liabilities by: PSPS 3.3% SASPS 2.6%

The sensitivity of the underlying pension scheme liabilities as shown above does not directly equate to an impact on shareholders' profit or shareholders' funds due to the allocation of a share of the interest in financial position of the PSPS and SASPS to the Company's with-profits fund as described above.

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

Share-based payments

The Company maintains a number of main share award and share option plans relating to Prudential plc shares, which are described below.

Notes on the financial statements (continued)

(i) Prudential Long-term Incentive Plan (PLTIP)

The PLTIP is a conditional share plan: the shares which are awarded will ordinarily be released to participants after three years to the extent that performance conditions have been met. If performance conditions are not achieved in full, the unvested portion of any award lapses and performance cannot be retested. The performance conditions attached to PLTIP awards are: Relative Total Shareholder Return (TSR) (50 per cent of award); and Group IFRS profit (50 per cent of award); or Business Unit IFRS profit (50 per cent of award). The performance conditions attached to each award is dependent on the role of the participants. The Relative TSR is measured over three years. The TSR is measured against a peer group of international insurers (currently 18) which are similar to Prudential in size, geographic footprint and products. IFRS profit is the three year cumulative IFRS operating profit assessed at Group or Business Unit level. Threshold and maximum achievement levels will be set at the beginning of the performance periods in line with the three year business plan.

(ii) Savings Related Options

The Company participates in share option schemes satisfied by the issue of new shares: UK-based executive directors and eligible employees are eligible to participate in the Prudential HM Revenue & Customs (HMRC)-approved UK savings related share option scheme (SAYE scheme). These schemes allow all eligible employees to save towards the exercise of options over Prudential plc shares with the option price set at the beginning of the savings period at a discount of up to 20 per cent of the market price.

Participants can elect to enter into savings contracts of up to £500 per month for a period of three or five years. At the end of this term, participants may exercise their options within six months and purchase shares. If an option is not exercised within six months, participants are entitled to a refund of their cash savings plus interest if applicable under the rules. Shares are issued to satisfy those options which are exercised. No options may be granted under the schemes if the grant would cause the number of shares which have been issued, or which remain issuable pursuant to options granted in the preceding 10 years under the scheme and other share option schemes operated by the Company, or which have been issued under any other share incentive scheme of the Company, to exceed 10 per cent of the Company's ordinary share capital at the proposed date of grant.

(iii) Share Incentive Plan

UK-based executive directors and employees are also eligible to participate in the Company's HMRC-approved Share Incentive Plan (SIP). All UK-based employees are able to purchase shares of Prudential plc up to a value of £150 per month from their gross salary (partnership shares) through the SIP. For every four partnership shares bought, an additional matching share is awarded, purchased by Prudential on the open market. Dividend shares accumulate while the employee participates in the plan. Partnership shares may be withdrawn from the scheme at any time. If the employee withdraws from the plan, or leaves the Group, matching shares are forfeited.

(iv) Other Share Awards

In addition, there are other share awards, including the Prudential Corporation Deferred Bonus Plan and other arrangements. There are no performance conditions attached to deferred share awards made under these arrangements.

(v) Group Performance Share Plan (GPSP) and Business Unit Performance Plan (BUPP)

Prior to the approval of the PLTIP, the GPSP and the BUPP were the principal long-term incentive plans operated for executive directors and senior executives. The GPSP and BUPP are conditional share plans: the shares which were awarded will be released to participants to the extent that performance conditions have been met, over the three-year performance period. The performance measure for the awards is that Prudential's Total Shareholder Return (TSR) outperforms an index comprising of peer companies.

THE PRUDENTIAL ASSURANCE COMPANY LIMITED

10. Directors' emoluments

	2015	2014
	£	£
Aggregate emoluments	1,832,299	2,946,114
Aggregate amounts receivable (excluding shares) under long term incentive schemes	—	—
Excess retirement benefits:		
Current directors	23,900	179,353
Past directors	133,099	33,801
Other cash payments	—	—
	<u>1,989,298</u>	<u>3,159,268</u>
Highest Paid Director:		
Aggregate emoluments and amounts receivable (excluding shares) under long term incentive schemes	<u>1,169,425</u>	<u>1,909,007</u>

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. One director (2014: one) exercised share options during the year. Two directors (2014: three) were entitled to shares under Prudential's main long-term incentive scheme and no directors (2014: nil) were entitled to retirement funds under defined benefit schemes. The highest paid director in 2014 did not exercise any share options but did receive shares under long-term incentive schemes.

11. Auditor's remuneration

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

	2015	2014
	£m	£m
Audit services:		
Fees payable to KPMG for the audit of the Company's accounts	2	2

The Company has not disclosed the fees payable to KPMG for 'Non-audit services' as this information is included in the consolidated financial statements of Prudential plc.

Notes on the financial statements (continued)

12. Intangible assets

	Licence £m	Computer Software £m	Total £m
Cost:			
At 1 January 2015	174	4	178
Exchange differences	—	—	—
Additions	—	—	—
At 31 December 2015	174	4	178
Amortisation:			
At 1 January 2015	127	—	127
Exchange differences	—	—	—
Recognised in the long-term business technical account	16	1	17
At 31 December 2015	143	1	144
Net book value at 31 December 2015	31	3	34
Net book value at 31 December 2014	47	4	51

The licence represents the value of an agreement, which commenced in 1997, with a fellow subsidiary company for the use of certain Scottish Amicable assets, which is being amortised over a period of 20 years to 30 September 2017, on a basis consistent with the revenue stream from the agreement. Under this basis, the amortisation commenced in the year 2000, when the benefits from the agreement first started to arise, with the intention of the licence being fully amortised by 30 September 2017.

There have been no impairments during the year (2014: £Nil).

13. Land and buildings

	2015 £m	2014 £m
Current value		
Freeholds	4,144	4,492
Leaseholds with a term of over 50 years	3,281	2,813
Leaseholds with a term of less than 50 years	660	448
	8,085	7,753
Cost	5,284	5,397

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

	2015 £m	2014 £m
At cost	5,284	5,397
Aggregate depreciation	(3,164)	(3,050)
Net book value based on historical cost	2,120	2,347

Notes on the financial statements (continued)

(a) Company-occupied property

	2015 £m	2014 £m
Balance at 1 January	131	112
Revaluations	21	19
Balance at 31 December	152	131

(b) Investment property

	2015 £m	2014 £m
Balance at 1 January	7,622	6,212
Additions		
Resulting from acquisitions	384	853
Resulting from expenditure capitalised	46	37
Disposals	(552)	(197)
Net gain from fair value adjustments	508	744
Other changes	(75)	(27)
Balance at 31 December	7,933	7,622

The 2015 profit and loss account includes rental income from investment properties of £423m (2014: £420m).

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

	2015 £m			2014 £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	3	—	3	3	—	3
1 to 5 years	13	(2)	11	13	(2)	11
Over 5 years	578	(526)	52	619	(570)	49
Total	594	(528)	66	635	(572)	63

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. There was no contingent rent recognised as income or expense in 2015 or 2014. There are no restrictions on the realisability of investment property or the remittance of income and proceeds of disposal. The contractual obligations purchase or develop investment properties at 31 December 2015 were £409m (2014: £232m).

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:

	2015 £m	2014 £m
Less than 1 year	221	225
1 to 5 years	774	790
Over 5 years	1,998	2,109
Total	2,993	3,124

Notes on the financial statements (continued)

(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:

	2015 £m			2014 £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	—	—	—
1 to 5 years	9	(2)	7	—	—	—
Over 5 years	375	(351)	24	—	—	—
Total	386	(353)	33	—	—	—

14. Investments in group undertakings and participating interests

	Cost		Current value	
	2015 £m	2014 £m	2015 £m	2014 £m
Long-term fund investments	572	1,253	1,440	1,962
Shareholder investments	1,236	1,088	8,785	7,307
	1,808	2,341	10,225	9,269
Interest in joint ventures and associate				
Long-term fund investments	207	310	434	518
Debt securities issued by, and loans to group undertakings – long term funds	826	889	826	889
Total	2,841	3,540	11,485	10,676

Refer to note 32 for further information on the related undertakings of the Company.

15. Other financial investments

	Cost		Carrying value	
	2015 £m	2014 £m	2015 £m	2014 £m
Shares and other variable yield securities and units in unit trusts	29,899	23,670	36,114	30,496
Debt securities and other fixed income securities	41,417	41,041	43,630	45,030
Derivative assets	279	343	1,234	1,714
Participation in investment pools	1,733	1,739	2,533	2,468
Loans secured by mortgages	1,860	2,222	1,912	2,288
Loans to policyholders secured by insurance policies	8	10	8	10
Other loans	534	651	523	636
Deposits with credit institutions	9,108	10,616	9,108	10,616
	84,838	80,292	95,062	93,258

Notes on the financial statements (continued)

The change in carrying value of other financial investments included in the Profit and Loss account was a loss of £3,196m (2014: £2,624m gain) analysed between a loss of £3,225m (2014: £2,620m gain) included in the Long-term business technical account and a £29m gain (2014: £4m gain) included in the Non-technical account. The change in carrying value of £3,196m (2014: £2,624m gain) included a loss of £607m (2014: £74m loss) in respect of equity securities, a loss of £1,755m (2014: £2,409m gain) in respect of debt securities, a loss of £891m (2014: £87m gain) in respect of derivatives and a gain of £57m (2014: £202m gain) in respect of other financial instruments.

	Carrying value	
	2015	2014
	£m	£m
Amounts included in the above relating to listed investments:		
Shares and other variable yield securities and units in unit trusts	34,171	28,602
Debt securities and other fixed income securities	40,933	41,712
	75,104	70,314

The table below analyses the derivative positions of the Company:

	2015		2014	
	Fair value assets	Fair value liabilities	Fair value assets	Fair value liabilities
	£m	£m	£m	£m
Derivative financial instruments held to manage interest rate and currency profile:				
Interest rate swaps	951	129	1,101	219
Cross currency swaps	24	211	38	138
Currency exchange forward contracts	45	961	245	466
Bond futures	6	2	22	53
Credit Default Swaps	2	—	10	—
Inflation Swaps	115	86	115	80
Derivative financial instruments held to manage market risk and efficient investment management:				
Equity options	86	—	130	—
Equity futures	5	38	52	4
Equity warrants	—	—	1	—
Total	1,234	1,427	1,714	960

The nature of the derivative financial instruments, used by the Company in 2015, are similar to those used in 2014 and includes 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 in 2015. The use of derivatives is disclosed in note 29G.

16. Assets held to cover linked liabilities

	Cost		Carrying value	
	2015	2014	2015	2014
	£m	£m	£m	£m
Assets held to cover linked liabilities	9,757	9,906	11,861	12,254

Notes on the financial statements (continued)

17. Reinsurers' share of technical provisions

The reinsurers' share of the long-term business provision relates mainly to cessions to Prudential Retirement Income Limited and Prudential Hong Kong Limited, both subsidiaries of the Company. The reinsurers' share of the technical provisions for linked liabilities relates mainly to cessions to Prudential Pensions Limited and Prudential Hong Kong Limited, both subsidiaries of the Company. In 2015 PRIL wrote six longevity swaps which due to the quota share reinsurance arrangement resulted in one-off benefits of £60m to profit before tax.

Included in income and expense in the profit and loss account is £534m reflecting the movement in the reinsurers' share of technical provision to £14,931m at 31 December 2015 from £15,465m at 31 December 2014.

18. Other debtors

	2015 £m	2014 £m
Amounts owed by holding company	709	702
Amounts owed by fellow subsidiaries	50	31
Amounts owed by subsidiary companies, associate and joint ventures	115	296
Tax recoverable	125	94
Other	128	72
	1,127	1,195

Other debtors include £2m (2014: Nil) due after more than one year.

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 21, £139,153m (2014: £138,238m) is attributable to the long-term business fund.

21. Share capital

The Company's issued share capital is £329,517,064 comprising 970,468,254 ordinary shares of 25p each fully paid and 347,600,000 B Preference Shares of 25p each fully paid. No changes in the share capital of the Company took place during the year.

The B Preference Shares issued carry the right to receive a non-cumulative preferential dividend which shall accrue at the rate of two pence per annum. The B Preference Shares may not be redeemed otherwise than at the option of the Company at any time after the fifth anniversary of the date of issue of such B Preference Shares. The B Preference Shares carry no voting rights except if a resolution is proposed in relation to (i) the winding up of the Company, a voluntary arrangement with creditors of the Company or proposed receivership, administrative receivership or administration of the Company; or (ii) an alteration of the rights of the B Preference Shares or in relation to any other matter which will have detrimental effect upon the rights of the B Preference Shares.

Notes on the financial statements (continued)

22. Profit and loss account

	2015	2014
	£m	£m
Analysis of profit and loss account:		
Distributable retained profit	1,732	1,435
Undistributable retained profit	7,895	6,632
Total	<u>9,627</u>	<u>8,067</u>

23. Other creditors including tax and social security

	2015	2014
	£m	£m
Amounts owed to fellow subsidiaries and holding company	234	115
Amounts owed to subsidiary companies, associate and joint ventures	1,740	1,575
Tax	131	274
Derivative liability (see note 15)	1,427	960
Other creditors	1,971	1,643
	<u>5,503</u>	<u>4,567</u>

24. Preference shares

	2015	2014
	£m	£m
A preference shares of £1 each	1	1

The A Preference Shares issued shall be redeemed by the Company without notice on 8 May 2016. The premium payable on redemption amounts to 28.08p, which is increased by the percentage of the RPI from a date 30 days prior to the first issue of any preference shares to a date 30 days prior to redemption. The A Preference Shares carry the right to receive an index linked cumulative preferential dividend, payable annually. The A Preference Shares carry no voting rights except if a resolution is proposed abrogating, varying or modifying any of the rights or privileges of the holders of the A Preference Shares, but carry preferential rights in priority to other shareholders to payment on a return of capital in the event of the winding up of the Company.

25. Ultimate parent company

The ultimate and immediate parent company is Prudential plc, which is the parent company that prepares group accounts. Copies of these accounts can be obtained from the Company Secretary, Laurence Pountney Hill, London EC4R 0HH.

26. 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.

In 2014 £58m was recharged to the Company from Prudential Health Services Limited for services provided in respect of the PruProtect product underwritten by the Company. An agreement was entered into on 3 September 2007 which allowed the Company to borrow from Prudential Health Holdings Limited up to an aggregate amount of £250m. The loan amount is principally linked to the emergence of regulatory losses arising in respect of all

Notes on the financial statements (continued)

income and costs associated with selling and underwriting the Flexible Protection Plan and PruProtect Plan. The loan was to be repaid as regulatory surpluses arose in the future. In 2014 the Company repaid £8m under this arrangement. At 31 December 2014 the outstanding balance, including accrued interest, was £70m.

On 14 November 2014 the Company sold its 25% equity stake in the PruHealth and PruProtect businesses to Discovery Group Europe Limited.

Notes on the financial statements (continued)

27. Long-term business provision

i Analysis of movements in insurance liabilities including FFA

	Technical Provisions		
	Technical Provisions £m	Linked liabilities £m	Total £m
At 1 January 2014			
Comprising			
Technical provisions	103,557	18,051	121,608
Fund for future appropriations	12,043	—	12,043
	115,600	18,051	133,651
Premiums	4,259	97	4,356
Surrenders	(2,653)	(476)	(3,129)
Maturities/Deaths	(4,412)	(615)	(5,027)
Shareholders' transfers post tax	(200)	—	(200)
Switches	(167)	167	—
Investment-related items and other movements	11,941	728	12,669
Foreign exchange translation differences	(49)	6	(43)
Deductions on disposals	(8,153)	(1,263)	(9,416)
Assumption changes	(40)	—	(40)
Other	(1,834)	558	(1,276)
As at 31 December 2014/1 January 2015	114,292	17,253	131,545
Comprising			
Technical provisions	103,816	17,253	121,069
Fund for future appropriations	10,476	—	10,476
	114,292	17,253	131,545
Premiums	6,758	359	7,117
Surrenders	(3,136)	(630)	(3,766)
Maturities/Deaths	(4,494)	(597)	(5,091)
Shareholders' transfers post tax	(214)	(1)	(215)
Switches	(189)	189	—
Investment-related items and other movements	1,521	216	1,737
Foreign exchange translation differences	14	—	14
Assumption changes	(41)	—	(41)
Other	(25)	26	1
As at 31 December 2015	114,486	16,815	131,301
Comprising			
Technical provisions	103,727	16,815	120,542
Fund for future appropriations	10,759	—	10,759
	114,486	16,815	131,301

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:

Notes on the financial statements (continued)

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:

- (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 specimen asset shares for the purpose of bonus setting.

The 2015 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	3.62%	3.15%	1.22%	2.57%
Net return	3.23%	2.77%	1.14%	2.34%

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 our 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 mortality assumption has been set to the realistic component of the statutory basis. This means that for a given business class, the margin for adverse deviations (MAD) has been removed from the corresponding statutory assumption.

Notes on the financial statements (continued)

The table below shows the mortality bases used for the valuation at 31 December 2015:

Product	Mortality Table (M/F)	Age Rating Years	Multiplier % (M/F)
Prudence Bond	AM92 / AF92	-1/-1	90 / 90
PSA / PIB	AM92 / AF92	-0.5/-0.5	70 / 70
Personal Pensions	AM92 / AF92	-1/-1	95 / 95
Ordinary Branch assurances	AM92 / AF92	-0.5/-0.5	85 / 85
Industrial Branch	PAC 78 WL (Internal Table)	+0 / +0	55 / 55
With-Profit Deferred Annuities	AM92 / AF92	-1/-1	95 / 95
SAIF Conventional With-Profits	AM92 / AF92	+1 / +1	70 / 70
SAIF/Ex-SAL Accumulating With-Profits Life	AM92 / AF92	+1 / +1	70 / 70

For persistency, the assumptions for most products are based on those used for European Embedded Value calculations. 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.

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.

The risk free rate was assumed to be the UK gilt rate.

Separate asset models are used for the risk free 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 from the returns available on appropriate investments and, for equity and property assets, are based on expected income and/or earnings with no allowance for potential future capital growth. Allowance is made as follows for the risk that some or all of the anticipated future income will not be received:

- (a) For equity and property assets the income is restricted where necessary to ensure that no individual holding had a yield in excess of the annual yield on the Merrill Lynch over 10 years corporate bond index, less a risk margin.
- (b) For fixed interest securities, aggregate bond asset yields have been adjusted to allow for potential defaults within the non-linked and index-linked asset portfolios respectively.

Notes on the financial statements (continued)

The following discount and mortality bases were used:

	Interest Rate %	Actuarial Mortality Table Reference*
UK (excluding Scottish Amicable Insurance Fund)		
Term assurances - life business	2.25	AM/AF92+1
Term assurances - pensions business	2.75	75% AM/AF92+1
Ex-PAL Annuities (Fixed)	3.09	95% - 97% PCMA00 + CMI_2014_PRU_M[2.25]; 91% - 103% PCFA00 + CMI_2014_PRU_F[1.50]**
Ex-PAL Annuities (Linked)	-0.20	95% - 97% PCMA00 + CMI_2014_PRU_M[2.25]; 91% - 103% PCFA00 + CMI_2014_PRU_F[1.50]**
PRIL Quota Share Annuities (Fixed)	3.34	93% PCMA00 + CMI_2014_PRU_M[2.25]; 83% - 96% PCFA00 + CMI_2014_PRU_F[1.50]**
PRIL Quota Share Annuities (Linked)	0.09	93% PCMA00 + CMI_2014_PRU_M[2.25]; 83% - 96% PCFA00 + CMI_2014_PRU_F[1.50]**
Other NPSF Annuities (Fixed)	3.41	83% PCMA00 + CMI_2014_PRU_M[2.25]; 74% PCFA00 + CMI_2014_PRU_F[1.50]**
Other WPSF Annuities (Fixed)	2.75	97% PCMA00 + CMI_2014_PRU_M[2.25]; 91% PCFA00 + CMI_2014_PRU_F[1.50]**
Other WPSF Annuities (Linked)	1.00	97% PCMA00 + CMI_2014_PRU_M[2.25]; 91% PCFA00 + CMI_2014_PRU_F[1.50]**
Scottish Amicable Insurance Fund		
Term assurances - life business	1.50	90% AM/AF92+1
Term assurances – pensions business	1.00	90% AM/AF92+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.

** CMI_2014_PRU_M[2.25] and CMI_2014_PRU_F[1.50] are the male and female improvement rates produced by Prudential's internal calibration of the 2014 CMI model, with long term rates of 2.25% and 1.50%.

Linked business in the Non-Profit Sub-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	2.50% gross
Fund Growth	5.25% gross
Mortality	AM/AF92+1 plus 1/3 AIDS "R6A" for most contracts
Administration Expenses	£38 to £187 p.a. depending on the product type
Expense Inflation	4.25%

Compared with the 2015 valuation the assumptions regarding administration expenses have been revised to allow for actual and forecast costs.

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	2.75% gross
Fund Growth	5.25% gross
Mortality	AM/AF92 -3 years
Administration Expenses	£49 to £244 p.a. depending on the product type
Expense Inflation	5.75%

Compared with the 2015 valuation the assumptions regarding administration expenses have been revised to allow for actual and forecast costs.

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 28.

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

For the with-profits sub-fund, the aggregate effect of assumption changes and modelling adjustments in 2015 was a net charge to the FFA of £114m (2014: net credit of £200m), relating to changes in mortality assumptions, offsetting releases of margins, and altered expense, persistency and economic assumptions, where appropriate in the two periods.

28. 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. Prudential met the requirement of the FSA (the UK insurance regulator at the time) to issue offers to all cases by 30 June 2002.

At 31 December 2015, the pension mis-selling provision was £429m (2014: £328m) and is included within the long-term business provision. The table below summarises the change in the pension mis-selling provision for the year ended 31 December 2015.

	Year Ended 31 December 2015	Year Ended 31 December 2014
	£m	£m
Balance at start of the period	328	286
Changes to actuarial assumptions and method of calculation	144	74
Discount unwind	2	1
Redress paid to policyholders	(44)	(32)
Payment of administrative costs	(1)	(1)
Balance at end of the period	429	328

The pension mis-selling provision at 31 December 2015 of £429m is stochastically determined on a discounted basis. The average discount rate implied in the movement in the year is 2.0 per cent (2014: 2.0 per cent).

Provisions in respect of the costs associated with the review have been included in the change in long-term

Notes on the financial statements (continued)

technical provisions in the Company's long-term technical account and the transfer to or from the fund for future appropriations has been determined accordingly.

The directors believe that, based on current information, the provision, together with future investment return on the assets backing the provision, will be adequate to cover the costs of pension mis-selling including administration costs. Such provision represents the best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

The costs associated with the pension mis-selling review have been met from the inherited estate. 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, Prudential stated that deducting mis-selling costs from the inherited estate would not impact its bonus or investment policy and it gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged. The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing.

This review was completed on 30 June 2002. The assurance will continue to apply to any policy in force at 31 December 2003, both for premiums paid before 1 January 2004, and for subsequent regular premiums (including future fixed, 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.

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 (the UK regulator at the time) 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 £0.4m (2014: £0.4m) in the non-profit sub-fund and £3.8m (2014: £3.8m) in SAIF were held at 31 December 2015 to cover potential compensation in respect of mortgage endowment product mis-selling claims. As SAIF is a separate sub-fund of the Company's long-term business 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 £0.8m in respect of mortgage endowment products mis-selling claims in the year ended 31 December 2015 (2014: £1.1m) and held a technical provision of £12.7m at 31 December 2015 (2014: £12.7m) in respect of further compensation. In line with the time limit prescribed by the FSA, the insurance regulator at that time, 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 £47m at 31 December 2015 (2014: £50m) within the main with-profits fund to honour guarantees on these products.

Notes on the financial statements (continued)

The Company's main exposure to guaranteed annuities in the UK is through the Scottish Amicable Insurance Fund (SAIF) and a technical provision of £412m was held in SAIF at 31 December 2015 (2014: £549m) to honour the guarantees.

Guarantees and Commitments

Since 2012 the Company has agreed to guarantee the funding obligation that Prudential Distribution Limited (PDL), a service company within the Prudential Group and principal employer, and other participating employers have to the Scottish Amicable Pension Scheme. The funding obligation arises from the deficit in this pension scheme. Payment under the guarantee would be exercised should PDL fail to meet its funding obligation. The guarantee expires on 31 March 2024.

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.

Inherited Estate

The assets of the with-profits sub-fund (WPSF) within the long-term fund of the Company comprise the amounts that it expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the WPSF is equal to the policyholders' accumulated asset shares plus any additional payments that may be required by way of smoothing or to meet guarantees. The balance of the assets of the WPSF is called the 'inherited estate' and has accumulated over many years from various sources.

The inherited estate, as working capital, enables the Company to support with-profits business by providing the benefits associated with smoothing and guarantees, by providing investment flexibility for the fund's assets, by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies. The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

Support 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, the Scottish Amicable Insurance 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 2013 because technical provisions are set at a level at which the realistic working capital is zero). 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 long-term fund would be liable to cover any such deficiency in the first instance.

Notes on the financial statements (continued)

The Polish branch became operational in March 2013. The Company's inherited estate is contributing to the costs of establishing the branch. The inherited estate is expected to recoup this funding over time from charges levied, however, if experience is not as expected there is an obligation of the Company's shareholder funds to ensure the inherited estate will be repaid in full with interest.

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 of £15m (plus interest) by the trustees of a pension scheme administered by the Company in relation to a historical administration matter and a claim for £159 million in respect of which the Company is one of a number of defendants relating to the financial restructuring carried out by a borrower in one of the Company's investments. The outcome of litigation is always uncertain but the Company believes it has good grounds to defend these claims. In addition, a judgment has been made in favour of the Company (as a lending noteholder) in response to the partial early redemption of notes from a commercial property investment and a £10m early redemption payment is currently in escrow, which, subject to any appeal, will be released to the Company.

While the outcome of these 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.

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 2014 the Company put in place an arrangement to formalise circumstances in which capital support would be made available to Prudential Retirement Income Limited (PRIL). The drawdown of support would be triggered by a breach of pre-specified solvency conditions in PRIL on a Pillar I and Pillar II basis.

Following the domestication of the Hong Kong branch a series of intra-group capital support arrangements have been put in place:

- **New Business Support Commitment:**

For a period of three years from the transfer date of 1 January 2014 capital support shall be provided from the Company's shareholders' fund to its with-profits fund to enable it to maintain the expectations of its with-profits policyholders as if the assets of the inherited estate had not been transferred to the new business sub-fund of PHKL. The maximum amount of support available is £90m. In the event that the Company has to provide capital support under this arrangement, Prudential plc shall, in turn, provide capital support to the Company to the extent that there are insufficient assets in the Company's shareholders' fund for it to provide the capital support required by the with-profits fund.

- **PHKL Pension Mis-selling Costs Assurance:**

The PHKL shareholder fund will provide capital support to enable PHKL to satisfy its obligations to manage its in-force sub-fund as if the Company's pension mis-selling costs had not been deducted from the PHKL inherited estate. The Company, in turn, will provide capital support from its shareholders' fund to PHKL to the extent that there are insufficient assets in the PHKL shareholders' fund to enable PHKL to support its obligations to its in-force sub-fund.

- **Capital Support from Prudential plc:**

Prudential plc will also provide capital support as necessary to PHKL and PGHK to support new business growth and to maintain solvency. These support arrangements meet a condition set by the Hong Kong regulator (amongst other matters) for its approval of the domestication of the Hong Kong branch.

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 is provided by the Company's with-profits fund, it is subject to support from the

Notes on the financial statements (continued)

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.

29. 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.

2015	Fair value through profit and loss £m	Loans and receivables £m	Total carrying value £m	Fair value £m	
Financial Assets					
Deposits with credit institutions	—	9,108	9,108	9,108	
Equity securities and portfolio holdings in unit trusts	36,114	—	36,114	36,114	
Debt securities and other fixed income securities (note i)	43,630	—	43,630	43,630	
Loans (note ii):	256	2,187	2,443	2,763	
Participation in investment pools	2,533	—	2,533	2,533	
Derivative assets	1,234	—	1,234	1,234	
Assets held to cover linked liabilities	11,861	—	11,861	11,861	
Deposits with ceding undertakings	—	4,584	4,584	4,584	
Debtors arising out of direct insurance	—	45	45	45	
Debtors arising out of reinsurance ops	—	5	5	5	
Accrued investment income	—	863	863	863	
Other debtors	—	1,002	1,002	1,002	
Cash at bank and in hand	—	1,462	1,462	1,462	
Finance Lease asset	33	—	33	33	
Total	95,661	19,256	114,917	115,237	
	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	—	66	—	66	66
Other borrowings not owed to credit institutions (note iii)	—	175	—	175	175
Investment contracts with discretionary participation features (note iv)	—	—	42,709	42,709	—
Investment contracts without discretionary participation features	6,749	—	—	6,749	6,749
Creditors arising out of direct insurance operations	—	147	—	147	147
Creditors arising out of reinsurance operations	—	78	—	78	78
Deposits received from reinsurers	—	1,133	—	1,133	1,133
Other creditors	258	3,687	—	3,945	3,945
Derivative liabilities	1,427	—	—	1,427	1,427
Total (note v)	8,434	5,286	42,709	56,429	13,720

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2014	Fair value through profit and loss £m	Loans and receivables £m	Total carrying value £m	Fair value £m
Financial Assets				
Deposits with credit institutions	—	10,616	10,616	10,616
Equity securities and portfolio holdings in unit trusts	30,496	—	30,496	30,496
Debt securities and other fixed income securities (note i)	45,030	—	45,030	45,030
Loans (note ii):	266	2,668	2,934	3,368
Participation in investment pools	2,468	—	2,468	2,468
Derivative assets	1,715	—	1,714	1,714
Assets held to cover linked liabilities	12,254	—	12,254	12,254
Deposits with ceding undertakings	—	4,755	4,755	4,755
Debtors arising out of direct insurance	—	38	38	38
Debtors arising out of reinsurance ops	—	56	56	56
Accrued investment income	—	837	837	837
Other debtors	—	1,101	1,101	1,101
Cash at bank and in hand	—	1,075	1,075	1,075
Total	92,229	21,146	113,374	113,808

	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	—	63	—	63	63
Other borrowings not owed to credit institutions (note iii)	—	70	—	70	70
Investment contracts with discretionary participation features (note iv)	—	—	39,059	39,059	—
Investment contracts without discretionary participation features	6,714	—	—	6,714	6,714
Creditors arising out of direct insurance operations	—	76	—	76	76
Creditors arising out of reinsurance operations	—	75	—	75	75
Deposits received from reinsurers	—	1,360	—	1,360	1,360
Other creditors	258	3,075	—	3,333	3,333
Derivative liabilities	960	—	—	960	960
Total (note v)	7,932	4,719	39,059	51,710	12,651

Notes

- (i) As at 31 December 2015, £477m (2014: £449m) 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 £8m (2014: £15m losses).
- (iii) As at 31 December 2015, £175m (2014: £70m) 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.
- (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 2015 and 2014.

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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 principles issued by the CFO Forum of European Insurance Companies in May 2004 and expanded by the Additional Guidance on European Embedded Value Disclosures issued in October 2005. Investments in other subsidiaries are valued based net asset value where the directors consider that net asset value provides a close approximation to fair values.

The loans and receivables have been shown net of provisions for impairment. The fair value of loans has been estimated from discounted cash flows expected to be received. The rate of discount used was the market rate of interest 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.

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 FRS102.34 *Specialist Activities Financial Institutions* (FRS 102.34) para. 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 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 possibly 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 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 £39,795m (2014: £42,106m), £3,597m (2014: £3,780m) 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 significance of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

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

Level 3 principally includes investments in private equity funds, 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 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.

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	31 December 2015			
	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
With-profits				
Investment properties	—	2	7,722	7,724
Equity securities and portfolio holdings in unit trusts	33,388	2,186	506	36,080
Debt securities	4,640	36,937	200	41,777
Loans	—	864	401	1,265
Other investments (including derivative assets)	13	1,704	2,205	3,922
Derivative liabilities	(40)	(1,325)	—	(1,365)
Total financial investments, net of derivative liabilities	38,001	40,368	11,034	89,403
Percentage of total	43%	45%	12%	100%
Unit-linked				
Assets held to cover linked liabilities	7,830	—	—	7,830
Total financial investments net of derivative liabilities	7,830	—	—	7,830
Investment contract without discretionary participation features held at fair value	—	(6,749)	—	(6,749)
Total	7,830	(6,749)	—	1,081
Percentage of total	724%	(624%)	—%	100%
Non-linked shareholder-backed				
Investment properties	—	—	209	209
Equity securities and portfolio holdings in unit trusts	34	—	—	34
Debt securities	1,103	2,858	9	3,970
Loans	—	1,493	7	1,500
Other investments (including derivative assets)	—	5	1	6
Derivative liabilities	—	(62)	—	(62)
Total financial investments, net of derivative liabilities	1,137	4,294	226	5,657
Percentage of total	20%	76%	4%	100%
Company total				
Investment properties	—	2	7,931	7,933
Equity securities and portfolio holdings in unit trusts	33,422	2,186	506	36,114
Debt securities	5,743	39,795	209	45,747
Loans	—	2,357	408	2,765
Other investments (including derivative assets)	13	1,709	2,206	3,928
Assets held to cover linked liabilities	7,830	—	—	7,830
Derivative liabilities	(40)	(1,387)	—	(1,427)
Total financial investments, net of derivative liabilities	46,968	44,662	11,260	102,890
Investment contract without discretionary participation features held at fair value	—	(6,749)	—	(6,749)
Total	46,968	37,913	11,260	96,141
Percentage of total	49%	39%	12%	100%

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

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	31 December 2014			Total £m
	Level 1 £m	Level 2 £m	Level 3 £m	
With-profits				
Investment properties	—	—	7,400	7,400
Equity securities and portfolio holdings in unit trusts	27,693	2,186	532	30,411
Debt securities	4,401	39,315	147	43,863
Loans	—	1,712	59	1,771
Other investments (including derivative assets)	87	2,088	2,168	4,343
Derivative liabilities	(57)	(816)	—	(873)
Total financial investments, net of derivative liabilities	32,124	44,485	10,306	86,915
Percentage of total	37%	51%	12%	100%
Unit-linked				
Assets held to cover linked liabilities	8,177	—	—	8,177
Total financial investments net of derivative liabilities	8,177	—	—	8,177
Investment contract without discretionary participation features held at fair value	—	(6,714)	—	(6,714)
Total	8,177	(6,714)	—	1,463
Percentage of total	559%	(459%)	—%	100%
Non-linked shareholder-backed				
Investment properties	—	—	222	222
Equity securities and portfolio holdings in unit trusts	1	84	—	85
Debt securities	683	2,791	—	3,474
Loans	—	1,600	—	1,600
Other investments (including derivative assets)	—	1	1	2
Derivative liabilities	—	(87)	—	(87)
Total financial investments, net of derivative liabilities	684	4,389	223	5,296
Percentage of total	13%	83%	4%	100%
Company total				
Investment properties	—	—	7,622	7,622
Equity securities and portfolio holdings in unit trusts	27,694	2,270	532	30,496
Debt securities	5,084	42,106	147	47,337
Loans	—	3,312	59	3,371
Other investments (including derivative assets)	87	2,089	2,169	4,345
Assets held to cover linked liabilities	8,177	—	—	8,177
Derivative liabilities	(57)	(903)	—	(960)
Total financial investments, net of derivative liabilities	40,985	48,874	10,529	100,388
Investment contract without discretionary participation features held at fair value	—	(6,714)	—	(6,714)
Total	40,985	42,160	10,529	93,674
Percentage of total	44%	45%	11%	100%

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

Assets held to cover 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 £1,752m (2014: £1,606m) of assets which comprise the total assets held to cover linked liabilities, which consist mainly of cash at bank, other debtors and property.

Interest income and expense

The interest income on financial assets not at fair value through profit and loss was £154m for the year ended 31 December 2015 (2014: £170m).

The interest expense on financial liabilities not at fair value through profit and loss was £5m for the year ended 31 December 2015 (2014: £4m).

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 Group Risk Framework.

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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 and/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 position, 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 of the Company, 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 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.

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-backed non-profit sub-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 declared policyholder bonuses. During 2013 the Company entered into a partial equity hedge of the shareholder transfers expected to emerge from the with-profits sub-fund in order to mitigate this risk and it was extended in 2015. The investment assets of the Company's with-profits fund are subject to market risk. However, changes in their carrying value, net of the related changes to asset-share liabilities of with-profit contracts, affect the level of funds for future appropriations, which 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 correspond to the shareholders' share of the cost of bonuses declared on the with-profits business. This currently corresponds to one-ninth of the cost of bonuses declared.

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

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.

Shareholder-backed non-profit sub-fund

The Company's non-profit sub-fund principally comprises annuity business previously written by Scottish Amicable Life, annuity business accepted from the quota share reinsurance arrangement with Prudential Retirement Income Ltd, credit life, unit-linked and other non-participating business. The financial assets covering the liabilities for those types of business are subject to market risk. The liabilities for annuity contracts are subject to market risk arising from changes in the returns of the attaching assets. Except mainly to the extent of any minor asset/liability duration mismatch, and exposure to credit risk, the sensitivity of the Company's non-profit sub-fund's annuity business' results to market risk for movements in the carrying value of liabilities and covering assets is broadly neutral on a net basis.

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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 non-profit sub-fund are broadly insensitive to market risk.

The principal items affecting the results of the Company's non-profit sub-fund are mortality and credit experience.

C. Market Risk

As described in section B market risk is the risk that the fair value or future cash flows of a financial instrument or, in the case of liabilities of insurance contracts, their carrying value will fluctuate because of changes in market prices.

Market risk comprises three types of risk, namely:

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

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.

Interest rate risk

The net exposure to interest rate movement for the Company is very substantially ameliorated by virtue of the close matching of assets with appropriate duration to the liabilities.

The close matching by the Company of assets of appropriate duration to its non-profit sub 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 within the assumptions required under the PRA regulatory solvency basis not included for FRS 103 reporting purposes. As a result FRS 103's shareholders' funds are higher than regulatory capital and therefore more sensitive to interest rate risk.

The estimated sensitivity of the shareholder-backed business to a movement in interest rates of 1% and 2% as at 31 December 2015 and 2014 are as follows:

	2015				2014			
	Fall of 1% £m	Rise of 1% £m	Fall of 2% £m	Rise of 2% £m	Fall of 1% £m	Rise of 1% £m	Fall of 2% £m	Rise of 2% £m
Carrying value of debt securities and derivatives	537	(445)	1,216	(825)	548	(433)	1,288	(789)
Long term business provision	(406)	338	(899)	621	(447)	369	(993)	677
Related tax effects	(24)	19	(57)	37	(20)	13	(59)	22
Net sensitivity of profit after tax and shareholders' funds	107	(88)	260	(167)	81	(51)	236	(90)

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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.

	2015		2014	
	Decrease of 20%	Decrease of 10%	Decrease of 20%	Decrease of 10%
	£m	£m	£m	£m
Pre-tax profit	(49)	(24)	(61)	(31)
Related deferred tax effects	10	5	12	6
Net sensitivity of profit after tax and shareholders' funds	<u>(39)</u>	<u>(19)</u>	<u>(49)</u>	<u>(25)</u>

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. If equity markets were to fall by more than 20 per cent, the Company believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Company would be able to put in place mitigating management actions.

Currency Risk

As at 31 December 2015 the Company held 38% and 2% (2014: 36% 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 82% (2014: 81%) are held by the with-profit fund, allow the fund to obtain exposure to foreign equity markets.

The financial liabilities, of which 87% (2014: 89%) are held by the with-profit fund, mainly relate to investment contracts with discretionary participation features.

The exchange risks inherent in these exposures are 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 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.

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Debt Securities and Other Fixed Income Securities

The following table summarises by rating the securities held by the Company as at 31 December 2015 and 2014.

	With-profits sub fund	Other funds	Total 2015	With-profits sub fund	Other funds	Total 2014
	£m	£m	£m	£m	£m	£m
S&P – AAA	4,003	530	4,533	3,863	386	4,249
S&P – AA+ to AA-	5,695	452	6,147	5,623	388	6,011
S&P – A+ to A-	7,846	700	8,546	10,804	836	11,640
S&P – BBB+ to BBB-	10,650	716	11,366	9,253	714	9,967
S&P – Other	1,857	57	1,914	2,076	44	2,120
	30,051	2,455	32,506	31,619	2,368	33,987
Moody's – Aaa	1,261	50	1,311	1,368	51	1,419
Moody's – Aa1 to Aa3	1,926	884	2,810	1,727	531	2,258
Moody's – A1 to A3	936	188	1,124	874	167	1,041
Moody's – Baa1 to Baa3	573	29	602	554	49	603
Moody's – Other	82	—	82	75	—	75
	4,778	1,151	5,929	4,598	798	5,396
Fitch – AAA	113	—	113	130	1	131
Fitch – AA+ to AA-	10	—	10	19	—	19
Fitch – A+ to A-	135	14	149	155	19	174
Fitch – BBB+ to BBB-	41	—	41	68	1	69
Fitch – Other	2	—	2	21	—	21
	301	14	315	393	21	414
Other	4,531	349	4,880	4,946	287	5,233
Total debt securities and other fixed income securities	39,661	3,969	43,630	41,556	3,474	45,030

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 2015 which are not externally rated, £2,474m (2014: £2,452m) were internally rated AAA to A-, £1,832m (2014: £2,059m) were internally rated BBB+ to B- and £574m were internally rated as below B- or unrated (2014: £722m). 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 which covers the "other funds" in the table above.

Excluded from the table above is £2,289m (2014: £2,554m) of assets backing unit-linked and index-linked contracts which are included within assets held to cover linked liabilities. The holders of these contracts bear the credit risk arising from these assets.

The Company's exposure to the eurozone sovereigns of Portugal, Italy, Ireland, Greece, Spain and Cyprus is £80m (2014: £82m) with £77m (2014: £79m) in the with-profits fund and £3m (2014: £3m) in the shareholder funds. The Company's exposure to banking operations in these eurozone countries is £62m (2014: £82m) with £59m (2014: £79m) in the with-profits fund and £3m (2014: £3m) in the shareholder funds. The Company had no exposure in Greece or Cyprus in 2015 or 2014.

Loans and receivables

In accordance with accounting policy, impairment reviews were performed for loans and receivables. During the year ended 31 December 2015, impairment losses of £2m (2014: £7m) and reversal of impairment losses of £9m (2014: £60m) were recognised for loans and receivables.

Of the total loans and receivables held £1m (2014: £2m) are past their due date but have not been impaired. 100% (2014: 99%) of the loans and receivables that are past due but not impaired are less than one year past their due date for 2015. The Company expects full recovery of these loans and receivables.

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Reinsurer's share of technical provisions

The majority of the reinsurers' share of technical provisions relate to cessions to subsidiaries of the Company. See note 17.

Of the reinsurer's share of technical provisions at 31 December 2015 of £14,931m (2014: £15,465m), 4% (2014: 4%) of the balance relates to companies outside of the Prudential Group and of this 76% (2014: 75%) of the balances were from reinsurers with S&P's rating of AA- and above, based on the ratings at the time of signing these financial statements.

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 2015, the Company had lent £4,687m (2014: £3,129m) of securities and held collateral under such agreements of £5,002m (2014: £3,400m).

At 31 December 2015, the Company had entered into reverse repurchase transactions under which it purchased securities and had taken on the obligation to resell the securities for the purchase price. The fair value of the collateral held in respect of these transactions was £9,074m (2014: £11,575m).

During 2015 and 2014 the Company did not take possession of any other collateral held as security.

Collateral and pledges under derivative transactions

At 31 December 2015, the Company had pledged £550m (2014: £650m) for liabilities and held collateral of £795m (2014: £1,361m) 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.

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, the Company assumes that current rates of mortality continue to improve over time at levels based on the Company's calibration of the Continuous Mortality Investigations (CMI) 2014 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 other life-threatening diseases) that would require the Company to strengthen its longevity assumptions would have an impact on the Company's results. The Company continues to seek opportunities to transfer longevity risk to reinsurers or to the capital markets.

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 dependant 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. Morbidity risk is mitigated by appropriate underwriting and use of reinsurance.

Shareholder-backed non-profit sub-fund

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

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

A decrease in assumed mortality rates of 1 per cent would decrease pre-tax profits by approximately £19m (2014: £27m). A decrease in renewal expenses (excluding asset management expenses) of 5 per cent would increase pre-tax profits by £11m (2014: £10m). 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 £7m (2014: £13m). This analyses has been determined by varying the relevant assumption as at the reporting date while holding all other assumptions constant.

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 future expected shareholder transfers.

F. Liquidity Risk

As described in section B 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.

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

2015	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total un- discounted cashflows	Total carrying value
Financial Liabilities	£m	£m	£m	£m	£m	£m	£m	£m	£m
Amounts owed to credit institutions	3	11	19	7	6	20	—	66	66
Other borrowings not owed to credit institutions	5	170	—	—	—	—	—	175	175
	8	181	19	7	6	20	0	241	241

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2014	1 year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total undiscounted cashflows	Total carrying value
Financial Liabilities	£m	£m	£m	£m	£m	£m	£m	£m	£m
Amounts owed to credit institutions	3	17	16	12	9	6	—	63	63
Other borrowings not owed to credit institutions	5	65	—	—	—	—	—	70	70
	8	82	16	12	9	6	0	133	133

ii) Maturity analysis of derivatives and investment contracts

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

2015	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	(193)	(193)	—	—	—	(193)

2014	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	754	754	—	—	—	754

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

	2015	2014
	£m	£m
Derivative assets (note 15)	1,234	1,714
Derivative liabilities (note 15 and note 23)	(1,427)	(960)
Net derivative position	(193)	754

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.

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 undiscounted value	Total carrying value
	£bn	£bn		£bn	£bn	£bn	£bn	£bn
2015								
Life assurance investment contracts	5	19	18	13	9	8	72	49
2014								
Life assurance investment contracts	6	20	19	14	10	9	78	46

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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 below.

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:

2015	With-profits business			Other			Ex-PAL Business
	Insurance contracts	Investment contracts	Total	Insurance contracts	Investment contracts	Total	Insurance contracts
	%	%	%	%	%	%	%
0-5 years	36	39	38	32	35	35	33
5-10 years	23	27	25	24	23	23	25
10-15 years	15	17	16	16	17	16	18
15-20 years	10	10	10	11	12	11	11
20-25 years	7	4	5	7	7	7	6
Over 25 years	9	3	6	10	6	8	7

2014	With-profits business			Other			Ex-PAL Business
	Insurance contracts	Investment contracts	Total	Insurance contracts	Investment contracts	Total	Insurance contracts
	%	%	%	%	%	%	%
0-5 years	36	39	38	30	35	32	30
5-10 years	23	26	24	23	23	22	25
10-15 years	15	17	16	17	16	17	18
15-20 years	11	10	11	12	11	12	12
20-25 years	7	5	6	8	8	8	7
Over 25 years	8	3	5	10	7	9	8

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.

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 interest rate, currency, credit and other business risks.

The Company uses various interest rate derivative instruments such as interest rate swaps 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.

The Company also holds interest-rate sensitive investments that contain credit risks on which a certain level of defaults is expected. The Company purchases swaptions in order to manage the default risk on certain underlying assets and hence reduce the amount of regulatory capital held to support the assets.

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All over-the-counter derivative transactions are conducted under standardised ISDA (International Swaps and Derivatives Association Inc) master agreements and 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 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 Pillar II solvency and 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 bucketed interest rate exposure) representing the liabilities has been determined, based on characteristics of the with-profits liability. The Company deals in an appropriate amount of hedging instruments so that movements in the instruments held reflect movements in the benchmark put options representing the liabilities. The actual and required hedging positions are monitored at least monthly, and the 1-month Value at Risk between the assets and benchmark is calculated. If this amount is significant, then an assessment is made as to whether or not to address the balance, and how much to rebalance. Automatic rebalancing is triggered if the monthly Value at Risk position of the hedges exceed the agreed threshold.

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 and it was extended in 2015. The effect in 2015 is an unrealised gain of £29m (2014: unrealised gain of £4m) and a realised loss of £36m (2014: realised loss of £34m) charged to the non-technical account.

30. Capital Requirements and Management

Up to 31 December 2015, UK insurers, regulated by the PRA, had to hold capital resources equal at least to the Minimum Capital Requirement (MCR) under the Solvency I basis. In addition the rules required insurers to perform Individual Capital Assessments. Under these rules insurers assessed for themselves the amount of capital needed to back their business. If the PRA viewed the results of this assessment as insufficient, it might draw up its own Individual Capital Guidance for a firm, which could be superimposed as a requirement. These requirements were replaced by the Solvency II regime on 1 January 2016 which is discussed further in the Strategic Report.

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

Under PRA Solvency I rules, insurers with with-profits liabilities of more than £500m must hold capital equal to the higher of the MCR and the Enhanced Capital Requirement (the "ECR"). The ECR is intended to provide a more risk responsive and "realistic" measure of a with-profit insurer's capital requirements, whereas the MCR is broadly speaking equivalent to the previous required minimum margin under the Interim Prudential Sourcebook and satisfies the minimum EU Standards.

Determination of the ECR involves the comparison of two separate measurements of the firm's resources requirement, which the PRA refers to as the "twin peaks" approach. The two separate peaks are:

- (i) the requirement comprised by the mathematical reserves plus the "Long-Term Insurance Capital Requirement" (the "LTICR"), together known as the "regulatory peak"; and
- (ii) a calculation of the "realistic" present value of the insurer's expected future contractual liabilities together with projected "fair" discretionary bonuses to policyholders, plus a risk capital margin, together known as the "realistic peak".

Available capital of the WPSF and SAIF and DCPSF of £7.6bn (2014: £7.2bn) represents the excess of assets over liabilities on the PRA realistic basis. Unlike the previously discussed FRS 103 basis, realistic liabilities on the regulatory basis include the shareholders' share of future bonuses. These amounts are shown before deduction of the risk capital margin (RCM) which is £1.1bn (2014: £1.0bn) at 31 December 2015.

The PRA's basis of setting the RCM is to target a level broadly equivalent to a Standard & Poor's credit rating of BBB and to judge this by ensuring there are sufficient assets to absorb a 1 in 200 year event. The RCM calculation achieves this by setting rules for the determination of margins to cover defined stress changes in asset values and yields for market risk, credit risk and termination risk for with-profits policies.

The Company has discretion in its management actions in the case of adverse investment conditions. Management actions encompass, but are not confined to, investment allocation decisions, levels of reversionary bonuses, crediting rates and total claim values. To illustrate the flexibility of management actions, rates of regular bonus are

Notes on the financial statements (continued)

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

When target bonus levels change, the Company's board has regard to the overall financial strength of the long-term fund when determining the length of time over which it will seek to achieve the amended product target bonus level.

In normal investment conditions, the Company expects changes to regular bonus rates to be gradual over time and changes are not expected to exceed one per cent per annum over any year. However, discretion is retained as to whether or not a regular bonus is declared each year, and there is no limit on the amount by which regular bonus rates can be changed.

As regards smoothing of maturity and death benefits, in normal circumstances the Company does not expect most pay-out values on policies of the same duration to change by more than 10 per cent up or down from one year to the next, although some larger changes may occur to balance pay-out values between different policies. Greater flexibility may be required in certain circumstances, for example following a significant rise or fall in market values (either sudden or over a period of years) and in such situations the Company's board may decide to vary the standard bonus smoothing limits to protect the overall interests of policyholders.

For surrender benefits, any substantial fall in the market value of the assets of the with-profits sub-fund would lead to immediate changes in the application of Market Value Reductions (MVRs) for accumulating with-profits policies, firstly to increase the size of MVRs already being applied and, secondly, to extend the range of policies for which an MVR is applied.

Non-Profit Sub-Fund

The available capital of £490m (2014: £194m) reflects the excess of regulatory basis assets over liabilities of the Company. The regulatory capital resources requirement of £499m (2014: £491m) is covered in part (as is permitted by the PRA Regulations) by assets in the shareholder funds. The available capital and capital resources requirement is monitored during the year. In addition, a realistic assessment of available capital and capital requirements sufficient to cover a 1 in 200 year event is undertaken. Additional capital is sought from the parent company as necessary.

The capital requirement required by regulation was maintained during the year.

The Company's capital position for life assurance business with reconciliations to shareholders' funds is shown below. Available capital for each fund is determined by reference to the PRA regulations at 31 December 2015 and 2014.

Transferability of available capital

Up until 31 December 2015, under Solvency I basis for PAC and all other UK long-term insurers, long-term business assets and liabilities must, by law, be maintained in funds separate from those for the assets and liabilities attributable to non-life insurance business or to shareholders. Only the 'established surplus', the excess of assets over liabilities in the long-term fund determined through a formal valuation, may be transferred so as to be available for other purposes. Distributions from the with-profits sub-fund to shareholders reflect the shareholders' one-ninth share of the cost of declared policyholders' bonuses.

Any excess of assets over liabilities of the PAC with-profits fund is retained within that fund. The retention of the capital enables it to support with-profits and other business of the fund by, for example, providing the benefits associated with smoothing and guarantees. It also provides investment flexibility for the fund's assets by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies.

For other UK long-term business subsidiaries, the amounts retained within the companies are at levels which provide an appropriate level of capital strength in excess of the regulatory minimum.

Notes on the financial statements (continued)

The concept of long-term fund as described above was abolished under the Solvency II regime, which came into effect on 1 January 2016. The PAC with-profits funds will still fall to be treated as a ring-fenced structure under the new regime. Therefore the consideration of an "established surplus" that needs to be formally transferred no longer exists. However companies as a whole will be required to meet the new capital requirements. Further information on the Solvency II capital requirements is provided in the Strategic Report.

31 December 2015							
	SAIF	WPSF and DCPSF	Total with-profits fund	Non-profit sub-fund	Total life assurance	Shareholders' funds	Company total
	£m	£m	£m	£m	£m	£m	£m
Shareholders' funds							
Held outside long-term funds							
Net assets	—	—	—	—	—	9,533	9,533
Goodwill	—	—	—	—	—	—	—
Total	—	—	—	—	—	9,533	9,533
Held in long-term funds (note i)	—	—	—	960	960	—	960
Total shareholders' funds	—	—	—	960	960	9,533	10,493
Adjustments to regulatory basis							
Funds for future appropriation (note ii)	—	10,730	10,730	29	10,759		
Shareholders' share of realistic liabilities	—	(2,346)	(2,346)	—	(2,346)		
Deferred acquisition costs of non-participating business and intangible assets (distribution rights and licence) not recognised for regulatory reporting purposes	—	(4)	(4)	(89)	(93)		
Adjustment from FRS17 basis pension surplus attributable to WPSF to pension liability for regulatory purposes	—	(125)	(125)	—	(125)		
Valuation difference on non-profit annuity liabilities	—	(113)	(113)	—	(113)		
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis) (note iii)	—	(554)	(554)	(410)	(964)		
Total adjustments	—	7,588	7,588	(470)	7,118		
Total available capital resources of life assurance businesses on PRA regulatory bases		7,588	7,588	490	8,078		

Notes on the financial statements (continued)

31 December 2014							
	SAIF	WPSF and DCPSF	Total with-profits fund	Non-profit sub-fund	Total life assurance	Shareholders' funds	Company total
	£m	£m	£m	£m	£m	£m	£m
Shareholders' funds							
Held outside long-term funds							
Net assets	—	—	—	—	—	8,241	8,241
Goodwill	—	—	—	—	—	—	—
Total	—	—	—	—	—	8,241	8,241
Held in long-term funds (note i)	—	—	—	692	692	—	692
Total shareholders' funds	—	—	—	692	692	8,241	8,933
Adjustments to regulatory basis							
Funds for future appropriation (note ii)	—	10,433	10,433	43	10,476		
Shareholders' share of realistic liabilities	—	(2,503)	(2,503)	—	(2,503)		
Deferred acquisition costs of non-participating business and intangible assets (distribution rights and licence) not recognised for regulatory reporting purposes	—	(7)	(7)	(114)	(121)		
Adjustment from FRS17 basis pension surplus attributable to WPSF to pension liability for regulatory purposes	—	(51)	(51)	—	(51)		
Valuation difference on non-profit annuity liabilities	—	(251)	(251)	—	(251)		
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis) (note iii)	—	(462)	(462)	(427)	(889)		
Total adjustments	—	7,159	7,159	(498)	6,661		
Total available capital resources of life assurance businesses on PRA regulatory bases		7,159	7,159	194	7,353		

Notes

- (i) The term shareholders' funds held in long-term funds refers to the excess of assets over liabilities attributable to shareholders of funds which are required by law to be maintained with segregated assets and liabilities.
- (ii) Other adjustments to shareholders' funds and funds for future appropriation include amounts for the value of non-participating business for with-profits funds, deferred tax, admissibility and other items measured differently on the regulatory basis.
- (iii) Included insurance business accounted for as financial instruments under FRS102.11.

Notes on the financial statements (continued)

31. Transition to FRS 102

This is the first year that the Company has presented its results under FRS 102 and FRS 103. The last financial statements under UK GAAP were for the year ended 31 December 2014. The date of transition to FRS 102 was 1 January 2014. Set out below are the changes in accounting policies which reconcile profit for the financial year ended 31 December 2014 and the total equity as at 1 January 2014 and 31 December 2014 between UK GAAP as previously reported and FRS 102.

Profit for the financial year		2014	
		£m	£m
UK GAAP - As previously reported			530
Revaluation of investments in shareholder subsidiaries	A	4,127	
Investment income from land and buildings	B	(16)	
Unrealised gains on investments	B	16	
Unrealised gains on investments	D	(19)	
Transfer from the fund for future appropriations	D	19	
		<hr/>	
FRS 102			4,657

Other comprehensive income		2014	
			£m
UK GAAP - As previously reported			3,854
Revaluation of investments in shareholder subsidiaries	A		(4,122)
Revaluation of company-occupied property	D		19
Transfer (to) the fund for future appropriations	D		(19)
			<hr/>
FRS 102			(268)

Notes on the financial statements (continued)

Balance Sheet		1 January 2014			31 December 2014		
		UK GAAP As previously reported £m	Effect of transition £m	FRS 102 £m	UK GAAP As previously reported £m	Effect of transition £m	FRS 102 £m
ASSETS							
		147	—	147	51	—	51
Intangible assets							
Land and buildings	B, C	6,315	9	6,324	7,762	(9)	7,753
Investment in group undertakings and participating interests	A	6,284	20	6,304	10,651	25	10,676
Other financial investments		93,475	—	93,475	93,258	—	93,258
Deposits with ceding undertakings		6,949	—	6,949	4,755	—	4,755
Assets held to cover linked liabilities		13,060	—	13,060	12,254	—	12,254
Reinsurers' share of technical provisions		13,469	—	13,469	15,465	—	15,465
Debtors		1,377	—	1,377	1,289	—	1,289
Other assets		1,246	—	1,246	1,075	—	1,075
Accrued interest and rent		691	—	691	669	—	669
Deferred acquisition costs		182	—	182	70	—	70
Accrued external dividends receivable		39	—	39	38	—	38
Other prepayments and accrued income	B	133	88	221	130	72	202
Pension asset	E	23	6	29	15	4	19
Total assets		143,390	123	143,513	147,482	92	147,574
LIABILITIES							
Share capital		330	—	330	330	—	330
Revaluation reserve	A	2,085	(2,085)	—	6,211	(6,211)	—
Other reserves		536	—	536	536	—	536
Profit and loss account	A	1,983	2,105	4,088	1,831	6,236	8,067
Fund for future appropriations		12,043	—	12,043	10,476	—	10,476
Technical provisions		103,557	—	103,557	103,816	—	103,816
Technical provisions for linked liabilities		18,051	—	18,051	17,253	—	17,253
Deferred taxation	E	682	6	688	715	4	719
Obligations under finance leases	C	—	97	97	—	63	63
Other		49	—	49	49	—	49
Deposits received from reinsurers		137	—	137	1,360	—	1,360
Creditors		3,836	—	3,836	4,789	—	4,789
Accruals and deferred income		101	—	101	116	—	116
Total liabilities		143,390	123	143,513	147,482	92	147,574

Notes on the financial statements (continued)

A. Revaluation of investments in shareholder subsidiaries

Under previous UK GAAP the revaluation of investments in shareholder subsidiaries was taken to the Statement of Total Recognised Gains and Losses. Under FRS 102 the same accounting treatment must be applied to each class of investments. As the revaluation of investments in subsidiaries held in the long-term fund is required to be taken to the profit and loss account under Schedule 3 of the Regulations then the revaluation of the investments in shareholder subsidiaries must also be taken to the profit and loss account. The unrealised gains/(losses) on investments in shareholder subsidiaries will be shown in the non-technical account.

B. Reclassification of lease incentives

Under previous UK GAAP lease incentives, including rent free periods, were spread over the shorter of the lease period or the period to when the rental was set to a fair market rent. FRS 102 requires that such incentives be spread over the lease period. This adjustment is reclassifying the lease incentives amounts from within the carrying value of land and buildings to accrued income in the balance sheet and investment income to unrealised gains in the profit and loss account.

C. Reclassification of obligations under finance leases

The Company has land and buildings which are held under finance leases. Under the previous UK GAAP the finance lease obligation was not separately disclosed on the face of the balance sheet but was incorporated within the carrying value. On transition to FRS 102 the Company's obligations under finance leases have been reclassified from land and buildings to separate obligations under finance leases line item on the balance sheet. There is no effect on equity as it is a balance sheet reclassification.

D. Revaluation of company-occupied property

Under previous UK GAAP, for insurance companies, the revaluation of company-occupied property was taken to the profit and loss account. Under FRS 102 gains arising on revaluation are recognised in other comprehensive income and accumulated in equity. Losses arising on revaluation are recognised in the profit and loss account except to the extent that they reverse a previously recognised gain accumulated in equity. The unrealised gains on revaluation of company-occupied property have been reclassified from unrealised gains in the long-term business technical account to other comprehensive income. There is no impact on profit as there is a corresponding adjustment to the transfer to the fund for future appropriations.

E. Reclassification of deferred tax on pension asset

Under previous UK GAAP the deferred tax liability arising on the pension asset was offset against the pension asset on the balance sheet. Under FRS 102 the deferred tax liability arising on the pension asset is now included within deferred taxation on the balance sheet. There is no effect on equity as it is a balance sheet reclassification.

32. Related Undertakings

On 6 April 2015 "The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015" came into force and are effective for financial years beginning on or after 1 January 2016. Notwithstanding this effective date, the exemption available under the Act to only list the principal subsidiary undertakings of the Company is no longer available for accounts approved on or after 1 July 2015.

The following is a list of related undertakings of the Company at 31 December 2015.

(i) Direct subsidiary undertakings

Name	Classes of Shares held	Proportion held	Country of Incorporation
Carroway Guildford General Partner Limited	Ordinary Shares	100%	United Kingdom
Central Square Leeds Limited	Ordinary Shares	100%	United Kingdom
Cribbs Mall Nominee (1) Limited	Ordinary Shares	100%	United Kingdom
Edger Investments Limited	Ordinary Shares	100%	United Kingdom

Notes on the financial statements (continued)

Name	Classes of Shares held	Proportion held	Country of Incorporation
Empire Holding S.a.r.l. (in liquidation)	Ordinary Shares	100%	Luxembourg
Euro Salas Properties Limited	Ordinary Shares	100%	United Kingdom
Greenpark (Reading) Limited Partnership (The)	Limited Partnership Interest	100%	United Kingdom
LIPP S.à r.l. (in liquidation)	Ordinary Shares	100%	Luxembourg
Manchester Nominee (1) Limited	Ordinary Shares	100%	United Kingdom
MM&S (2375) Limited (In liquidation)	Ordinary Shares	100%	United Kingdom
NAPI REIT, Inc.	Ordinary Shares	99%	USA
Oaktree Business Park Limited	Ordinary Shares	12.5%	United Kingdom
Optimus Point Management Company Limited	Ordinary Shares	99.95%	United Kingdom
Pacus (UK) Limited	Ordinary Shares	100%	United Kingdom
PPMC First Nominees Limited	Ordinary Shares	100%	United Kingdom
Prudential Annuities Limited (In liquidation)	Ordinary Shares	100%	United Kingdom
Prudential Corporate Pensions Trustee Limited	Ordinary Shares	100%	United Kingdom
Prudential Dublin Investment Ltd	Ordinary Shares	100%	Ireland
Prudential General Insurance Hong Kong Limited	Ordinary Shares	100%	Hong Kong
Prudential Holborn Life Limited	Ordinary Shares	100%	United Kingdom
Prudential Hong Kong Limited	Ordinary Shares	100%	Hong Kong
Prudential International Assurance plc	Ordinary Shares	100%	Ireland
Prudential International Management Services Limited	Ordinary Shares	100%	Ireland
Prudential Investments (Luxembourg) 2 S.à r.l.	Ordinary shares	100%	Luxembourg
Prudential Lifetime Mortgages Limited	Ordinary Shares	100%	United Kingdom
Prudential Pensions Limited	Ordinary Shares	100%	United Kingdom
Prudential Properties Trusty Pty Limited	Unclassified Shares	100%	Australia
Prudential Property Investments Limited	Ordinary Shares	100%	United Kingdom
Prudential Real Estate Investments 2 Limited	Ordinary Shares	100%	United Kingdom
Prudential Real Estate Investments 3 Limited	Ordinary Shares	100%	United Kingdom
Prudential Retirement Income Limited	Ordinary Shares	100%	United Kingdom
Prutec Limited	Ordinary Shares	100%	United Kingdom
PVM Partnerships Limited	Ordinary Shares	100%	United Kingdom
Scottish Amicable Finance plc	Ordinary Shares	100%	United Kingdom
Scottish Amicable ISA Managers Limited (In liquidation)	Ordinary Shares	100%	United Kingdom
Scottish Amicable Life Assurance Society	No Share Capital	100%	United Kingdom
Sealand (No 1) Limited	Ordinary Shares	100%	Jersey
Sealand (No 2) Limited	Ordinary Shares	100%	Jersey
Smithfield Limited	Ordinary Shares	100%	United Kingdom
The Forum, Solent, Management Company Limited	Ordinary Shares	100%	United Kingdom
The Green (Solihull) Management Company Ltd	Ordinary shares	100%	United Kingdom
The Hub (Witton) Management Company Limited	Ordinary Shares	100%	United Kingdom

Notes on the financial statements (continued)

Name	Classes of Shares held	Proportion held	Country of Incorporation
Two Snowhill Birmingham s.a.r.l.	Ordinary shares	100%	Luxembourg
Warren Farm Office Village Limited	Ordinary Shares	100%	United Kingdom
Wessex Gate Limited	Ordinary Shares	100%	United Kingdom
Westwacker Limited	Ordinary Shares	100%	United Kingdom

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

Name	Classes of Shares held	Proportion held	Country of Incorporation
AGR Holdco Ltd	Ordinary Shares	43.06%	United Kingdom
Bracknell Boulevard Management Company Limited	Ordinary Shares	29.1%	United Kingdom
BWAT Retail Nominee (1) Limited	Ordinary Shares	50%	United Kingdom
BWAT Retail Nominee (2) Limited	Ordinary Shares	50%	United Kingdom
Calera Capital Partners IV - A AIV I, L.P.	Limited Partnership Interest	32.87%	USA
Carraway Guildford (Nominee A) Limited	Ordinary Shares	100%	Jersey
Carraway Guildford (Nominee B) Limited	Ordinary Shares	100%	Jersey
Carraway Guildford Investments Unit Trust	Units	100%	Jersey
Carraway Guildford Limited Partnership	Limited partnership interest	100%	United Kingdom
CCC Investment S.a.r.l.	Ordinary Shares	52.24%	Luxembourg
Centaurus Retail LLP	Limited Partnership Interest	50%	United Kingdom
Centre Capital Non-Qualified Investors IV AIV Orion, L.P.	Membership Interest	45.77%	USA
Centre Capital Non-Qualified Investors IV AIV-ELS, L.P.	Membership Interest	45.92%	USA
Centre Capital Non-Qualified Investors IV AIV-RA, L.P.	Membership Interest	34.16%	USA
Centre Capital Non-Qualified Investors IV, L.P.	Membership Interest	45.67%	USA
Centre Capital Non-Qualified Investors V AIV-ELS LP	Membership Interest	36.58%	USA
Centre Capital Non-Qualified Investors V LP	Membership Interest	33.74%	USA
CF European Qualified Investor Scheme	Ordinary Shares	91.08%	United Kingdom
CF Japanese Qualified Investor Scheme	Ordinary Shares	86.92%	United Kingdom
CF North American Qualified Investor Scheme	Ordinary Shares	70.94%	United Kingdom
CF Prudential Pacific Markets Trust Fund	Ordinary Shares	88.78%	United Kingdom
CF UK Growth Qualified Investor Scheme	Ordinary Shares	65.78%	United Kingdom
Cimbria Holdings Limited	Ordinary Shares	41.78%	Denmark
Creatrade Luxembourg S.a.r.l	Ordinary Shares	52.27%	Luxembourg
Cribbs Causeway JV Limited	Ordinary Shares	50%	United Kingdom
Cribbs Causeway Merchants Association Ltd	Limited by Guarantee		United Kingdom
Daisy 2015 Topco Limited	Ordinary Shares	24.08%	United Kingdom
Eastspring Investments - Asia Pacific Equity Fund	Ordinary Shares	24.44%	Luxembourg
Eastspring Investments Asian Bond Fund	Ordinary Shares	30.27%	Luxembourg
Fee Retail S.a.r.l	Ordinary Shares	52.24%	Luxembourg
Foudry Properties Limited	Ordinary Shares	50%	United Kingdom
Harvest Partners V, L.P.	Membership interest	25.13%	USA
Infracapital Partners	Limited partnership interest	33.04%	United Kingdom

Notes on the financial statements (continued)

Name	Classes of Shares held	Proportion held	Country of Incorporation
Infracapital Partners II LP	Limited partnership interest	25.98%	United Kingdom
Ivy TopCo Limited	ordinary Shares	35.43%	Guernsey
Jefferies Capital Partners V, L.P.	Limited Partnership Interest	21.92%	USA
JNL PPM America Strategic Income Fund	Ordinary Shares	100%	USA
Kalle Luxembourg S.a.r.l.	Ordinary Shares	37.74%	Luxembourg
Lion Credit Opportunity Fund III	Ordinary Shares	29.1%	Ireland
Lion Credit Opportunity Fund XII	Ordinary Shares	38.94%	Ireland
M&G Asia Property Fund	Ordinary Shares	34.06%	Luxembourg
M&G Dividend Fund	Ordinary Shares	53.36%	United Kingdom
M&G Emerging Markets Bond Fund	Ordinary Shares	46.36%	United Kingdom
M&G Episode Defensive Fund	Ordinary Shares	93.72%	United Kingdom
M&G Episode Macro Fund	Ordinary Shares	58.38%	United Kingdom
M&G European Credit Investments Fund	Ordinary Shares	100%	Luxembourg
M&G European High Yield Credit Investments Fund	Ordinary Shares	100%	Luxembourg
M&G European Property Fund	Ordinary Shares	38.23%	Luxembourg
M&G European Select Fund	Ordinary Shares	31.39%	United Kingdom
M&G Global Corporate Bond Fund	Ordinary Shares	79.34%	United Kingdom
M&G Global Credit Investments Fund	Ordinary Shares	100%	Luxembourg
M&G Managed Growth Fund	Ordinary Shares	21.94%	United Kingdom
M&G Pan European Dividend Fund	Ordinary Shares	25.75%	United Kingdom
M&G Property Portfolio Feeder	Ordinary Shares	26.61%	United Kingdom
M&G Real Estate Debt Fund LP	Limited partnership interest	29.15%	Guernsey
M&G Traditional Credit Fund	Ordinary Shares	40.24%	Ireland
M&G UK Companies Financing Fund II LP	Limited partnership interest	48.32%	United Kingdom
Manchester JV Limited	Ordinary Shares	50%	United Kingdom
NB Distressed Debt	New Global Shares	25.66%	Guernsey
Orizon Luxembourg S.a.r.l	Ordinary Shares	78.49%	Luxembourg
Phase One Imaging Holdings Ltd	Ordinary Shares	30.54%	United Kingdom
Property Partners (Two Rivers) Limited	Ordinary Shares	50%	United Kingdom
Prudential Development Management Limited	Ordinary Shares	100%	United Kingdom
Prudential Dynamic 10-40 Portfolio	Ordinary Shares	24.75%	United Kingdom
Prudential Dynamic 20 - 55 Portfolio	Ordinary Shares	31%	United Kingdom
Prudential Dynamic 40-80 Portfolio	Ordinary Shares	32.98%	United Kingdom
Prudential Dynamic 60-100 Portfolio	Ordinary Shares	33.86%	United Kingdom
Prudential Dynamic Focused 0-30 Portfolio	Ordinary Shares	61.28%	United Kingdom
Prudential Dynamic Focused 10-40 Portfolio	Ordinary Shares	65.29%	United Kingdom
Prudential Dynamic Focused 20 - 55 Portfolio	Ordinary Shares	42.2%	United Kingdom
Prudential Dynamic Focused 40-80 Portfolio	Ordinary Shares	86.96%	United Kingdom
Prudential Dynamic Focused 60-100 Portfolio	Ordinary Shares	94.18%	United Kingdom
Prudential Equity Release Mortgages Limited	Ordinary Shares	100%	United Kingdom
Prudential Europe Assurance Holdings Limited (In liquidation)	Ordinary Shares	100%	United Kingdom
Prudential Greenfield LP	Limited partnership interest	100%	United Kingdom

Notes on the financial statements (continued)

Name	Classes of Shares held	Proportion held	Country of Incorporation
Prudential M&G UK Companies Financing Fund LP	Limited partnership interest	34.42%	United Kingdom
Prudential Real Estate Investments 1 Limited	Ordinary Shares	100%	United Kingdom
Prudential Vietnam Finance Company Limited	Ownership Interest	100%	Vietnam
SBP Management Limited	Ordinary Shares	27.7%	United Kingdom
Scottish Amicable PEP and ISA Nominees Limited (In liquidation)	Ordinary Shares	100%	United Kingdom
SES Manager Limited	Ordinary shares	50%	United Kingdom
St Edward Homes Limited	Ordinary Shares	100%	United Kingdom
The Heights Management Company Limited	Ordinary Shares	50%	United Kingdom
The St Edward Homes Partnership	Limited Partnership Interest	49.95%	United Kingdom
The Strand Property Unit Trust	Units	50%	Jersey
The Two Rivers Trust	Units	50%	Jersey
Wynnefield Private Equity Partners II, LP	Limited Partnership Interest	99%	USA

33. Domestication of the Hong Kong Branch

On 1 January 2014, following consultation with the Company's policyholders, the regulators and court approval, the entire business of the Hong Kong branch was transferred to two new Hong Kong-incorporated companies, both subsidiaries of the Company, one providing life insurance and the other providing general insurance - Prudential Hong Kong Limited (PHKL) and Prudential General Insurance Hong Kong Limited (PGHK) respectively. The purpose of the transfer was to better align the legal entity structure with the Prudential Group's management structure.

The two subsidiaries, PHKL and PGHK, issued shares to the Company. The transfer of the assets and liabilities was at carrying value as at the transfer date and as such there is no goodwill. In addition, to maintain the reasonable benefit and security expectations of the with-profits policies transferring to PHKL, a portion of the inherited estate of the Company, £1,701m, was also transferred on the transfer date. This movement is shown on the Long-term Business Technical Account as "Other technical charges".

Following the transfer of the Hong Kong branch in 2014 the returns from these operations are now reported in the non-technical account as dividends received, or in the non-technical account as a revaluation of the investment in the subsidiaries, rather than on a line-by-line basis. In the balance sheet for 2014 there was a reduction in the value of gross assets and liabilities as the balance sheet now only records the value of the Hong Kong operations in investments in group undertakings and a corresponding value within shareholders equity as opposed to the gross assets and liabilities of the underlying insurance operations.

34. Acquisition and disposal of material subsidiaries and participating interests

On 9 November 2015 Prudential Annuities Limited, a wholly owned subsidiary of the Long-term fund went into liquidation. The original cost was £648m.

On 18 December 2015 as part of a restructuring arrangement Prudential Europe Assurance Holdings Limited (PEAH) and MM&S subsidiaries owned by the Shareholder fund went into liquidation. The original cost was £40m. The companies paid dividends of £210m satisfied by the transfer of ownership PIA and PIMS companies previously owned by PEAH. The companies were transferred to PAC at a fair value of £195m.

On 14 November 2014 the Company sold its 25% equity stake in the PruHealth and PruProtect businesses to Discovery Group Europe Limited for £155m. The profit on disposal was £61m. The profit was calculated as the difference between the proceeds of £155m less transaction costs of £3m and future costs provided of £2m and the revalued amount at the date of disposal of £89m.

