As filed with the Securities and Exchange Commission on June 1, 2001

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2000

Commission File Number: 1-15040

PRUDENTIAL PUBLIC LIMITED COMPANY

(Exact Name of Registrant as Specified in its Charter)

England and Wales
(Jurisdiction of Incorporation)

Laurence Pountney Hill,
London EC4R 0HH, England
(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
American Depositary Shares, each representing 2 Ordinary Shares, 5 pence par value each	New York Stock Exchange
Ordinary Shares, 5 pence par value each	New York Stock Exchange*

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

The number of outstanding shares of each of the issuer's classes of capital or common stock as of December 31, 2000 was:

1,981,406,182 Ordinary Shares, 5 pence par value each

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes X No ____

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 ____ Item 18 X

* Not for trading, but only in connection with the registration of American Depositary Shares.

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Item 3. Key Information

SELECTED HISTORICAL FINANCIAL INFORMATION OF PRUDENTIAL

The following table sets forth Prudential's selected consolidated financial data for the periods indicated. This data is derived from Prudential's audited consolidated financial statements prepared in accordance with UK GAAP under which insurance business is accounted for on the modified statutory basis (MSB). These accounting principles differ in certain significant respects from US GAAP. The Prudential audited consolidated financial statements included elsewhere in this document include a description of the differences between UK GAAP and US GAAP that are significant to the financial statements. This table is only a summary and you should read it in conjunction with Prudential's consolidated financial statements, the related notes and "Operating and Financial Review and Prospects" included elsewhere in this document.

The profit and loss account and balance sheet data for and as at the years ended December 31, 1996 to 2000 have been derived from Prudential's audited consolidated financial statements and have been restated to reflect accounting policies adopted by Prudential in the year ended December 31, 2000. The consolidated financial statements for the three years ended December 31, 1998 have been audited by PricewaterhouseCoopers, or its predecessor Price Waterhouse, and for the two years ended December 31, 2000 by KPMG Audit Plc.

	Year Ended December 31,					
	2000[1]	**2000**	**1999**	**1998**	**1997**	**1996**
	(In $ Millions)			**(In £ Millions)**		
Profit and loss account data—UK GAAP basis						
Gross premiums from continuing operations including acquisitions:						
— Long-term business	**21,118**	**14,173**	14,826	10,640	9,641	8,653
— General business	**496**	**333**	318	310	306	303
	21,614	**14,506**	15,144	10,950	9,947	8,956
Gross premiums from discontinued operations:						
— Long-term business	**—**	**—**	—	423	665	1,930
— General business	**—**	**—**	—	—	—	304
	—	**—**	—	423	665	2,234
Reinsurance and change in unearned premiums	**(194)**	**(130)**	(91)	(87)	(72)	(323)
Total earned premiums, net of reinsurance	**21,420**	**14,376**	15,053	11,286	10,540	10,867
Investment returns	**7,519**	**5,046**	17,232	12,612	12,134	7,758
Operating profit before amortization of goodwill and tax[2]						
Continuing operations:						
UK operations	**702**	**471**	452	394	421	373
US operations	**694**	**466**	451	411	367	328
Asian operations	**33**	**22**	15	13	11	12
European operations	**(15)**	**(10)**	6	4	1	—
Group activities	**(162)**	**(109)**	(78)	38	34	(55)
UK restructuring	**—**	**—**	(70)	—	—	—
Continuing operations	**1,252**	**840**	776	860	834	658
Discontinued operations[3]	**—**	**—**	—	8	30	196
Operating profit before amortization of goodwill and tax[4]	**1,252**	**840**	776	868	864	854
Short term fluctuations in investment returns[5]	**(72)**	**(48)**	28	24	83	(37)
Amortization of goodwill	**(125)**	**(84)**	(54)	—	—	—
Profit on flotation of Egg and business disposals	**356**	**239**	—	249	18	797
Reclassification of shareholder reserves of Australian operation[6]	**—**	**—**	—	—	204	—
Total profit on ordinary activities before tax	**1,411**	**947**	750	1,141	1,169	1,614
Profit after tax:						
Operating profit (including post-tax longer term investment returns)	**919**	**617**	567	654	618	636
Profit for the period (including post-tax actual investment returns)	**1,025**	**688**	542	880	837	1,407

	Year Ended December 31,					
	2000[1]	2000	1999	1998	1997	1996
	(In $ Millions)	(In £ Millions)				
Statement of income and comprehensive income data —US GAAP basis						
Insurance policy revenues	**5,850**	**3,926**	4,899	3,592	3,328	
Investment results	**6,957**	**4,669**	12,793	8,599	10,197	
Non-operating income: Profit on Egg flotation	**177**	**119**	—	—	—	
Other income	**924**	**620**	600	165	431	
Total revenue	**13,908**	**9,334**	18,292	12,356	13,956	
Net income	**748**	**502**	888	801	1,082	
Total comprehensive income	**1,003**	**673**	431	761	1,233	

	At December 31,					
	2000[1]	2000	1999	1998	1997	1996
	(In $ Millions, Except Per Share Information)	(In £ Millions, Except Per Share Information)				
Balance sheet data—UK GAAP basis						
Total assets	**230,876**	**154,950**	150,643	118,786	108,223	78,439
Long-term business provision	**135,667**	**91,052**	84,476	76,760	69,512	51,668
Technical provision for linked liabilities	**27,891**	**18,719**	19,043	9,996	10,167	7,198
Debenture loans	**2,362**	**1,585**	1,546	1,031	820	672
Total shareholders' funds	**5,990**	**4,020**	3,424	3,249	2,783	2,757
Balance sheet data—US GAAP basis						
Total assets	**228,006**	**153,024**	148,922	117,762	108,355	
Policyholder benefit liabilities	**114,299**	**76,711**	71,179	62,878	56,346	
Separate account liabilities	**48,182**	**32,337**	33,477	23,450	22,684	
Total shareholders' equity	**9,618**	**6,455**	6,046	5,997	5,627	
Other data						
Long-term business (including investment products)						
New business from continuing operations:						
Single premiums sales	**19,897**	**13,354**	11,834	7,189	6,780	6,119
New regular premiums sales[7]	**848**	**569**	509	468	487	448
Total	**20,745**	**13,923**	12,343	7,657	7,267	6,567
Funds under management	**245,850**	**165,000**	170,000	128,300	118,700	91,000
Basic earnings per share:						
Based on operating profit from continuing operations before amortization of goodwill and before tax on a UK GAAP basis	**63.9¢**	**42.9p**	39.9p	44.3p	43.2p	34.3p
Based on operating profit before amortization of goodwill and after tax and minority interest on a UK GAAP basis	**46.9¢**	**31.5p**	29.1p	33.7p	32.0p	33.2p
Based on total profit for the financial year after tax on a UK GAAP basis	**52.3¢**	**35.1p**	27.8p	45.3p	43.3p	73.4p
Net income per share on a US GAAP basis	**38.1¢**	**25.6p**	45.6p	41.4p	56.1p	
Diluted earnings per share—UK GAAP	**52.2¢**	**35.0p**	27.7p	45.0p	43.0p	72.8p
Diluted earnings per share—US GAAP	**38.0¢**	**25.5p**	45.3p	41.0p	55.8p	
Dividend per share[8]	**36.5¢**	**24.5p**	23.0p	21.0p	19.1p	17.3p
Equivalent cents per share[8][9]	**—**	**35.0¢**	36.9¢	34.0¢	31.4¢	30.3¢
Market price at end of period	**$ 16.05**	**1,077.0p**	1,220.0p	908.0p	734.0p	492.0p
Share capital	**148**	**99**	98	98	97	96
Number of shares outstanding (in millions)		**1,981**	1,954	1,949	1,939	1,924
Average number of shares (in millions)		**1,959**	1,947	1,942	1,932	1,917

(1) Amounts stated in US dollars have been translated from pounds sterling at the rate of $1.49 per £1.00 (the noon buying rate in New York City on December 31, 2000).

(2) Investment returns credited to operating results for investments attributable to shareholders are determined using the longer term rate of return. For the purposes of determining longer term investment returns, Jackson National Life averages realized investment gains and losses over five years.

(3) Discontinued operations are restated on an annual basis in order that continuing operations reflect those operations which form part of the group as at the most recent year-end date.

(4) Due to the long-term nature of Prudential's business, the basis of presentation of operating profit may not be comparable with other UK companies. See Note 4 of the notes to Prudential's consolidated financial statements for a description of the basis.

(5) Short-term fluctuations in investment returns represent the difference between the longer term return credited to operating profit and the actual investment returns achieved for the year.

(6) Following the introduction of the margin on services basis of financial reporting for Australian life insurers, the allocation between shareholders and policyholders of the life funds of Prudential's Australian operation was clarified by the local supervisory authority. This resulted in a reclassification to shareholders in 1997 of £204 million before tax, which was credited directly to the profit and loss account. Prudential sold its Australian operation in the following year.

(7) New regular business sales are reported above on an annualized basis, which represents a full year of installments in respect of regular premiums irrespective of the actual payments made during the year.

(8) The final dividend with respect to any year is paid in the following year after approval at Prudential's annual general meeting. Final dividends are included in the year to which they relate rather than in the year paid.

(9) Translated into US dollars at the noon buying rate on the dates each payment is made. Annual dividends are comprised of both interim and final dividend payments. The amounts shown represent the annual dividend accrual rather than the cash payments made in each year.

Dividend Data

Prudential's dividend policy is to grow dividends in line with the underlying growth in earnings of its principal businesses, with due regard for its cash and balance sheet position. Future dividends will depend on Prudential's results of operations, financial condition, cash requirements, future prospects and other factors. Under UK company law, Prudential may pay dividends only if "distributable profits" are available for that purpose. "Distributable profits" are accumulated, realized profits not previously distributed or capitalized less accumulated, realized losses not previously written off. Even if distributable profits are available, Prudential pays dividends only if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves (such as, for example, the share premium account and the capital redemption reserve) and the payment of the dividend does not reduce the amount of its net assets to less than that aggregate.

As a holding company, Prudential is dependent upon dividends and interest from its subsidiaries to pay cash dividends. Many of its insurance subsidiaries are subject to regulations that restrict the amount of dividends that they can pay to Prudential. These restrictions are discussed in more detail in Item 4, "Information on the Company—Supervision and Regulation of Prudential—UK Supervision and Regulation—Insurance Regulation—Distribution of Profits".

Historically, Prudential has declared an interim and a final dividend for each year (with the final dividend being paid in the year following the year to which it relates). Subject to the restrictions set out above, Prudential's directors have the discretion to determine whether to pay a dividend and the amount of any such dividend but must take into account the company's financial position.

Under the UK-US Income Tax Treaty, some US holders of Prudential ordinary shares and ADSs are entitled to a UK tax credit, also called the associated UK tax credit, in respect of a dividend from Prudential equal to the tax credit to which UK resident individuals generally are entitled in respect of the dividend. This UK tax credit, however, is subject to a withholding tax under the UK-US Income Tax

Treaty. See Item 10, "Additional Information—Taxation—UK Taxation of Dividends" for a more detailed description of the withholding tax.

The following table shows certain information regarding the dividends that Prudential paid for the periods indicated in pounds sterling and converted into US dollars at the noon buying rate in effect on each payment date. The final dividend with respect to any calendar year is paid in the following calendar year after approval at Prudential's annual general meeting. Interim dividends for a specific year have generally had a record date in September and a payment date in November of that year, and final dividends have generally had a record date in the following March and a payment date in the following May.

Historical Dividend Information

Year	Interim Dividend per Share	Interim Dividend per Share	Final Dividend per Share	Final Dividend per Share
	(pence)	(US Dollars)	(pence)	(US Dollars)
1995	5.3	0.08626	10.4	0.16718
1996	5.8	0.10342	11.5	0.19924
1997	6.4	0.10700	12.7	0.20736
1998	7.0	0.11598	14.0	0.22369
1999	7.7	0.12292	15.3	0.24620
2000	8.2	0.11652	16.3	0.23105

Exchange Rate Information

Prudential publishes its consolidated financial statements in pounds sterling. References in this document to "US dollars", "US$", "$" or "¢" are to US currency and references to "pounds sterling", "£", "pounds", "pence" or "p" are to UK currency (there are 100 pence to each pound). The following table sets forth the average noon buying rate on the last business day of each month, as certified for customs purposes by the Federal Reserve Bank of New York, for pounds sterling expressed in US dollars per pound sterling for each of the five most recent fiscal years. Prudential has not used these rates to prepare its consolidated financial statements.

Year ended December 31,	Average
1996	$1.57
1997	1.64
1998	1.66
1999	1.61
2000	1.50

The following table sets forth the high and low noon buying rates for pounds sterling expressed in US dollars per pound sterling for each of the previous six months:

	High	Low
December 2000	1.50	1.44
January 2001	1.50	1.46
February 2001	1.48	1.44
March 2001	1.47	1.42
April 2001	1.45	1.42
May 2001	1.44	1.41

On May 31, 2001, the noon buying rate in New York City was £1.00 = $1.42.

Forward-Looking Statements

This annual report contains certain "forward-looking statements". All statements regarding Prudential's future financial condition, results of operations and businesses, strategy, plans and objectives are forward-looking. Statements containing the words "believes", "intends", "expects" and words of similar meaning are also forward-looking. Such statements involve unknown risks, uncertainties and other factors that may cause Prudential's results, performance or achievements or conditions in the markets in which it operates to differ from those expressed or implied in such statements. These factors include regulatory changes, technological development, globalization, levels of spending in major economies, the levels of marketing and promotional expenditures, actions of competitors, employee costs, future exchange and interest rates, changes in tax rates and future business combinations or dispositions.

In particular, the following are forward-looking in nature:

- certain statements in Item 4, "Information on the Company" with regard to strategy and management objectives, trends in market shares, prices, market standing and product volumes and the effects of changes or prospective changes in regulation, and
- certain statements in Item 5, "Operating and Financial Review and Prospects" with regard to trends in results, prices, volumes, operations, margins, overall market trends, risk management and exchange rates and with regard to the effects of changes or prospective changes in regulation.

Item 4. Information on the Company

BUSINESS OF PRUDENTIAL

Overview

Prudential is a leading international financial services group, providing retail financial services and fund management in its chosen markets of the United Kingdom, the United States, Asia and continental Europe. At December 31, 2000, Prudential was one of the 20 largest public companies in the United Kingdom in terms of market capitalization on the London Stock Exchange. Prudential is not affiliated with Prudential Insurance Company of America.

Prudential has been writing life insurance in the United Kingdom for over 150 years and has had the largest long-term fund in the United Kingdom for over a century. Prudential began writing property and casualty insurance in 1915, and expanded its business into British Commonwealth countries, including Singapore and Malaysia, in the 1920s and 1930s. In 1986, Prudential acquired Jackson National Life Insurance Company, a US insurance company writing life and fixed annuity business. In 1996, Prudential established its direct banking operations. In 1998, Prudential launched Egg, a leading e-commerce retail financial services provider, and in 1999, Prudential acquired M&G, a leading UK fund manager. In 1999 and 2000, Prudential expanded its operations in Asia and continental Europe. In June 2000, Prudential completed its listing on the New York Stock Exchange and completed an initial public offering of Egg plc on the London Stock Exchange.

In the United Kingdom, Prudential offers a range of retail financial products and services, including long-term insurance and asset accumulation products (life insurance, pensions and pensions annuities), personal lines property and casualty insurance, retail investment and unit trust products, fund management services and banking products. Prudential distributes these products through independent financial advisers, referred to as IFAs, and direct marketing, by telephone, mail and the internet as well as through its company salesforce, which is being phased out.

At December 31, 2000, in the United Kingdom Prudential was:

- the second-largest life insurance company in terms of market capitalization,
- the proprietor of the largest long-term fund of investment assets supporting long-term insurance products,
- a top three mutual fund manager in terms of funds under management,
- a leading e-commerce retail financial services provider, and
- rated AAA by Standard & Poor's in terms of financial strength rating for Prudential Assurance's long-term fund.

In the United States, Prudential offers a range of products through Jackson National Life Insurance Company, including fixed, equity-indexed and variable annuities, life insurance, guaranteed investment contracts and funding agreements. Prudential distributes these products through independent insurance agents, securities broker-dealers and banks, credit unions and other financial institutions. At December 31, 2000, in the United States Jackson National Life was:

- the 20th-largest life insurance company in terms of total assets,
- the fifth-largest provider of individual fixed annuities in terms of sales,
- the third-largest provider of equity-indexed annuities in terms of sales,
- the 20th-largest provider of variable annuities in terms of sales,
- a top ten provider of stable value products in terms of in-force liabilities, and
- rated AAA by Standard & Poor's and A+ by A.M. Best Co. in terms of financial strength rating.

In Asia, Prudential has operations in eleven countries and offers life insurance with health insurance options, personal lines property and casualty insurance and investment products, which it tailors to suit the local markets. Prudential distributes these products primarily through its agency salesforces and through bancassurance arrangements, including Standard Chartered Bank, and through banks and brokers for investment products in India. At December 31, 2000, in Asia, Prudential was:

- the second-largest life insurance company in Singapore, in terms of new weighted premium business,
- the second-largest life insurance company in Malaysia, in terms of new regular premium business,
- the fourth-largest life insurance company in Hong Kong, in terms of new regular premium business,
- one of only two foreign companies licensed to write life insurance in the city of Guangzhou, China, and
- one of only two foreign wholly-owned companies with a license to sell life insurance in Vietnam.

In Europe, Prudential currently offers life insurance and pensions in Germany and a single premium savings product in France. Prudential has also entered into non-exclusive strategic distribution arrangements with leading local distributors in both France and Germany.

Prudential's operating profit before amortization of goodwill and tax for the periods indicated is set forth in the table below.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
Prudential Insurance Services	**346**	378	333
Prudential Financial Services	**28**	36	22
Prudential Intermediary Business	**127**	101	88
M&G	**125**	87	28
Egg	**(155)**	(150)	(77)
Total UK operations	**471**	452	394
US operations	**466**	451	411
Asian operations	**22**	15	13
European operations	**(10)**	6	4
Group activities	**(109)**	(78)	38
UK restructuring	**—**	(70)	—
Continuing operations	**840**	776	860

Strategy

Shareholder Focus

Prudential's commitment to its shareholders is to maximize the value over time of their investment. Prudential has a clear focus on managing for value, which drives how it sets its strategic goals, monitors business performance and incentivises and rewards management. Prudential's aim is to deliver top quartile performance within the FTSE 100 in terms of total shareholder returns. For the three-year period ended December 31, 2000, Prudential's total shareholder return was ranked in the 26th percentile of relevant comparable companies. For the three-year periods ended December 31, 1998 and 1999, Prudential was ranked in the 14th and 9th percentiles, respectively.

Building the Platform

In recent years, the global retail financial services industry has undergone significant change. Changes in underlying demographics, government attitudes, technology and customer demands are all driving fundamental change in the industry. Prudential is determined to deliver superior returns to its shareholders and has therefore fundamentally reconfigured its business to compete more effectively in this changing environment.

In the last five years, Prudential has transformed itself from a business with a narrow product range and limited distribution channel focus to a multi-channel, multi-brand business with a broad product range and a clear retail financial services focus. At the same time, Prudential has withdrawn from those operations or markets that did not meet its target returns or that did not offer the opportunities to achieve critical mass.

Prudential has significantly restructured its traditional insurance operations in both the United Kingdom and the United States to improve customer focus and management accountability and to broaden its product range and distribution reach.

In the United Kingdom, Prudential has restructured its businesses into smaller, more accountable business units with a clear customer and marketing focus and in February 2001 announced its intentions to further restructure its direct salesforce, shifting its focus to alternative distribution channels. Prudential has also acquired Scottish Amicable and M&G Group plc (M&G) to increase its exposure and range of products within the critical independent financial adviser market. The launch of Prudential Banking and Egg has added banking products to Prudential's portfolio and anticipated the growth in customer use of e-commerce.

In the United States, Prudential has significantly diversified its product range and distribution strategy. Prudential has launched and developed its own equity-based, index-linked and stable value product ranges, successfully entered the broker-dealer market and significantly grown its presence in the bank channel.

In Asia, Prudential has expanded its operations from three to eleven countries through a combination of acquisition, corporate ventures and organic initiatives. Prudential has made considerable progress in both growing its more established markets of Hong Kong, Singapore and Malaysia, and establishing itself in its newer markets of India, Taiwan, Vietnam, China and Japan. Prudential is one of only three pan-Asian insurance providers and has a significant presence across the region.

The cost of development initiatives has adversely impacted, and will continue to adversely impact, short-term earnings, but Prudential believes that each of these investments is building long-term shareholder value. This value is clearly demonstrated by the scale and mix of Prudential's new business sales. In 2000, new business inflows exceeded £13.9 billion with over 25% coming from investment product sales, and over 50% coming from outside the United Kingdom.

This transformation has created a strong platform to pursue strategic initiatives for future growth and shareholder value creation.

Growing the Business

Prudential is conscious that the retail financial services industry continues to change, and it expects to continue to adapt its business to build competitive advantage and deliver superior returns to shareholders. Prudential will pursue its key strategic themes of maintaining focus on its customers, developing leading technology and e-commerce capabilities to improve further customer access and service, driving down costs, and driving growth in new and expanding markets.

Focusing on Customers

Prudential's goal is to deliver the products that its customers want, through the distribution channels they wish to use. Prudential is continually exploring opportunities to expand its distribution reach and broaden its product offering.

Within the United Kingdom, Prudential now has a leading position in its chosen distribution channels and product ranges. Prudential occupies leading positions in the IFA and direct and e-commerce channels. Prudential's products range from traditional pensions and long-term savings products to pension annuities, unit trusts and retail banking products. Prudential's stable of brands includes both the "Prudential" and "M&G" brands, two of the most respected names in life insurance and retail fund management, respectively, together with one of the United Kingdom's most recognized internet banking brands, "Egg".

The initial public offering of a minority stake in Egg in June 2000 was an important step towards ensuring that Prudential realizes the full potential of this business. This independent quotation is designed to provide Egg with the ability to grow and expand with its own acquisition currency and to enhance its ability to recruit, retain and incentivize staff. At the same time, Prudential will continue to invest in all of its UK businesses to ensure it retains its market-leading positions.

In the United States, Prudential, through Jackson National Life, is one of the few providers to have a significant market position across the range of fixed, variable and equity-indexed annuity products. It also offers life and stable value products. Jackson National Life has expanded its distribution channels to include independent agents, broker-dealers and banks and other financial institutions. Prudential will continue to seek opportunities to expand its product range and distribution capability in the United States, both through acquisition and organic initiatives, and its exposure to equity-based products, including variable annuities and mutual funds.

Across Asia, Prudential is a market leader in developing innovative savings and insurance products. It has leveraged its UK and US product expertise and proactively worked with Asian regulators to bring new products to market. Prudential has offered mutual fund products in India since 1998, and at December 31, 2000 had £695 million of funds under management. In October 2000, Prudential acquired an 89% interest in a Taiwanese mutual fund company, Core Pacific Securities Investment Trust Enterprise, renamed Prudential Securities Investment Trust Enterprise (Prudential SITE). Building on its initiatives in India and Taiwan, Prudential intends to develop mutual fund offerings in other Asian countries. Prudential is also working to create a multi-channel distribution capability including e-commerce initiatives across the region. In addition to its core agency distribution channel, Prudential has established bancassurance operations in Singapore, Hong Kong, Malaysia and Indonesia.

Investing in Technology

Prudential believes that technology is a key enabler in its industry in both driving efficiency through lower costs of administration and as a major distribution channel across the group. Prudential is investing significant resources in technology because it believes technology to be a source of considerable competitive advantage.

The development of Egg is the most visible and high profile example of Prudential's investment in technology. Prudential believes that Egg has developed significant first-mover advantage in the e-commerce retail financial services market in the United Kingdom. Egg is, however, just one example of a number of developments Prudential has underway; all parts of Prudential are rapidly progressing in making e-commerce integral to the way Prudential does business.

In the United Kingdom, Prudential Financial Services is using the latest e-commerce technology to provide corporate pensions and services designed to increase employee participation and drive down costs. Prudential Intermediary Business has an extranet service for IFAs. This enables IFAs to have instant access to online services and information and is an integral part of Prudential's service proposition in the IFA market.

In the United States, Prudential already uses the internet to service agents and customers and has launched new services, including online transactions, customized illustrations and presentations. Prudential's financial planner broker-dealer has been built around a highly efficient e-commerce platform; currently 90% of its general securities trades are processed over the internet.

In Asia, internet usage is anticipated to grow in the next few years and Prudential is actively engaged in developing e-commerce solutions across the region.

Driving Growth in New and Expanding Markets

Within its existing markets of the United Kingdom, the United States and Asia, Prudential believes fundamental shifts in demographics and in pension provision will create significant opportunities for future profitable growth.

At the same time as driving growth in its existing markets, Prudential continues to seek new markets in which it believes it can create value for its shareholders. In 1999, Prudential announced a return to continental Europe with agreements with CNP Assurances, France's leading life assurer, and Signal Iduna, one of Germany's major insurance providers. Prudential believes that many of the characteristics of the European market, such as an aging population, the gradual shift in retirement provision from state to individual, and the historical absence of equity-based investment products, make it a potentially significant growth market.

Prudential's strategy for continental Europe involves harnessing its equity-based product expertise and tailoring it for individual European markets. Prudential plans to distribute its products through a series of non-exclusive strategic partnerships with leading local financial service providers, focusing on the four most populous markets of France, Germany, Spain and Italy.

Prudential believes that Asia also offers significant opportunities for growth. During 1999 and 2000, Prudential made considerable progress in establishing itself in new markets in Asia. In China, Prudential received a license to write life assurance business in the city of Guangzhou and commenced operations in the last quarter of 2000. Prudential will endeavor to obtain licenses for other cities in China. During 1999, Prudential also acquired Chinfon Life in Taiwan, subsequently renamed Prudential Life Assurance Company, and obtained a life insurance license in Vietnam. In Hong Kong, Prudential formed a joint venture with the Bank of China International to target the compulsory Mandatory Provident Fund market.

In February 2001, Prudential commenced writing life insurance business in Japan following its acquisition of Orico Life.

In India, Prudential has successfully entered the mutual fund market in a venture with The Industrial Credit and Investment Corporation of India Ltd. (ICICI) and has re-established the Prudential brand in India. Following the liberalization of the Indian life insurance market in 2000, ICICI Prudential Life Insurance, Prudential's venture with ICICI, received a life insurance license in India.

The success of Prudential's mutual fund operation in India has encouraged it to initiate the development of similar offerings across Asia and in October 2000, Prudential acquired an 89% interest in Prudential SITE in Taiwan. This, together with the anticipated growth in internet usage across the region, provides Prudential with potentially significant opportunities to accelerate its growth and profits from the Asian market.

Prudential continues to consider opportunities to acquire businesses to further the strategy of growing its business, particularly in new and expanding markets. Prudential may finance these acquisitions with bank borrowings, debt or equity issuances or a combination of such financings.

Summary

Prudential's strategic initiatives over the past five years have significantly changed the shape and focus of its group and have built a platform for further growth and value generation. Prudential believes that by continuing to implement its strategy of investing in broader distribution and product innovation for the benefit of its customers, continuing to invest in technology to drive efficiency and expand e-commerce channels, and driving growth in its newer markets, it will maximize value for its shareholders both now and over the long term.

Significant Subsidiaries

The table below sets forth Prudential's significant subsidiaries.

Name of Company	Percentage owned(1)	Country of incorporation
Jackson National Life Insurance Company(2) . .	100%	United States
Prudential Annuities Limited(2)	100%	England and Wales
The Prudential Assurance Company Limited . .	100%	England and Wales
Prudential Assurance Company Singapore (Pte) Limited(2)	100%	Singapore
Prudential Banking plc(2)(3)	79%	England and Wales
M&G Investment Management Limited(2)	100%	England and Wales
Scottish Amicable Life plc(2)	100%	Scotland

(1) Percentage of equity owned by Prudential directly or indirectly. The percentage of voting power held is the same as the percentage owned.

(2) Owned by a subsidiary of Prudential.

(3) Prudential Banking plc is a wholly-owned subsidiary of Egg plc, a listed subsidiary of Prudential. Following its initial public offering of approximately 21% of the shares of Egg plc in June 2000, Prudential owns approximately 79% of Egg plc.

Information Regarding Merger with American General Corporation

On March 12, 2001, Prudential announced an all-share merger with American General Corporation, a Texas corporation. The terms of the merger agreement provided for a share exchange ratio of 3.6622 Prudential shares (or 1.8311 Prudential American depository shares) for each American General share. Based on the ten day trailing average closing prices on March 9, 2001, the merger agreement created an implied value of US$49.52 per American General share and a total fully diluted equity value of American General equal to £18.1 billion (US$26.5 billion). On May 11, 2001, the merger agreement between Prudential and American General was terminated. In accordance with the merger agreement, American General paid Prudential the full termination fee of £423 million (US$600 million) required under the contract.

UK Business

Introduction

The following discussion of Prudential's UK business describes:

- the UK retail financial services market,
- Prudential's UK business units,
- Prudential's products, including reinsurance arrangements and reserving practices,
- shareholders' participation in Prudential's long-term insurance business, and
- other matters, including pensions misselling, other general compliance matters, UK restructuring and implications of stakeholder pensions.

In 2000, Prudential's UK operations generated operating profit before amortization of goodwill and tax of £471 million compared with £452 million in 1999. In 2000, Prudential's total new business insurance and investment premiums were £6,269 million, 71% of which came from IFAs, 21% of which came from Prudential's company salesforce and 8% of which were sold directly. At December 31, 2000, Egg had deposits of £7,128 million and a mortgage and credit book of £3,779 million. Egg achieved its original five-year deposits target within seven months of its launch.

UK Retail Financial Services Market Overview

The United Kingdom is the world's third-largest life insurance market in terms of premiums and is one of the largest retail banking markets. In recent years, the UK insurance and banking markets have changed significantly and are continuing to evolve as a result of changes in regulation and government policy, demographics, technological development and consumer awareness and attitudes. Retail financial services providers are adapting to these changes by broadening the range of products that they offer and the means by which those products are distributed to and accessed by customers.

The historical divisions between insurance, banking and other financial products have been eroded. It is increasingly common for providers to offer a range of pension products, life products and services, property and casualty insurance, banking products and retail investment products and services. Consumers are increasingly being offered access to these products through direct marketing and e-commerce, as well as through the traditional company salesforce, IFA and bank branch distribution channels.

New entrants to the retail financial services market have capitalized on the relatively simple nature of many savings, investment, property and casualty insurance and banking products designed for direct distribution channels and used their established retail brands and advanced technology to market these products. New entrants are also taking advantage of the lower cost barriers to entry afforded by internet distribution, especially in the area of retail banking.

Competition among retail financial service companies is focused on product range, distribution reach, brand, investment performance, specific benefits offered by products, charges and financial strength.

Distribution

Retail financial services and products are distributed face-to-face, through branches, tied agents, company salesforces and IFAs, or directly by mail, telephone and over the internet. Tied agents are exclusive agents who represent only one insurer and must offer customers the products most suitable to their needs, but only from the range of products offered by that insurer. The insurance company that employs the agent is responsible for the agent's conduct. IFAs are required by law to provide the best advice to customers, considering all of the products available in the market and the customer's particular circumstances, and are legally responsible for their own advice. In contrast, company salesforces may only sell the products of the company by which they are employed, but they must also provide the best advice concerning the products offered by their company and the customer's particular circumstances. A company has legal responsibility for the advice its salesforce provides.

Increasingly, consumers require access that is compatible with their lifestyle. IFAs, banks, direct marketing and e-commerce distribution are gaining market share at the expense of traditional company salesforces. Direct and e-commerce distribution methods are generally lower-cost than other methods but have not been conducive to providing financial advice to the consumer to date. Accordingly, products distributed directly are generally more straightforward and have lower, often fee-based, charges. Although the e-commerce market is still small, it is expanding rapidly and Prudential believes it has considerable potential for further growth.

More complex products that require advice are not typically offered by direct marketing, but are distributed face-to-face through IFAs or by company salesforces, permitting advice to be provided.

Products

The traditional life insurance product offered by UK life insurance companies was a long-term savings product with a life insurance component. The life insurance element conferred tax advantages that distinguished the traditional life insurance products offered in the United Kingdom from the savings products offered by banks, building societies and unit trust companies. The gradual reduction of these tax advantages and increasing sales of single premium life products has resulted in the distinction between life insurance and other long-term savings products becoming less important. Pension products remain tax-advantaged within certain limits.

Demand for private personal pension and savings products has increased during recent years, in part reflecting a change in the UK government's approach to social security that has encouraged long-term savings through tax advantages, but also in reaction to the growing realization that state-provided pensions are unlikely to provide sufficient retirement income. An aging population is focusing on asset-accumulation and other retirement products to supplement their state benefits, while younger generations are focusing on pension and long-term savings products as well as health and income protection cover.

In 1988, the UK government introduced new pension legislation intended to encourage more individuals to make their own arrangements for their pensions. During the period from 1988 to 1994, many individuals were encouraged by insurance companies and intermediaries not to join their occupational pension plans, to opt out of their occupational plans or to transfer their accumulated pension entitlement to a private pension product. Subsequently, the UK regulator determined that this was not the best advice for many individuals. Providers of UK long-term products are required to compensate those individuals who were incorrectly sold private pension products. Pensions misselling adversely affected consumer confidence in the financial services industry. However, the pensions industry has worked closely with the UK regulator to resolve this issue and is currently in the second phase of a review of missold products to determine compensation and settle claims.

During the late 1980s, the UK government began encouraging individuals to invest in equities, with particular emphasis on UK equities. The UK government's privatization program and the introduction of tax-advantaged Personal Equity Plans, referred to as PEPs, in 1988 have considerably widened the UK equity investor base. The current UK government replaced PEPs in April 1999 with Individual Savings Accounts, referred to as ISAs, a new tax-advantaged product that offers equity, insurance and deposit investment options.

The UK government introduced "stakeholder pensions" in April 2001. Stakeholder pensions are discussed under "—Implications of Stakeholder Pensions" in this section below.

With-profits Products

The majority of the life and pensions business traditionally written in the United Kingdom is with-profits business. For with-profits products, the policyholder's premiums are paid into a life insurance company's with-profits fund, which is part of a company's long-term fund. In the with-profits fund, the premiums are invested in a range of assets, including equities, real estate and fixed interest securities. The with-profits policyholders receive a share of the profits arising from these investments.

The policyholder's share of the profits is distributed through a combination of annual bonuses, which are added to policies each year and guaranteed in accordance with the terms of the particular product, and terminal bonuses, added on death, maturity or surrender. It is typical in the industry to transfer to shareholders in respect of bonuses an amount equal to one-ninth of amounts allocated to with-profits policyholders through bonuses from the company's with-profits fund.

UK Business Units

Overview

Prudential's UK business is structured into business units, each focusing on their respective target customer markets. Prudential's UK business units are:

- UK insurance, comprising
  - Prudential Financial Services,
  - Prudential Insurance Services, and
  - Prudential Intermediary Business,
- M&G and
- Egg.

The business units target different sectors of the UK financial services market and enable Prudential to provide a multi-brand, multi-distribution offering in the United Kingdom. These business units, together with their respective products, brands, distribution channels and principal corporate entities, are set forth in the diagram below.

	Prudential Financial Services	Prudential Insurance Services	Prudential Intermediary Business		M&G	Egg
Brands	• Prudential	• Prudential	• Scottish Amicable	• Prudential	• M&G	• Egg
Products Manufactured	• Group pensions	• Life products • Individual pensions • Personal lines property and casualty insurance	• Life products • Individual pensions • Company pensions • Pension annuities • Investment products	• Insurance products • Pension annuities	• Retail investment products • Institutional fund management	• Banking products — Deposits — Mortgages — Loans — Credit card
Products Distributed	• All of the above • Individual and group pensions • Pension annuities • Life products • Banking products • Retail investment products • Personal lines property and casualty insurance	• All of the above	• All of the above	• All of the above	• Retail investment products • Institutional fund management services	• All of the above • Intermediated retail shopping • Intermediated financial services
Distribution Channels	• Company salesforce • Direct marketing • IFAs • Asset consultants • Company intranets	• Company salesforce • Direct marketing — Internet — Mail — Telephone	• IFAs • Tied agents	• IFAs	• IFAs • Direct marketing • Asset consultants • Prudential company salesforce	• Direct marketing — Internet — Mail — Telephone • Prudential company salesforce
Principal Corporate Entities	• The Prudential Assurance Company Limited	• The Prudential Assurance Company Limited	• Scottish Amicable Life plc	• The Prudential Assurance Company Limited • Prudential Annuities Limited	• M&G Group Limited • Prudential Collective Investments Limited	• Egg plc • Prudential Banking plc

Prudential Financial Services

Prudential Financial Services comprises Prudential's company salesforce distribution channel and its group pensions product manufacturing and service operations. Prudential's company salesforce provides advice about Prudential's products and sales service at the time and place of its customers' choosing.

Prudential offers a wide range of products through its company salesforce, which are marketed under the "Prudential" brand. The products distributed include:

- long-term products:
  - — life insurance savings-type products and pure protection products,
  - — individual and corporate pensions, and
  - — pension annuities,
- personal lines property and casualty insurance,
- retail investment products, and
- banking products.

In addition to distribution through its company salesforce, Prudential Financial Services also distributes Prudential's corporate pension products and markets its plan administration services through consulting actuaries, benefits advisers and its company salesforce. Both consulting actuaries and benefits advisers are IFAs, but are not generally the same as the retail IFAs with whom Prudential works through Prudential Intermediary Business.

The following table shows total long-term new business premiums for Prudential Financial Services for the periods indicated.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions, Except Percentages)		
Total long-term new business premiums	**2,247**	2,528	2,143
Percent of total UK long-term new business premiums	**45%**	38%	48%

On February 13, 2001, Prudential announced a plan to restructure its direct salesforce and customer service channels in its UK insurance operations. Prudential is shifting its focus from a large direct salesforce to alternative distribution channels. The changes include an expanded customer service offering through the telephone, the internet and the workplace; greater accessibility to a comprehensive product range; a smaller face-to-face salesforce focusing on financial planning services; and back-office administration and support functions.

Under the restructuring plan,

- The 1,400 current direct sales consultants will be replaced by a smaller specialist force of qualified advisers providing a face-to-face financial planning service. This team is expected to grow to around 250 advisers.
- A team of 100 consultants will provide information and advice on pensions and other products to customer groups within corporate business clients, small and medium enterprises and affinity groups.
- A simple financial healthcheck service is expected to be available online or over the telephone from 2002 in an effort to provide financial decision-making tools to help customers assess their individual needs.

Prudential anticipates that the restructuring will result in 2,000 jobs being made redundant and expects to incur costs of £110 million, of which £13 million will be borne by the shareholders' funds.

Prudential Financial Services also intends to be a major provider of stakeholder pensions. Prudential is developing a marketing and distribution platform that uses the latest e-commerce technology to provide corporate pensions products and services, thereby increasing employee participation and enabling it to deliver products in an increasingly competitive market. See "—Implications of Stakeholder Pensions" in this section below.

Prudential Insurance Services

Prudential Insurance Services comprises the product manufacturing and service operations for the majority of the Prudential-branded products. The products manufactured include:

- long-term products:
  - — life insurance savings type products and pure protection products, and
  - — individual pensions,
- personal lines property and casualty insurance.

Long-term products are distributed through Prudential's company salesforce and over the telephone. Prudential Insurance Services also provides service to customers who hold any of Prudential's UK life and pensions products, including those that are now closed to new business.

Prudential's personal lines property and casualty insurance is distributed by telephone and the internet, including through Egg's general insurance supermarket, in addition to sales by the company salesforce.

Prudential Intermediary Business

Prudential Intermediary Business markets a range of products under the Scottish Amicable and Prudential brands, including the Prudence Bond.

Prudential Intermediary Business offers the following products to IFAs to sell to their clients:

- long-term products:
  - life insurance, including savings-type products and pure protection products,
  - individual pensions,
  - company pensions,
  - pensions annuities and
- retail investment products.

The following table shows total long-term new business premiums for the Prudential Intermediary Business unit for the periods indicated.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions, Except Percentages)		
Total long-term new business premiums	**2,766**	4,130	2,346
Percent of total UK long-term new business premiums	**55%**	62%	52%

The operations of Prudential Intermediary Business are based in Craigforth, Scotland. Prudential has a network of approximately 15,000 IFAs and 280 tied agents through whom it markets its IFA products throughout the United Kingdom. Prudential Intermediary Business also provides administrative support and services to third parties.

Larger IFAs and IFA networks maintain "panels" of preferred providers for each type of product. Prudential's goal is to provide IFAs with high-quality products, service and support so that it maintains its position as a preferred provider in each of its chosen market segments.

Prudential has continued to develop products to satisfy the requirements of its customers and in response to demand from the IFAs through whom it distributes. In 1999, Prudential launched significant new initiatives, including a range of unit-linked IFA products, ISAs and unit trusts. Prudential also launched a new Scottish Amicable-branded group pension product in 2000 to meet the expected criteria of the UK government's proposed stakeholder pensions legislation. Prudential Intermediary Business is also using technology as an integral part of its IFA distribution channel. An extranet service for IFAs was launched in early 2000 that enables IFAs to have instant access to online services and information and to further improve the quality of service offered to IFAs.

Prudential also offers pensions annuities under the Prudential brand. Its pension annuity operations offer pension annuities through IFAs and the company salesforce. Prudential has recently expanded its pension annuity product offering to include bulk annuities, in addition to traditional individual pensions annuities.

Distribution of products to IFAs will be increased through the formation of a new company, Scottish Amicable Financial Services, that will distribute both Scottish Amicable and Prudential-branded products through a combined wholesale salesforce.

M&G

Prudential's fund management business in the United Kingdom and Europe is M&G. This business currently comprises a retail fund management business and fixed income institutional and internal fund management activities.

Following the acquisition of M&G Group plc in 1999, Prudential has merged its existing UK fund management operation, Prudential Portfolio Managers, or PPM, into the M&G operation.

In the United Kingdom M&G specializes in those areas of fund management where it believes that it has a competitive advantage. These areas are unit trusts, fixed income and pooled life and pension funds. M&G therefore sold its UK institutional equity businesses in 2000.

The following table shows funds managed by M&G at the dates indicated.

	At December 31,		
	2000	**1999**	**1998**
	(In £ Billions)		
Retail fund management	**18**	15	3
Institutional fund management	**6**	22	15
Internal fund management	**106**	106	88
Total	**130**	143(1)	106

(1) Includes £12 billion relating to M&G's institutional equity business, which was sold in 2000.

Retail Fund Management

M&G's retail fund management business comprises distribution of its retail investment products and the management of the funds invested in these products by its customers. Total new business premiums for the year ended December 31, 2000 for M&G products, distributed directly and through the IFA channel, were £1,097 million and comprised 17% of total UK new business premiums.

M&G markets and distributes its range of retail investment products through IFAs, directly and through Prudential's company salesforce. In addition, M&G was one of the first UK providers to offer unit trust purchases over the internet.

M&G provides retail fund management skills and experience, complementing its internal investment management skills. Prudential believes that retail fund management will continue to increase in importance as individuals, encouraged by UK government policy, increasingly demand transparent investment products.

M&G believes that investment products, such as unit trusts, will increasingly form the core products of future savings and pensions plans in the United Kingdom and Europe.

Internal Fund Management

M&G's internal fund management activities are based in the United Kingdom. Its largest client is Prudential Assurance's long-term fund, which had £90 billion of funds at December 31, 2000. Where M&G chooses to invest internal funds in the US or Asia, this is done through PPM America and PPM Asia, respectively. M&G monitors global investment and economic conditions, while the regional fund management offices provide M&G with local knowledge and experience.

In the United Kingdom, M&G is one of the largest investment managers, with £130 billion of funds under management at December 31, 2000 (including the funds allocated to PPM America and PPM Asia). These funds represent £106 billion of internal funds, £6 billion of institutional funds and £18 billion of retail funds.

Prudential's funds have generally enjoyed the benefit of being more heavily invested in equities than those of its traditional life insurance competitors. However, in common with other value-oriented investment managers, a number of its key funds under-performed their relevant stock market indices in 2000 and 1999. This under-performance was due to a number of factors, including the concentration of performance in a limited number of sectors and stocks, together with stretched valuations in major equity markets, which created difficult investment conditions for all value-oriented investors.

Egg

Egg offers banking products and services under the Egg and Prudential brands through the internet as well as through the company salesforce. In June 2000, approximately 21% of the shares of Egg plc were offered in an initial public offering. The offering was intended to enable Egg to maximize potential growth in the UK domestic market and, over time, internationally. Egg has continued to develop and enhance its range of products and services, adopting new technologies for the benefit of customers while growing rapidly and retaining its market-leading position.

The following table shows the actual balances for Egg products at the dates indicated.

	At December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
Mortgage loans	**2,405**	1,622	642
Personal loans	**445**	207	33
Credit card receivables	**929**	228	—
Funds supermarket	**42**	—	—
Customer deposits	**7,128**	8,157	2,188

Egg currently offers Egg-branded and Prudential-branded banking products and intermediated services on the internet (*www.egg.com*). Egg was launched in October 1998 with the goal of attracting new customers and developing a direct distribution channel. Egg's target customer base is relatively affluent, and it has designed its products and services for customers who manage their own financial affairs, do not need advice, seek consistently good value, simple products and prefer the flexibility offered by remote access. Prudential believes that Egg will continue to develop into a significant business as internet access becomes more commonplace and technology improves.

At Egg's launch, the initial goal was to attract £5 billion in deposits in the first five years. That goal was achieved in the first seven months of operation, principally through opening accounts by telephone, and later over the internet. In April 1999, Egg began accepting new applications for deposit accounts exclusively through the internet. At December 31, 2000, Egg had approximately 1.35 million customers.

Egg has also added a new product to its range of savings products that can only be serviced through the internet and launched an internet application process for both mortgages and personal loans. Egg's internet-only savings product offers better rates of interest than its other deposit accounts, which can also be serviced over the telephone and by mail. Administration fees are waived on Egg's internet mortgage products. In September 1999, Egg launched the Egg Card, the UK's first credit card designed for the internet. In April 2000, Egg announced a partnership with The Boots Company plc to distribute a joint credit and loyalty card to Boots customers.

Egg also launched an online shopping portal on its website in September 1999. Customers who purchase through this shopping site with the Egg Card receive cash back on their purchases. In addition, customers are able to use search functionality to compare products according to selected criteria, including price.

Egg also launched an independent, execution-only unit trust supermarket on its website in March 2000. The site, which enables customers to purchase and manage their unit trusts online, offers interactive educational and information tools to help customers assess their investment needs, a personal balance sheet to help them manage their wealth, and a wide range of over 220 funds from leading investment fund managers. At December 31, 2000, funds under management totalled £42 million.

Egg launched an independent, execution-only insurance intermediation service in the second half of 2000. The site offers a range of personal lines property and casualty insurance products from a number of insurance companies, including Prudential.

In July 2000, Egg acquired a 39.6% stake in IFonline plc. IFonline operates a business-to-business internet mortgage transaction-processing service for financial intermediaries and mortgage product providers and will provide the platform for Egg's mortgage supermarket. Egg's mortgage supermarket will give borrowers access to hundreds of mortgages from leading suppliers, including Egg, through a single website.

In December 2000, Egg announced the launch of a new third-party mortgage administration joint venture with Marlborough Stirling, a UK software and services provider to financial services markets, including the mortgage market.

Prudential believes that Egg has gained a significant advantage in the provision of internet-based financial services by being among the first to the market with the services and products it offers. Egg has developed into an online marketplace, enabling clients to obtain products and services ranging from core banking products (deposit accounts, mortgages, personal loans and credit cards) and related financial services to intermediated financial and non-financial products and services. Egg continues to explore other electronic channels, including mobile telephone, digital television and broadband communications, and is currently investigating a number of opportunities in several markets and product sectors in the United Kingdom and internationally.

Prudential's UK Products

Prudential offers a range of products in the United Kingdom, including long-term insurance products, personal lines property and casualty insurance, banking products, retail investment products and fund management and other services. Prudential's long-term products comprise life insurance, pension products and pensions annuities. The discussion that follows focuses on Prudential's core products for each type of business.

The following table shows Prudential's UK new business insurance and investment premiums by product line and distribution channel for the periods indicated. New business premiums include deposits for policies with limited or no life contingencies.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
Life insurance			
With-profits	**2,047**	2,948	1,860
Unit-linked	**212**	126	202
Other	**—**	5	4
Total life insurance	**2,259**	3,079	2,066
Pensions			
With-profits individual	**181**	172	152
Unit-linked individual	**163**	162	215
DSS rebates	**234**	239	208
Corporate	**953**	731	537
Total pensions	**1,531**	1,304	1,112
Pensions annuities			
Fixed	**1,097**	2,184	1,084
With-profits	**157**	155	77
Total pensions annuities	**1,254**	2,339	1,161
	5,044	6,722	4,339
Investment products	**1,225**	632	150
	6,269	7,354	4,489
By distribution channel			
Company salesforce	**1,318**	1,817	1,562
Independent financial advisers	**4,472**	5,329	2,927
Direct	**479**	208	—
	6,269	7,354	4,489

Life Insurance Products

Prudential's UK life insurance products are predominantly medium to long-term savings products with life cover attached, and also include whole life products and pure protection (term) products. The savings products Prudential offers include investment bonds and endowment plans. Each of these products provides a death benefit in addition to the savings feature.

Savings Products Investment Bonds

Prudential's investment bonds are single premium products that may be with-profits or unit-linked products, although the with-profits products represent the vast majority of its new business premiums.

The Prudence Bond is one of the UK's leading investment bond products, with total premiums of over £10,000 million from its launch in 1991 to December 31, 2000. In 1994, Prudential launched a similar product, the Prudential Investment Bond. In 2000, new business premiums attributable to these products amounted to approximately £1,500 million and £484 million, respectively.

The Prudence Bond is a single premium, unitized with-profits policy with no fixed term, sold through Prudential Intermediary Business. The Prudential Investment Bond is a similar product in terms of product characteristics, and is sold through Prudential's company salesforce. The product aims to provide capital growth over the medium to long-term, access to this capital growth, and access to different investment areas without the risks associated with direct investment into these areas. Capital growth for the policyholder on with-profits bonds is achieved by the addition of reversionary or regular bonuses, both of which are credited to the bond on a daily basis from investment returns achieved within the with-profits fund. A terminal bonus may also be added when the bond is surrendered. Capital growth on unit-linked bonds is achieved by the movement of the assets underlying those funds.

Savings Products Endowment Plans

Endowment plans are long-term regular premium with-profits or unit-linked savings products that are designed to provide a lump sum at the end of a fixed term and death cover during the term. Surrender values are available but are determined by Prudential in the case of with-profits policies. Endowment products are often used in the United Kingdom to provide a lump sum for mortgage repayment with the borrower taking out an endowment assurance policy for the same term as the mortgage loan. Prudential's endowment plans are mainly with-profits products, although unit-linked policies are available through Scottish Amicable. In 2000, Prudential sold £29.7 million in endowment plans.

In April 2001, Prudential announced that, due to the shift within the marketplace towards repayment mortgages over the past two years, and the consequent significant fall in demand for endowment products, Scottish Amicable would withdraw from the mortgage endowment sales market.

Pension Products

Prudential provides both individual and corporate pension products. In 2000, new business premiums totalled £344 million for individual pensions and £953 million for corporate pensions. Pension products are tax-advantaged long-term savings products that comply with rules established by the UK Inland Revenue and are designed to supplement state-provided pensions. These rules require that, upon retirement, maturity benefits are used to purchase pension annuities, although they do permit a limited sum to be taken as a tax-free lump sum. These products typically have minimal mortality risk and are primarily considered investment products.

In addition, Prudential has recently introduced products that meet the criteria of the UK government's stakeholder pension program. See "—Implications of Stakeholder Pensions" in this section below.

Most of the pension products Prudential offers are with-profits products or offer the option to have all or part of the contributions allocated to a with-profits fund. Where funds invested in the with-profits fund are withdrawn prior to the pension date specified by the policyholder, Prudential may apply a market value adjustment to the amount paid out.

Individual Pensions

Prudential's individual pension products include personal pension plans and free standing additional voluntary contribution products. Prudential's free standing additional voluntary contribution plans permit individuals to supplement the pension benefits they accumulate in their occupational pension plan. Both of these products are either unit-linked or unitized with-profits products or contain options to permit premiums to be paid into a unitized with-profits fund.

Department of Social Security Rebates

Prudential also provides individual personal pension products through the "DSS Rebate" arrangement. Under this arrangement, individuals may elect to contract out of the UK's State Earnings

Related Pension Scheme administered by the UK Department of Social Security. If an individual elects to contract out, then he or she will designate a pensions provider, such as Prudential, with which he or she would like to have a pension product. Premiums on the product are met through "rebates" from the Department of Social Security, which represent the amount that would be otherwise paid into the state pension scheme. Rebate amounts are invested to provide benefits to the individual. Premiums from Department of Social Security rebates are typically reported in the first quarter of each year. In 2000, Prudential received total premiums of £234 million from Department of Social Security rebates.

Corporate Pensions

There are two categories of corporate pension products: defined benefit and defined contribution. Prudential has an established defined benefit plan client base that ranges from small unlisted companies to some of the largest companies in the United Kingdom.

UK regulations require that all companies that offer a defined benefit pension plan must also offer a group additional voluntary contribution plan to their employees. Additional voluntary contribution plans enable employees to make additional pension payments, either regularly or as a lump sum, to supplement their occupational pension plans. Prudential's additional voluntary contribution business is the second largest in the United Kingdom in terms of premium income.

Defined benefit plans and products continue to dominate the corporate pensions market in terms of funds under management. In recent years most new plans established have been defined contribution products. The products Prudential offers to the corporate pensions market are group unit-linked policies and with-profits deposit administration policies. Prudential's defined contribution products are additional voluntary contribution plans, money purchase plans, grouped personal pension plans, self-invested personal pension plans and executive pension plans.

Pension Annuities

Prudential offers immediate annuities that are either fixed annuities, where annuity payments are guaranteed from the outset, or with-profits annuities. Prudential also offers bulk annuities, whereby it manages the assets of a company pension scheme, to company pension funds, usually when they are in the process of winding up. Due to the nature of the product, the volume of Prudential's bulk annuity sales is unpredictable. In 2000, 51% of Prudential-branded annuity sales represented internal vestings. There were no significant sales of Prudential-branded bulk annuities in 2000.

Prudential's immediate annuity products provide guaranteed income for a specified time, usually the life of the policyholder, in exchange for a lump-sum capital payment. No surrender value is available under any of these products. The primary risk to Prudential from fixed annuity products, therefore, is mortality risk.

Fixed Annuities

Prudential offers three types of fixed annuities: level, fixed-increase and index-linked. The level annuity offered provides a fixed amount of income for the specified term. Prudential's fixed-increase annuity incorporates automatic increases by fixed amounts over the specified period. The index-linked annuities Prudential offers provide for a regular payment to which an additional amount based on the increase in the UK Retail Prices Index is added periodically. In 2000, sales of fixed annuities were £1,097 million.

With-profits Annuities

Prudential is one of only a few companies in the United Kingdom writing with-profits annuities. In 2000, Prudential wrote £157 million of with-profit annuities. Prudential's with-profits annuities combine the income features of annuity products with the smoothing feature of with-profits products and enable policyholders to obtain equity-type returns. Policyholders select an "anticipated bonus" from the specific range Prudential offers for the particular product. The value of the annuity payment each year depends upon the anticipated bonus rate selected by the policyholder when the product is purchased and the bonuses Prudential declares each year during the term of the product. If bonus rates fall below the anticipated rate then the annuity income falls.

Personal Lines Property and Casualty Insurance Products

Prudential's personal lines property and casualty insurance products in the United Kingdom are primarily household and motor insurance for individuals, referred to as personal lines. Prudential offers its personal lines products primarily through direct marketing and in connection with its banking business. Home insurance gross premiums of £276 million in 2000 accounted for 83% of Prudential's personal lines property and casualty premiums. Prudential's motor policies provide coverage to individuals for third-party liability, including property damage and bodily injury, theft, fire and collision damage. Prudential also offers redundancy and disability insurance and mortgage guarantee policies in connection with Prudential's banking products, and creditor insurance, primarily for credit cards and loans sold by Egg. In addition, Prudential offers personal lines property and casualty insurance through Egg.

The following table shows gross premiums for Prudential's UK personal lines property and casualty insurance products for the periods indicated.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
Home	**276**	274	273
Motor insurance	**57**	44	37
Total	**333**	318	310

Closed Business

Prior to 1993, Prudential wrote a wide range of property and casualty insurance business, including commercial cover, which it sold through brokers and its company salesforce. Prudential also had a London Market operation and specialist marine and aviation insurance operations. Prudential had withdrawn from all of these areas by the end of 1993 and, consequently, these businesses are now in run-off. The total claims provisions established for these closed businesses amounted to £139 million at December 31, 2000. Prudential believes these provisions are prudent and does not currently anticipate that it will need to make any further provisions in respect of these closed businesses.

Retail Investment Products

Prudential's retail investment products are unit trusts, individual savings accounts (ISAs), personal equity plans (PEPs) and investment trusts.

Unit Trusts

Unit trusts are the UK equivalent of mutual funds. These products are designed for medium to long-term savings and either lump-sum or regular contributions may be made. Investors purchase "units" of the unit trust. A unit represents an interest in the pool of investments underlying the unit trust. The return to investors is determined by the performance of these investments.

Individual Savings Accounts

ISAs were introduced on April 6, 1999, in accordance with UK government policy. ISA products effectively replaced both PEPs and tax-exempt special savings accounts, or TESSAs, which had been popular. PEPs provided a tax-free method for investors to invest in a number of funds and were often "wrapped" around Prudential's and M&G's unit trust products, adding tax advantages to the product. TESSAs were tax-advantaged cash savings accounts.

ISA products are savings products that provide a tax advantage in that the income and capital gains arising are tax-free. Contributions may be made regularly or in a lump sum, subject to the £7,000 maximum per tax year specified by the UK tax authorities until 2005/2006. The UK tax authorities have announced that the ISA product's tax advantages are guaranteed to remain in place until at least 2009. Prudential offers ISA products that "wrap" equity-based and corporate bond-based investment products.

Investment Trusts

Investment trusts are similar to closed-end mutual funds and are listed on the London Stock Exchange. The trusts invest in specified investments, typically equities and government securities. Investors purchase shares in the trusts. The return to the investor is based on the trading price of the shares. Prudential offers investment trusts only through M&G.

Banking Products

Egg's banking products include deposit savings accounts, mortgages, personal loans and credit cards. At December 31, 2000, Egg had total deposits of £7,128 million and over 1.35 million customers. In addition to its traditional deposit account, which can be serviced both over the internet and by telephone, Egg launched in 1999 an internet-only deposit account that may only be applied for and serviced over the internet. This account offers a more competitive rate of interest than Egg's traditional deposit accounts. At December 31, 2000, Egg's mortgage loan book amounted to £2,405 million and its personal loan book was £445 million. Egg's credit card was launched in September 1999, and at December 31, 2000, the balance outstanding on credit cards was £929 million. Egg also launched an independent, execution-only unit trust supermarket on its website in March 2000. At December 31, 2000, funds under management totalled £42 million.

Internet-Enabled Products

As part of its customer proposition, Egg has developed an online shopping portal on its website, selling intermediated retail products. In addition, in March 2000, Egg launched an execution-only investment supermarket offering unit trust products from a variety of providers and an execution-only personal lines insurance supermarket featuring products from a variety of providers.

Reinsurance

Long-term Insurance

In view of the size and spread of the long-term insurance fund, there is little need for reinsurance to protect this business. Some limited reinsurance is maintained and treaties relating to critical illness and permanent health insurance and term insurance are in place.

Personal Lines Property and Casualty Insurance

In common with other insurance companies, Prudential cedes some of its personal lines property and casualty insurance risks to companies outside its group. Prudential cedes risks primarily to reduce its potential liability on a major weather-related event under its domestic insurance policies.

Reinsurance can also provide some protection against individual large losses. Reinsurance does not discharge the original insurer's primary liability to the insured.

Prudential's catastrophe reinsurance treaties provide reinsurance for losses arising from any one incident in excess of £50 million (and up to £250 million) on the whole property account.

On its motor account, Prudential has excess of loss reinsurance arrangements in place to provide cover against individual claims in excess of £500,000. Prudential also reinsures, on a quota share basis, 90% of the risk arising under mortgage guarantee business and 75% of the risk arising under legal expense cover offered as optional benefits under household and motor policies.

Prudential places catastrophe reinsurance and motor reinsurance with a large number of reinsurers, including Lloyd's of London and specialist reinsurance companies. Prudential requires all its reinsurance to be ceded to reinsurance companies that have a credit rating of A or above.

In addition, in accordance with UK accounting regulations, a claims equalization provision is retained that could be drawn upon in the event the claims ratio on Prudential's domestic insurance business exceeds 72.5%. At December 31, 2000, this provision was £38 million.

Reserves

In the United Kingdom, a long-term insurance company's reserve requirements are determined by its appointed actuary, subject to minimum reserve requirements. These minimum reserve requirements are established by regulations under the Insurance Companies Act 1982 and have been interpreted by mandatory professional guidance notes.

The reserves are published in annual returns to the UK supervisory authority. In practice similar provisions are included in the life insurance company's statutory accounts with limited adjustments. Whether an employee of, or consultant to, an insurance company, an appointed actuary must give due regard to policyholders' reasonable expectations in making recommendations to a company's board of directors. Mandatory professional guidance notes require an appointed actuary to report directly to the UK supervisory authority any serious concerns regarding a company's ability to meet the reasonable expectations of its policyholders.

Prudential's reserving for with-profits products takes into account annual bonuses/annual interest credited to policyholders because these are "attached" to the policies and are guaranteed. Prudential also makes implicit allowance for future annual bonus and interest as required by the UK regulations. No reserves are provided for terminal bonuses, except for the period for which they have been declared.

Prudential reserves for unit-linked products on the basis of the value of the unit fund and additional reserves are held for expenses and mortality where this is required by the contract design.

On May 29, 2000, new, more stringent valuation regulations were introduced by the UK regulatory authorities. The new regulations require reserves to be held to cover a large part of the terminal bonus on unitized with-profits business.

Financial Strength of Prudential Assurance's Long-term Fund

A common measure of financial strength in the United Kingdom for long-term insurance business is the free asset ratio. The free asset ratio represents the ratio of assets less liabilities to liabilities and is expressed as a percentage of liabilities. At December 31, 2000, Prudential Assurance's free asset ratio was 17%, compared to a ratio of 29% at December 31, 1999. The principal reason for the lower ratio at December 31, 2000 was the introduction on May 29, 2000, of the new, more stringent, valuation regulations, which require the establishment of reserves to cover part of the terminal bonus in respect of unitized with-profits policies. The effect of these regulations, had they been in force at December 31, 1999, would have been to reduce the free asset ratio from 29% to 19%.

For Prudential Assurance, the free assets in the long-term fund provide cover for the minimum solvency margin required by regulations under the UK Insurance Companies Act 1982. At December 31, 2000, Prudential Assurance had a solvency margin equal to 326% of the statutory minimum. The long-term fund remains well capitalized. Prudential Assurance's long-term fund is currently rated AAA by Standard & Poor's and Aaa by Moody's.

Shareholders' Interests in Prudential's Long-term Insurance Business

In common with other UK long-term insurance companies, Prudential's products are structured as either with-profits or non-participating products, which include unit-linked products. For statutory and management purposes, Prudential Assurance's long-term fund consists of a number of sub-funds in which shareholders and policyholders have varying interests.

With-profits Products

With-profits products provide an equity-type return to policyholders through bonuses that are "smoothed". There are two types of bonus: "annual" and "terminal". Annual bonuses, often referred to as reversionary bonuses, are declared and credited annually and, once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, terminal bonuses are not guaranteed. Terminal bonuses are only credited on a product's maturity or surrender or on the death of the policyholder. Terminal bonuses typically represent a substantial portion, which can be as much as 70% of the total, of the ultimate return to policyholders.

With-profits policies are supported by a with-profits fund. Prudential's primary with-profits fund is part of Prudential Assurance's long-term fund. With-profits products provide benefits that are generally either the value of the premiums paid, or the guaranteed maturity benefit, plus the bonuses declared. Smoothing of investment returns is an important feature of with-profits products. It is designed to reduce the impact of fluctuations in investment return from year to year and is accomplished predominantly through the level of terminal bonuses declared.

The return to Prudential's shareholders in respect of bonuses on the with-profits products Prudential writes is currently an amount equal to up to one-ninth of the value of the bonuses Prudential credits or declares in that year. Prudential has a large block of in-force with-profits business with varying maturity dates that generates a relatively stable stream of shareholder profits from year to year.

Prudential's With-profits Bonus Policy

Prudential Assurance's board of directors, with the advice of its appointed actuary, determines the amount of annual and terminal bonuses to be declared each year on each group of contracts.

When determining policy payouts, including terminal bonuses, Prudential follows an actuarial practice of considering "asset shares" for specimen policies. Asset shares broadly reflect the value of premiums paid in respect of a policy accumulated at the investment return on the assets Prudential notionally attributes to the policy. In calculating asset shares, Prudential takes into account the following items:

- the cost of mortality risk and other guarantees (where applicable),
- the effect of taxation,
- expenses, charges and commissions,
- the proportion of the amount determined to be distributable to shareholders, and
- the surplus arising from surrenders and non-participating business included in the with-profits fund.

However, Prudential does not take into account the surplus assets of the long-term fund, or their investment return, in calculating asset shares. Asset shares are used in the determination of terminal bonuses together with policyholders' reasonable expectations, the need to smooth claim values and payments from year to year and competitive considerations.

Prudential is required by UK law and regulation to consider the reasonable expectations of its policyholders in setting bonus levels. The concept of policyholders' reasonable expectations is established by statute but is not defined. In practice, it provides one of the guiding principles for decision-making in respect of with-profits products.

The overall return to policyholders is an important competitive measure for attracting new business. The ability to declare competitive bonuses depends, in part, on the financial strength of Prudential Assurance's long-term fund, enabling it to maintain high levels of investment in equities, which have historically provided a return in excess of fixed interest securities.

Surplus Assets in Prudential Assurance's Long-term Fund

Surplus assets are the assets of the long-term fund less all non-participating liabilities and the policyholder asset shares aggregated across all with-profits policies and any additional amounts expected at the valuation date to be paid to in-force policyholders in the future in respect of smoothing costs and guarantees. Thus surplus assets are amounts in excess of what Prudential expects to pay to policyholders.

These surplus assets have accumulated over many years from a variety of sources and provide the long-term fund with working capital. This working capital permits Prudential to invest a substantial portion of the assets of the long-term fund in equities and real estate, smooth investment returns to with-profits policyholders, keep its products competitive, write new business without being constrained as to cash flows in the early years of the policy and demonstrate solvency.

In addition, Prudential can use surplus assets to absorb the costs of significant events, such as fundamental strategic change in its long-term business and, as approved by the UK regulator, the cost of its pensions misselling, without affecting the level of distributions to policyholders and shareholders. The costs of fundamental strategic change may include investment in new technology, redundancy and restructuring costs, cost overruns on new business and the funding of other appropriate long-term insurance-related activities, including acquisitions.

The aggregate with-profits policyholder asset shares upon which the calculation of surplus assets is based are not used in any form of external reporting or for internal financial reporting and do not form part of Prudential's accounting books and records. Asset share methodology has evolved only over the past 20 to 30 years for actuarial purposes to assist in the determination of bonus rates. It is only in recent years that the application of this methodology has been extended to calculating aggregate asset shares.

The calculation of aggregate with-profits policyholder asset shares, unlike the calculation for determining bonuses, depends upon the experience for each type of policy in respect of mortality, surrenders, expenses, investment returns, taxation and transfers to shareholders over the duration that current policies have been in-force. As Prudential has not been using this methodology since the inception of a significant proportion of its in-force policies, it does not have the detailed historical data for all policies required to calculate a precise aggregate asset share for each class of policy. Without a precise calculation of aggregate asset shares on which to base its calculation of the surplus assets within the fund for future appropriations, Prudential can only estimate this amount.

The amount of surplus assets changes from year to year to reflect the achieved investment performance of the fund and any change over the year in the anticipated costs of smoothing and guarantees for the in-force business. The anticipated costs of smoothing and guarantees depend upon the projection of claim values and asset shares and hence on assumptions, which themselves vary from year to year, about future experience for mortality, surrenders, expenses, investment return and taxation.

For the reasons set out above, there is significant difficulty in calculating surplus assets. Prudential estimates that at December 31, 2000, its surplus assets, after taking into account pensions misselling costs and the anticipated costs of fundamental strategic change amounted to between £7 billion and £9 billion. This estimate is inherently uncertain.

Prudential continues to pursue opportunities to resolve the ultimate attribution of the surplus assets in Prudential Assurance's long-term fund, and has, since 1996, been discussing this attribution with the relevant UK supervisory authorities. The attribution of surplus assets has also been a subject of public debate in the United Kingdom. Prudential's discussions may or may not result in a portion of the surplus assets in the long-term fund being attributed solely to shareholders. On December 14, 2000, a policyholder filed proceedings against Prudential Assurance in connection with its treatment of its surplus assets. See "Legal Proceedings" in this section below.

The amount and timing of any attribution to shareholders is sufficiently uncertain that it is not possible to accurately estimate any potential attribution. In addition, it is likely that if any surplus assets are attributed to shareholders, they will remain in Prudential Assurance's long-term fund to support the long-term business, and accordingly, they are unlikely to be distributed to shareholders for some considerable period of time, if at all.

Depletion of Surplus Assets and Shareholders' Contingencies

As a proprietary insurance company, Prudential remains liable to meet its obligations to policyholders even if the assets of its long-term fund are insufficient to do so. The surplus assets in Prudential's long-term fund could be materially depleted over time, by, for example, a significant or sustained equity market downturn, significant fundamental strategic change costs, or material increases in the pensions misselling provision. In the unlikely circumstance that the depletion of the surplus assets within the long-term fund was such that Prudential believed that its ability to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or for Prudential to contribute shareholders' funds to the long-term fund to provide financial support.

The SAIF Sub-Fund and Accounts

The SAIF sub-fund is a ring-fenced sub-fund of Prudential Assurance's long-term fund and was formed following the acquisition of Scottish Amicable in 1997. No new business may be written in SAIF, although regular premiums are still being paid on policies in force at the time of the acquisition and "top-ups" are permitted on these policies.

This fund is solely for the benefit of those Scottish Amicable Life Assurance Society policyholders whose policies were transferred to SAIF. Shareholders have no interest in the profits of this fund, although they are entitled to the investment management fees paid on this business. The brand name and rights to profit on new business were transferred to a new Prudential subsidiary, Scottish Amicable Life plc, which operates for the benefit of shareholders.

At the time of the acquisition, Prudential Assurance's long-term fund made payments of £276 million to the SAIF sub-fund for the unit-linked life business and non-participating life business and the future profits from unitized with-profits life business. Prudential Assurance also agreed to set up a memorandum account of £1.3 billion that is considered in determining SAIF's investment policy. The sub-fund pays an annual charge to the other part of Prudential Assurance's long-term fund with respect to this memorandum account.

Prudential Assurance's long-term fund made a further payment of £185 million to qualifying Scottish Amicable Life Assurance Society policyholders for the use of the Scottish Amicable brand and future expense synergies. This payment of £185 million will be recovered by the long-term fund by means of a combination of a service agreement and a license fee agreement with Craigforth Services Limited, a shareholder-owned service company set up at the time of the acquisition.

In addition to the payments described above, shareholders paid £415 million to qualifying Scottish Amicable Life Assurance Society policyholders representing goodwill, and £70 million for certain Scottish Amicable Life Assurance Society strategic investments.

Non-participating Business

The vast majority of Prudential-branded non-participating business is written in Prudential Assurance's long-term fund or by subsidiaries owned by the fund. Prudential's principal non-participating business is Prudential Annuities Limited. The profits on this business are attributable to the fund and not to shareholders. In 2001, Prudential started to write new bulk annuity business through Prudential Retirement Income Limited (PRIL), from which the profits are attributed solely to shareholders.

The unit-linked business written by Scottish Amicable Life plc and Scottish Amicable Life International is written against capital provided by shareholders. All profit from this business goes to shareholders.

Small amounts of long-term sickness and accident cover are written against capital provided by shareholders and, accordingly, all profit on this business goes to shareholders.

Compliance

Within Prudential's UK businesses, matters arise from time to time as a result of inspection visits or other regulatory activity, which need to be discussed or resolved with the regulators. At any one time, there are a number of these issues and Prudential ensures that programs of corrective activity are discussed and agreed with the appropriate regulator, that such programs are properly planned, managed and resourced (using external resources as necessary), that, where appropriate, policyholders who have been disadvantaged are properly compensated, and that progress is reported to the regulators on a regular basis.

In April 1997, Prudential's primary UK regulator reported its findings after making a monitoring inspection visit earlier in the year. The report was critical of Prudential's compliance record and approach, with particular emphasis on problems in its company salesforce. Prudential was formally reprimanded by the UK regulator in December 1997 as a result of its findings.

The findings of the regulator partly influenced the decision to restructure Prudential's UK business into smaller, more transparent and more accountable business units. Prudential also specifically responded to the report by implementing a program to address the problems the UK regulator identified, by reorganizing its compliance department through significantly increasing headcount, resources and expertise and by enhancing the importance of compliance throughout the business. Prudential was advised and assisted in these efforts by external consultants and worked closely with the regulator.

Prudential undertook a number of initiatives with respect to its company salesforce, including redesigning its training programs, reassessing its marketing practices, voluntarily imposing a moratorium on recruiting and increasing central checking (a process called "validation") to 100% of all new business generated. Prudential also revised its branch monitoring program. Prudential's current primary UK regulator performed a limited review of some of the areas that had been previously criticized, and provided a report dated February 1999, which indicated the regulator does not have any significant concerns about Prudential's new compliance program. As with all such reports, however, the regulator did not comment on areas it had not reviewed or areas where it had not identified any problems.

Prudential recommenced selective recruitment in December 1998 and introduced a risk-based branch monitoring program in May 1999. In 1999 Prudential also moved away from its program of 100% validation to a risk-based validation program. These actions reflect Prudential's confidence in the effectiveness of the compliance actions it has taken.

In addition to general compliance, there are several further industry-wide issues that affect Prudential. These industry issues are discussed in more detail below. Although Prudential's relations with regulators have improved considerably since 1997, its previous regulatory position requires that it continue to focus on compliance.

Mortgage Endowment Products

One industry issue concerns low-cost endowments related to repay residential mortgages. At sale, the initial sum is set at a level such that the projected benefits assured, including an estimate of the annual bonus receivable over the life of the policy and allowing for an estimate of the expenses to be charged, will equal or exceed the mortgage debt. Because of the decrease in expected future investment returns, the UK regulator is concerned that some policies may not achieve the repayment amount. The UK regulator has worked with industry representatives to devise a program whereby companies will write to customers indicating if they may have a possible anticipated shortfall and outlining the actions customers can take to prevent this possibility.

Prudential's primary exposure in this area is in connection with Scottish Amicable's "ring-fenced" with-profits fund with regard to policies written by Scottish Amicable prior to its acquisition by Prudential. The UK regulator announced in November 2000 that as part of its review of the sale of endowment policies, it would look into instances where it considered policy holders had not been treated fairly due to "product flaws". The UK regulator has notified a number of companies including Scottish Amicable of their concerns about the basis of premium calculation. This matter is under discussion with the UK regulator.

The UK regulator issued a report in March 2001 raising concerns regarding Scottish Amicable's conduct of sales of mortgage endowments since 1999. Scottish Amicable is considering its response and will work with the regulator to resolve the concerns raised.

In April 2001, Prudential announced that, due to the shift within the marketplace towards repayment mortgages over the past two years, and the consequent significant fall in demand for endowment products, Scottish Amicable would withdraw from the mortgage endowment sales market.

Pensions Misselling

In 1988, the UK government introduced new pensions legislation in the UK Income and Corporation Taxes Act 1988 intended to encourage more individuals to make their own arrangements for their pensions. During the period from April 1988 to June 1994, many individuals were advised by insurance companies, IFAs and other intermediaries to not join, to transfer from, or to opt out of their occupational pension schemes and to invest in private pension products. The UK regulators subsequently determined that many individuals were incorrectly advised and would have been better off not purchasing the private pension product sold to them. Industry participants are responsible for compensating the persons to whom pensions were missold.

The UK regulators have established a program for the pension industry that provides the framework for reviewing cases of misselling, determining the appropriate remedial action and apportioning costs of remedial action and associated expenses. The UK regulators have divided the review into two phases. Phase 1 cases, originally referred to as priority cases, consist primarily of cases where the investor was close to retirement or had died or retired since purchasing the pension product. Phase 2 cases, originally referred to as non-priority cases, are primarily younger investors who have retirement dates that are not near-term. The regulators established deadlines for reviewing Phase 1 cases and have the power to impose sanctions where companies fail to meet the deadlines or otherwise do not comply with the regulators' guidelines for the resolution of cases of pensions misselling.

In 1997, Prudential was criticized by the regulators for the conduct of its pensions review. However, in line with other industry participants, Prudential has subsequently been working with regulators to resolve cases of pensions misselling. Prudential has established a pensions review unit that continues to review potential cases of misselling to determine what remedial action needs to be taken. The review of potential cases of misselling is difficult, requiring a complicated comparison of the value of the pension product provided to the value of the pension that the individual would have had if the individual had joined or remained with an occupational scheme. This is further complicated by the fact that the comparisons are dependent on information that has to be obtained from third parties.

Prudential agreed with the UK regulator on a process for settling certain Phase 1 cases by December 31, 1998. This target has been achieved. However, there are many cases involving reinstating affected individuals to the pension schemes they left. Because Prudential cannot control how long it will take for other pension schemes to process applications for reinstatement, there are still a number of these cases that are not finally closed.

As part of Phase 1, the UK regulator carried out a visit and, as a result, has raised concerns relating to the proper completion of certain aspects of this phase. Those concerns are the subject of a further review by external consultants on behalf of the regulator. The outcome of this review is currently uncertain. As a result of this review, additional corrective action may be initiated.

Prudential is not permitted to offer cash to its customers affected by pensions misselling. The preferred form of redress is reinstatement, but where this is not possible, Prudential has either enhanced the benefits under the personal pension or issued investors with a "guarantee". The nature of these "guarantees" is such that Prudential will guarantee that the value of the benefits payable under a personal pension will be at least equal to the value of the benefits that would have been provided by the occupational pension scheme.

Phase 2 began in 1999 and Prudential completed the initial mailings in accordance with the timetable laid down by the UK regulators. The plan Prudential submitted to the UK regulators includes completion of Prudential's review of Phase 2 cases by June 2002.

In connection with the pensions misselling review, Prudential established an initial provision in 1994 that was increased to £450 million by 1998. Subsequent movements in the pensions misselling provision have been as follows:

	Year Ended December 31,		
	2000	**1999**	**1998**
		(In £ Millions)	
Balance at January 1	**1,700**	1,100	450
Change in case numbers	**—**	202	759
Change in actuarial assumptions and method of calculation	**(117)**	261	—
Increase in provision for administrative expenses	**50**	190	—
Discount accretion	**102**	66	27
Redress to policyholders	**(134)**	(73)	(110)
Payments of administrative costs	**(126)**	(46)	(26)
Balance at December 31	**1,475**	1,700	1,100

In 2000, the provision for pensions misselling decreased by £225 million compared with an increase in 1999 of £600 million.

In 1999, the scope of the pensions misselling review was expanded by the UK regulator to include Phase 2 cases. As a result, Prudential increased the provision to reflect the increase in the number of cases to be reviewed and the possible increase in the amount to be paid to policyholders. The increase in the provision as a result of this expansion in scope amounted to £759 million in 1998 and £202 million in 1999. There were no changes in scope in 2000.

In 2000, the liability was decreased by £117 million and in 1999, the liability was increased by £261 million, to reflect changes in the method of calculation resulting from new requirements issued by the UK regulator and changes in the interest rate and mortality assumptions used.

The increase in the provision for administrative expenses of £50 million and £190 million in 2000 and 1999, respectively, reflects the additional administrative costs expected to be incurred predominantly due to the shortening of Prudential's deadline for completing the Phase 2 cases by the UK regulator from December 2004 to June 2002.

The pensions misselling liability represents the discounted value of future expected payments and as a consequence, to the extent that amounts have not been paid, the provision increases each year reflecting the accretion of the discount. The increase in the provision relating to accretion of the discount amounted to £102 million in 2000, £66 million in 1999 and £27 million in 1998.

Prudential believes that, based on current information, the pensions misselling liability, together with future investment return on the assets backing the liability, will be adequate to cover the costs of pensions misselling as well as the costs and expenses of Prudential's pension review unit established to identify and settle such cases. The 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. Prudential has estimated, based on current regulatory guidelines, that the discounted present value of reasonably possible losses might range up to an additional £160 million over that provided at December 31, 2000. This potential additional provision has been determined using more stringent assumptions, in respect of customer responses to mailings and redress in comparison to external occupational schemes, applied to those cases identified at December 31, 2000.

The calculation of the pensions misselling provision is dependent upon a number of assumptions and requirements provided by the UK regulator. Throughout the pensions misselling review process, the UK regulator has made changes to its requirements. Therefore, it is not possible to predict any additional changes to its requirements and any resultant changes to the provision that might be made in the future.

As approved by the UK regulator, the total cost of Prudential's pensions misselling is funded from the surplus assets of Prudential Assurance's with-profits fund and not from amounts set aside to fund expected future payments to existing policyholders and the related shareholder transfers. Given the strength of the with-profits fund, Prudential believes that charging the provision to the surplus assets in the fund will not have an adverse impact on the levels of bonus paid to policyholders or their reasonable expectations. In the unlikely event that this proves not to be the case, Prudential intends that an appropriate contribution to the with-profits fund be made from shareholders' funds. In view of the uncertainty, it is not practicable to estimate the level of this potential contribution.

Misselling of personal pension products has not been limited to company salesforces. Tied agents, including some of the tied agents of Scottish Amicable Life Assurance Society, have also been found to have missold personal pension products. Compensation in respect of misselling by Scottish Amicable Life Assurance Society tied agents is being paid from the "ring-fenced" SAIF with-profits sub-fund established for this business.

Free Standing Additional Voluntary Contribution Business

In February 2000, the UK regulator ordered a review of Free Standing Additional Voluntary Contribution business, which constitutes sales of personal pensions to members of company pension schemes. Individuals who have purchased these pensions instead of the Additional Voluntary Contributions ("AVC") scheme connected to their company's pension scheme may have been in a better financial position by investing their money, and any matching contributions from their employers, in their company's AVC scheme. The purpose of the UK regulator's review is to ensure that any employees disadvantaged due to not being properly informed of the benefits foregone from not investing in their AVC scheme are compensated.

The review requires companies to identify relevant investors and contact them offering to review their individual case. As a result of the work completed to date, Prudential has established a provision at December 31, 2000 of £68 million. The deadline for completing the reviews is June 30, 2002.

Prudential believes 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 reviewing Free Standing Additional Voluntary Contribution business as well as the costs and expenses of Prudential's review unit established to identify and settle such cases. The provision represents Prudential's best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

Guaranteed Annuities

During the 1970s and 1980s, life insurance companies sold personal and corporate pension policies with a guaranteed annuity rate on maturity. Due to prevailing bond yields in the late 1990s, the guaranteed levels of typically £110 per annum for a lump sum of £1,000 is now significantly above the prevailing market level (around £70 per £1,000). Prudential Assurance did not sell significant volumes of these products and has established a provision of £33 million to honor the guarantees on the products sold. Scottish Amicable Life Assurance Society sold significant volumes of these policies and provisions of £816 million have been established within the segregated with-profits SAIF sub-fund to deal with this exposure. Accordingly, this provision has no impact on shareholders.

UK Restructurings

In 1999, Prudential carried out a review of its UK operations and the board approved plans to restructure certain of its operations. The cost of the restructuring in 1999 was £148 million. Of this amount, £78 million was borne by Prudential Assurance's long-term fund and £70 million was borne by shareholders' funds in 1999.

The cost of restructuring largely related to reductions in the company salesforce pursuant to an involuntary redundancy program, reductions in associated sales management, sales support and administration staff and related property and closure provisions which in total amounted to £131 million, of which £78 million was borne by the long-term fund and £53 million charged directly to shareholders. The reduction of the salesforce by 600 consultants, the administrative and processing support staff by 800 and the sales related management and sales branch support staff by almost 800 employees will cost in total £74 million in termination benefits and related salary costs payable to former employees. The reduction in salesforce headcount reflected the removal of lower performing consultants from Prudential's business. The reduction in administrative and processing support staff is in line with a smaller salesforce. There are associated transition, downsizing and systems-related costs as a reduction of the salesforce and administration functions of £21 million in total, payable to third-party suppliers. The closure of the existing retail branch network and other retail head office and administrative buildings will cost in total £65 million in lease break, vacant lease possession and dilapidation costs. These amounts are payable to property lessors. Prudential expects the restructuring of Prudential Financial Services to result in annualized savings of approximately £175 million by 2002. The amount spent as of December 31, 2000 in connection with the above restructuring was £97 million.

Following the acquisition of M&G Group plc, integration costs associated with merging M&G's and Prudential Portfolio Managers' institutional and retail fund management operations amounted to £17 million. These costs comprise £9 million of termination benefits and other redundancy and retention costs for staff, £2 million of vacant property costs and £6 million of other consultancy and restructuring related costs. These costs were borne directly by shareholders and were fully accrued in 1999.

In February 2001, Prudential announced a plan to restructure further its direct salesforce and customer service channels in its UK insurance operations. See "—UK Business Units—Prudential Financial Services" in this section above.

Implications of Stakeholder Pensions

In 1999, the UK government announced changes that are intended to encourage more individuals to provide retirement income for themselves through increased rates of private saving. The current UK government's program began with the introduction of ISAs in April 1999 and continued with the introduction of stakeholder pensions in April 2001 and reform to the UK state pension system.

The stakeholder pension is intended to provide a pension for individuals identified as earning enough to be able to afford to make contributions towards a pension but who are not currently doing so. Key elements of the requirements include capped, lower and transparent charges based on an annual proportion of funds under management and the requirement that all employers with five or more employees make a stakeholder, occupational or group personal pension scheme available to their employees. Membership of a stakeholder pension is not, however, compulsory.

The introduction of stakeholder pensions has implications for, among other things, how Prudential designs, administers, charges for and distributes pension products. The most significant requirements involve the capping of charges and establishing a minimum acceptable contribution. The government has capped charges at 1% of the policyholder account balance per annum for stakeholder pensions, which is significantly below the charges on personal private pension products currently generally available from the UK pensions industry. In common with most providers, Prudential will need to achieve significant cost reductions to be able to operate profitably within this limit. The charge cap leaves little room for sales commissions, with the result that traditional methods of distribution, through company salesforces and IFAs, may not be commercially viable.

Stakeholder pensions have already had a significant impact on the UK pensions industry. The UK regulator has suggested that individuals who purchase personal pension products with traditional charging structures instead of waiting to purchase stakeholder pensions when they are introduced may have a claim that they have been misadvised. To minimize this risk, a number of providers of traditional regular premium products, including Prudential, have already either modified their charges on pension products or issued a guarantee that the value of the pension fund accumulated at the time stakeholder pensions are introduced will at least match the gross premiums paid to date by the individual. There was also a risk that individuals may transfer their pension business to another provider if, under existing contracts, Prudential could not match the charging structure of stakeholder pensions. For that reason, on October 17, 2000, Prudential announced that effective April 2001 charges on existing personal pensions contracts would be reduced in line with the anticipated charging for stakeholder policies.

There is also likely to be a further impact in the corporate pensions market where all employers will need to review their existing pension arrangements and ensure they fully comply with the new regulations. As part of this review, it is likely they will assess and compare product features such as charges and flexibility and, if appropriate, consider using an alternative provider.

Prudential believes that the structure of stakeholder pensions, in particular the capped cost structure, will mean that only a limited number of providers will be able to successfully offer these products. Prudential believes that both employers and employees will prefer an established brand and will focus on financial strength and security. Prudential's strong brands and financial strength position it to compete in the market that it is anticipated will develop following the introduction of stakeholder pensions.

Prudential offers stakeholder pension products through Prudential Financial Services and Prudential Intermediary Business. Prudential Financial Services plans to distribute stakeholder pensions primarily through consulting actuaries, benefits advisers and employers' corporate intranet facilities. Prudential Intermediary Business will distribute stakeholder pensions through IFAs. Prudential believes that this approach will enable it to provide stakeholder pension products that will be competitive with other offerings in the marketplace.

As of December 31, 2000, Prudential had been selected as the preferred supplier for the British Chambers of Commerce (BCC) and the Trades Union Congress (TUC) stakeholder pension schemes. To date, BCC chambers, representing 90,000 employers, have indicated that they will be supporting the BCC Stakeholder Scheme. Trade unions representing over 4.7 million individuals have expressed their support for the TUC Stakeholder Scheme, which has a potential market reach of more than 10 million individuals.

US Business

Prudential conducts its US insurance operations through Jackson National Life Insurance Company and its subsidiaries. The US operations also include PPM America, Prudential's US internal and institutional fund manager, Prudential's US broker-dealer operations (National Planning Corporation, SII Investments, Inc., IFC Holdings, Inc. and Investment Centers of America, Inc.), and Jackson Federal Bank, Prudential's savings and loan institution. In 2000, total new business premiums were up 19% over 1999 to £4,855 million and operating profit from Prudential's US operations was £466 million. However, in the first three months of 2001, US sales of new insurance premiums decreased by 20% over the corresponding period in 2000 to £1.2 billion. This decrease is primarily due to significant market corrections experienced in the US equity markets in recent months. At December 31, 2000, Prudential's US operations had approximately 1.5 million policies and contracts in effect and £30 billion of funds under management in the United States.

US Market Overview

The United States is the world's largest life insurance market in terms of premiums. Many of the factors that have affected the UK life insurance market in recent years, such as an aging population and strong economic conditions, have also affected the US market. Uncertainties surrounding the adequacy of public and private pensions benefits are increasing the incentive to fund a secure retirement privately, and the demand for income products is also expected to increase as the baby boomer generation and its parents age.

Despite favorable demographics, the US insurance industry faces a number of challenges, both from within and outside of the industry. The life insurance business is projected to grow only slowly, if at all, and competition is fierce. While the growth prospects for the annuity industry are more favorable, there are many players fighting for market share. Likewise, there is competition for retirement savings from other financial services providers, in particular, mutual fund companies and banks.

Mutual fund companies have set the standard for cost structure and service in the US financial services industry. Mutual fund products are inherently less complex, permitting providers to have a cost structure that allows more of the investment returns generated by the investment portfolios to flow to the customer. This fact and the relatively strong historical financial markets over recent years have resulted in the long-term trend of mutual fund companies taking market share from both banks and insurance companies.

There has been increasing convergence between US retail financial services providers as regulatory barriers have begun to erode and competition in the US life insurance industry has increased. Overcapacity in the industry generally has also contributed to competitive pricing and fueled consolidation, presenting opportunities to companies with below industry-average cost structures and financial strength.

Products

The demographic factors described above, as well as the increased reliance on defined contribution plans (such as 401(k) plans), have resulted in a shift in the financial services market. This shift has been away from risk protection products, such as traditional life insurance, to tax deferred savings (or asset accumulation) products, such as fixed and variable annuities. These products tend to be spread or fee based and have accounted for a significant portion of the growth in the US insurance industry in recent years.

When life insurance and annuity products initially became popular in the United States, they were interest-rate based and provided a minimum guaranteed rate of return. Declining interest rates have eroded the after-tax benefits of these products. At the same time there has been significant growth in equity markets. As a result, equity-based and equity-linked products, with and without guarantees, have become increasingly important product offerings. Reflecting this shift, industry sales of individual variable annuity products grew from $28.5 billion in 1992 to $128.2 billion in 2000, a compound annual growth rate of 20.7%. During the same period, industry individual variable annuity assets grew from $212 billion to $971 billion, a compound annual growth rate of 20.9%.

The mutual fund industry has also benefited from the shift to equity-based products. The strong equity markets in the late 1990s fueled a growth in assets under management, both through investment returns and increased contributions from the retail sector. In particular, fund managers with strong brands and investment performance have provided strong competition for individuals' retirement savings.

Distribution

Traditionally, insurance companies distributed their products through career or independent agencies. The career agencies typically received office space, training and administrative support from the sponsoring insurance company in return for directing a significant portion of their business to them. Independent agencies may receive some support from a specific insurance company, but are typically not required to specifically sell their products. The independent agencies have the ability to sell products from any insurance company.

In contrast, broker-dealers are licensed to sell products regulated by the Securities and Exchange Commission, such as variable annuities. Broker-dealers maintain "panels" of preferred providers for each type of product. Broker-dealers are often organized into firms and networks typically depending on size and function. These consist of large broker-dealers specializing in security sales and underwriting, regional broker-dealers who sell securities and perform some underwriting functions, and independent broker-dealers who primarily specialize in financial planning activities. Recently, there has been an industry trend towards insurance companies owning financial planner broker-dealers.

Until recently, regulatory barriers prohibited banks from developing and selling their own insurance products. Banks have therefore generally developed favorable supplier relationships with insurance companies and distributed their products through bank branches. These barriers to entry have begun to diminish, and alliances such as Citigroup are developing the bancassurance model in the United States market.

Direct distribution is relatively mature in the United States. Consumers are accustomed to purchasing less complex retail financial products remotely, both by telephone and via e-commerce. The mutual fund providers have led this expansion within the retail financial services industry, setting the standard for cost structure and service.

Jackson National Life

Jackson National Life is a leading provider of long-term savings and retirement products to retail and institutional customers throughout the United States. Jackson National Life offers variable annuities, equity indexed annuities, individual fixed annuities, life insurance and stable value products. By developing and offering a wide variety of products, Jackson National Life believes that it has positioned itself to compete effectively in various stock market and interest rate environments. Jackson National Life markets its retail products through various distribution channels, including independent agents, broker-dealer firms, including financial planners, and banks.

The interest-sensitive fixed annuities, equity-indexed fixed annuities, immediate annuities and life insurance products are sold through independent agents, broker-dealers and banks. For variable annuity products, which can only be sold through broker-dealers licensed by the US National Association of Securities Dealers, Jackson National Life has selling agreements with such firms and is continuing to focus on its own broker-dealer distribution channel. Its group pension department sells stable value products.

Products

The following table shows total new business premiums in the United States by product line and distribution channel for the periods indicated, and policyholder reserves by product line. Total new business premiums include deposits for investment contracts with limited or no life contingencies.

	Year Ended December 31,			Policyholder Reserves At December 31,
	2000	**1999**	**1998**	**2000**
	(In £ Millions)			
By Product				
Annuities				
Fixed annuities				
Interest-sensitive	**985**	783	630	**11,097**
Equity-indexed	**409**	431	283	**1,557**
Immediate	**71**	43	40	**690**
Variable annuities	**1,709**	1,187	531	**3,662**
Total	**3,174**	2,444	1,484	**17,006**
Life insurance				
Term life	**15**	16	17	**437**
Interest-sensitive life	**10**	8	11	**3,063**
Total	**25**	24	28	**3,500**
Stable value products				
GICs	**241**	263	342	**771**
Funding agreements	**1,415**	1,355	1,009	**3,967**
Total	**1,656**	1,618	1,351	**4,738**
Total	**4,855**	4,086	2,863	**25,244**
By Distribution Channel				
Independent agents	**1,099**	942	770	
Bank	**631**	467	267	
Broker dealer	**1,469**	1,059	475	
Group pensions department	**1,656**	1,618	1,351	
	4,855	4,086	2,863	

Annuities

The annuity products offered include:

- fixed annuities, including:
  - — interest-sensitive,
  - — equity-indexed, and
  - — immediate annuities and
- variable annuities.

Fixed Annuities

Interest-sensitive Annuities

In 2000, interest-sensitive fixed annuities accounted for 20% of total new business premiums and 44% of policyholder reserves of the US operations. Interest-sensitive fixed annuities are primarily deferred annuity products that are used for retirement planning and for providing income in retirement. They permit tax-deferred accumulation of funds and flexible payout options.

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

The policy provides that at Jackson National Life's discretion it may reset the interest rate on each policy anniversary, subject to a guaranteed minimum. By law, the minimum guarantee may not be less than 3% but for some older business it may be higher. In resetting rates and establishing minimum guarantees, the yield characteristics of Jackson National Life's investment portfolio, surrender assumptions and industry pricing are all taken into account. Administrative charges are subject to contractual maximums.

When the annuity matures, Jackson National Life either pays the amount in the accumulation account to the policyholder or begins making payments in the form of an immediate annuity product, in accordance with the policyholder's instructions. Fixed annuity policies provide for surrender charges to be assessed on surrenders generally for the first seven to nine years of the policy.

Approximately 24% of the interest-sensitive fixed annuities Jackson National Life wrote in 2000 provide for an adjustment, referred to as a market value adjustment, on surrenders in the surrender period of the policy, typically for the first nine years. This adjustment does not depend on the performance of specific assets (as in a variable annuity), but is linked to a formula that helps to match the surrender value to the value of the accumulation account at the time of surrender. The minimum guaranteed rate is not affected by this adjustment.

Jackson National Life bears the investment and surrender risk on interest-sensitive fixed annuities, and its profits come from the spread between the yield on investments and the interest credited to policyholders less initial and recurring management expenses.

Equity-indexed Annuities

In recent years, Jackson National Life's fixed annuity sales have benefited from the introduction of equity-indexed annuity products. In 2000, Jackson National Life was the third-largest provider of equity-indexed annuities in the United States based on gross premiums. During that period, equity-indexed annuities accounted for 8% of total new business premiums and 6% of policyholder reserves of US operations.

Equity-indexed annuities are deferred annuities that enable policyholders to obtain a portion of an equity-linked return but provide a guaranteed minimum return. Jackson National Life guarantees an annual minimum interest rate of 3%, but actual earnings may be higher and are based on a participation (referred to as the index participation rate) in an equity index over its term. Jackson National Life may reset the index participation rate for each premium deposit. The participation rate set applies for the term selected.

Jackson National Life hedges the equity return risk on equity-indexed products by purchasing futures and options on the relevant index. The cost of these hedges is taken into account in setting index participation rates. Recent volatility in the equity markets combined with lower bond yields has increased the cost of these hedges. In response, Jackson National Life has reduced its index participation rates on new business and developed new products with index participation rates that are less sensitive to changes in these variables.

Jackson National Life bears the investment and surrender risk on equity-indexed fixed annuities. Profit arises from the difference between the premiums received plus the associated investment income and the combined costs of meeting expenses, purchasing fixed interest securities to fund the basic guaranteed liability and purchasing options to hedge the equity return element of the policy benefits.

Immediate Annuities

In 2000, immediate annuities accounted for 1% of total new business premiums and 3% of policyholder reserves of US operations. Immediate annuities guarantee a series of payments beginning within a year of purchase and continuing over either a fixed period of years or the life of the policyholder. If the term is for the life of the policyholder, then Jackson National Life's primary risk is mortality risk. This product is generally used to provide a guaranteed amount of income for policyholders and is used both in planning for retirement and in retirement itself. Jackson National Life expects the market for this product to grow as more people reach retirement age. The implicit interest rate on these products is based on the market conditions that exist at the time the policy is issued and is guaranteed for the term of the annuity.

Variable Annuities

Jackson National Life began offering variable annuity products in November 1995. In 2000, variable annuities accounted for 35% of total new business premiums and 15% of policyholder reserves of US operations. Variable annuities are deferred annuities that have the same tax advantages and payout options as interest-sensitive and equity-indexed fixed annuities. They also are used for retirement planning and to provide income in retirement.

The primary differences between variable annuities and interest-sensitive and equity-indexed fixed annuities are investment risk and return. If a policyholder chooses a variable annuity, the rate of return will depend upon the performance of the underlying fund portfolio. The policyholder bears the investment risk, except for fixed-rate account options, where Jackson National Life guarantees a minimum fixed rate of return.

Jackson National Life credits premiums on variable annuities to a separate account. The policyholders determine how the premiums will be allocated by choosing to allocate all or a portion of their accounts either to a variety of variable sub-accounts, with a choice of investment managers, or to guaranteed fixed-rate options. The value of the portion of the separate account allocated to variable sub-accounts fluctuates with the underlying investment. Jackson National Asset Management, LLC, earns fee income as the investment adviser for the underlying funds and has retained the services of a number of other investment advisers to act as sub-advisers to Jackson National Life.

Variable annuity products are backed by specific assets that are held in a separate account. The assets in this separate account are legally "ring-fenced" and do not form part of the assets in the US general account, which backs the remainder of the insurance business in the United States. Amounts held in the separate account are not chargeable with liabilities arising out of any other business Jackson National Life may conduct. All of the income, gains or losses from these assets less specified management charges are credited to or against the policies and not any other policies that Jackson National Life may issue.

Jackson National Life earns fee income through the sale, investment and administration of the variable account options of variable annuity products. It also earns income on the spread between the interest credited on the fixed rate account and the investment income on the funds allocated to the accounts.

Life Insurance

Reflecting the competitive life insurance market place and the overall trend towards asset accumulation products, Jackson National Life's life insurance products accounted for less than 1% of the total new business premiums and 14% of policyholder reserves of US operations in 2000. The products offered include term life insurance and interest-sensitive life insurance. Each of these types of insurance policies can be modified using several options and riders to provide particular benefits, including waiver of premium, accidental death benefit, supplemental term insurance and guaranteed purchase options.

Term Life

Jackson National Life offers term life insurance products that are renewable annually as well as ten-, fifteen-, twenty- and thirty-year level premium plans. Premiums are set when the policy is purchased. Premium payment levels are subject to the guaranteed maximums specified in the contract. Coverage may often be renewed at an increased premium. Term life products do not contain an accumulation component and, accordingly, have no cash value. Term life products offer pure insurance cover for the specified period of time.

Beginning in late 1995, Jackson National Life entered into reinsurance agreements to cede 80% of new writings of level premium term life products to take advantage of favorable reinsurance pricing. Currently, it cedes 90% of new writings of level premium term products.

Interest-sensitive Life

Interest-sensitive life insurance products include universal life insurance plans and a variety of fixed premium interest-sensitive whole life insurance products. Jackson National Life sold interest-sensitive whole life insurance for many years and began to sell universal life insurance in early 1995.

Universal life insurance has flexible premiums and adjustable death benefits. Jackson National Life credits to the policyholder's account an amount equal to premiums less specified charges. In addition, interest is credited at the rate set. The interest rate set is subject to contractual minimums and typically relates to general market interest rate movements. Jackson National Life also establishes the level of administrative charges, subject to contractual maximums, which are deducted from the account value.

Interest-sensitive whole life insurance is similar to universal life insurance except that premium levels and guaranteed minimum non-forfeiture values are specified in the policy. The guaranteed minimum non-forfeiture values depend upon the payment of the specified premiums.

Stable Value Products

Stable value products are guaranteed investment contracts (GICs) and funding agreements. In 2000, stable value products accounted for 34% of total new business premiums and 19% of policyholder reserves of US operations. Jackson National Life began marketing GICs to institutional investors in December 1995. The GICs are marketed by its group pension department to defined contribution pension and profit-sharing retirement plans. Funding agreements are marketed to institutional investors, including corporate cash accounts and securities lending funds, as well as money market funds. At December 31, 2000, Jackson National Life was a top ten provider of stable value business in terms of liabilities.

Four types of stable value products are offered:

- traditional GICs,
- funding agreements,
- medium term note funding agreements and
- synthetic GICs.

Traditional Guaranteed Investment Contracts

Under a traditional GIC, the policyholder makes a lump sum deposit. Interest is paid on the deposited funds, usually on a quarterly basis. The interest rate paid is fixed and is established when the contract is issued.

Traditional GICs have a specified term, usually two to three years, and typically provide for phased pay outs. Jackson National Life tailors the scheduled pay outs to meet the liquidity needs of the particular retirement plan. If deposited funds are withdrawn earlier, an adjustment is made that approximates a market value adjustment.

Jackson National Life sells GICs to retirement plans, in particular 401(k) plans. The traditional GIC market is extremely competitive. This is due in part to competition from synthetic GICs.

Funding Agreements

Under a funding agreement, the policyholder either makes a lump-sum deposit or makes specified periodic deposits. Jackson National Life agrees to pay a rate of interest, which may be fixed but which is usually a floating short-term interest rate linked to an external index. Interest is paid quarterly to the policyholder. The average term for the funding agreements is one to two years. At the end of the specified term, policyholders typically re-deposit the principal in another funding agreement. Jackson National Life makes its profit on the spread between the yield on its investment and the interest rate credited to policyholders.

Typically, brokerage accounts and money market mutual funds are required to invest a portion of their funds in cash or cash equivalents to ensure sufficient liquidity to meet their customers' requirements. The funding agreements permit termination by the policyholder on 7 to 90 days' notice, and thus qualify as cash equivalents for the clients' purposes. Funding agreements terminable by the policyholder with less than 90 days' notice account for less than 1.3% of Jackson National Life's total policyholder reserves.

Medium Term Note Funding Agreements

Jackson National Life has also established a European medium-term note program that accesses a new market for Prudential. The notes offered may be denominated in any currency. Notes are issued to institutional investors by a special purpose vehicle and are secured by funding agreements issued by Jackson National Life.

Synthetic Guaranteed Investment Contracts

Under a synthetic GIC, the policyholder does not deposit any funds with Jackson National Life. Instead, the policyholder continues to own its plan assets and Jackson National Life agrees to guarantee that the plan will have sufficient liquid funds to meet its obligations to its participants.

This guarantee is provided for a fee. The event that could, in practice, cause a payment to be made under this guarantee would be an unexpected surge of withdrawals by scheme members at a time when asset values are depressed. This risk is mitigated through careful underwriting and through a number of features associated with these contracts, including controls on the plan's investments, requirements for "buffer funds" to absorb unexpected fluctuations in member withdrawals and, for most contracts, experience rating of the crediting rates granted to scheme members.

Jackson National Life sells its synthetic GICs to retirement plans primarily as an accommodation for its existing customers and therefore do not expect this business to grow much, if at all, beyond its current size. At December 31, 2000, Jackson National Life guaranteed £31 million of synthetic GICs. Because Jackson National Life does not own the assets underlying synthetic GICs, it does not recognize premium income or establish reserves, but it does recognize fee income.

Distribution and Marketing

Jackson National Life distributes products in all 50 states of the United States and in the District of Columbia, although not all products are available in all states. Operations in the State of New York are through a New York insurance subsidiary.

Jackson National Life has focused on independent distribution systems and has avoided the fixed costs associated with recruiting, training and maintaining employee agents. It supports its network of independent agents and brokers with education and training programs. A substantial portion of the costs associated with generating new business are not fixed costs but vary directly with the level of business produced. As a result, industry figures show that the costs are low relative to other US insurers.

In recent years Jackson National Life has been actively diversifying the methods by which it distributes its products. In part, this diversification of distribution reflected the strategy of product diversification. For instance, variable annuities can only be sold by registered broker-dealers and stable value products are targeted at institutions and direct plan sponsors and intermediaries acting on their behalf. Jackson National Life has developed and tailored its distribution capabilities accordingly.

Jackson National Life offers internet-based support to its broker-dealers. It continues to expand its internet-based services, increasing amounts of information available for both customers and agents.

Independent Agents

The insurance and fixed annuity products are distributed through independent agents located throughout the United States. These 56,500 licensed insurance agents or brokers, who also may represent other companies, are supported by 16 regional marketing offices. Jackson National Life has continued to review its ranks of licensed agents during the year, actively identifying non-performing agents and removing them from their books. This initiative is aimed at improving Jackson National Life's ability to service its top agents and assist them in generating greater productivity. Jackson National Life generally deals directly with writing agents and brokers thereby eliminating intermediaries, such as general agents. This distribution channel, called "Deal Direct", has enabled it to generate significant volumes of business on a low, variable cost basis.

While historically all independent agents have been treated the same regardless of their characteristics and levels of production, recently Jackson National Life has been distinguishing between the agent producer groups and supporting them differently according to their production levels and specific needs. In some cases it has terminated relationships that were believed to be unproductive. Jackson National Life believes this will create incentives to generate more new business and will enable effective focused sales support.

Jackson National Life is responsible for providing agents with product information and sales materials.

Broker-dealers

Jackson National Life Distributors, Inc., a broker-dealer, is the primary wholesale distribution channel for the variable annuity products. Jackson National Life Distributors also sells equity-indexed annuities and fixed annuities. An internal network of wholesalers supports this distribution channel. These wholesalers meet directly with broker-dealers and financial planners and are supported by an extensive home office sales staff. There are approximately 650 active selling agreements with regional and independent broker-dealer organizations throughout the United States. These selling agreements provide Jackson National Life with access to approximately 20,000 registered representatives.

In September 2000 Jackson National Life acquired IFC Holdings Inc., which incorporated INVEST Financial Corporation and Investment Centers of America Inc. Together with National Planning Corporation and SII Investments, Inc., Jackson National Life's existing broker-dealers, it has contracts with approximately 2,300 registered representatives.

Jackson National Life is responsible for training its broker-dealers, providing them with product information and sales materials and monitoring their activities from a compliance perspective.

Banks, Credit Unions and Other Financial Institutions

Jackson National Life distributes its life insurance and annuity products through banks, credit unions and other financial institutions and through third-party marketing organizations that serve these institutions.

Jackson National Life is a leading provider of annuities offered through banks and credit unions. This channel has access to over 15,000 financial institution representatives.

Jackson National Life has established distribution relationships with medium-sized regional banks, which it believes are unlikely to develop their own insurance product capability. Consolidation in the US banking industry is directly impacting this strategy and Jackson National Life will continue to review how to participate effectively in this market.

Group Pension Department

Jackson National Life markets its stable value products principally through its group pension department. It has direct contacts with banks, municipalities, asset management firms and direct plan sponsors. Stable value products are distributed and marketed through intermediaries to these groups.

Factors Affecting Pricing of Products and Asset Liability Management

Jackson National Life prices products based on assumptions about future mortality, investment yields, expenses and persistency. Pricing is influenced by competition and by its objectives for return on capital. Although Jackson National Life includes a profit margin in the price of its products, the variation between the assumptions and actual experience can result in the products being more or less profitable than it was assumed they would be. This variation can be significant.

Jackson National Life designs its interest-sensitive products and conducts its investment operations to match closely the duration of the assets in its investment portfolio with the annuity, whole life, universal life and guaranteed investment contract product obligations. Jackson National Life seeks to achieve a target spread between what it earns on its assets and what it pays on its liabilities by investing principally in fixed-rate securities and in options to match the equity-related returns under its equity-indexed products.

Jackson National Life segregates its investment portfolio for certain investment management purposes and as part of its overall investment strategy into four parts: annuity without market value adjustment, fixed annuity with market value adjustment, equity-indexed annuities and stable value liabilities. The portfolios backing fixed annuities with and without market value adjustments have similar characteristics and differ primarily in duration. The portfolio backing the stable value liabilities has its own mix of investments that meet more limited duration tolerances. Consequently the stable value portfolio is managed to permit less interest rate sensitivity and limited exposure to mortgage-backed securities. At December 31, 2000, less than 6.2% of the stable value portfolio was invested in residential mortgage-backed securities.

The fixed-rate products may incorporate surrender charges, market value adjustments, two-tiered interest rate structures or other limitations relating to when policies can be surrendered for cash, in order to encourage persistency. At December 31, 2000, approximately 71% of Jackson National Life's fixed annuity reserves had surrender penalties or other withdrawal restrictions. Substantially all of the stable value portfolio had withdrawal restrictions or market value adjustment provisions.

Underwriting

The decision to underwrite a particular life policy depends upon the assessment of the risk to Jackson National Life represented by the proposed policy. The risk selection process is performed by the underwriters who evaluate policy applications on the basis of information provided by the applicant and other sources. Specific medical tests may be used to evaluate policy applications based on the size of the policy, the age of the applicant and other factors.

Jackson National Life's underwriting rules and procedures are designed to produce mortality results consistent with the assumptions used in product pricing while providing for competitive risk selection.

Reserves

Jackson National Life uses reserves established on a US GAAP basis as the basis for consolidation into Prudential's UK GAAP accounts.

For the fixed and variable annuity contracts and stable value products, the reserve is the policyholder's account value. For the immediate annuities, reserves are determined as the present value of future policy benefits. Mortality assumptions are based on the 1983a Individual Annuitant Mortality Table. Interest rate assumptions currently range from 5.35% to 8.00%.

For the traditional term life contracts, reserves for future policy benefits are determined using the net level premium method and assumptions as to mortality, interest, policy persistency and expenses. Mortality assumptions, based upon the 1975-1980 Basic Select and Ultimate tables, range from 50% to 90%, depending on underwriting classification and policy duration. Interest rate assumptions range from 6.0% to 9.5%. Persistency and expense assumptions are based on experience.

For the interest-sensitive life reserves and single premium life reserves, reserves approximate the policyholder's accumulation account.

Reinsurance

Jackson National Life reinsures portions of the coverage provided by its insurance products with other insurance companies under agreements of indemnity reinsurance. Reinsurance assumed from other companies is not material.

Indemnity reinsurance agreements are intended to limit a life insurer's maximum loss on a large or unusually hazardous risk or to obtain a greater diversification of risk for the life insurer. Indemnity reinsurance does not discharge the original insurer's primary liability to the insured. Jackson National Life's reinsured business is ceded to numerous reinsurers and the amount of business ceded to any one reinsurer is not material. Typically, the reinsurers have a rating of A or higher.

Jackson National Life limits the amount of risk it retains on new policies. Currently, the maximum risk that is retained on new policies is $1.0 million ($1.5 million on last survivor life business). Jackson National Life is not a party to any risk reinsurance arrangement with any reinsurer pursuant to which the amount of reserves on reinsurance ceded to such reinsurer equals more than 1% of total policy reserves.

Beginning in late 1995, Jackson National Life entered into reinsurance agreements to cede 80% of its new level premium term life insurance business written in the United States to take advantage of competitive pricing in the reinsurance markets. Beginning January 1, 1999, it began to cede 90% of new writings of level premium term products. Jackson National Life intends to continue to cede an increased proportion of new term life insurance business for as long as pricing in the reinsurance markets remains favorable.

Policy Administration

Jackson National Life provides a high level of administrative support for both new and existing policyholders. Jackson National Life's ability to implement new products quickly and provide customer service is supported by integrated computer systems that propose, issue and administer complex life-insurance and annuity contracts. Jackson National Life continues to upgrade its life insurance administration and underwriting systems and its fixed and variable annuity administration systems to enhance the service capabilities for both new and existing policies.

Jackson Federal Bank

Prudential further diversified its business in the United States through the purchase in 1998 of a federally chartered savings association, First Federal Savings and Loan Association of San Bernardino, which is now called Jackson Federal Bank. The addition of a federally chartered savings association has resulted in an expanded product range in the United States and is expected to give Jackson National Life the option to roll out a wider range of banking products including loans, checking accounts and credit cards. In 2000, Jackson National Life further expanded its banking operations in the United States. In February 2000, Jackson National Life announced the acquisition of three Fidelity Federal Branches and in September 2000 Jackson National Life acquired Highland Bancorp Incorporated, the holding company for Highland Federal Bank, for US$110 million. Highland Federal Bank and the three Fidelity Federal Branches were merged with and renamed as Jackson Federal Bank.

PPM America

PPM America is Prudential's US fund management operation, with offices in Chicago and New York. Its primary focus is to manage funds for Jackson National Life and therefore the majority of funds under management are fixed interest in nature. PPM America has developed considerable expertise in managing credit risk and has increasingly invested its funds in higher credit risk investments. Recently, PPM America has launched a number of institutional high yield and special investment vehicles to leverage these capabilities into new profitable areas.

Asian Business

Prudential has operations in eleven Asian countries. Prudential's primary insurance businesses are in Singapore, Hong Kong, Malaysia and Taiwan. Prudential also has operations in Thailand, Indonesia, The Philippines, China, Vietnam, India and Japan as well as retail mutual fund operations in India, Japan and Taiwan.

Development of Prudential's Asian Business

Prudential's Asian operations are managed by its Hong Kong-based regional head office. The savings, protection and investment products it offers in Asia are tailored to the local markets in which it operates. Prudential is the largest UK-based life insurer in Asia.

Prudential's operations in Asia date from 1923, when it opened a branch office in India, which served the Indian sub-continent and several Middle Eastern countries with historic ties to the United Kingdom. In 1924 Prudential opened a branch office in Malaysia. Prudential expanded into Singapore in 1931 and opened a branch office in Hong Kong in 1964. In 1956, Prudential's Indian operations were nationalized and, in 1984, the Malaysian government required Prudential to sell a majority interest in its Malaysian operations to a local company. Prudential began expanding again in Asia during the mid-1990s, establishing operations in Thailand, The Philippines and Indonesia.

Prudential launched its mutual fund business in India in 1998 through its joint venture Prudential ICICI Asset Management with The Industrial Credit and Investment Corporation of India Ltd. (ICICI). As of December 31, 2000, Prudential ICICI Asset Management had £695 million of funds under management.

In Vietnam, Prudential was awarded a license to write life insurance during the last quarter of 1999. In November 1999, Prudential established a wholly-owned subsidiary in Vietnam to write life insurance. Prudential is one of only five companies licensed to write life insurance in Vietnam.

In late 1999, Prudential acquired a 74% interest in Chinfon Life Insurance Company Limited, a Taiwanese life insurance company, and following acquisitions of minority stakes during 2000, Prudential's ownership increased to 81% as of December 31, 2000. During 1999, Prudential also entered into a joint venture with the Bank of China International to serve the Hong Kong Mandatory Provident Fund, which came into effect in December 2000. Prudential's joint venture with the Bank of China International (in which Prudential has a 36% interest) provides Prudential with access to the Mandatory Provident Fund market in Hong Kong through one of the largest retail bank branch networks in Hong Kong.

In 1999, Prudential became the first UK life insurance company to be invited by the People's Republic of China to apply for a license to write life insurance. In 2000 Prudential established a fifty-fifty joint venture with the China International Trust & Investment Corporation and received a license to write life insurance in the city of Guangzhou, China. This joint venture (CITIC Prudential Life Insurance Company) began operations in late 2000. There is only one other foreign insurance company that has a license to write life insurance in Guangzhou.

In October 2000, Prudential acquired an 89% interest in a Taiwanese mutual fund company, renamed Prudential Securities Investment Trust Enterprise (Prudential SITE), further expanding its growing Asian portfolio. Prudential SITE's funds under management at December 31, 2000 were £0.9 billion. In November 2000 Prudential announced that ICICI Prudential Life Insurance, its joint venture with ICICI Ltd. (in which Prudential has a 26% interest), had received a license from the Insurance Regulatory and Development Authority to commence life insurance operations in India.

In February 2001, Prudential acquired Orico Life in Japan, an operationally and financially sound modern Japanese life insurance company, for £133 million.

PPM Asia, Prudential's Asian fund management operation, has offices in Singapore, Hong Kong and Tokyo. At December 31, 2000, PPM Asia had US$12.1 billion (£8.1 billion) of funds under management. Prudential's first unit trust in Japan was launched in August 2000.

Prudential's strategy in Asia is to diversify its products and distribution and to expand geographically. Historically, Prudential's local agent salesforces have been its primary distribution channel. However, in April 1999, through its agreement with Standard Chartered Bank, Prudential added a bancassurance distribution channel to sell life insurance products in Singapore and Hong Kong, and this was extended to Malaysia in 2000. Prudential was already selling products in Indonesia through its Indonesian joint venture partner, Bank Bali.

New Business Premiums

Asian market conditions have improved from the economic uncertainty experienced in 1998, and accordingly, Prudential's new business insurance premiums have increased. In 2000, Prudential had the third-largest market share in new regular premium business and the second-largest share in new single premium business in Singapore. Prudential also improved to second place in Malaysia in respect of new regular premium business and ranked fourth in Hong Kong in respect of new regular premium business.

The following table shows Prudential's Asian life insurance new business premiums and UK GAAP policyholder reserves by territory for the periods indicated. In this table "Other Countries" includes Thailand, Indonesia, The Philippines, Vietnam, China, and India. The 1999 result includes two months of operations in Taiwan acquired in 1999.

	Years Ended December 31,			Policyholder Reserves At December 31,
	2000	**1999**	**1998**	**2000**
	(In £ Millions)			
Singapore	**285**	192	66	**2,051**
Hong Kong	**62**	44	30	**506**
Malaysia	**47**	35	21	**300**
Taiwan	**79**	5	—	**442**
Other countries	**31**	13	4	**41**
Total	**504**	289	121	**3,340**

In addition, for the year ended December 31, 2000, Prudential had £2,259 million in gross sales of investment products in India, Taiwan and Japan.

Products

The savings and protection products offered in Asia are generally similar to the products offered in the United Kingdom and include with-profits, non-participating and, in some countries, unit-linked products. However, unlike the United Kingdom, where savings products predominate, Prudential's business in Asia is more balanced between savings and protection products. In 2000, with-profits products represented 33% of Asia's total new business insurance premiums.

Prudential offers debt, equity and money market mutual fund investment products in India, Taiwan and Japan.

In Hong Kong, Prudential's life insurance business is supplemented by personal lines property and casualty insurance products. In 2000 this business had gross premiums of £11.2 million.

Singapore

Prudential established its operations in Singapore in 1931 and conducts them through Prudential Assurance Company Singapore (Pte) Limited, a wholly-owned subsidiary of The Prudential Assurance Company Limited. In 2000, Prudential was the second-largest life insurer in Singapore in terms of new single premiums and the third largest in terms of new regular premium business. Prudential's Singapore operation was the largest of its Asian operations in terms of total premiums in 2000, contributing 57% of total Asian new business insurance premiums.

Fourteen companies are authorized to operate in the life insurance market in Singapore. Four companies account for over 80% of the market in terms of new weighted premiums. The Monetary Authority of Singapore closely regulates this mature and highly competitive market. In 1999, insurance penetration was estimated to be 76% in a country of 3.2 million people.

Singapore has a Central Provident Fund in which each employed individual has an account in which he or she is obliged to make contributions, currently equal to 20% of their salary. Employers are obliged to make contributions to their employees' accounts. This amount was reduced from 20% of salary to 10% at the start of 1999, although it has since increased to 12% of salary.

The Central Provident Fund was liberalized as of January 1, 1997 and participants were permitted to use a greater proportion of their funds to purchase authorized insurance, pension and other regulated products. As a result, single premium business volumes increased for the Singapore life insurance industry generally in 1997. This liberalization was an exceptional event that resulted in increased single premium business volumes for Prudential in that year. Business volumes for 1999, however, returned to levels similar to those experienced in 1996.

The products Prudential offers in Singapore include a range of with-profits and non-participating term, whole life and endowment life insurance policies and unit-linked products. Prudential also offers health, critical illness and accident cover as supplements to its life products. In 1993, Prudential was the first life insurance company to introduce unit-linked products to the Singapore market. In 1999, Prudential launched a health benefit product designed specifically for women and in 2000, a comprehensive children's education and health plan. In addition, in 2000 Prudential launched PRUeSaver, its first insurance product designed specifically for distribution via the internet.

Prudential distributes its products in Singapore primarily through its local agent salesforce. In 1999, Prudential began distributing products through consultants based in branches of Standard Chartered Bank.

Hong Kong

Prudential's Hong Kong operations are conducted through a branch office of The Prudential Assurance Company Limited. Prudential opened its branch in 1964 writing property and casualty insurance. It operates in a competitive and relatively mature market. According to the Hong Kong Office of the Commissioner of Insurance's annual report for 2000, in 1999 insurance penetration was approximately 63% in a country of 6.7 million people. In 2000, Prudential was the fourth-largest life insurer in Hong Kong in terms of new regular premium business.

As from December 1, 2000, employees, employers and the self-employed became obliged to make contributions to the Mandatory Provident Fund (MPF). The plans that comprise the Mandatory Provident Fund are defined contribution pension plans with immediate vesting, preservation until retirement (or some other event specified by legislation) and full portability, with plans arranged at the employer level, rather than the individual level. Individuals are required to make mandatory contributions of 5% of salary and employers make contributions equal to 5% of the employee's salary to the individual's accounts in the Fund. Both employee and employer contributions are subject to a maximum amount, currently HK$1,000 per month. The funds are invested in a range of mututal funds offered by the MPF provider. Additional contributions are possible, and are tax deductible, up to 15% of salary for the majority of employees.

The Mandatory Provident Fund Authority licenses providers to establish and manage plans and Prudential's venture with BOCI was awarded a license in November 1999. Total annual contributions are expected to exceed HK$20 billion (£1.6 billion) for the first year of the Mandatory Provident Fund, which was launched on December 1, 2000. Prudential expects that the market will be highly competitive, with many of the major banks, insurance companies and fund managers competing for market share.

Prudential offers both individual and group products in Hong Kong, including life insurance, health insurance and pensions. The individual life insurance products offered include with-profits products, unit-linked products and other non-participating products, together with accident and critical illness policies. The property and casualty insurance Prudential writes in Hong Kong is primarily personal lines, with a small book of commercial business.

Many of the most popular products in Hong Kong are US-style products and not UK-style with-profits products. Although Prudential does not offer US-style products, it has introduced a new product that is an adaptation of its with-profits product. This product offers guaranteed benefits (both protection and cash value) and allows policyholders to withdraw in cash amounts equal to the annual bonuses declared and credited to their accumulation accounts. Terminal bonuses are also paid in cash. This cash payment feature distinguishes Prudential's Hong Kong with-profits products from similar products it offers elsewhere in Asia.

Prudential's products in Hong Kong are distributed primarily through its local agent salesforce. At December 31, 2000, Prudential had a salesforce of over 1,800 agents selling its products face-to-face. In April 1999, Prudential began marketing and distributing products to customers of Standard Chartered Bank.

Malaysia

Prudential's Malaysian office opened in 1924 as a branch of The Prudential Assurance Company Limited. Prudential began writing life insurance there in 1931. In 2000, Prudential ranked second in Malaysia in terms of new regular premium business. There are 18 licensed life insurance companies covering a market of 23 million people.

The products Prudential traditionally offers in Malaysia are with-profits and non-participating products and include whole life, health insurance and accident and critical illness cover products.

Prudential introduced unit-linked products to the Malaysian market. In 1997, Prudential was the first company to offer single-premium unit-linked products and, in August 1999, it was the first company to offer a regular-premium unit-linked product.

Prudential distributes its products in Malaysia almost entirely through its local agent salesforce of over 5,700 agents, as at December 31, 2000. In 2000, Prudential extended its bancassurance agreement with Standard Chartered Bank into Malaysia.

Taiwan

In 2000, Prudential's Taiwanese operation was the second-largest of its Asian operations in terms of total new business insurance premiums and the largest in terms of new regular premium insurance business. For the ten months ended October 2000, Prudential was the eighth-largest life insurance company in Taiwan in terms of first year individual life premiums with a market share of 2.4%. Taiwan had a population of 22 million people in 2000.

In October 2000 Prudential acquired an 89% interest in Prudential SITE. Prudential SITE was established in 1992 and at December 31, 2000 was the eleventh-largest unit trust company in Taiwan. Its product range includes 13 equity funds and four bond funds, held by more than 80,000 investors, as at December 31, 2000.

China

Prudential was granted a license to write life insurance in the city of Guangzhou in China. During 1999, Prudential formed a venture with the China International Trust & Investment Company to write life insurance policies under this license and in October 2000 its life insurance operation in China was officially launched. Currently, only one other foreign company offers life insurance products in the city of Guangzhou. Guangzhou had a population of approximately seven million people in 2000.

India

In 1998, Prudential entered into an agreement with ICICI, a leading Indian financial services company, pursuant to which it has a 55% stake in an entity that offers mutual fund products in India. Prudential's funds offer a choice of different risk profiles to an investor. At December 31, 2000, Prudential had £695 million of funds under management.

Prudential distributes its investment products in India through brokers and bank branches, as well as an agent salesforce. The direct and broker channels have been Prudential's primary distribution channels to date, accounting for more than 90% of its sales in 2000.

Following the Insurance Regulatory and Development Authority Act passed by the Indian government, ICICI Prudential Life Insurance received a license from the Insurance Regulatory and Development Authority and commenced life insurance operations in India in November 2000. In 2000, India had a population of approximately one billion people.

Thailand, Indonesia, The Philippines and Vietnam

Prudential also has life insurance operations in Thailand, Indonesia, The Philippines and Vietnam. In Thailand, The Philippines and Vietnam, Prudential's primary distribution channel is its local agent salesforces. In Indonesia, in addition to its local agent salesforce, Prudential also has a bancassurance distribution channel with its joint venture partner, Bank Bali. Bank Bali has over 200 branches in Indonesia. In Vietnam, Prudential was the first foreign wholly-owned company with a license to sell life insurance, and in 2000 it sold over 100,000 policies. In April 2001 Prudential announced its acquisition of the majority holdings of Allstate's life operations in Indonesia and The Philippines, subject to regulatory approvals.

Japan

In February 2001, Prudential acquired Orico Life in Japan, an operationally and financially sound modern Japanese life insurance company, for £133 million. Orico Life, established in 1990, is based in Tokyo and has operations in a further 10 locations in Japan. It has over 240,000 policies in force, with total assets at March 31, 2000 of £650 million. It offers a wide range of products including term, saving and protection products. It uses a multi-channel distribution system that includes professional agents, financial institutions and accountants. In 2000, Japan had a population of 127 million.

European Business

In November 1999, Prudential announced the formation of Prudential Europe, a new business segment formed to implement its strategy in continental Europe. Prudential's European operations encompass both the manufacture and distribution of products under the Prudential and Scottish Amicable brands into continental Europe through Prudential's existing operations and strategic distribution arrangements into which Prudential has entered and into which it aims to enter in the future.

Continental Europe is a market that is attractive to Prudential because many of the demographic and economic trends familiar in the United Kingdom and the United States are also evident in continental Europe. Prudential believes its skills in developing equity-backed products and its rapidly developing e-commerce skills will provide it with opportunities to participate in the broader European financial services market.

Germany

The products offered in Germany include unit-linked pension and protection products marketed into Germany by Scottish Amicable Life International, an Irish company that has the benefit of tax advantages applicable to offshore companies. Prudential achieved an estimated 3% market share of that business in 2000. Prudential distributes its products in Germany through its local agent salesforce.

In 1999 Prudential established a non-exclusive distribution arrangement with Signal Iduna, one of Germany's largest life insurance companies. Prudential commenced selling a long-term care bond under the Prudential brand through this joint venture in June 2000.

France

Prudential is in the process of building a local management team in France and has established a Paris branch of Prudential Assurance, demonstrating its commitment to developing its position in the French market.

During 2000, Prudential obtained regulatory approval to sell an equity-backed life insurance product, Prudential Europe Vie. This is a single premium savings product that offers a choice of investment through the Prudential life fund or Réactif, a unit-linked fund provided by Véga Finance. The product was launched in January 2001 and is initially being sold through independent financial advisers approved by Centre Français du Patrimoine, a subsidiary of Crédit Foncier de France and the largest multi-brokerage network in France.

Prudential has continued to co-operate with CNP Assurance, the largest distributor of financial products in France, with whom it entered into a memorandum of understanding in 1999. This arrangement gives Prudential access to local markets and large-scale distribution networks.

Investments

General

The overall financial strength of the Prudential group and the results, both current and future, of the insurance business are in part dependent upon the quality and performance of the various investment portfolios in the United Kingdom, the United States and Asia.

Prudential's Total Investments

The following table shows Prudential's insurance and non-insurance investments at December 31, 2000. The "Other" column includes central funds and funds in respect of non-insurance operations. Assets held to cover linked liabilities relate to unit-linked and variable annuity products.

In this table, investments are valued as set out in Note 3 of the notes to Prudential's consolidated financial statements.

	At December 31, 2000							
	Insurance						Banking	
	UK	US	Asia	Europe	Other	Sub-total	UK and US	Total
	(In £ Millions)							
Other financial investments								
Debt and other fixed income securities	**28,271**	**18,882**	**1,382**	**11**	**48**	**48,594**	**3,721**	**52,315**
Equity securities	**50,077**	**312**	**770**	**3**	**70**	**51,232**	**8**	**51,240**
Loans and other	**2,771**	**4,822**	**474**	**33**	**199**	**8,299**	**4,614**	**12,913**
Total other financial investments	**81,119**	**24,016**	**2,626**	**47**	**317**	**108,125**	**8,343**	**116,468**
Real estate								
Investment	**9,976**	**16**	**81**	**—**	**—**	**10,073**	**—**	**10,073**
Company-occupied	**136**	**37**	**44**	**—**	**13**	**230**	**12**	**242**
Total real estate	**10,112**	**53**	**125**	**—**	**13**	**10,303**	**12**	**10,315**
Sub-total	**91,231**	**24,069**	**2,751**	**47**	**330**	**118,428**	**8,355**	**126,783**
Participating interests	**—**	**—**	**—**	**—**	**83**	**83**	**—**	**83**
Total investments	**91,231**	**24,069**	**2,751**	**47**	**413**	**118,511**	**8,355**	**126,866**
Assets held to cover unit-linked liabilities	**13,359**	**3,739**	**644**	**581**	**—**	**18,323**	**—**	**18,323**
Total	**104,590**	**27,808**	**3,395**	**628**	**413**	**136,834**	**8,355**	**145,189**

Prudential's Investment Yields

The following table shows the income from the investments of Prudential's continuing operations by asset category for the periods indicated. This table does not include investment income from unit-linked and variable annuity products, or from banking investments. Yields have been calculated using the average of opening and closing balances for the appropriate asset.

	Year Ended December 31,					
	2000		1999		1998	
	Yield	Amount	Yield	Amount	Yield	Amount
	(In £ Millions, except percentages)					
Debt and other fixed income securities						
Net investment income	**7.4%**	**3,264**	7.1%	2,732	7.5%	2,645
Net realised investment gains	**1.2%**	**533**	0.6%	212	1.3%	462
Net unrealized investment (losses) gains	**(1.6)%**	**(717)**	(4.1)%	(1,571)	3.6%	1,257
Ending assets		**48,594**		39,833		37,185
Equity investments						
Net investment income	**2.3%**	**1,268**	2.7%	1,451	3.2%	1,527
Net realised investment gains	**11.1%**	**6,022**	8.2%	4,368	4.9%	2,331
Net unrealized investment (losses) gains	**(13.1)%**	**(7,146)**	11.3%	6,024	4.0%	1,889
Ending assets		**51,232**		57,693		49,088
Loans and other						
Net investment income	**8.7%**	**721**	8.3%	629	8.4%	534
Net realised investment gains	**0.0%**	**4**	0.4%	30	1.5%	97
Net unrealized investment gains	**1.0%**	**87**	0.0%	1	1.0%	63
Ending assets		**8,299**		8,341		6,741
Real estate						
Net investment income	**7.5%**	**716**	7.7%	617	8.3%	567
Net realised investment gains	**1.5%**	**143**	1.3%	103	0.5%	32
Net unrealized investment gains	**3.9%**	**369**	7.8%	627	4.0%	253
Ending assets		**10,303**		8,763		7,298
Total (excluding unit-linked and cash)						
Net investment income	**5.1%**	**5,969**	5.1%	5,429	5.5%	5,273
Net realised investment gains	**5.8%**	**6,702**	4.4%	4,713	3.0%	2,922
Net unrealized investment (losses) gains	**(6.4)%**	**(7,407)**	4.7%	5,081	3.6%	3,462
Ending assets		**118,428**		114,630		100,312

Prudential's Insurance Investment Strategy and Objectives

Prudential's insurance investments support a range of businesses operating in many geographic areas. Each of the operations formulates a strategy, based on the nature of its underlying liabilities, its level of capital and its local regulatory requirements. Where the nature of underlying liabilities, level of capital and local regulatory requirements permit, Prudential tends to invest its assets predominantly in equities and real estate that have, over longer periods, provided superior returns to fixed interest assets.

Management of Insurance Funds

Except for a small amount of unit-linked business and variable annuity business, amounting to less than 4% of Prudential's own funds under management at December 31, 2000, Prudential manages its insurance funds principally through its fund management businesses, M&G in the United Kingdom together with PPM America in the United States and PPM Asia in Singapore, Hong Kong and Tokyo.

In each of the operations, local management analyzes the liabilities and determines asset allocation, benchmarks and permitted deviations from these benchmarks appropriate for its operation. These benchmarks and permitted deviations are agreed with internal fund managers, who are responsible for implementing the specific investment strategy through its local fund management operations.

Investments Relating to UK Insurance Business

Strategy

In the United Kingdom, Prudential tailors its investment strategy for long-term business, other than unit-linked business, to match the type of product a portfolio supports. The primary distinction is between with-profits portfolios and non-participating portfolios, which include the annuity portfolios. Generally, the objective is to maximize returns while maintaining investment quality and asset security and adhering to the appropriate government regulations.

With-profits contracts are long-term contracts with minimal guaranteed amounts, the nature of which permits Prudential to invest primarily in equities and real estate. Accordingly, the with-profits fund investment strategy emphasizes a well-diversified equity portfolio (containing some international equities), UK real estate, UK and international fixed income securities and cash.

For Prudential's UK pensions annuities business and other non-participating business the objective is to maximize profits while ensuring stability by closely matching the cashflows of assets and liabilities. To achieve this matching, the strategy is to invest in fixed income securities of appropriate maturity dates.

For Prudential's unit-linked business, the primary objective is to maximize investment returns subject to following an investment policy consistent with the representations Prudential has made to its unit-linked product policyholders.

Prudential's property and casualty business has investment requirements that differ from long-term insurance business. This is because the property and casualty insurance liabilities tend to have a shorter duration than the long-term insurance liabilities and because shareholder funds bear all of the investment risk on this business. As a result, the portfolio has a higher component of investments in fixed income securities than the with-profits fund to match the mean term of the liabilities and to reduce volatility. However, Prudential can and does invest in equities to the extent that there is sufficient capital to absorb the volatility. Prudential's property and casualty business investment strategy is designed to maximize after-tax return while maintaining appropriate liquidity and capital levels.

Investments

The following table shows the investments relating to Prudential's UK insurance business, other than its unit-linked business, at December 31, 2000. In this table, investments are shown at market value. The with-profits fund also includes two other businesses, SAIF and Prudential Annuities Limited. The investments in respect of SAIF are shown separately in the table below. The investments in respect of Prudential Annuities Limited are included within the Annuities column in the table below. The

"Other" column includes investments relating to solvency capital of unit-linked funds and investments relating to non-life, long-term business.

	At December 31, 2000						
	With-Profits	Annuities	SAIF	Property and Casualty	Other	Total	Total %
	(In £ Millions, Except Percentages)						
Equity securities							
United Kingdom							
Listed	30,985	—	6,535	369	219	38,108	
Unlisted	122	—	8	27	—	157	
Total United Kingdom	31,107	—	6,543	396	219	38,265	41.9
International							
United States	2,378	—	483	16	—	2,877	
Europe (excluding the United Kingdom)	3,608	—	711	7	—	4,326	
Japan	1,352	—	279	26	—	1,657	
Pacific (excluding Japan)	1,844	—	370	—	—	2,214	
Other	647	—	91	—	—	738	
Total international	9,829	—	1,934	49	—	11,812	13.0
Total equity securities	40,936	—	8,477	445	219	50,077	54.9
Debt and other fixed income securities							
UK government	243	370	337	29	62	1,041	
US government	1,302	6	265	49	—	1,622	
Other	12,106	9,268	4,076	57	101	25,608	
Total fixed income securities	13,651	9,644	4,678	135	163	28,271	31.0
Real estate							
Investment property	8,351	120	1,505	—	—	9,976	
Company-occupied property	136	—	—	—	—	136	
Total real estate	8,487	120	1,505	—	—	10,112	11.1
Loans and other							
Loans	91	247	183	—	3	524	
Deposits	1,589	20	387	23	228	2,247	
Total loans and other	1,680	267	570	23	231	2,771	3.0
Total	64,754	10,031	15,230	603	613	91,231	100.0

Equity Securities

Prudential's UK insurance operations, excluding unit-linked business, had £50,077 million invested in equities at December 31, 2000. Most of these equities support Prudential Assurance's with-profits fund and the SAIF fund, both of which are managed using the same general investment strategy. The following table shows the geographic spread of this equity portfolio by market value.

	At December 31, 2000	
	Market Value	%
	(In £ Millions, Except Percentages)	
United Kingdom	**38,265**	**76.4**
United States	**2,877**	**5.8**
Europe (excluding the United Kingdom)	**4,326**	**8.6**
Japan	**1,657**	**3.3**
Pacific (excluding Japan)	**2,214**	**4.4**
Other	**738**	**1.5**
Total	**50,077**	**100.0**

The UK equity holdings are well diversified and broadly mirror the FTSE All-Share Index. Prudential holds equities in more than 700 UK companies. At December 31, 2000, the ten largest holdings in UK equities amounted to £16,414 million, accounting for 42.9% of the total UK equity holdings of £38,265 million supporting the UK insurance operations. The following table shows the market value of the ten largest holdings in UK equities at December 31, 2000.

	At December 31, 2000	
	Market Value	%
	(In £ Millions, Except Percentages)	
Vodafone Group	**3,289**	**8.6**
B.P. Amoco	**2,723**	**7.1**
Glaxo Smith Kline	**2,534**	**6.6**
HSBC Holdings ORD	**1,837**	**4.8**
Shell Transport and Trading	**1,298**	**3.4**
Astra Zeneca	**1,198**	**3.1**
Barclays	**1,003**	**2.6**
British Telecom	**893**	**2.4**
Lloyds TSB Group	**885**	**2.3**
The Royal Bank of Scotland Group	**754**	**2.0**
Total	**16,414**	**42.9**

All industry sectors are represented in Prudential's equity portfolio. At December 31, 2000, within the £38,265 million in UK equities supporting the UK insurance operations, Prudential had £26,625 million, or 69.6% of the holdings invested in ten industries. The following table shows the primary industry concentrations based on market value of the portfolio of UK equities relating to the UK insurance business at December 31, 2000.

	At December 31, 2000	
	Market Value	% of UK Equity Holdings
	(In £ Millions, Except Percentages)	
Banks	**5,970**	**15.6**
Telecommunications Services	**4,975**	**13.0**
Oil & Gas	**4,336**	**11.3**
Pharmaceuticals	**3,877**	**10.1**
Media and Photography	**2,241**	**5.9**
General Retailers	**1,118**	**2.9**
Investment Companies	**1,096**	**2.9**
Life Assurance	**1,060**	**2.8**
Electricity	**1,056**	**2.8**
Construction & Building Materials	**896**	**2.3**
Total	**26,625**	**69.6**

Debt and Other Fixed Income Securities

At December 31, 2000, 74.6% of Prudential's fixed income securities supporting the UK insurance operations were issued by corporations, 3.7% were issued or guaranteed by the UK government, 5.7% were issued or guaranteed by the US government and 14.9% were issued or guaranteed by other overseas governments. These guarantees relate only to payment and, accordingly, do not provide protection against fluctuations in market price that may occur during the term of the fixed income securities. The remaining 1.1% of Prudential's fixed income securities supporting the UK insurance operations consists mainly of local UK government issues.

The following table shows the market value of the fixed income securities portfolio by maturity at December 31, 2000.

	At December 31, 2000	
	Market Value	%
	(In £ Millions, Except Percentages)	
Securities maturing:		
within one year	**725**	**2.6**
over one year and up to five years	**4,282**	**15.2**
over five years and up to ten years	**7,071**	**25.0**
over ten years and up to fifteen years	**3,066**	**10.8**
over fifteen years	**13,127**	**46.4**
Total	**28,271**	**100.0**

Approximately 66.8% of the fixed income securities portfolio was rated by Standard & Poor's at December 31, 2000, of which 25.3% was rated AAA, 8.0% was rated between AA- and AA+, 23.1% was rated between A- and A+, 8.8% was rated between BBB- and BBB+ and 1.6% was rated below BBB-. A further 15.8% of this portfolio was rated by Moody's Investors Services at December 31, 2000, of which approximately 4.8% was rated Aaa, 4.2% was rated between Aa1 and Aa3, 4.1% was rated between A1 and A3, 1.7% was rated between Baa1 and Baa3 and 1.0% was rated below Baa3.

Real Estate

At December 31, 2000, Prudential's UK insurance operations had £10,112 million of investments in real estate in the United Kingdom. The following table shows the real estate portfolio by type of investment. The real estate investments are shown at market value in accordance with the policies described in Note 3 to the consolidated financial statements.

	At December 31, 2000	
	Market Value	%
	(In £ Millions, except percentages)	
Office buildings	**3,577**	**35.4**
Shopping centers/commercial	**5,215**	**51.5**
Retail warehouses/industrial	**768**	**7.6**
Development	**443**	**4.4**
Other	**109**	**1.1**
Total	**10,112**	**100.0**

59.7% of the UK real estate investments are located in London and Southeast England with the remaining 40.3% located throughout the rest of the United Kingdom.

Loans and Other

At December 31, 2000, the loans and other portfolio of the UK insurance operations amounted to £2,771 million. The following table shows the loans and other portfolio by value at December 31, 2000.

	At December 31, 2000
	(In £ Millions)
Loans collateralized by mortgages	**326**
Loans to policyholders collateralized by insurance policies	**95**
Other loans	**103**
Deposits with credit institutions	**2,206**
Other	**41**
Total	**2,771**

Investments Relating to US Insurance Business

Strategy

Jackson National Life's investment strategy, for business other than its variable annuity business, is to maintain a diversified and largely investment grade debt and fixed income securities portfolio that maintains a desired investment spread between the yield on the portfolio assets and the rate credited on policyholder liabilities. Interest rate scenario testing is continually used to monitor the effect of changes in interest yields on cash flows, the present value of future profits and interest rate spreads.

Jackson National Life's investment portfolio consists primarily of fixed income securities, although the portfolio also contains investments in mortgage loans, policy loans, common and preferred stocks, cash and short-term investments and miscellaneous other investments.

Investments

The following table summarizes Jackson National Life's total insurance investments other than the investments supporting its variable annuity business at December 31, 2000.

	December 31, 2000			
	Non-Stable Value	Stable Value	Total	Total %
	(In £ Millions, Except Percentages)			
Other financial investments				
Debt and other fixed income securities				
Corporate securities and commercial loans	**8,397**	**3,281**	**11,678**	**48.5**
Residential mortgage backed securities	**4,767**	**304**	**5,071**	**21.1**
Commercial mortgage backed securities	**1,305**	**756**	**2,061**	**8.6**
Other	**41**	**31**	**72**	**0.3**
Total debt and other fixed income securities	**14,510**	**4,372**	**18,882**	**78.5**
Loans and other	**4,822**	**—**	**4,822**	**20.0**
Equity securities	**286**	**26**	**312**	**1.3**
Total other financial investments	**19,618**	**4,398**	**24,016**	**99.8**
Real estate	**53**	**—**	**53**	**0.2**
Total	**19,671**	**4,398**	**24,069**	**100.0**

Debt and other fixed income securities are shown at amortized cost, with the exception of certain securities held by the US fund management operation, which are shown at market value. Loans and other, equity securities, and real estate are shown at market value, with the exception of interests in associate undertakings (included in equity securities). Interests in associate undertakings are carried at Jackson National Life's proportionate share of net assets. The market value of unlisted securities is estimated by Jackson National Life's board of directors, using independent pricing services or analytically determined values.

Debt and Other Fixed Maturities

Corporate Securities and Commercial Loans

At December 31, 2000, Jackson National Life had £11,678 million of corporate securities and commercial loans, representing 48.5% of US insurance total investments. Of the £11,678 million, £8,376 million consisted of publicly traded and Rule 144A fixed income securities and £3,302 million consisted of investments in non-Rule 144A privately placed fixed income securities.

The following table shows the credit quality of the portfolio of publicly traded and Rule 144A fixed income securities at December 31, 2000.

	At December 31, 2000	
	Book Value	% of Total
	(In £ Millions, Except Percentages)	
NAIC Designation		
1	**2,091**	**25.0**
2	**4,866**	**58.1**
3	**524**	**6.2**
4	**759**	**9.1**
5	**61**	**0.7**
6	**75**	**0.9**
Total	**8,376**	**100.0**

In recent years, Jackson National Life has been increasing its holdings of non-Rule 144A private placement investments. The following table shows the credit quality of the non-Rule 144A private placement portfolio at December 31, 2000.

	At December 31, 2000	
	Book Value	% of Total
	(In £ Millions, Except Percentages)	
NAIC Designation		
1	**909**	**27.5**
2	**1,340**	**40.6**
3	**488**	**14.8**
4	**448**	**13.6**
5	**86**	**2.6**
6	**31**	**0.9**
Total	**3,302**	**100.0**

Residential Mortgage-Backed Securities

At December 31, 2000, Jackson National Life had £5,071 million of residential mortgage-backed securities, including commercial mortgage obligations, representing 21.1% of US insurance total investments. Although this percentage is high compared to the average US insurance company, Jackson National Life believes these securities provide additional yield and liquidity. At December 31, 2000, 87.9% of Jackson National Life's mortgage-backed securities were rated AAA or the equivalent by a nationally recognized statistical ratings organization, and 96.1% were rated NAIC 1.

The primary investment risk associated with residential mortgage-backed securities is that a change in the interest rate environment could cause payment of the underlying obligations to be made more slowly or quickly than was anticipated at the time of their purchase. If interest rates decline, then this risk is called "pre-payment risk" and the underlying obligations will generally be repaid more quickly when the yields on reinvestment alternatives are lower. Alternatively, if interest rates rise, the risk is called "extension risk" and the underlying obligations will generally be repaid more slowly when reinvestment alternatives are higher. Residential mortgage-backed securities offer additional yield to compensate for these risks. Jackson National Life manages pre-payment risk, in part, by reducing crediting rates on its products.

Commercial Mortgage-Backed Securities

At December 31, 2000, Jackson National Life had £2,061 million, representing 8.6% of US insurance total investments invested in commercial mortgage-backed securities. 100% of this total was rated by Standard & Poor's or Moody's Investors Services and 97.7% were rated investment grade. Due to the structures of the underlying commercial mortgages, these securities do not present the same pre-payment or extension risk as residential mortgage-backed securities.

Loans and Other

Loans and other totalled £4,822 million, representing 20.0% of US insurance total investments at December 31, 2000. Of the £4,822 million, £2,940 million consisted of loans and £1,882 million consisted of other financial investments.

Loans

Loans represented 12.2% of US Insurance total investments at December 31, 2000. £2,480 million related to commercial mortgage loans and £460 million to policy loans.

Commercial Mortgage Loans. Commercial mortgage loans represented 10.3% of US insurance total investments at December 31, 2000. This total included 468 first mortgage loans with an average loan balance of approximately £5 million, collateralized by properties located in Canada and the United States. The vast majority of Jackson National Life's investments have been directly originated in the last 5 years.

Jackson National Life intends to address the risk of these investments by building a portfolio that is diverse both in geographic distribution and property type, emphasizing four main institutional property types: multi-family residential, retail, suburban office and warehouse/distribution facilities. These investments are often structured to minimize pre-payment risk through make-whole or lock-out pre-payment provisions.

As of December 31, 2000, approximately 25.9% of the portfolio was industrial, 19.2% multi-family residential, 23.5% retail, 23.4% suburban office and 6.7% hotel. Approximately 26.0% of the portfolio is secured by properties in Texas and 7.2% of the portfolio is secured by properties in California, with no other state representing more than 5% of the total origination.

Commercial mortgages generally involve more credit risk than residential mortgages due to several factors, including larger loan size, general and local economic conditions, local real estate conditions and the credit quality of the underlying tenants for the properties. Jackson National Life's investment policy and strict underwriting standards are designed to reduce these risks while maintaining attractive yields. In contrast to residential mortgage loans, commercial mortgage loans have minimal or no pre-payment and extension risk.

Policy Loans. Policy loans represented 1.9% of US insurance total investments at December 31, 2000. Policy loans are fully secured by individual life insurance policies or annuity policies and are contractual arrangements made under the policy.

Other

Other financial investments, representing 7.8% of US insurance total investments at December 31, 2000, were made up of £1,309 million of cash and short-term investments, £498 million of investments in limited partnerships and £75 million of other miscellaneous investments.

The largest investment in the limited partnerships category is a £96 million interest in the PPM America Private Equity Fund. The remainder of this category consists of diversified investments in 118 other partnerships managed by independent money managers that invest in various equity and fixed income loans and securities.

Equity Securities

Equity securities supporting US insurance operations totalled £312 million at December 31, 2000 and consisted of £235 million of common stocks and £77 million of preferred stocks.

Common Stock

The £235 million of investments in common stocks included £87 million of investments in mutual funds and £148 million of other investments in common stocks, at December 31, 2000. The majority of investments in mutual funds are investment capital related to the variable annuity business. Approximately £13 million of the other investments are investments in affiliates.

Preferred Stock

The £77 million of investments in preferred stocks includes £34 million of real estate investment trust perpetual preferred stocks, at December 31, 2000.

Real Estate

At December 31, 2000, Jackson National Life had £53 million of investments in real estate, £37 million of which is real estate Jackson National Life occupies and uses.

Investments Relating to Asian Insurance Business

Prudential's Asian operations' investments, other than investments in respect of unit-linked business, largely support the business of its Singapore, Hong Kong, Malaysia and Taiwan operations. The products Prudential offers in Asia are designed to enable it to invest a substantial proportion of the with-profits funds in equities, although local regulatory restrictions in some Asian countries limit the amount that may be invested in equities. Prudential's equity investments in Asia are spread across the principal Southeast Asian equity markets.

The following table shows Prudential Asia's investments, other than investments from unit-linked business at December 31, 2000. In this table, investments are valued on the same basis as in the consolidated financial statements.

	At December 31, 2000	
	Market Value	% of Total
	(In £ Millions, Except Percentages)	
Debt and other fixed income securities	1,382	50.2
Equity securities	770	28.0
Loans and other	474	17.2
Real estate	125	4.6
Total	2,751	100.0

With the exception of a deliberate policy to hold short-term assets in Indonesia, Prudential manages interest rate risk in Asia by matching liabilities with fixed interest assets of the same duration to the extent possible. Asian fixed interest markets however, have a relatively short bond issue term, which makes complete matching impossible. A large proportion of the Hong Kong liabilities is denominated in US dollars and Prudential holds US fixed interest securities to back these liabilities.

Investments Relating to Banking Business

At December 31, 2000, Prudential had total banking investments of £8,355 million. The following table summarizes the investment portfolios relating to the UK and US banking businesses. In this table, investments are valued on the same basis as in the consolidated financial statements.

	At December 31, 2000			
	UK	US	Total	Total %
	(In £ Millions, Except Percentages)			
Other financial investments				
Debt and other fixed income securities	3,686	35	3,721	44.6
Loans and other	3,974	640	4,614	55.2
Equity securities	—	8	8	0.1
Total other financial investments	7,660	683	8,343	99.9
Real estate	8	4	12	0.1
Total	7,668	687	8,355	100.0

Of the £3,686 million debt and other fixed income securities relating to the UK banking business, £868 million was in respect of certificates of deposit maturing in less than three months.

The following table shows UK banking business loans by type and repayment period at December 31, 2000.

	At December 31, 2000				
	Due in One Year or Less	Due in Over One Year and Up to Five Years	Due in Over Five Years	Provision for bad and doubtful debts	Total
	(In £ Millions)				
Unsecured personal loans	9	425	11	(17)	428
Credit card receivables	929	—	—	(23)	906
Residential mortgages	—	38	2,367	(3)	2,402
Loans to banks	238	—	—	—	238
Total	1,176	463	2,378	(43)	3,974

The following table shows UK banking business loans by type and interest rate at December 31, 2000.

	At December 31, 2000			
	Fixed Rate	Floating Rate	Provision for bad and doubtful debts	Total
	(In £ Millions)			
Unsecured personal loans	445	—	(17)	428
Credit card receivables	—	929	(23)	906
Residential mortgages	328	2,077	(3)	2,402
Loans to banks	—	238	—	238
Total	773	3,244	(43)	3,974

Description of Property

The Prudential group occupies 176 properties in the United Kingdom. These properties are primarily offices with some ancillary storage/warehouse facilities. Its headquarters located in London, together with other offices in London, Reading, Chelmsford, Dudley and Derby in England and Stirling in Scotland, are the most significant of these properties. It holds the Stirling property, a property in Chelmsford and a property in Derby on a freehold basis and the remaining properties as long-term leaseholds. Apart from three freehold offices, the balance of the 176 properties consists of smaller office space that are held as leaseholds, in the majority of cases, with a shorter term unexpired.

In addition to these properties, the Prudential group owns the freehold of a sports facility in Reading and a training/conference center outside of Watford that is operated by an external conference operator.

The Prudential group also holds leaseholds on approximately 159 other properties in the United Kingdom. This surplus accommodation consists primarily of small offices spread geographically across the United Kingdom. Prudential holds approximately 2,958,000 square feet of property in the United Kingdom on a freehold and leasehold basis.

Prudential is in the process of refurbishing, and has plans to continue to refurbish throughout 2001, certain of its UK office space to more efficiently house its restructured business units. The estimated cost of these projects is approximately £15.6 million, to be financed using internal funds.

Within France and Germany, Prudential currently leases approximately 29,000 square feet of office space and has plans to increase its leased office space to approximately 50,000 square feet in those countries.

In the United States, the company owns Jackson National Life's executive and principal administrative offices. These offices are located in Michigan. Prudential also leases premises in Michigan, Colorado, California, New Jersey and Georgia for certain of its operations. Prudential leases regional marketing sales offices in 16 locations, and holds 21 operating leases with respect to office space, throughout the United States. Prudential also has plans to move and renovate certain regional sales offices at an aggregate estimated cost of $200,000, to be financed using internal funds and to be completed in the second half of 2001. In the United States, Prudential owns and leases a total of approximately 647,000 square feet of property.

In addition, Prudential owns or leases properties elsewhere, principally in Hong Kong, Singapore, Malaysia, Indonesia, Thailand, The Philippines, China, Taiwan, Japan, Vietnam and India. Within these countries, Prudential holds 37 offices on a freehold basis, 56 offices on a leasehold basis and 107 operating leases in respect of office space totaling approximately 1,905,000 square feet of property. In addition, Prudential holds 15 freeholds in Taiwan and two operating leases in Vietnam relating to storage/warehousing facilities, totaling approximately 25,000 square feet of property.

In Taiwan, Prudential is in the process of completing a building of approximately 256,000 square feet, to be completed in July 2001 at an estimated cost of NT$730 million (£15 million) and to be used as office space. In addition, Prudential will be entering into a new leasehold in Malaysia at a cost of approximately Rm9 million (£1.5 million) in 2001, to which the headquarters of its Malaysian business will be relocated. In connection with its strategy of branch consolidation, Prudential will also be selling four of its freehold properties in Malaysia in 2001. Finally, Prudential plans to lease approximately 11,000 square feet of additional office space in Hong Kong in 2001, at a cost of HK$4.5 million (£0.4 million).

Prudential believes that its facilities are adequate for its present needs in all material respects.

Prudential had tangible assets, principally computer equipment, furniture and fixtures of £288 million and £239 million at December 31, 2000 and 1999, respectively.

M&G is in the process of refurbishing, relocating and acquiring properties in connection with its operations in Chelmsford, London and Berlin. Such projects, which are estimated to cost, in aggregate, £10 million, are scheduled to be completed by September 2001. Prudential has also undertaken to improve facilities of its UK operations in Reading and Euston, at an estimated cost of £9 million and with an estimated completion date of December 2001.

Competition

General

There are significant participants in each of the financial service markets in which Prudential operates. Its competitors include both mutual and stock financial companies. In addition, regulatory and other developments in many of Prudential's markets have obscured traditional financial service industry lines and opened the market to new competitors and increased competition. Some new entrants are taking advantage of the low barriers to entry afforded by internet distribution, especially in the area of retail banking. In some of Prudential's markets, other companies may have greater financial resources, allowing them to benefit from economies of scale, and may have stronger brands than Prudential does in that market.

The principal competitive factors affecting the sale of Prudential's products in its chosen markets are:

- price and yields offered;
- financial strength and ratings;
- commission levels, charges and other expenses;
- range of product lines and product quality;
- brand strength, including reputation and quality of service;
- distribution channels;
- investment management performance; and
- historical bonus levels.

An important competitive factor is the ratings Prudential receives in some of its target markets, most notably in the United States, from recognized rating organizations. The intermediaries with whom Prudential works, including IFAs, agents, brokers, wholesalers and financial institutions consider ratings as one factor in determining from which provider to purchase financial products. Prudential Assurance's long-term fund is currently rated AAA and Jackson National Life is rated AAA by Standard & Poor's. Jackson National Life is currently rated AA+ by Duff & Phelps and Aa3 by Moody's Investors Services. Any change in Prudential's current ratings could affect the sale of its products and the persistency of its in-force business. A downgrade in ratings could adversely affect Prudential sales in the same markets.

The United Kingdom

Prudential offers different products in its different markets of the United Kingdom, the United States and Asia and, accordingly, faces different competitors and different types of competition in these markets.

Prudential's principal competitors include all the major stock and mutual retail financial services and fund management companies operating in the United Kingdom. These companies include CGNU, Legal & General, Standard Life, Lloyds TSB, Halifax, Abbey National, Aegon, AXA, Zurich Financial Services, Fidelity and Perpetual. Prudential competes with other providers of financial products to be included on the preferred panels of IFAs.

In the United Kingdom, the level of bonuses on Prudential's with-profits products is an important competitive measure for attracting new business through IFAs. The ability to declare competitive bonuses depends, in part, on a company's financial strength, which enables it to adopt an investment approach with a higher weighting in equity and smooth the fluctuations in investment performance upon which bonuses are based. Returns on Prudential's pensions policies are in line with those of its major competitors.

The United States

Jackson National Life's competitors in the United States include major stock and mutual insurance companies, mutual fund organizations, banks and other financial services companies. National banks, in particular, may become more significant competitors in the future for insurers who sell annuities, as a result of recent legislation, court decisions and regulatory actions. Jackson National Life's principal life insurance company competitors in the United States include AXA, Lincoln National Corporation, Transamerica Corporation, Nationwide Financial Services, Inc., Sunamerica Inc. and Hartford Life, Inc.

Jackson National Life does not have a career agency salesforce in the United States and, consequently competes for distributors such as banks, broker-dealers and wholesalers. Jackson National Life also competes with other providers of financial products to be placed at the top of the independent agents' list of sources.

Asia

Competition in the Asian markets in which Prudential operates is currently focused on distribution, with particular emphasis on the size and composition of the agency salesforce. Within the Asian region, its principal competitors are non-Asian financial companies, including AIG, Manulife, ING/Aetna and AXA. Prudential also faces competition within each country from local and Asian financial companies, including Great Eastern Life in Singapore and Malaysia, Malaysia Assurance Alliance in Malaysia and CathayLife in Taiwan.

Intellectual Property

Prudential does not operate in the United States under the Prudential name. There have been long-standing arrangements between it and Prudential Insurance Company of America relating to their respective uses of the Prudential name in various countries. Prudential and Prudential Insurance Company of America have made competing trademark claims in various jurisdictions around the world. Although the companies have been in discussions, these issues have not, to date, been resolved, and there is a possibility that disputes or legal proceedings in connection with these matters could result.

Legal Proceedings

Prudential Assurance

Surplus Assets

In recent years, a number of UK life insurance companies have reached agreement with the relevant UK supervisory authority to permit them to attribute a proportion of the surplus assets in their long-term funds to their shareholders while retaining it in their long-term funds. To date, the supervisory authority has permitted companies to distribute only a modest proportion of the amounts attributed to them.

Prudential continues to pursue opportunities to resolve the ultimate attribution of the surplus assets in Prudential Assurance's long-term fund, and has, since 1996, been discussing this attribution with the relevant UK supervisory authorities. The attribution of surplus assets has also been a subject of public debate in the United Kingdom. Prudential's discussions may or may not result in a portion of the surplus assets in the long-term fund being attributed solely to shareholders.

The amount and timing of any attribution to shareholders are sufficiently uncertain that it is not possible to accurately estimate any potential attribution. In addition, it is likely that if any surplus assets are attributed to shareholders, they will remain in Prudential Assurance's long-term fund to support the long-term business, and accordingly, they are unlikely to be distributed to shareholders for some considerable period of time, if at all.

On December 14, 2000, proceedings were issued against Prudential Assurance by a policyholder relating to the surplus assets in Prudential Assurance's long-term fund. The claims ask the court to decide whether and, if so, to what extent, the surplus assets should be paid out to or applied for the benefit of policyholders and/or shareholders. Prudential is considering the proceedings and the issues raised by them with its legal advisers.

Jackson National Life

Since 1996, plaintiffs have filed numerous actions in state and federal courts seeking to represent a class of purchasers of Jackson National Life's whole life policies, who allegedly bought their policies in reliance on false and misleading representations by Jackson National Life that the premiums payable on such policies would "vanish" after a certain number of premium payments. Originally, certain of the cases sought certification of a national class of more than 300,000 persons, but in October 1998 the federal judge in Lansing, Michigan ruled that a national class could not be certified under applicable law. In July 2000, the federal judge granted summary judgment on all of the individual plaintiffs' claims except one. To avoid the cost of further proceedings, the parties subsequently negotiated a settlement with the five original plaintiffs plus plaintiffs in a Texas class action transferred to Michigan and denied class action certification in May 2000. Jackson National Life faces similar claims in various jurisdictions but expects that such claims will either be resolved favorably or settled for immaterial amounts. In any event, Prudential believes its potential exposure in relation to claims currently outstanding will not be material to its consolidated financial condition and results of operations.

Jackson National Life is a defendant in a class action filed in Texas in April 1999 that also involves claims of vanishing premium misrepresentations as well as allegations of illegal sales of life insurance and annuities in Mexico. The plaintiffs are Mexican residents who bought interest-sensitive life insurance policies from a Jackson National Life broker in Texas, but claim that the applications were actually signed in Mexico in violation of Mexican law. The plaintiffs seek to represent a class of all Mexican residents who purchased policies that are not valid or enforceable in Mexico. The plaintiffs also seek to represent a class of Mexican purchasers of interest-sensitive whole life policies that were allegedly told that their policies would be "paid up" after a limited number of premium payments. Jackson National Life removed the case to federal court and transferred it to Lansing, Michigan for further proceedings.

Jackson National Life is also a defendant in a suit in Birmingham, Alabama by an annuity purchaser who seeks to represent a national class of persons who allegedly received a lower first year interest rate than purchasers of other "substantially similar" Jackson National Life annuities. Plaintiff claims that it is "unfairly discriminatory" to offer similar annuities with different interest rates (based on different commission rates), and that Jackson National Life has a duty to disclose all available annuity products to consumers. This case is in its infancy, but Prudential does not expect that the proposed class will be certified or that the case will be successful on its merits. In any event, Prudential does not believe the potential exposure will be material to its consolidated financial condition and results of operations.

A class action filed in New Mexico in November 2000 against Jackson National Life involves alleged fraudulent concealment of "modal premium charges" paid by policyholders who pay their life insurance premiums other than annually (i.e., semi-annually, quarterly or monthly), and thus pay a higher total annual premium. Jackson National Life has filed a motion to dismiss the case. Although it is too early to evaluate Jackson National Life's potential exposure in the event of an unfavorable outcome, it does not expect the potential exposure will be material to its consolidated financial condition and results of operations.

Jackson National Life is also involved in a suit filed in state court in Mississippi by three life insurance purchasers (complaining that their policies were not "paid up" as their agents had represented) that resulted in actual damages of $23,000 and a $32.5 million punitive damages jury verdict in August 1999. That matter is on appeal. No amount has been accrued in 2000 in respect of the punitive damages, as Prudential expects that its appeal will be successful.

Prudential Group

In addition to matters discussed above, Prudential is involved in a number of legal proceedings across its group related to the normal conduct of its business. Prudential does not believe that its liabilities related to this or other individual legal proceedings are likely to be, in the aggregate, material to its consolidated financial condition and results of operations.

Sources

Throughout this annual report, Prudential describes the position and ranking of its overall business and individual business units in various industry and geographic markets. The sources for such descriptions come from a variety of conventional sources generally accepted as relevant business indicators by members of the financial services industry. These sources include information available from the Association of British Insurers, the UK Department of Trade and Industry, Association of Unit Trusts and Investment Funds, AM Best, Life Insurance Marketing and Research Association, the Variable Annuity Research Data Service, referred to as VARDS, Townsend and Schupp, The Advantage Group, the Life Insurance Association of Singapore, the Hong Kong Federation of Insurers, Life Insurance Association of Malaysia, Life Insurance Association of Taiwan and the Taiwanese Securities Investment Trust Consulting Association.

SUPERVISION AND REGULATION OF PRUDENTIAL

Prudential's principal insurance and banking operations are in the United Kingdom and the United States. Accordingly, it is subject to applicable UK and US insurance, banking and other financial services regulation, as discussed below.

Prudential operates in eleven Asian countries and is subject to the respective insurance and, in the case of India, Taiwan and Japan, investment regulations of each such country.

UK Supervision and Regulation

General

On May 20, 1997, the UK government announced a proposal to establish a single statutory regulator for financial services businesses, including banks. On October 28, 1997, it was announced that the new financial regulator would be called the Financial Services Authority, referred to as the FSA. On July 23, 1997, the UK government confirmed that the single regulator would also assume supervisory responsibility for insurance companies. As a transitional measure, responsibility for insurance supervision was transferred from the UK Department of Trade and Industry to the UK Treasury on January 5, 1998. With effect from January 1, 1999, the UK Treasury has delegated to the FSA the majority of its functions under the Insurance Companies Act (while retaining certain powers, including the power to make regulations). UK Treasury ministers remain accountable to the UK parliament for insurance. As of June 1, 1998, the UK government transferred responsibility for banking supervision to the FSA, pursuant to the UK Bank of England Act 1998. Notwithstanding the transfer of its responsibilities to the FSA, the Bank of England has retained its monetary policy role and remains responsible for the overall stability of the UK financial system.

Currently, the responsibility for regulating authorized investment businesses mostly remains with the self-regulating organizations, or SROs, established under the UK Financial Services Act 1986. In practice, the work of the SROs is now carried out by the staff of the FSA, operating under contract and working within the single FSA management arrangements. It is anticipated that the SROs will be phased out with the implementation of the Financial Services and Markets Act 2000, referred to below as the 2000 Act.

In January 2000 the FSA set out its proposals for a new risk-based regulatory approach to all financial business, which will integrate and simplify the different approaches adopted by current regulators. Its primary concern is to minimize the risk that the objectives for the FSA set out in the 2000 Act will not be met. Under the new approach, each firm's risk will be assessed on a common FSA-wide model covering the firm's business risks, control risks, and customer risks together with an assessment of the potential impact on consumer protection and market stability of financial or compliance failure in that firm. The FSA is currently starting to implement this approach.

New Regulatory Regime

The transfers of responsibility described above implemented the first step in the UK government's program to overhaul the UK financial regulatory system and to harmonize the provisions of the Insurance Companies Act, the Financial Services Act and the Banking Act into one new piece of legislation, the 2000 Act. The 2000 Act was enacted in June 2000 and is expected to come into force no later than the end of November 2001.

Through the 2000 Act, the FSA is seeking to harmonize the various rules and regulations currently in operation. However, it is not possible to describe with any certainty how the current system of regulation may change since the bulk of secondary regulation required under the 2000 Act has yet to be published in its final form and many of the rules to be produced by the FSA have yet to be finalized. In addition, to the extent that UK legislation incorporates requirements imposed by EC directives, those requirements should remain unchanged unless and until changes take place at a European level. The FSA has issued a number of consultation papers on the rules that are likely to be implemented and has, in some cases, indicated the likely final form of the rules in question.

A review of pensions legislation resulted in government proposals for "stakeholder" pension legislation, which came into effect on April 6, 2001. These products are subject to low charges and allow individuals to make a very low level of contribution. Apart from the new stakeholder pensions and a new defined contribution tax regime introduced in April 2001, the UK government is introducing a new second state pension that will replace the existing state funded earnings and related schemes, possibly in 2002. This is still at the consultation stage.

Current Regime

Insurance business in the United Kingdom is currently subject to regulation under the UK Insurance Companies Act 1982. The Insurance Companies Act grants authorization and regulatory powers to the UK Treasury, the exercise of which (with certain exceptions) it has now delegated to the FSA. The Insurance Companies Act focuses on prudential regulation and, as a result, contains few rules on the marketing and sale of insurance.

Banking business in the United Kingdom is currently subject to regulation under the UK Banking Act 1987. The supervision of entities authorized under the UK Banking Act 1987 is carried out by the FSA. The requirements of the Banking Act have been supplemented by directives of the European Community, referred to as the EC.

In addition, investment business, which is defined to include certain types of insurance business, carried on by Prudential's insurance companies and Prudential's banking subsidiary in the United Kingdom is currently regulated under the UK Financial Services Act 1986. In the case of insurance business, the Financial Services Act is predominantly concerned with the marketing and sales process, while prudential regulation is covered by the Insurance Companies Act. The 2000 Act will introduce a new regulatory regime for investment business in the United Kingdom with the FSA as the regulator responsible for regulation. The existing self-regulating organizations will cease to have regulatory powers.

The following sets forth the current regulators to which Prudential's principal insurance, investment and banking subsidiary companies are subject in the United Kingdom:

Company	Applicable UK Regulators
The Prudential Assurance Company Limited	UK Treasury/Financial Services Authority Personal Investment Authority(1) Occupational Pensions Regulatory Authority
Scottish Amicable Life plc	UK Treasury/Financial Services Authority Personal Investment Authority(1)
Prudential Annuities Limited	UK Treasury/Financial Services Authority Personal Investment Authority(1)
M&G Life Assurance Co. Limited	UK Treasury/Financial Services Authority Personal Investment Authority(1)
M&G Pension & Annuity Co	UK Treasury/Financial Services Authority Personal Investment Authority(1)
Prudential Portfolio Managers Limited	Investment Management Regulatory Organisation(1)
M&G Financial Services Limited	Personal Investment Authority(1) Investment Management Regulatory Organisation(1)
Prudential Banking plc	Financial Services Authority

(1) To be replaced by Financial Services Authority.

The following discussion considers the main features of the current regulatory regime applicable to Prudential's insurance, investment and banking business in the United Kingdom.

Insurance Regulation

Some of Prudential's subsidiaries, including The Prudential Assurance Company Limited, Scottish Amicable Life plc, Prudential Annuities Limited, M&G Life Assurance Co. Limited and M&G Pension & Annuity Co. Limited, are authorized to carry on insurance business in the United Kingdom and are supervised by the FSA under the Insurance Companies Act. Under the Insurance Companies Act, an insurance company is restricted from carrying on any activities other than in connection with or for the purposes of its insurance business.

Authorization

Subject to certain exemptions set out in the Insurance Companies Act, no person may carry on insurance business in the United Kingdom unless authorized to do so or passported under the applicable EU directives. In deciding whether to grant authorization, the FSA must determine whether the applicant satisfies the requirements of the Insurance Companies Act, including a requirement for sound and prudent management. The criteria for sound and prudent management are set out in the legislation, and include a requirement for certain persons, including directors and controllers of the applicant, to be fit and proper. In connection with its authorization, the FSA may impose conditions relating to the operation of the company and the writing of insurance business. In addition, the UK Treasury retains power to waive compliance with various provisions of the Insurance Companies Act and underlying regulations, including some of those referred to below.

The equivalent provisions in and under the 2000 Act are expected to be broadly similar in effect.

Long-term Assets and Liabilities

Long-term business assets—those assets backing, broadly, certain life and health insurance policies—must be kept separate from the assets attributable to non-life insurance business or to shareholders. Separate accounting and other records must be maintained and a separate long-term fund or sub-fund must be established to hold all receipts of long-term business.

The extent to which long-term fund assets may be used for purposes other than long-term business is restricted by the Insurance Companies Act. Only the excess of assets over liabilities in the long-term fund, as determined by an investigation by the appointed actuary, may be transferred so as to be available for other purposes. Restrictions also apply to the payment of dividends by the insurance company or its parent, as described below. In practice, the level of assets held in the long-term fund will need to remain well in excess of the insurer's long-term liabilities. Requirements in relation to the maintenance of the long-term fund are expected to be broadly the same once the new regulatory regime comes into force.

The Prudential Assurance Company Limited is also subject to the specific restrictions set out in the scheme for the transfer of the long-term business of Scottish Amicable Life Assurance Society to The Prudential Assurance Company Limited. See "—Business of Prudential—UK Business—Shareholders' Interests in Prudential's Long-term Insurance Business—The SAIF Sub-Fund and Accounts" in this Item 4.

Solvency Requirements

The Insurance Companies Act requires insurance companies to maintain a solvency margin at all times, the calculation of which in any particular case depends on the type and amount of insurance business a company writes. The method of calculation of the solvency margin is set out in the UK Insurance Companies Regulations 1994, as amended and, for these purposes, an insurer's assets and its liabilities are subject to specific valuation rules. Failure to maintain the required solvency margin is one of the grounds on which wide powers of intervention conferred upon HM Treasury (now the FSA on its behalf) by in the Insurance Companies Act may be exercised. These solvency requirements are expected to remain broadly the same after the 2000 Act comes into force, as they derive from EC directives.

Appointed Actuary

Under the Insurance Companies Act, every insurance company that carries on long-term business must appoint an actuary who must prepare an annual report for the company's directors quantifying the company's long-term liabilities and determining the value of any surplus. An abstract of the appointed actuary's report, including the methods and assumptions adopted, is part of the annual return that the company must submit to the FSA.

The role of the appointed actuary is to monitor the financial well-being of the company and to make recommendations to the board of directors. The appointed actuary has a professional duty to be satisfied at all times as to the solvency of the company and that policyholders' reasonable expectations are safeguarded. The UK Institute of Actuaries and the UK Faculty of Actuaries require all members, including appointed actuaries, to comply with their Professional Conduct Standards. The 2000 Act contains powers for the FSA to make detailed rules concerning the qualifications, duties and "whistle-blowing" obligations of appointed actuaries.

Distribution of Profits

An insurance company carrying on long-term business, and any parent of such a company, cannot declare a dividend when the liabilities of the long-term business exceed the assets of the long-term fund. The Insurance Companies Act also has the effect that, once an allocation of surplus in a with-profits fund has been made to policyholders, no transfer of assets representing any part of a subsequent surplus can be made to shareholders unless either the "relevant minimum" (as defined in the Insurance Companies Act) of the surplus has been allocated to policyholders or a statutory notification procedure has been followed. Calculation of the relevant minimum is based upon the percentage of the relevant surplus previously allocated to eligible policyholders.

Under the rules proposed by the FSA, the insurance company itself, and not the parent of any such company, is restricted in terms of declaring dividends. The Treasury, however, is given power under the 2000 Act to make regulations preventing an insurer's parent from doing anything to lessen the effectiveness of any "asset identification rules" made by the FSA, which will include in this context rules requiring insurers to maintain the solvency of the long-term fund.

Reporting Requirements

UK insurance companies must prepare their financial statements under the UK Companies Act 1985, as amended, which requires them to file, and provide their shareholders with, audited financial statements and related reports. In addition, the Insurance Companies Act requires insurance companies to file audited accounts and other prescribed documents with the FSA within six months of the end of the relevant financial year.

The FSA has issued proposals to reduce the period insurers have for lodging their annual returns once the 2000 Act comes into force.

Equalization Reserves

Each insurance company writing property, business interruption, marine, aviation or nuclear insurance or reinsurance business is required to maintain an equalization reserve in respect of financial years ending on or after December 23, 1996. Prudential establishes equalization reserves to mitigate against exceptionally high loss ratios for classes of property and casualty business displaying a high degree of claims volatility.

Supervision of Management and Change in Control

No person may become a "controller" of an insurance company, including its managing director or chief executive, without the FSA's approval. Approval is deemed to have been given if the FSA is notified and does not object within three months of notification. For these purposes, in addition to managing director and chief executive, "controller" means:

- a managing director of a body corporate of which the insurance company is a subsidiary,
- a chief executive of an insurance company of which the insurance company is a subsidiary,
- a person in accordance with whose directions or instructions the directors of the insurance company, or of a body corporate of which it is a subsidiary, are accustomed to act, or
- a person who either alone or with any "associates" (1) holds 10% or more of the shares in, or is entitled to exercise or control the exercise of 10% or more of, the voting power at any general meeting of the company, or of another company of which it is a subsidiary undertaking or (2) is able to exercise a significant influence over the management of the company by virtue of a holding of shares in or an entitlement to exercise or control the exercise of voting power at any general meeting of such a company.

Prior approval of the FSA is required where any person who is already a controller of an insurance company seeks to acquire a holding, either directly or through control of voting power and either alone or with any associates, of 10% or more, 20% or more, 33% or more, 50% or a majority in any insurance company or another company of which the insurance company is a subsidiary undertaking.

Once the 2000 Act comes into force, these rules are broadly intended to remain the same to the extent that they apply to persons who intend to acquire control, or increase the level of their control, over an authorized insurer by virtue of shareholding or voting rights. Management, on the other hand, will be covered by the new "approved persons" regime, which provides that prior FSA approval must be obtained for individual and corporate suppliers of certain functions. In June 2000, the FSA published a consultation paper that proposed that specific functions, known as controlled functions, should not be carried out by an individual or by another person before he has been approved by the FSA. The regime is limited to those who:

- exert significant influence over the firm,
- deal with its customers, or
- deal with the property of its customers.

In February 2001, the FSA published a paper which sets forth its proposals on who should fall within the new regime. In the case of insurers, the FSA's powers of approval extend beyond those persons currently falling within the Insurance Companies Act definition of a "controller" to the key members of management of insurance groups (for example, directors, non-executive directors, chief executive officers, compliance officers, money laundering reporting officers, appointed actuaries, finance officers, risk control officers, internal auditors, heads of underwriting and heads of claims) and those who deal with policyholders or potential policyholders (for example, life and pensions advisers, pension transfer advisers and investment advisers).

The consequences for the relevant individual of being "approved" are potentially far-reaching. Failure to comply with FSA's statements of principle and codes of practice will expose an approved person to the FSA's disciplinary powers, including the power to censure or levy unlimited fines.

Intervention

The FSA, or, in some cases, the UK Treasury, has extensive powers to intervene in the affairs of an insurance company if it determines that:

- it is desirable for protecting policyholders or potential policyholders against the risk that the company may be unable to meet its liabilities or, in the case of long-term business, to fulfill the reasonable expectations of policyholders or potential policyholders,
- the criteria of sound and prudent management may not be fulfilled, or the company or its parent or subordinate company has failed to comply with obligations under the relevant legislation,
- the company has furnished misleading or inaccurate information;
- satisfactory reinsurance arrangements have not been made, or
- there has been a substantial departure from any proposal or forecast submitted to the FSA.

The FSA's powers of intervention under the 2000 Act appear to be more extensive than at present, and the criteria for its exercise is widely expressed. The main difference from the current regime, though, lies in the fact that, whereas prudential regulation is currently based only on powers of intervention established by the Insurance Companies Act, the new regime will, as well as the power to intervene, have significant disciplinary powers for breach of both prudential and "conduct of business rules", as defined in the 2000 Act.

Winding-up Rules

The general insolvency laws applicable to UK companies are modified in certain respects in relation to insurance companies. In particular, insurance companies are not subject to the administration procedures in the UK Insolvency Act 1986 and holders of long-term policies are permitted to claim not only what is owing to them but also in respect of their reasonable expectations. Furthermore, instead of making a winding-up order where an insurance company has proved unable to pay its debts, a UK court may reduce the amount of the insurance company's contracts on terms and subject to conditions which the court considers just. Where an insurance company is in financial difficulties but not in liquidation, the Policyholders Protection Board has certain powers, including the power to take measures for securing the transfer of all or part of the business to another insurance company.

Changes anticipated in relation to the insurance insolvency regime as a consequence of the 2000 Act include conferring a power on the Treasury to make an order removing the prohibition on putting insurance companies into administration. The Treasury has indicated that it intends to make use of this power. Also included in the 2000 Act is a provision removing the current prohibition on the voluntary winding up of an insurer which carries on long term insurance business, subject to obtaining the FSA's prior permission. The Policyholders Protection Board will be replaced under the new regime. See "—Bank Regulation—Deposit Protection and Investors Compensation" in this section below.

Legislative Restrictions on Ownership

There are generally no restrictions in the United Kingdom on investments by foreign persons. However, as described under "—Supervision of Management and Change in Control" in this section above, there are restrictions on the accumulation of holdings, of 10% or more, in insurance and other financial services companies or their holding companies.

Other Regulation

Supervision

Most long-term insurance products are investments for the purpose of the Financial Services Act and, accordingly, firms carrying on investment business must be regulated under that Act. The Personal Investment Authority is currently the main regulator for the retail marketing of life insurance. The Investment Management Regulatory Organisation is the regulator for investment management business. In due course, both the Personal Investment Authority and the Investment Management Regulatory Organisation will be subsumed within the FSA.

Regulatory requirements of the Personal Investment Authority and the Investment Management Regulatory Organisation include, among other things, requirements relating to advertisements, disclosure of information (particularly the level of costs and commissions borne by products), complaints procedures and restrictions on certain practices. The Personal Investment Authority rules contain stringent training and competence standards for sales staff. Before an employee may advise on any investment product, he or she must have passed the requisite examinations. In addition, the Personal Investment Authority rules impose what is known as "polarization" under which directly employed staff or tied agents can usually sell only the products of one company or group, while independent financial advisers must offer best advice across the whole range of products offered by companies in the relevant sector.

In February 2000, the FSA announced that it would be carrying out a review of the polarization rules. The FSA's announcement follows the publication of a report on polarization by the Director General of Fair Trading in August 1999. The Director General of Fair Trading concluded that the existing polarization rules affected competition by preventing innovation. The review, which was carried out by London Economics, was completed in mid-2000.

In November 2000, the FSA proposed a two-stage approach to modernizing the polarization regime. The first of these stages proposed changing the regime's influence on products conforming to minimum standards and on direct offer financial promotions. The second stage would consider a range of options for the rest of the polarization regime. The FSA published a consultation paper in January 2001 proposing a number of changes.

The new rules in relation to stakeholder pensions and direct offer advertisements were introduced on March 29, 2001 when the FSA published the Financial Services (Conduct of Business)(Modification of Polarisation) Rules 2001. A provider firm is now able to "adopt" into its product range stakeholder pension schemes provided by companies outside its marketing group and is permitted to provide advice on the adopted package product. It may approve and issue direct offer advertisements for any packaged product, including those that have not been adopted by it, provided the advertisements do not contain advice. In addition, it may approve and issue direct offer advertisements for adopted packaged products which may contain advice. The FSA plans to consult more widely on polarisation later this year.

The FSA issued a consultation paper in relation to its proposed conduct of business requirements in February 2000. The final text of the Conduct of Business Sourcebook was published in February 2001. The aim is to produce a consolidated set of rules that are simplified and harmonized where possible and are substantially smaller in volume than the rulebooks it replaces. In line with this aim, the FSA's general approach has been to replace and integrate existing standards, principally as currently set out in the rulebooks of the various self-regulating organizations, rather than to introduce material changes in the currently applicable rules. The "final" rules will take effect from the date the 2000 Act comes into force. These new measures may lead to greater competition among product providers such as Prudential.

Policyholders Protection Board

The UK Policyholders Protection Act 1975 established the Policyholders Protection Board. The Policyholders Protection Board's duty is to provide a full or partial indemnity to certain policyholders who may be affected by the inability of insurance companies to meet their liabilities. In addition, the Policyholders Protection Board has the powers referred to in "—Winding-up Rules" in this section above.

The Policyholders Protection Board is funded by levies on authorized insurance companies, calculated by reference to premium income. Separate levies are imposed on long-term and general business. In March 1997, the UK Policyholders Protection Act 1997 was passed, but has only been implemented to a very limited extent to extend the definition of "policyholder" in the 1975 Act.

The 2000 Act provides for the establishment of a new compensation scheme (the Financial Services Compensation Scheme) in relation to all financial services business, including insurance. Once that scheme comes into effect, it will replace that currently applying under the Policyholders Protection Act.

Data Protection

The UK Data Protection Act 1998 limits the ability to hold and use personal information relating to the customers of a UK company.

The law requires that UK companies notify the Data Protection Commissioner of their activities concerning the processing of personal data and obtain a registration prior to commencing those activities. In addition, companies regulated by the Data Protection Act 1998 must comply with a code of good conduct called the "data protection principles" and submit to requests from the individual who is the subject of the data concerning matters such as access to the data and rights to object to incorrect data being held or to direct marketing.

European Union Directive on Group Supervision

The European Union formally adopted directive 98/78/EC on the supplementary supervision of insurance undertakings within a group, referred to here as the "Insurance Groups Directive", in October 1998. Currently, under European law, insurance regulation, including in respect of solvency, is directed at individual insurance companies, (so-called "solo supervision") and makes no specific provision for particular issues which arise in the context of a member of a group. The directive does not change this basic approach, but requires member states to introduce the following measures to strengthen supervision of insurance companies which are part of a group,

- An adjustment to the solo supervision solvency calculation in relation to participating interests in other insurance undertakings is designed to eliminate "double-gearing", which is the use of the same capital to cover different risks within a group,
- An additional parent-undertaking solvency margin calculation introduced formal consolidated supervision of insurance groups for the first time. The calculation is analogous to the adjusted solo solvency margin test but is applied at the level of the parent undertaking,
- Member states will be required to introduce new solo-supervision requirements including rules as to internal control within the insurance undertaking regarding the production of information relevant to supplementary supervision, the exchange of information within the group and the supervision of intra-group transactions,
- Further provisions are aimed at ensuring co-operation between competent regulatory authorities of member states.

The directive requires that its requirements be adopted for financial years beginning on or after January 1, 2001.

The United Kingdom intends to implement requirements of the directive which are new to the United Kingdom by issuing notes and guidance under powers to be conferred on it under the Financial Services and Markets Act 2000, once in force. For the most part it will be achieved through amendments to the draft text of the Interim Prudential Sourcebook for Insurers, the most recent draft of which was published in March 2001. When implemented, these provisions are likely to impact on the capital requirements of the different companies within the Prudential group.

Investment Business Regulation

Investment business in the United Kingdom (other than the wholesale money markets) is currently primarily regulated under the provisions of the Financial Services Act. The Financial Services Act prohibits any person from carrying on investment business in the United Kingdom unless he is an authorized or exempt person. "Investment business" includes selling investments, arranging deals in investments, managing investments belonging to another person and giving investment advice. "Investments" include equities, debentures, options, warrants, units in collective investment schemes and certain long-term insurance contracts. Prudential is authorized to carry out investment business in the United Kingdom by virtue of Prudential's membership of a self-regulating organization. Exempt persons include "appointed representatives" whose principals accept responsibility for investment business activities carried out on their behalf.

A firm authorized by a self-regulating organization must comply with its rules. These set out, inter alia, minimum levels of financial resources to be maintained by each member and conduct of business rules (which, broadly, cover the marketing and provision of services to customers). Self-regulating organizations also review the adequacy of a firm's systems to conduct the investment business for which it is authorized and the fitness and properness of its controllers, directors and key employees.

Bank Regulation

The FSA has primary responsibility for banking supervision in the United Kingdom and has wide discretionary powers in relation to the banks that it authorizes to carry on banking business.

Authorization

Under the Banking Act, no one may accept deposits in the United Kingdom from the public as part of a deposit-taking business without authorization from the FSA, unless (1) he is authorized to do so by the FSA, (2) he utilizes the European Economic Area "passport" to take deposits in the United Kingdom (in which case he must be authorized in another member state of the European Economic Area) or (3) an exemption applies. In deciding whether to authorize banking business, the FSA must consider whether the applicant meets the requirements of the Banking Act. For example, the FSA must be satisfied that:

- the institution can conduct its business in a prudent manner;
- the institution has the prescribed minimum net assets or initial capital; and
- the directors, controllers and managers of the institution are fit and proper persons to hold the positions concerned.

Supervision and Change in Control

In its role as supervisor of banks, the primary objective of the FSA is to fulfill its responsibilities under the Banking Act relating to the safety and soundness of banks with the aim of strengthening, but not guaranteeing, the protection of depositors. The FSA carries out this prudential supervision of banks through the collection of information from statistical returns, through review of accountants' reports, by visits to banks and through regular formal interviews.

The FSA has adopted a risk-based approach to the supervision of banks. Under this approach the FSA performs a formal risk assessment of every bank or banking group in the United Kingdom during each supervisory period, which varies in length according to the risk profile of the bank. The FSA performs the risk assessment by analyzing information which it receives during the normal course of its supervision, such as regular prudential returns on the financial position of the bank, or which it acquires through a series of meetings with senior management of the bank. After each risk assessment, the FSA will inform the bank of its views on the bank's risk profile. This will include details of any remedial action which the FSA requires the bank to take and the likely consequences if this action is not taken by the bank (this may include increasing the bank's capital ratios or, in extreme cases, revoking the bank's authorization).

Throughout the supervisory period, the FSA will evaluate the information it receives and, at the end of the period, a formal evaluation will be undertaken to ensure that the bank has completed its original work plan.

In June 1998, the FSA issued its Guide to Banking Supervisory Policy. The guide sets out the FSA's prudential policy for its supervision of institutions authorized under the Banking Act. Each bank submits regular reports to the FSA that provide material for supervisory assessment. Supervision has become increasingly formalized with the introduction of the guide, which covers, among other things, liquidity, large exposures to a single counterparty or related group of counterparties, the adequacy of accounting and other records and internal control systems, money laundering, loan transfers and securitization of loans, advertising and the FSA's relationship with a bank's external auditors.

The Banking Act provisions with respect to change in control require the FSA to give prior approval to a person intending to acquire 10% or more of the shares in, or who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of the company, or any company of which it is a subsidiary, or who exercises significant influence over the management of the company, or any company of which it is a subsidiary. Prior approval is also required where any person who is already a controller of a bank seeks to increase its holding, either directly or through control of voting power, to 10% or more, 20% or more, 33% or more, 50% or more or 75% or more of the bank or any company of which it is a subsidiary.

Once the 2000 Act comes into force, these rules are broadly intended to remain the same to the extent that they apply to those who intend to acquire control or increase the level of their control, over an authorized bank, by virtue of shareholder or voting rights.

Where an individual exerts significant influence over the bank, he may need to be approved by the FSA under the new "approved persons" regime. Directors, non-executive directors, chief executive officers, compliance officers, money laundering officers, finance officers, risk control officers and internal auditors might need to receive such approval. See "—Supervision and Change in Control" in this section above.

Reporting Requirements

The Banking Act requires banks authorized in the United Kingdom to provide the FSA with information that the FSA may reasonably require to perform its functions under the Banking Act. Banks have primary responsibility for informing the FSA of matters that are relevant to the FSA's functions as supervisor under the Banking Act. There are regular prudential meetings and reporting procedures designed to help banks meet this obligation and to provide a forum for discussion, explanation and debate on matters such as the control environment and risk profile of the bank. The FSA can also require banks to commission reports from their reporting accountants and to forward these reports to it.

The Banking Act requires a bank to notify the FSA in advance of any proposed exposure to any one counterparty (or related group of counterparties) exceeding 25% of its capital base and any actual exposure to any one counterparty exceeding 10% of its capital base. The implementation in the United Kingdom of the EC Large Exposures Directive supplemented the notification requirements under the Banking Act with a prohibition against certain large exposures. The Large Exposures Directive places an explicit or hard limit of 25% of capital on exposures to an individual counterparty or a group of related counterparties, and an explicit limit of 800% of capital on the aggregate of non-exempt exposures that exceed 10% of capital. Certain exposures are exempt from these limits.

Deposit Protection and Investors Compensation

Following amendments made to the Banking Act to implement the EC Directive on Deposit Guarantee Schemes, banks are required, on request, to provide all depositors and potential depositors with details of the deposit protection scheme to which they belong and the conditions and procedures for making a claim under that scheme. All banks authorized under the Banking Act are members of the UK Deposit Protection Scheme, which covers most types of deposit, but does not, for example, include deposits by other financial institutions or deposits by companies in the same group as a bank. The scheme covers 90% of a bank's total liability to a depositor, subject to a maximum payment to any one individual of £18,000 or €20,000, whichever is greater. The scheme requires all UK institutions authorized under the Banking Act to contribute to the Deposit Protection Fund.

Securities and other investment business is currently regulated under the Financial Services Act. Prudential Banking is authorized to conduct investment business in the United Kingdom through its membership of self-regulating organizations recognized by the FSA. Firms authorized to conduct investment business are also required to participate in, and contribute to, an investors compensation scheme. The UK Investors Compensation Scheme provides for payments to private investors up to an established limit, currently £48,000, if a firm regulated by a self-regulating organization or the FSA cannot meet its investment business liabilities.

The proposed Financial Services Compensation Scheme will be funded by industry participants and will deal with claims that arise in the event of the default of a firm authorized by the FSA. The new scheme will replace the existing compensation schemes covering the financial services industry, including the UK Deposit Protection Scheme and the UK Investors Compensation Scheme. It is envisaged that the new single compensation scheme will come into operation when the 2000 Act comes into force later this year.

Solvency Requirements

The requirement to have adequate capital is one of the criteria for authorization under the Banking Act. A bank should have sufficient capital to provide a stable resource to absorb any losses arising from the risks in its business. In assessing a bank's capital adequacy, the FSA takes into account not only the level of a bank's own funds but also other matters such as concentration of the loan book (large exposures) and liquidity.

The FSA applies capital adequacy guidelines that accord with relevant EC directives and the Basel Accord of 1988, which established a framework for measuring the capital adequacy of international banking organizations. These guidelines implement a number of EC directives, including the Own Funds Directive, concerning capital requirements, the Solvency Ratio Directive, concerning solvency ratios that credit institutions must maintain, and the Capital Adequacy Directive, as amended, referred to as CAD, requiring credit institutions to provide capital for market risk. The FSA's guidelines impose on banks a requirement that they maintain a minimum level of capital to support on and off-balance sheet exposures, weighted according to broad categories of risk. Each bank subject to the FSA's guidelines must maintain a capital adequacy ratio of total capital to risk-weighted assets, of no less than 8%.

The FSA introduced a new market risk regime as from October 1, 1998 for implementation of its policy based on the Basel Accord and the parallel EC Market Risk Directive, known as the "CAD Amending Directive". Both the 1996 Basel Amendment to the Basel Accord and the CAD Amending Directive enable banks to use internal value-at-risk models to calculate capital charges for market risks. Banks that have a trading book over a certain size are obliged to meet the trading book capital requirements of the CAD and the CAD Amending Directive in respect of the market- and credit-related risks arising from their trading activities. This involves splitting their business between trading and banking books.

UK banks are required to maintain, in interest-free accounts at the Bank of England, a cash balance, known as the cash ratio deposit, which is based on eligible liabilities, primarily pound sterling deposits less amounts on loan to other monetary institutions. Although these balances count towards the liquidity requirements for the real time gross settlement system introduced in the United Kingdom during 1996, they are generally regarded as non-operational and, accordingly, do not count towards overall liquidity requirements. Cash ratio deposits became statutory under the Bank of England Act 1998. The current ratio is 0.15% of eligible liabilities in excess of £400 million.

The liquidity standard for sterling, which the UK government introduced in January 1996, requires the maintenance of sufficient holdings of liquid assets to cover potential cash outflows over the next five business days. This policy applies to UK-incorporated retail banks and group UK-based sterling operations.

In June 1999, the Basel Committee on Banking Supervision issued a proposal for a new capital adequacy framework to replace the Basel Accord of 1988. The new capital framework consists of three "pillars": minimum capital requirements that will expand and develop the standardized rules set out in the 1988 Accord, a supervisory review of an institution's capital adequacy and internal assessment process, and effective use of market discipline to strengthen disclosure and encourage safe banking practices.

On November 23, 1999, the European Commission published a consultation document on its proposals to review the existing capital adequacy framework for EU credit institutions and investment firms. The Commission's paper complements the Basel Committee's paper and also contains proposals on minimum capital requirements, supervisory review, and disclosure as an aid to market discipline.

The consultation period for these first two papers has now passed and more concrete proposals have been put forward. The Basel Committee published on January 16, 2001 its consultation paper entitled "The New Basel Capital Accord". The consultation period is due to close on May 31, 2001. The proposal is based on three "pillars" (mentioned above) that allow banks and supervisors to evaluate properly the various risks that banks face. The New Basel Capital Accord focuses on minimum capital requirements (seeking to refine the measurement framework set out in the 1988 Accord), supervisory review of an institution's capital adequacy and internal assessment process and market discipline, through effective disclosure to encourage safe and sound banking practices.

The European Commission also launched on February 5, 2001 a second round of consultations on a new capital adequacy framework for banks and investment firms. New proposals will be drafted in light of the response to the second consultation, but their broad aim will be to:

- reflect market change by taking into account the different needs of global players and locally acting institutions, with the one-size fits all approach likely to be abandoned,
- align capital charges and underlying economic risk more closely,
- provide incentives for enhanced risk mitigation standards, and
- provide a framework to support a comprehensive assessment of the risks banks/investment firms are exposed to.

These new proposals are in their infancy and, accordingly, the potential impact of the new solvency framework for Prudential is difficult to assess. The proposals are expected, however, to improve the efficiency of Prudential in its use of capital, risk management and disclosure.

US Supervision and Regulation

General

Prudential conducts its US insurance activities through Jackson National Life, which is a stock life insurance company licensed to transact its insurance business in, and subject to regulation and supervision by, the District of Columbia and 49 of the 50 states; Jackson National operates a subsidiary, Jackson National Life Insurance Company of New York, in the state of New York. The extent of such regulation varies, but most jurisdictions have laws and regulations governing the financial aspects of insurance companies, including standards of solvency, reserves, reinsurance and capital adequacy and the business conduct of insurance companies. In addition, statutes and regulations usually require the licensing of insurers and their agents and the approval of policy forms and related materials. These statutes and regulations in Jackson National Life's state of domicile, which is Michigan, also set out the permitted types and concentration of investments.

Insurance regulatory authorities in each of the jurisdictions in which Jackson National Life does business require it to file detailed quarterly and annual financial statements, and these authorities have the right periodically to examine its operations and accounts. In addition, Jackson National Life is generally subject to federal and state laws and regulations that affect the conduct of its business. New York and Michigan require their state insurance authorities to conduct an examination of an insurer under their jurisdiction at least once every five years. The New York Insurance authorities conducted an examination of Jackson National Life of New York in 2000 and the report included no material findings. Michigan insurance authorities are currently conducting a routine examination of Jackson National Life. The previous Michigan examination, which covered the period ending December 31, 1996, did not contain any material findings or recommendations. Jackson National Life has been notified that the insurance authorities of North Carolina and California will also be conducting routine examinations later in 2001.

Jackson National Life's ability to pay shareholder dividends is limited under Michigan insurance law. The commissioner may limit, or not permit the payment of, shareholder dividends if the commissioner determines that an insurer's surplus, as regards policyholders, is not reasonable in relation to its outstanding liabilities and is not adequate to meet its financial needs as required by Michigan insurance law. Jackson National Life must report any shareholder dividends to the Michigan insurance commissioner before they can be paid. In the case of an extraordinary shareholder dividend or distribution, an insurer must give 30 days' advance notice to the commissioner and may not pay the dividend or distribution if the commissioner disapproves within such 30-day period. For this purpose, an extraordinary dividend or distribution means any dividend or distribution of cash or other property whose fair market value together with that of other dividends or distributions that an insurer made within the preceding twelve months exceeds the greater of 10% of the insurer's surplus as regards policyholders as of December 31 of the immediately preceding year, or the net gain from operations of the insurer, not including realized capital gains, for the prior year. In 1998, 1999 and 2000, Jackson National Life paid shareholder dividends of $589.6 million, $96.3 million, and $176.3 million, respectively. A portion of the 1998 dividend was extraordinary and paid with prior approval of the commissioner.

State regulators also require prior notice or regulatory approval of changes in control of an insurer or its holding company and of certain material transactions with affiliates. Under New York and Michigan insurance laws and regulations, no person, corporation or other entity may acquire control of an insurance company or a controlling interest in any parent company of an insurance company, unless that person, corporation or entity has obtained the prior approval of the regulator for the acquisition. For the purpose of New York and Michigan law, any person acquiring, directly or indirectly, 10% or more of the voting securities of an insurance company is presumed to have acquired "control" of the company. To obtain approval of any change in control, the proposed acquiror must file an application with the New York superintendent of insurance or the Michigan insurance commissioner, as appropriate. This application requires the proposed acquiror to disclose, among other information, its background, financial condition, the financial condition of its affiliates, the source and amount of funds by which it will effect the acquisition, the criteria used in determining the nature and amount of consideration to be paid for the acquisition, proposed changes in the management and operations of the insurance company and other related matters.

Guaranty Associations and Similar Arrangements

Each of the 50 states of the United States, the District of Columbia and Puerto Rico have laws requiring insurance companies doing business within their jurisdictions to participate in various types of guaranty associations or other similar arrangements. These associations and arrangements provide certain levels of protection to policyholders from losses under insurance policies that impaired or insolvent insurance companies issue. Typically, these associations levy assessments, up to prescribed limits, on member insurers on a basis that is related to the member insurer's proportionate share of the business in the relevant jurisdiction of all member insurers in the lines of business in which the impaired or insolvent insurer is engaged. Some jurisdictions permit member insurers to recover assessments that they paid through full or partial premium tax offsets, usually over a period of years.

Asset Valuation Reserve

State regulators generally require that insurers establish an asset valuation reserve that consists of two components: a default component to provide for future credit-related losses on fixed income investments and an equity component to provide for losses on all types of equity investments. The asset valuation reserve establishes statutory reserves for fixed maturity securities, equity securities, mortgage loans, equity real estate and other invested assets. The reserve is designed to capture all realized and unrealized gains and losses on such assets, other than those resulting from changes in interest rates. The level of reserves is based on both the type of investment and its rating. Contributions to the reserve may result in a slower growth in surplus or a reduction of Jackson National Life's unassigned surplus, which, in turn, reduces funds available for shareholder dividends or shareholder distributions. The extent of the impact of its asset valuation reserve on Jackson National Life's surplus depends in part on the future composition of the investment portfolio.

Interest Maintenance Reserve

State regulators generally require that insurers establish an interest maintenance reserve to defer noncredit-related realized capital gains and losses, net of taxes, on fixed income investments, primarily bonds and mortgage loans, which are amortized into net income over the estimated remaining periods to maturity of the investments sold. The extent of the impact of the interest maintenance reserve depends on the amount of future interest-rate related realized capital gains and losses on fixed maturity investments.

The National Association of Insurance Commissioner Ratios

On the basis of statutory financial statements that insurers file with state insurance regulators, the National Association of Insurance Commissioners annually calculates twelve financial ratios to assist state regulators in monitoring the financial condition of insurance companies. A usual range of results for each ratio is used as a benchmark and departure from the usual range on four or more of the ratios can lead to inquiries from individual state insurance departments. In 1998, Jackson National Life had one ratio that fell outside the usual range. It related to the net change in capital and surplus ratio and was associated with the year's extraordinary dividend approved by the Michigan insurance commissioner. For the purposes of calculating this ratio, a largely offsetting capital contribution was disregarded, which resulted in the ratio falling outside the normal range.

Policy and Contract Reserve Sufficiency Analysis

Michigan insurance law requires Jackson National Life to conduct annually an analysis of the sufficiency of interest-sensitive life and annuity reserves. A qualified actuary must submit to the insurance department an opinion that states that the reserves, when considered in the light of the assets that an insurance company holds with respect to such reserves, make good and sufficient provision for the associated contractual obligations and related expenses of the insurance company. If a qualified actuary cannot provide such an opinion, then the insurance company must set up additional reserves by moving funds from unassigned surplus. The 2000 opinion is not due yet. However Jackson National Life expects to provide the required 2000 opinion to the insurance department without any qualifications.

Jackson National Life's Capital and Surplus

Michigan insurance law requires Jackson National Life, as a domestic stock life insurance company, to maintain at least US$7,500,000 in unimpaired capital and surplus. In addition, insurance companies are required to have sufficient capital and surplus to be safe, reliable and entitled to public confidence.

As a licensed insurer in the District of Columbia and every state but New York, where it operates through a subsidiary, Jackson National Life is subject to the supervision of the regulators of each such jurisdiction. In connection with the continual licensing of Jackson National Life, regulators have discretionary authority to limit or prohibit new issuance of business to policyholders when, in their judgment, the regulators determine that such insurer is not maintaining minimum surplus or capital or if further transaction of business will be hazardous to policyholders.

Risk-based Capital

In 1992, the National Association of Insurance Commissioners approved risk-based capital standards for life insurance companies as well as a model act for state legislatures to enact. The model act requires that life insurance companies report on a formula-based, risk-based capital standard that they calculate by applying factors to various asset, premium and reserve items. The formula takes into account the risk characteristics of a company, including asset risk, insurance risk, interest rate risk and business risk. The National Association of Insurance Commissioners designed the formula as an early warning tool to identify potentially inadequately capitalized companies for purposes of initiating regulatory action. The National Association of Insurance Commissioners intended the formula as a regulatory tool only and did not intend it as a means to rank insurers generally. The model act imposes broad confidentiality requirements on those engaged in the insurance business (including insurers, agents, brokers and others) and on state insurance departments as to the use and publication of risk-based capital data.

The model act gives the state insurance commissioner of any state adopting it explicit regulatory authority to require various actions by, or take various actions against, insurance companies whose adjusted capital does not meet minimum risk-based capital standards. The Michigan insurance commissioner takes into account the National Association of Insurance Commissioners' risk-based capital standards to determine adequate compliance with Michigan insurance law. At December 31, 2000, Jackson National Life's total adjusted capital under the National Association of Insurance Commissioners' definition substantially exceeded model act standards.

Regulation of Investments

Jackson National Life is subject to state laws and regulations that require diversification of its investment portfolio, limit the amount of investments in certain investment categories such as below investment grade fixed income securities, equity real estate, foreign securities and common stocks and forbid certain other types of investments altogether. Jackson National Life's failure to comply with these laws and regulations would cause investments exceeding regulatory limitations to be treated by the Michigan Insurance Division as nonadmitted assets for purposes of measuring surplus, and, in some instances, the Michigan Insurance Division could require divestiture of such nonqualifying investments.

Federal Financial Services Regulation Initiatives

On November 12, 1999, the US president signed into law the Gramm-Leach-Bliley Act ("Gramm-Leach") which eliminates certain barriers to and restrictions on affiliations among banks, securities firms, insurance companies and other financial services organizations. Gramm-Leach permits bank holding companies, US banks and, in some cases, foreign banking organizations that meet certain criteria (relating to capital, management and service to low- and moderate-income communities) to affiliate with and engage in a wider range of financial activities, including securities underwriting and dealing, mutual fund distribution and merchant banking investing.

While Gramm-Leach relaxes restrictions on affiliations of banks with financial companies, it generally leaves in place restrictions on affiliations between banks and commercial firms. In addition, Gramm-Leach imposes new restrictions on affiliations between savings associations, or "thrifts," and commercial firms. Before Gramm-Leach, commercial companies were permitted to own a single thrift under certain conditions and were regulated as "unitary thrift holding companies" by the Office of Thrift Supervision. After Gramm-Leach, commercial companies are generally prohibited from acquiring or establishing even a single thrift.

Jackson National Life acted before Gramm-Leach to acquire a thrift and thereby achieved a "grandfathered unitary thrift holding company" status for itself and for Prudential plc. See "—Business of Prudential—US Business—Jackson Federal Bank" in this Item 4. Grandfathered unitary thrift holding company status is generally superior to the new affiliation powers authorized under Gramm-Leach for "financial holding companies". Gramm-Leach does not impose any affiliation restrictions on grandfathered unitary thrift holding companies. Thus, right now, if Jackson National Life or its holding companies wanted to acquire, for example, a computer chip maker or a grocery store, in the US or overseas, there would be no barrier to such a transaction under US banking laws.

This privilege exists only so long as the holding company preserves its status as a grandfathered unitary thrift holding company, however. The primary restrictions in this regard are that the holding company cannot undergo a change in control or acquire a separate US bank or thrift (unless the acquired institution is merged with the existing thrift subsidiary, Jackson Federal Bank).

Besides the general lack of restriction on affiliations, the other major consequences of being a grandfathered unitary thrift holding company is that the holding company is subject to the lighter supervisory regime of the Office of Thrift Supervision rather than that of the Federal Reserve Board.

On the other hand, because Jackson National Life and its holding companies are not currently engaged in commercial activities, Jackson National Life has the power to choose to become a "financial holding company" at a future date (e.g., by acquiring a bank or by converting Jackson Federal Bank into a bank), and thereby become subject to the Federal Reserve Board regulatory regime, if Jackson National Life discovers an advantage to doing so. The status of "grandfathered unitary thrift holding company" would be irretrievably forgone, however.

While the impact of Gramm-Leach is difficult to predict, there are a number of ways in which the legislation may affect Jackson National:

- Jackson National Life may face additional competition from larger financial services companies because banks, securities firms and insurance companies, both in the US and those currently engaged in such activities offshore, may affiliate with and form organizations that compete with Jackson National Life's businesses. In the year since Gramm-Leach was adopted, there have not been many mergers between banks and insurers, perhaps because insurers have been reluctant to subject themselves to the supervision of the Federal Reserve Board, and because banks may be reluctant to dilute their return on equity (averaging around 20% compared to returns for US insurers in the low teens). This could change, however, as economics change and as Federal Reserve Board supervision of insurers becomes more well-defined.
- Bank acquisitions of insurance agencies have accelerated (because Gramm-Leach provided additional empowerments to prior law which limited banks to selling insurance from places with populations of less than 5,000), intensifying the strategic importance of efforts to sell Jackson National Life products through banks and bank affiliates.

- Gramm-Leach requires all financial services providers to comply with new privacy requirements, including a provision permitting customers to decide not to permit financial providers to share nonpublic personal information with third parties who seek to market to these customers. All of Jackson National Life's companies will be subject to this requirement, but the requirement is not expected to add significant costs or competitive burdens.

Securities Laws

Jackson National Life, certain of its affiliates and certain policies and contracts that Jackson National Life offers are subject to various levels of regulation under the federal securities laws that the Securities and Exchange Commission administers.

The primary intent of these laws and regulations is to protect investors in the securities markets and generally grant supervisory agencies broad administrative powers, including the power to limit or restrict the conduct of business for failure to comply with such laws and regulations. Jackson National Life may also be subject to similar laws and regulations in the states in which it provides investment advisory services, offers the products described above or conducts other securities related activities.

Jackson National Asset Management LLC is registered with the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940 and a transfer agent under the Securities Exchange Act of 1934 (the "Securities Exchange Act"). The mutual funds for which Jackson National Asset Management LLC serves as investment adviser are subject to regulation under the Securities Act of 1933 (the "Securities Act") and the Investment Company Act of 1940, as amended (the "Investment Company Act"). In addition, variable annuities and the related separate accounts of Jackson National Life are subject to regulation by the Securities and Exchange Commission under the Securities Act and the Investment Company Act as well as applicable insurance laws.

Each of Jackson National Life Distributors, Inc., National Planning Corporation, SII Investments, Inc., INVEST, and ICA is registered as a broker-dealer under the Securities Exchange Act. National Planning Corporation was formerly known as Jackson National Financial Services, Inc. Jackson National Life Distributors, National Planning Corporation and SII Investments are subject to regulation and supervision by the Securities and Exchange Commission, state securities authorities, (to the extent that they transact business in that state), and the National Association of Securities Dealers, Inc., each of which has broad administrative and supervisory powers relative to all aspects of the broker-dealer business and may examine a broker-dealer's business and accounts at any time.

Prudential conducts its US investment management activities through PPM America, Inc., which is registered with the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940. PPM America, Inc. serves as the investment adviser to Jackson National Life, certain mutual funds, several private investment funds and structured finance vehicles, and the US equity and fixed income portions of portfolios of certain UK affiliates of PPM America, Inc. The mutual funds for which PPM America, Inc. serves as investment adviser or sub-adviser are subject to regulation under the Securities Act and the Investment Company Act.

PPM America, Inc. and certain of its subsidiaries are subject to various levels of regulation under the federal securities laws that the Securities and Exchange Commission administers. The primary intent of these laws and regulations is to protect investors in the securities markets and generally grant supervisory agencies broad administrative powers, including the power to limit or restrict the conduct of business for failure to comply with such laws and regulations.

To the extent that PPM America, Inc. manages assets for certain types of employee benefit plans subject to ERISA, the Employee Retirement Income Security Act of 1974, as amended, certain activities of PPM America, Inc. are potentially subject to the same types of regulatory restrictions that ERISA and the Internal Revenue Code impose. Such restrictions are the same as those described with respect to Jackson National Life concerning Employee Benefit Plan Compliance. See "—Employee Benefit Plan Compliance" in this section below. The Department of Labor and the Internal Revenue Service have interpretive and enforcement authority over these provisions of ERISA and the Internal Revenue Code.

Thrift Regulation

JNL Thrift Holdings, Inc., a subsidiary of Jackson National Life, is the immediate parent company and a unitary thrift holding company for Jackson Federal Bank, a federally chartered savings association, or "thrift".

The Office of Thrift Supervision, a component of the U.S. Department of the Treasury (an agency of the federal government), regulates unitary thrift holding companies and the thrift.

A thrift holding company is subject to statutory and regulatory requirements that control transactions between affiliates, limit the activities that holding companies and their affiliates may engage in unless specific requirements are met and require registration and periodic filings with the Office of Thrift Supervision. Thrift holding companies and their subsidiaries are also subject to periodic examination to evaluate the financial condition and managerial ability of the holding company. The Office of Thrift Supervision has examined Jackson Federal Bank and the thrift holding company, subsequent to the acquisition by Jackson National Life and is current on all applicable regulatory exams.

Employee Benefit Plan Compliance

Jackson National Life issues certain types of general account stable value products, such as GICs and funding agreements, to employee benefit plans and to investment vehicles that pool the investments of such plans. To a large extent, these plans are retirement plans that are subject to the fiduciary standards of ERISA, and that are tax qualified under the Internal Revenue Code. As such, certain activities of Jackson National are potentially subject to certain regulatory restrictions that ERISA and the Internal Revenue Code impose. These restrictions include:

- the requirement under ERISA that fiduciaries must perform their duties solely in the interests of ERISA plan participants and beneficiaries,
- the requirements under ERISA and the Internal Revenue Code that fiduciaries may not engage in conflict of interest transactions, and
- the requirements under ERISA and the Internal Revenue Code that a fiduciary may not cause a covered plan to engage in certain prohibited transactions with certain persons who provide services to the plan or are affiliated with the plan sponsor or a plan service provider.

The Department of Labor and the Internal Revenue Service have interpretive and enforcement authority over these provisions of ERISA and the Internal Revenue Code.

In the instance where an insurer issues a guaranteed benefit policy to a plan, ERISA provides that the insurer need not become a fiduciary with respect to the plan solely as a result of the issuance of the policy. Under Section 401 of ERISA, a guaranteed benefit policy means an insurance policy to the extent such policy provides for benefits the amount of which the insurer guarantees.

In 1993, in *John Hancock Mutual Life Insurance Company v. Harris Trust & Savings Bank*, the US Supreme Court held that, with respect to a portion of the funds held under a general account group annuity contract, an insurer could be subject to the fiduciary requirements of ERISA and the prohibited transaction provisions of ERISA and the Code. This decision was in contradiction to interpretations that the Department of Labor had previously issued.

As part of the Small Business Job Protection Act of 1996, Congress offered some relief from the impact of the *Harris Trust* decision for certain policies issued on or before December 31, 1998. This Act also required the Department of Labor to issue regulations for the purpose of determining, in cases where an issuer issues general account policies to or on behalf of employee benefit plans, which assets of the insurer will be subject to the fiduciary responsibility and prohibited transaction provisions of ERISA. In addition, the Act provided some protection from lawsuits claiming breaches of fiduciary duties under ERISA for actions arising prior to the finalization of such regulations for policies.

Nonetheless, the relief provided by the Small Business Job Protection Act is only transitional and the Department of Labor has not to date provided detailed guidance on the application of the *Harris Trust* decision to a determination of whether one or more policies will qualify as a guaranteed benefit policy. Accordingly, although Prudential does not believe that the *Harris Trust* decision will have a material adverse effect on Jackson National Life's business, financial condition or operations results, and Jackson National Life is proceeding with its general account products with the understanding that their issuance will not alone make Jackson National Life subject to ERISA's fiduciary standards and prohibited transaction provisions, the full impact of the *Harris Trust* decision is not entirely clear.

In addition, for plans that are not subject to ERISA or the prohibited transaction provisions of the Internal Revenue Code, such as pension plans maintained by state or local governments, state and local laws may apply in lieu of these fiduciary standards. Although Prudential does not believe that such laws will have a material adverse effect on Jackson National Life's business, financial condition or operations results, the application of these laws is generally less developed than the federal pension laws.

Financial Services Regulatory and Legislative Issues

The US President has in the past proposed to increase the taxes levied against the insurance industry to increase the federal budget. The industry has been very successful in resisting these proposals on the grounds that an increase in taxes on insurance companies or insurance policies would have a negative affect on US citizens saving for their retirement. The insurance industry is very vigilant in monitoring these proposals and taking action to oppose them.

States regulate the business of insurance and each state regularly enacts or promulgates legislation and regulations that affect the way insurers do business within the state's boundaries. A major issue at the state level involves genetic information and whether insurers should be able to use such information when underwriting insurance policies. Many states have passed legislation restricting a health insurer's ability to use this information, but, at present, life insurance companies have not been made subject to similar restrictions. Prudential expects that similar legislative initiatives will continue to be passed into law.

Item 5. Operating and Financial Review and Prospects

OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion and analysis should be read in conjunction with Prudential's consolidated financial statements and the related notes to Prudential's consolidated financial statements included elsewhere in this document. Prudential's consolidated financial statements have been prepared in accordance with UK GAAP, which differs in certain material respects from US GAAP. For a summary of the material differences between UK GAAP and US GAAP relevant to Prudential's financial statements, see notes 33 and 34 of the notes to Prudential's consolidated financial statements.

The results discussed below are not necessarily indicative of the results to be expected in any future periods. This discussion contains forward-looking statements based on current expectations, which involve risks and uncertainties. Actual results and the timing of certain events may differ significantly from those projected in these forward-looking statements due to a number of factors, including those set forth in the section below entitled "—Factors Affecting Results of Operations" and elsewhere in this document.

Introduction

Prudential provides a broad range of financial products and services, primarily to the retail market. The period since 1996 has been one of significant change as Prudential has positioned its group to compete and succeed in the new millennium. In 1996, Prudential disposed of its reinsurance operations, Mercantile and General Reinsurance, and its small business in The Netherlands, and launched Prudential Banking. In 1997, Prudential acquired Scottish Amicable and disposed of its small Italian business.

In 1998, Prudential:

- launched a new direct marketing banking operation, Egg,
- disposed of its Australian and New Zealand operations and
- initiated a fundamental organizational restructuring of its main UK operations.

In 1999, Prudential:

- completed the acquisition of M&G,
- expanded its Asian and European operations,
- further re-organized its UK retail and fund management operations and
- further developed Egg.

These activities have adversely impacted earnings in these periods. The restructuring of the UK retail and fund management operations gave rise to a charge to profit before tax of £70 million in 1999, while Egg reported net operating losses before tax of £77 million in 1998, £150 million in 1999 and £155 million in 2000. M&G's profits of £56 million in 1999, which reflect eight months of operations, were more than offset by goodwill amortization costs of £51 million and acquisition funding costs of £75 million. Although Prudential expects these activities and other initiatives, such as its plans to expand its business in continental Europe, to continue to adversely impact earnings in the short-term, it has fundamentally changed the focus, structure, product range and distribution reach of its group and is designed to deliver long-term growth and profitability.

In 2000, Prudential:

- completed its listing on the New York Stock Exchange, and
- completed an initial public offering of Egg plc on the London Stock Exchange.

Total proceeds from the Egg offering, net of expenses, amounted to £239 million, of which approximately £90 million related to the sale of shares by the parent company after deduction of expenses and the remainder related to new share capital issued by Egg. The offering resulted in a profit for the group of £119 million.

Factors Affecting Results of Operations

General

Prudential's results of operations are affected, to a greater or lesser degree, by a variety of factors, including demographics, general economic and market conditions, government policy and legislation, regulation, competition and exchange rate fluctuations. In addition, the recent change in the composition of its businesses and the execution of its growth strategy may result in increased variation in profits from year to year.

Since 1998, Prudential's results have also been adversely impacted by its initial investment in its internet banking operation, Egg. Internet banking is an unproven market in the United Kingdom and the future profitability of Egg will depend on the continued growth in internet usage in the United Kingdom, the continued acquisition and retention of internet-enabled customers, the provision of additional products for these customers to cross-buy and the leveraging of cost advantages of internet distribution.

General Economic and Market Conditions

In the 1990s, retail financial services and fund management markets in the United Kingdom and the United States benefited from generally favorable economic and market conditions. During that period, both the United Kingdom and the United States experienced strong economic growth, stable interest rates, low inflation rates and very strong growth in stock market prices. More recently, these markets have experienced significant volatility. Despite these recent fluctuations, Prudential believes that the historical strength of the UK and US equity markets, combined with demographic factors and governmental efforts to increase individual savings and self-provision for retirement, has resulted in increased consumer focus on savings and investment products.

Changes in interest rates and returns from equity, real estate and other investments as well as volatility in these items may affect Prudential's profitability. In the United Kingdom, where Prudential invests in debt and other fixed income securities, equity securities and real estate, shareholders' profits under UK GAAP are largely a function of the bonuses it declares on with-profits products. These products, which are described in more detail under Item 4, "Information on the Company—Business of Prudential—UK Business—With-Profits Products", are life and pension products that provide for the policyholder to participate in a share of the profits of the fund into which premiums are paid through a mix of annual and terminal bonuses. As described in more detail under "—Basis of Profit" in this section below, the most important influences on the rates of these bonuses are the overall rate of return earned on investments and Prudential's expectations of future investment returns. Because shareholders' profits from the with-profits fund under UK GAAP represent an amount of up to one-ninth of the value of that year's bonus declaration to policyholders, they are affected by Prudential's expectations of interest rates and the achieved growth in equity markets, although this effect is smoothed to the extent bonuses are smoothed. In recent years, Prudential's long-term expectations of lower investment returns have had a negative impact on annual bonus rates and, as a result, shareholders' profit. A sustained fall in equity markets would have a negative impact on terminal bonus rates and, consequently, shareholders' profit. Under US GAAP, 90% of the current year's earnings before the bonus declaration are allocated to policyholders and the remainder to shareholders. Therefore, on a US GAAP basis, shareholders' profits are not smoothed and are affected by current year fluctuations in the value of the investment portfolio.

In the United States, fluctuations in prevailing interest rates, including changes in the difference between the levels of prevailing short-term and long-term rates, can affect results from Jackson National Life, which is predominantly a spread-based business with the majority of its assets invested in fixed income securities. A mismatch of interest-earning assets and interest-bearing liabilities in any given period may, in the event of changes in interest rates, have a material effect on Prudential's financial condition or results of operations. Prudential designs its US products and manages the investments supporting this business to reduce interest rate sensitivity. This has the effect of moderating the impact on Prudential's results of changes in prevailing interest rates. To reduce investment, interest rate and foreign currency exposures and to facilitate efficient investment management, Prudential uses derivative instruments. For a further discussion of Prudential's use of derivatives see Item 11, "Quantitative and Qualitative Disclosures About Market Risk—Use of Derivatives".

Government Policy and Legislation

Changes in government policy or legislation applying to companies in the financial services and insurance industries in any of the jurisdictions in which Prudential operates, particularly in the United Kingdom and the United States, may adversely affect the result of its operations. These include possible changes in the tax treatment of financial products and services, government pension arrangements and policies, the regulation of selling practices and solvency standards. These changes may affect Prudential's existing and future business by, for example, causing customers to cancel existing policies, requiring Prudential to change its range of products and services, redesign its technology or other systems, retrain staff, pay increased tax or incur other costs.

The UK government has introduced legislation covering new pensions products, referred to as stakeholder pensions, which require fundamental changes to the way Prudential's pensions products are designed, marketed and distributed. The requirements may make it more difficult to write profitable new pensions business and to retain existing business and the profit margins thereon, principally because the government has capped charges on new pensions business at 1% of the policyholder account balance per annum for stakeholder pensions, which is significantly below the charges currently generally available from the UK pensions industry. At the same time, Prudential believes that the requirements favor larger companies that can achieve economies of scale and have well-established brand names. Prudential believes that its strong brands and financial strength will position it to compete in the new stakeholder market and to provide pension products that will be competitive with other offerings in the market. Stakeholder pensions and their implications are discussed in more detail under Item 4, "Information on the Company—Business of Prudential—UK Business—Implications of Stakeholder Pensions".

On May 29, 2000, new, more stringent valuation regulations were introduced by the UK regulatory authorities. The new regulations require reserves to be held to cover a large part of the terminal bonus on unitized with-profits business. The effect of these regulations, had they been in force at December 31, 1999, would have been to increase liabilities under UK GAAP by approximately 9% and to reduce the free asset ratio from 29% to 19%. At December 31, 2000, Prudential Assurance's free asset ratio was 17%.

Regulation

In recent years, the insurance sectors in the markets in which Prudential operates have faced increased scrutiny. In 1997, Prudential was publicly criticized by its UK regulators for its treatment of pensions misselling and for failures to adequately monitor and train its salesforce. Pensions misselling is discussed in more detail under Item 4, "Information on the Company—Business of Prudential—UK Business—Compliance—Pensions Misselling". Additional regulation, scrutiny and related costs have put pressure on the margins on new business, particularly business distributed through the company salesforce in the United Kingdom. In the United States, Prudential has been the subject of regulatory sanctions and class actions. These class actions are discussed in more detail under Item 4, "Information on the Company—Business of Prudential—Legal Proceedings". Changes in pensions, financial services and tax regulation could have an impact on Prudential's results.

Competition

Prudential faces substantial competition in all of its markets for the types of insurance, investment and banking products it offers. Factors contributing to this include deregulation, consolidation, convergence, changing consumer awareness, the entry of new participants, the increased ability of other financial service companies to offer products similar to Prudential's and the development of new methods of distribution. This competition, combined with the regulatory factors described above, has put increasing pressure on margins and pressure on Prudential to reduce costs and achieve competitive investment returns. As a result, Prudential is altering the types of products it offers and the methods by which it distributes them, and it is continuing to look at new ways of distributing its products. Prudential believes that the trend towards intermediated and direct distribution, including through the internet, and away from company salesforce distribution, is likely to continue. Prudential expects this trend to be reflected in the relative contribution to sales and performance from its different UK businesses.

Exchange Rate Fluctuations

Prudential publishes its consolidated financial statements in pounds sterling. Its US operations represent a significant proportion of income and expense, and, accordingly, significant fluctuations in the US dollar could significantly affect Prudential's reported results from year to year. This impact is mitigated to some extent by the fact that revenues and expenses of its US operations, as well as assets and liabilities, are denominated in US dollars. For the years 1998, 1999 and 2000, the US dollar has remained relatively stable and, therefore, has not affected Prudential's reported results to any significant extent. The recent appreciation of the US dollar relative to pounds sterling may impact reported results from its US operations.

UK Restructurings

In 1999, the Prudential board approved plans to restructure certain of Prudential's UK operations. This restructuring, which is substantially complete, relates to both the integration of Prudential Portfolio Managers and M&G following the acquisition of M&G and the downsizing of the company's direct salesforce. Its effect on Prudential's results is discussed in "—1999 UK Restructuring".

On February 13, 2001, Prudential announced revised plans to further restructure its direct salesforce and customer service channels in its UK insurance operations. Prudential expects to incur costs of £110 million in connection with this restructuring, of which £13 million will be borne by the shareholders' funds in 2001. Provision will be made for this in the profit and loss account for the year ended December 31, 2001. See Item 4, "Information on the Company—Business of Prudential—UK Business—UK Business Units—Prudential Financial Services".

Basis of Profit

Prudential's results comprise an annual profit distribution to shareholders from its UK with-profits fund, as well as profits from its other businesses. Prudential's primary UK GAAP financial statements are prepared under the modified statutory basis of reporting as required by UK law. For most of its operations, other than its UK long-term insurance businesses, the modified statutory basis matches items of income and related expenditure within the same accounting period. This is achieved through the deferral of acquisition costs and application of the accruals concept.

For Prudential's UK long-term insurance business, the primary annual contribution to shareholders' profit comes from its with-profit products. With-profits products are designed to provide policyholders with smoothed investment returns through a mix of annual and terminal bonuses. Shareholders' profit in respect of bonuses from with-profit products represents an amount of up to one-ninth of the value of that year's bonus declaration to policyholders. The smoothing inherent in the bonus declarations provides for relatively stable annual shareholders' profit from this business.

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

The annual excess of premiums and investment return over operating expenses, benefit provisions and claims payments within Prudential's with-profits fund that are not distributed in that year as bonuses and related shareholders' profit are transferred to the fund for future appropriations by a charge to the profit and loss account of the long-term fund. Any shortfall in such amounts would result in a transfer from the fund for future appropriations by a credit to the profit and loss account of the long-term fund. Current year amounts in respect of premiums, investment return, operating expenses and unusual charges or credits do not directly affect the distribution of profit to shareholders from the with-profits business in that year. Current year claims, which include terminal bonus payments, do have an effect on shareholders' profit through the shareholders' proportion of the value of those terminal bonuses.

The fund for future appropriations comprises amounts Prudential expects to pay to policyholders in the future, the related shareholder transfers and surplus assets. These surplus assets, which are described in more detail under Item 4, "Information on the Company—Business of Prudential—UK Business—Shareholders' Interests in Long-term Insurance Business—Surplus Assets in Prudential Assurance's Long-term Fund", have accumulated over many years from a variety of sources and provide the long-term fund with working capital. This working capital permits Prudential to invest a substantial portion of the assets of the long-term fund in equity securities and real estate, smooth investment returns to with-profit policyholders, keep its products competitive, write new business without being constrained as to cash flows in the early policy years and demonstrate solvency.

In addition, Prudential can use surplus assets to absorb the costs of significant events, such as fundamental strategic change in its long-term business and, as approved by the UK regulator, the cost of its pensions misselling, without affecting the level of distributions to policyholders and shareholders. The costs of fundamental strategic change may include investment in new technology, redundancy and restructuring costs, cost overruns on new business and the funding of other appropriate long-term insurance related activities including acquisitions.

Within the modified statutory basis result, Prudential focuses on operating profit before amortization of goodwill and tax as the primary measure of current year performance. This excludes exceptional items, such as profits on business disposals, and includes the investment return for the UK shareholders' funds and personal lines property and casualty insurance business and Jackson National Life, using a longer term rate of return, rather than the actual return for the year, in accordance with the modified statutory basis of accounting. The analysis and discussion in "—Analysis by Geographic Region" in this section below is based upon operating profit before amortization of goodwill and tax. Due to the long-term nature of Prudential's business, its basis of presentation of operating profits may not be comparable with other UK companies. See note 4 to the notes to Prudential's consolidated financial statements for a description of the basis.

For all of Prudential's long-term insurance businesses (United Kingdom, United States, Asia and continental Europe), operating profit is generated principally from its in-force book of business. Prudential's in-force book is business that was written in earlier years and on which it continues to declare bonuses or credit interest to policyholders and generate profit for shareholders. These books of in-force business have been built up over many years with the result that, for Prudential's long-term insurance business, sales in any one year do not have a significant impact on shareholders' profit in that year, but may have an impact in subsequent years.

In order to identify value being generated by Prudential's long-term insurance businesses, management also uses the achieved profits basis of reporting. The achieved profits basis uses discounted cash flows to show the current value of future cash flows to shareholders of both new business and in-force business. The achieved profits basis of financial information is prepared in accordance with Guidance by the Association of British Insurers. This additional basis of presentation has received wide acceptance in the United Kingdom and such supplemental financial information is published annually by UK insurance companies listed on the London Stock Exchange.

Overview of Consolidated Results

The following discussion provides an overview of the components of Prudential's gross premiums and deposits from continuing operations and its profit both before and after tax. A detailed analysis of the trends underlying Prudential's operating profit before amortization of goodwill and tax is included in the analysis by geographic region.

Gross Premiums and Deposits from Continuing Operations

Gross premiums from continuing operations totalled £14,506 million in 2000, a decrease of 4% over 1999. Gross premiums from continuing operations in 2000 include £8,041 million from UK operations, a decrease of 19% primarily due to decreased sales by Prudential's IFA business, and £5,223 million from its US operations, an increase of 17% primarily from increased sales of fixed and variable annuities. In 1999, gross premiums from continuing operations totalled £15,144 million, an increase of 38% from 1998. Gross premiums from continuing operations in 1999 include £9,873 million from UK operations, an increase of 39% primarily from the with-profits business, and £4,449 million from US operations, an increase of 37% primarily from increased sales of fixed and variable annuities, and stable value products.

Total customer deposits for Egg in 2000 decreased by £1,029 million to £7,128 million at December 31, 2000 compared with total customer deposits at December 31, 1999. This decrease reflects increased competition in the banking industry and transfers of predominantly high-value account balances after Egg reduced its interest rates on deposits. In 1999, customer deposits increased by £5,969 million to £8,157 million, as Egg continued to attract new customers with competitive deposit rates via the telephone and over the internet. Egg was launched in October 1998.

Profit before Tax

The following table shows Prudential's consolidated total profit on ordinary activities before tax for the periods indicated.

	Year Ended December 31, 2000	1999	1998
	(In £ Millions)		
Operating profit before amortization of goodwill and tax[1]			
Continuing operations:			
UK operations	**471**	452	394
US operations	**466**	451	411
Asian operations	**22**	15	13
European operations	**(10)**	6	4
Group activities	**(109)**	(78)	38
UK restructuring	**—**	(70)	—
Continuing operations	**840**	776	860
Discontinued operations	**—**	—	8
Operating profit before amortization of goodwill and tax	**840**	776	868
Amortization of goodwill	**(84)**	(54)	—
Profit on flotation of Egg and business disposals	**239**	—	249
Short-term fluctuations in investment returns	**(48)**	28	24
Total profit on ordinary activities before tax	**947**	750	1,141

(1) Due to the long-term nature of Prudential's business, the basis of presentation of operating profit may not be comparable with other UK companies. See note 4 of the notes to Prudential's consolidated financial statements for a description of the basis.

Total profit before tax in 2000 was £947 million compared with £750 million in 1999 and £1,141 million in 1998. The increase in 2000 primarily relates to profit on business disposals of £239 million resulting from the sale of shares and flotation of a minority holding in Egg plc of £119 million, the profit on the sale of Prudential's holding in St. James's Place Capital plc of £99 million, and Prudential's share of the profit on the sale of a Bermudan fund manager held by St. James's Place Capital plc of £21 million. In 2000, profit before tax was also affected by an increase in goodwill amortization of £30 million, mainly due to a full twelve months amortization in respect of the M&G acquisition and a £76 million decrease in short-term fluctuations in investment returns due to market declines.

The decrease in profit before tax in 1999 primarily relates to profit on business disposals of £249 million in 1998, resulting from the sale of Prudential's Australian and New Zealand operations. These businesses were sold in September 1998 for cash consideration of £468 million. In 1999, profit before tax was also affected by a decrease in operating profit before amortization of goodwill and tax of £92 million. This primarily reflects increased losses relating to Egg included within UK operations and a £70 million charge for restructuring UK operations, which more than offset the improvements from US operations and other UK operations. Profit before tax in 1999 was further affected by amortization of goodwill in respect of the acquisition of M&G.

Profit after Tax

Profit after tax in 2000 was £688 million compared with £542 million in 1999 and £880 million in 1998. These movements reflect the movements in profit before tax in those years and effective tax rates of 30% in 2000, compared to 27.7% in 1999 and 22.9% in 1998. The increase in the effective tax rate in 2000 primarily reflects an increase in capital gains and other non-deductible expenses in 2000 compared to 1999, partially offset by non-taxable book gains on sales of subsidiaries and associates. The increase in the effective tax rate in 1999 partially reflects capital gains relating to sales of securities made to finance the acquisition of M&G. The effective tax rate in 1998 was also reduced due to the availability of tax reliefs relating to the profit on disposal of operations in Australia and New Zealand, as well as the availability in 1998 of unused tax losses, which reduced the effective tax rate by 1.6%.

Analysis by Geographic Region

Operating Profit from Continuing Operations before Amortization of Goodwill and Tax

As indicated under "—Basis of Profit" in this section above, Prudential focuses on operating profit before amortization of goodwill and tax by geographic region as the primary measure of current year performance.

UK Operations

The following discussion analyzes Prudential's UK results on the basis of whether or not they are derived from with-profits business. As discussed under "—Basis of Profit" in this section above, shareholders' profit from the with-profit business represents an amount of up to one-ninth of the value of that year's bonus declaration to policyholders. Consequently, current year amounts in respect of premiums, investment return and expenses related to the with-profits business do not directly affect profit to shareholders from the with-profits business in that year. These items do, however, affect bonus declarations over time and, thereby, profit to shareholders over time, and accordingly are discussed below.

Three of Prudential's UK business units—Prudential Financial Services, Prudential Insurance Services and Prudential Intermediary Business—derive their operating profit from a mixture of both with-profits business and other types of business, and accordingly, the results of these business units are discussed under both "—Year Ended December 31, 2000 Compared to Year Ended December 31, 1999—With-Profits Business" and "—Year Ended December 31, 2000 Compared to Year Ended December 31, 1999—Other Businesses" in this section below. Egg and M&G have no with-profits business and are discussed under "—Year Ended December 31, 2000 Compared to Year Ended December 31, 1999—Other Businesses" in this section below.

Prudential's with-profits fund also includes the results of two other businesses, the Scottish Amicable Insurance Fund ("SAIF") and Prudential Annuities Limited. All assets of the SAIF business are solely attributable to former policyholders of Scottish Amicable Life Assurance Society. The SAIF with-profits fund is discussed in more detail under Item 4, "Information on the Company—Business of Prudential—UK Business—Shareholders' Interest in Prudential's Long-term Insurance Business—The SAIF Sub-Fund and Accounts". Prudential Annuities Limited is a wholly-owned subsidiary of the with-profits fund, and, accordingly, profits from this business do not have a direct impact on shareholders' profits and affect shareholders' profits only to the extent that they affect the annual with-profits bonus declaration.

Operating Results

The table below shows the operating profit before amortization of goodwill and tax from the UK with-profits business and from Prudential's other UK businesses.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
With-profits business:			
Gross premiums	**5,956**	7,929	5,744
Reinsurance	**—**	(2)	(9)
Earned premiums	**5,956**	7,927	5,735
Investment income	**3,297**	13,035	9,749
Expenses	**(1,138)**	(1,221)	(1,026)
Taxation within the with-profits fund	**(525)**	(565)	(541)
Claims and withdrawals	**(6,067)**	(5,522)	(4,817)
Change in technical provisions	**(4,941)**	(7,103)	(7,238)
Transfers from/(to) the fund for future appropriations	**3,722**	(6,250)	(1,596)
Shareholders' profit after tax	**304**	301	266
Add-back: tax on shareholders' profit	**132**	129	120
Shareholders' profit before tax from with-profits business	**436**	430	386
Other businesses:			
Personal lines property and casualty operations	**33**	61	39
Unit-linked life and other operations	**32**	24	18
Fund management operations	**125**	87	28
Banking operations	**(155)**	(150)	(77)
Shareholders' operating profit before tax from other operations	**35**	22	8
Total operating profit before amortization of goodwill and tax(1)	**471**	452	394

(1) Due to the long-term nature of Prudential's business, the basis of presentation of operating profit may not be comparable with other UK companies. See note 4 of the notes to Prudential's consolidated financial statements for a description of the basis.

Year Ended December 31, 2000 Compared to Year Ended December 31, 1999

With-Profits Business

Gross premiums for the with-profits business decreased by 25% to £5,956 million in 2000 from £7,929 million in 1999. This decrease mainly reflects lower sales of Prudential's single premium with-profits bond, Prudence Bond and mortgage endowments through Prudential Intermediary Business and lower sales of life and pensions products from Prudential's direct salesforce, reflecting the further reductions in Prudential's salesforce in 2000. For a detailed description of the Prudence Bond, see Item 4, "Information on the Company—Business of Prudential—Prudential's UK Products—Life Insurance Products—Savings Products Investment Bonds".

Investment income represents the return on the assets supporting the UK with-profits fund. Total assets of the UK with-profits fund at December 31, 2000 were £90 billion. At December 31, 2000, 42% of these assets were invested in UK equities, 13% in overseas equities, 31% in fixed maturities, 11% in real estate and 3% in loans and deposits. Total investment income decreased by 75% to £3,297 million in 2000 from £13,035 million in 1999. In 2000, unrealized losses totalled £7,225 million compared to unrealized gains of £4,887 million in 1999. These decreases primarily reflect lower equity returns achieved across the major equity markets in 2000 compared to 1999. In 2000, the UK FTSE All-Share Index decreased by 8% compared with an increase of 24% in 1999.

Expenses were £1,138 million in 2000 compared to £1,221 million in 1999, a decrease of £83 million. The decrease in expenses primarily reflects redundancy and closure provisions associated with restructuring the company salesforce and systems-related expenditures recorded in 1999. For a discussion of this restructuring see "—1999 UK Restructuring" in this section.

Taxation within the with-profits fund in 2000 decreased to £525 million compared to £565 million in 1999. The decrease of 7% in the charge in 2000 primarily reflects an increase in deferred tax credits related to higher unrealized losses on investments supporting the with-profits fund, offset by higher current taxes related to increased realized gains on investments in 2000 compared to 1999. A detailed description of the treatment of taxation within the with-profits fund is included in note 3 of the notes to Prudential's consolidated financial statements.

Claims and withdrawals, which represent payments, including terminal bonuses, to policyholders in respect of maturities, surrenders and deaths, rose £545 million to £6,067 million in 2000 from £5,522 million in 1999, an increase of 10%. The increase primarily reflects an increase in maturities of endowment products as a result of a large book of ten year endowment policies written in 1990 and maturing in 2000.

Change in technical provisions primarily represents the movement in amounts owed to policyholders. This movement reflects the net growth in the in-force book during the year, including amounts credited to policyholders as annual bonuses, and changes in actuarial assumptions. The change in technical provisions was £4,941 million in 2000 compared to £7,103 million in 1999, a decrease of 30%, primarily reflecting the lower level of new business written in 2000. The annual movements in technical provisions also include changes in the pensions misselling provision, an increase in 1998 and 1999 and a decrease in 2000. For a detailed analysis of this provision, see Item 4, "Information on the Company—Business of Prudential—Pensions Misselling". As approved by the UK regulator, the total cost of pensions misselling is included within the transfer to the fund for future appropriations of Prudential Assurance's long-term fund. Payments related to pensions misselling will be met from the surplus assets in the long-term fund and not from amounts intended to fund existing and future bonuses. As described in "—Basis of Profit" above, because shareholders' profit from the with-profits fund represents an amount of up to one-ninth of the value of that year's bonus declaration to policyholders, shareholders' profit of the fund has not been affected by the increase in the provision for pensions misselling. Given the strength of the with-profits fund, Prudential does not believe that pensions misselling costs will have an adverse impact on the levels of bonus paid to policyholders and, therefore, shareholders' profit from the fund. In the unlikely event that this proves not to be the case, Prudential's intention would be that an appropriate contribution to the with-profits fund be made from shareholders' funds with a consequential impact on shareholders' profit.

Transfers from the fund for future appropriations in 2000 of £3,722 million compare to transfers to the fund for future appropriations of £6,250 million in 1999, a net change of £9,972 million. This change in 2000 predominantly reflects an investment return of 3% on the with-profits fund compared to 19.3% in 1999 due to lower equity returns in the UK investment market. The fund for future appropriations represents amounts within the with-profits fund not yet attributed to either policyholders or shareholders. The annual transfer to this fund represents amounts to be credited to policyholders as future terminal bonuses and the related shareholders' profit, and reflects the annual impact of smoothing current period investment returns to policyholders and additions to, or uses of, the surplus in the UK with-profits fund. As a result, the difference between premiums, investment return and claims and expenses in any given year is primarily reflected in the transfer to the fund for future appropriations in that year and not in shareholders' profit before tax. The transfer from the fund for future appropriations represents the shortfall in these amounts.

Shareholders' profit before tax from the with-profits business in 2000 totalled £436 million, compared with £430 million in 1999. Shareholders' profit from the UK with-profits fund in any single period reflects the shareholders' annual portion of an amount up to one-ninth of the value of bonuses declared to policyholders, and consequently is not directly impacted by the current year gross premiums, investment income and expenses described above.

Other Businesses

Personal Lines Property and Casualty Operations

Earned premiums from Prudential's personal lines property and casualty operations increased slightly to £312 million in 2000 from £302 million in 1999. The combined claims and expense ratio increased to 101% in 2000 from 89% in 1999. This increase was primarily attributable to higher claims due to floods in the second half of the year. Operating profit from continuing operations before amortization of goodwill and tax from the personal lines property and casualty operations decreased from £61 million in 1999 to £33 million in 2000.

Unit-linked Life and Other Operations

Prudential's long-term insurance business outside the with-profits fund primarily consists of its unit-linked life operations, under both the Prudential and Scottish Amicable brands, and an accident and health business. Operating profit from continuing operations before amortization of goodwill and tax from unit-linked life and other operations amounted to £32 million in 2000, a £8 million, or 33%, increase over 1999. This increase is due to non-recurrent surplus released on the transfer of the M&G long-term business, net of related transfer costs, offset by investment in the IT infrastructure for stakeholder pensions.

Fund Management Operations

Prudential's fund management operations consist of the M&G retail, internal and fixed-interest institutional fund management business and the Prudential-branded retail fund management business. In 2000, M&G's total operating profit from continuing operations before amortization of goodwill and tax was £125 million, £38 million greater than in 1999. This increase is primarily due to the inclusion of M&G for a full year in 2000 compared with only eight months in 1999 and increased fees from the life fund as a result of outperformance by the investments supporting the life fund against benchmarks.

The Prudential-branded retail fund management business sold through Prudential Financial Services' company salesforce recorded nil profit in 2000 compared with a loss of £12 million in 1999. This improvement was due to a decrease in new business volume generated by Prudential Financial Services, because of a reduction in headcount, resulting in lower acquisition costs.

Egg

Egg was launched in October 1998 and is currently reporting losses due to the high level of costs associated with building the business, including information technology, marketing and customer acquisition costs.

Net interest income from banking products in 2000 was £80 million, compared to £24 million in 1999. This increase reflects a reduction in the interest rate paid on customer deposits as well as a reduction in total customer deposits to £7,128 million at December 31, 2000 from £8,157 million at December 31, 1999.

Operating and administrative expenses for Egg totalled £235 million in 2000, an increase of £61 million over 1999. This increase in expenses was primarily due to an increase in brand, marketing and development costs of £35 million and an increase in the provision for doubtful debts of £28 million. These costs increased as a result of growth in the Egg business.

Egg's operating loss before taxes amounted to £155 million for the year ended December 31, 2000 compared with £150 million in 1999.

Year Ended December 31, 1999 Compared to Year Ended December 31, 1998

With-Profits Business

Gross premiums for the with-profits business rose by 38% to £7,929 million in 1999 from £5,744 million in 1998. This increase mainly reflects strong sales of pension annuity products, which were up 108% to £2,221 million, and increased sales of the Prudence Bond, which were up 52% in 1999 to £1,875 million, due to the increased appeal of this product in the prevailing low interest rate environment. The increase in pension annuity sales primarily reflects higher sales of bulk annuities, a market on which Prudential increased its focus in 1999.

Investment income represents the return on the assets supporting the UK with-profits fund. Total assets of the UK with-profits fund at December 31, 1999 were £90 billion. At December 31, 1999, 50% of these assets were invested in UK equities, 13% in overseas equities, 24% in fixed maturities, 10% in real estate and 3% in loans and deposits. Total investment income increased by 34% to £13,035 million in 1999 from £9,749 million in 1998. This increase reflects the stronger equity returns achieved across the major equity markets compared to 1998. In 1999, the UK FTSE All-Share Index increased by 24% compared with 11% in 1998.

Expenses were £1,221 million in 1999 compared with £1,026 million in 1998, an increase of £195 million, or 19%. The increase in expenses primarily reflects redundancy and closure provisions associated with restructuring the company salesforce and systems-related expenditure. For a discussion of this restructuring see Item 4, "Information on the Company—Business of Prudential—UK Business—UK Restructurings".

Taxation within the with-profits fund in 1999 was £565 million compared to £541 million in 1998, an increase of 4%. The increase in the charge in 1999 primarily reflects higher realized gains on the disposal of investments, partly offset by a regulatory change in the treatment of tax credits on dividend income.

Claims and withdrawals rose £705 million to £5,522 million in 1999 from £4,817 million in 1998, an increase of 15%. The increase primarily reflects an increase in death claims and an increase in maturities as a result of past patterns of writing business.

The change in technical provisions was £7,103 million in 1999 compared to £7,238 million in 1998, a decrease of 2%, mainly reflecting the impact of an increase in the interest rate used to calculate pension annuities liabilities and the impact of a single large surrender by an institutional pension fund, partly offset by increased technical provisions in respect of increased new business written by Prudential Intermediary Business. Movements in technical provisions also include increases in the pensions misselling provision, roughly the same in 1999 and 1998.

Transfers to the fund for future appropriations in 1999 of £6,250 million compares to a transfer of £1,596 million in 1998, an increase of £4,654 million, or 292%. This increase in 1999 predominantly reflects an investment return of 19.3% on the with-profits fund compared to 12.6% in 1998.

Shareholders' profit before tax from the with-profits business in 1999 totalled £430 million, compared with £386 million in 1998, an increase of 11%. The £44 million increase in profit reflects the impact of increased funds under management, mainly as a result of strong investment returns, increasing the shareholders' share of bonus payments by £27 million. In addition, the impact of increased terminal bonuses as more policies matured was to increase the shareholders' share of bonus payments by £43 million. This increase was partially offset by the impact of further reductions in annual bonus rates from 1998 to 1999, reducing total bonus payments and, consequently, the shareholders' share of these bonuses, by £22 million. In line with the rest of the UK life insurance industry, Prudential has and will continue to gradually reduce annual bonus rates to reflect its expectations of lower interest rates in the future and, consequently, lower average investment returns.

Other Businesses

Personal Lines Property and Casualty Operations

Earned premiums from personal lines property and casualty operations increased to £302 million in 1999 from £293 million in 1998, an increase of 3%. The combined claims and expense ratio improved from 96% in 1998 to 89% in 1999, which improved the operating profit by £11 million. The improvement in the combined ratio mainly reflects the impact of two severe weather incidents on profits in 1998. Investment return improved by £2 million due to the increased cash flows resulting from the higher premiums and better claims experience in 1999. Operating profit from continuing operations before amortization of goodwill and tax from personal lines property and casualty operations increased from £39 million in 1998 to £61 million in 1999, £58 million attributable to household insurance and £3 million to motor insurance.

Unit-linked Life and Other Operations

Operating profit from continuing operations before amortization of goodwill and tax from unit-linked life and other operations amounted to £24 million in 1999, a £6 million, or 33%, increase over 1998. This increase primarily reflects the growth of the relatively new Scottish Amicable book of business and a return to more normal levels of profitability following an exceptional level of investment in systems technology in 1998 of £5 million.

Fund Management Operations

In 1999, M&G's operating profit from continuing operations before amortization of goodwill and tax was £87 million, an increase of £59 million, or 211%, from 1998. The improved result is primarily due to the first-time inclusion of the M&G business, which contributed £56 million to operating profit from continuing operations before amortization of goodwill and tax for the eight months since acquisition.

Included within the above result is the Prudential-branded retail fund management business sold through Prudential Financial Services' company salesforce. This business recorded a loss of £12 million in 1999 and of £15 million in 1998. These losses are a consequence of the low margins on this type of product and small customer premium levels, which did not support the cost of this type of distribution. The improved result in 1999 reflects lower sales volumes.

Egg

In 1999, Egg earned net interest income from banking products of £24 million compared with £11 million in 1998. The increase in net interest income of 118% in 1999 is due to the increased interest income from capital injections during the year by Prudential plc and from the growth of the mortgage and loan book from £675 million at December 31, 1998 to £2,057 million at December 31, 1999. This increase was partly offset by the cost of the interest payable on Egg deposits, which grew from £2,188 million at December 31, 1998 to £8,157 million at December 31, 1999.

In 1999, operating and administrative expenses for Egg were £174 million compared to £88 million in 1998. The increased costs are due to the growth of the business in 1999 and resulted in losses of £150 million in 1999, up from £77 million in 1998. The £73 million increase in losses reflects the higher operating expenses in 1999, the cost of the competitive market rates on the Egg deposit accounts, the cost of the launch of the Egg credit card and development of future product launches.

US Operations

Prudential's US operations comprise its US insurance company, Jackson National Life, which includes Jackson Federal Bank, PPM America, its US internal and institutional investment manager, and its US broker-dealer operations, National Planning Holdings.

The profit on Jackson National Life's business predominantly arises from spread income from interest-sensitive products, such as fixed annuities and stable value products. For the purposes of UK reporting, deposits into these products are recorded as premiums, withdrawals and surrenders are included in benefits and claims and the resulting net movement is recorded under other reserve movements within benefits and claims. Benefits and claims also includes interest credited to policyholders in respect of deposit products and fees charged on these policies. While the disclosure of these items differs between UK GAAP and US GAAP, there is no net impact on operating profit. The UK GAAP modified statutory basis result for Jackson National Life is based on Jackson National Life's US GAAP results with an adjustment for a different treatment of realized investment gains.

Operating Results

The following table and accompanying commentary show operating profit before tax for the periods indicated.

	Year Ended December 31,		
	2000	**1999**	**1998**(1)
	(In £ Millions)		
Gross premiums	**5,223**	4,449	3,237
Reinsurance	**(70)**	(61)	(53)
Earned premiums	**5,153**	4,388	3,184
Investment income and realized gains	**1,744**	1,617	1,543
Adjustment from actual to averaged investment gains	**52**	15	(2)
Investment income based on long-term investment returns	**1,796**	1,632	1,541
Benefits and claims	**(6,171)**	(5,368)	(4,111)
Variable annuity fees	**50**	26	13
Other income and expenses — net	**(369)**	(221)	(216)
Net operating and investment expenses	**(319)**	(195)	(203)
Jackson National Life Total	**459**	457	411
National Planning Holdings	**—**	(4)	—
PPM America	**7**	(2)	—
US operations operating profit before tax	**466**	451	411

(1) The 1998 results for PPM America and National Planning Holdings, the holding company of Prudential's two broker-dealer operations, National Planning Corporation and SII Investments, Inc., were not included in the results for the US operations and have not been restated because they were classified as part of the UK and central group operations. In 1998, PPM America and National Planning Holdings both had losses of £1 million.

The following table shows a reconciliation between operating profit before tax on a UK GAAP and US GAAP basis for Prudential's US operations.

	Year Ended December 31,		
	2000	**1999**	**1998**
		(In £ Millions)	
Operating profit before tax on a UK GAAP basis	**466**	451	411
Adjustment from averaged to actual investment gains	**(52)**	(15)	2
Amortization of goodwill	**(1)**	—	—
Operating profit before tax on a US GAAP basis	**413**	436	413

The exchange rate between the US dollar and pounds sterling has remained fairly constant during all three years and consequently exchange rate fluctuations have had minimal impact on the results of US operations. The following year-on-year analysis focuses on the results of Jackson National Life only.

Year Ended December 31, 2000 Compared to Year Ended December 31, 1999

Gross Premiums

In 2000, gross premiums increased by 17% to £5,223 million compared to £4,449 million in 1999, reflecting increased volumes of fixed and variable annuity products.

The increase in fixed annuities reflects a strong recovery in sales in 2000 principally due to higher interest rates in the United States. Sales of fixed annuities (including immediate and equity-indexed) rose 16% in 2000 compared with 1999 to £1,464 million. Variable annuity sales of £1,709 million were 44% higher than in 1999, reflecting new product launches, product promotions and the continuing strength of the US equity market. Sales of stable value products rose by 2% in 2000 to £1,656 million and included approximately £1.3 billion of funding agreements sourced from overseas markets, which represented a new market for Jackson National Life's stable value products in 1999.

The increase in variable annuity sales has been assisted by the continued development of Jackson National Life's own broker-dealer distribution network, including the acquisition of IFC Holdings Inc. in 2000, the development of SII Investments, Inc., a company acquired in 1998, and by the continued development of National Planning Corporation, which was formed during 1998.

Investment Income

Investment income of £1,796 million in 2000 represented a 10% increase over 1999. Included in the balances for 2000 are average realized investment gains of £16 million compared to £32 million in 1999. Investment income, net of realized gains and certain investment and income expenses, was £1,632 million in 2000 and £1,485 million in 1999. These amounts reflect investment yields of 7.56% on average invested assets of £22,388 million in 2000 compared to investment yields of 7.67% on average invested assets of £19,835 million in 1999. The 13% growth in average invested assets is primarily attributable to investment income and net growth in stable value and equity-indexed annuity products. The decrease in investment yield is primarily attributable to the growth in lower yielding adjustable rate fixed income securities in the stable value portfolio, which accounts for a larger part of the total portfolio in 2000.

Benefits and Claims

Benefits and claims increased by 15% to £6,171 million in 2000 over 1999. This movement principally reflects a 36% increase in death benefits, maturities and surrenders of deposit products from £3,581 million in 1999 to £4,866 million in 2000 offset by a decrease of £452 in the change in technical provisions in 2000. The increase in death benefits, maturities and surrenders of deposit products is due to the maturing of the fixed annuity book, with an increasing amount of this business either passing the surrender penalty fee period or moving into a lower surrender penalty charge bracket combined with the competitive conditions in the annuity market and the prevailing interest rate environment.

Interest credited on deposit liabilities of £1,153 million in 2000 represents average interest credited rates of 5.45% on average deposit liabilities of £21,136 million and compares to interest credited of £1,030 million in 1999 representing average interest credited rates of 5.47% on average deposit liabilities of £18,840 million. The 12% growth in average deposit liabilities is primarily due to an increase in average stable value deposits.

Net Operating and Investment Expenses

Net operating and investment expenses of £319 million in 2000 were 64% higher than net operating expenses of £195 million in 1999. This increase was primarily due to a £94 million increase in investment expenses due to higher average balances of trust instruments supported by funding agreements. In 2000, the average liability was £1,539 million compared to an average liability of £433 million in 1999.

Operating Profit before Tax

In 2000, operating profit before tax from Jackson National Life was £459 million, which is consistent with 1999 operating profit before tax of £457 million.

Year Ended December 31, 1999 Compared to Year Ended December 31, 1998

Gross Premiums

In 1999, gross premiums increased by 37% to £4,449 million, reflecting increased volumes of fixed and variable annuity products and stable value products, offset by lower volumes of regular premium life business.

The increase in fixed annuities reflects a strong recovery in sales in the second half of 1999 principally due to higher interest rates in the United States. Variable annuity sales of £1,187 million were more than double sales in 1998, reflecting new product launches, product promotions and the continuing strength of the US equity market. Sales of equity-indexed annuities rose 52% in 1999 compared with 1998 to £431 million. Sales of stable value products rose by 20% in 1999 to £1,618 million and included more than $1 billion of funding agreements sourced from overseas markets, which represented a new market for Jackson National Life's stable value products in 1999.

The increase in variable annuity sales has been assisted by the continued development of Jackson National Life's own broker-dealer distribution network, including the development of SII Investments, Inc., a company acquired in 1998, and by the continued development of National Planning Corporation, which was formed during 1998.

Investment Income

Investment income of £1,632 million in 1999 represented a 6% increase over 1998. Included in the 1999 balance are average realized investment gains of £32 million compared to £25 million in 1998. Investment income, net of realized gains and certain investment and income expenses, was £1,485 million in 1999 and £1,422 million in 1998. These amounts reflect investment yields of 7.67% on average invested assets of £19,835 million in 1999 compared to investment yields of 8.00% on average invested assets of £18,253 million in 1998. The 9% growth in average invested assets is primarily attributable to investment income and net growth in stable value liabilities and equity-indexed annuity products. The decrease in investment yield is primarily attributable to the growth in lower yielding adjustable rate fixed income securities in the stable value portfolio, which accounts for a larger part of the total portfolio in 1999, and the lower interest rate environment in the United States.

Benefits and Claims

Benefits and claims increased by 31% to £5,368 million in 1999. This movement principally reflects a 44% increase in death benefits, maturities and surrenders of deposit products from £2,494 million to £3,581 million. This reflects the maturing of the fixed annuity book, with an increasing amount of this business either passing the surrender penalty fee period or moving into a lower surrender penalty charge bracket. In addition, as a result of the low interest-rate environment, customers continued to switch to equity-based rather than interest-based products.

Interest credited on deposit liabilities of £1,030 million in 1999 represents average interest credited rates of 5.47% on average deposit liabilities of £18,840 million and compares to interest credited of £1,004 million in 1998 on average interest credited rates of 5.78% with average deposit liabilities of £17,382 million. The 8% growth in average deposit liabilities is primarily due to a 39% increase in average stable value deposits. The decline in the average interest rate credited reflects actions by management to lower crediting rates in response to the lower yields available from the investment portfolio.

Net Operating and Investment Expenses

Net operating and investment expenses fell by 4% from £203 million in 1998 to £195 million in 1999. Increased amortization of acquisition costs and general expenses, up £22 million, were offset by increased variable fee income of £26 million, up £13 million on 1998 and a £17 million benefit in respect of cumulative changes to guarantee fund assessments. The near doubling of variable annuity fee income results from increased product sales, strong equity markets and the associated additional income arising from the growth in assets under management.

Operating Profit before Tax

In 1999, operating profit before tax from Jackson National Life was £457 million, an increase of £46 million, or 11%, over 1998. This increase reflects higher spread income resulting from the growth in deposit liabilities in 1999, specifically from sales of equity-oriented products and stable value products, increased variable annuity fees and the one-off impact of a change in accounting policy for guaranteed fund assessments of £17 million.

Asian Operations

The relatively recent growth of Prudential's Asian operations and the deferred emergence of profits from long-term insurance business means that these businesses currently make only a small contribution to group operating profit before amortization of goodwill and tax. Operating profit before amortization of goodwill and tax from Prudential's Asian operations in 2000 was £22 million, an increase of £7 million, or 47%, over 1999. This movement reflects increased profits from established operations and fund management operations, offsetting losses from new and emerging operations.

In 1999, operating profit before amortization of goodwill and tax from Prudential's Asian operations increased by £2 million, or 15%, to £15 million. This reflects increased profits from Prudential's established operations, up £3 million to £31 million due to favorable claims experience, reduced losses from Prudential's developing operations, down £1 million to £4 million, and increased development costs, up £2 million to £12 million.

Prudential's Asian operations are described in detail under Item 4, "Information on the Company—Business of Prudential—Asian Business—Development of Prudential's Asian Business".

European Operations

Operating profit before tax from Prudential's European operations represents profits from Scottish Amicable Life International, an Irish company, which markets unit-linked products into Germany and the United Kingdom and, since June 2000, profits from sales through Prudential's joint venture with Signal Iduna, one of Germany's largest life insurance companies. Operating loss before tax from Prudential's European operations was £10 million in 2000 compared to operating profits before tax of £6 million in 1999 and £4 million in 1998. The decrease in 2000 substantially reflects development expenses incurred in the period of £18 million, which offset the operating profit from long term business. The increase in operating profit before tax in 1999 represents growth in new business volumes.

Group Activities

Operating profit from group activities represents the longer term investment return on centrally retained shareholder capital and funds, interest expense on group borrowings and central corporate expenditure.

Operating loss before amortization of goodwill and tax for group activities increased to £109 million in 2000 from £78 million in 1999. This increase primarily reflects a £29 million increase in net investment expense to £67 million for 2000 compared to 1999, reflecting the full year funding cost related to the acquisition of M&G and additional funding for Egg in 2000 compared to 1999.

In 1999, operating profit before amortization of goodwill and tax for group activities decreased from a profit of £38 million in 1998 to a loss of £78 million. This decrease reflects a £122 million increase in net investment expenses to £38 million. This increase primarily reflects the impact of funding the M&G acquisition, continued investment in Egg and the impact of lower interest rates in 1999. These movements were partly offset by lower corporate expenditure in 1999, reflecting exceptional expenses in 1998 relating to the reorganization of Prudential's UK operations.

1999 UK Restructuring

In 1999, Prudential carried out a review of its UK operations and its board approved plans to restructure certain of its operations. In 1999, Prudential accrued £148 million in respect of the costs to be incurred, £78 million of which was borne by Prudential Assurance's long-term fund and £70 million was charged directly to shareholders. Prudential has allocated these costs between the long-term fund and shareholder businesses on the basis of the activity to which the costs relate. The restructuring costs borne by the long-term fund were predominantly associated with the cost of downsizing the company salesforce, whose activities primarily comprised selling the products of the long-term fund. The restructuring costs borne by shareholders represented the shareholders' share of the salesforce restructuring costs, as the company salesforce also sold certain products not supported by the long-term fund, and the integration costs of combining Prudential Portfolio Managers and M&G following the acquisition of M&G.

For US GAAP purposes, in 1999 Prudential expensed £120 million of restructuring costs, primarily comprising £56 million of termination benefits and salary costs relating to the reduction of the salesforce and associated staff and £53 million of costs relating to the closures of the existing retail branch network and other administrative buildings. These costs also included £11 million of other costs, such as systems-related costs. Additional restructuring costs recorded under UK GAAP in 1999 were recognized for US GAAP purposes in 2000. For a detailed discussion of this UK restructuring and a subsequent restructuring announced in February 2001, see Item 4, "Information on the Company— Business of Prudential—UK Business—UK Restructurings".

New UK Accounting Pronouncements

Several new accounting standards were issued during 1999 and 2000 that are pertinent to Prudential's UK GAAP consolidated financial statements. These are discussed in detail in note 3 of the notes to Prudential's consolidated financial statements.

US GAAP Analysis

Prudential's consolidated financial statements have been prepared in accordance with UK GAAP, which differs in certain material respects from US GAAP. A summary of these differences and their impact on Prudential's consolidated profit and loss accounts for 2000, 1999 and 1998 and shareholders' funds for 2000 and 1999, along with condensed US GAAP financial statements, is included in notes 33 and 34 to Prudential's consolidated financial statements.

The most significant difference in the results of operations between UK GAAP and US GAAP is the treatment of the with-profits business.

Under UK GAAP, profit attributable to shareholders in respect of Prudential's with-profits business reflects up to one-ninth of the value of bonuses paid to policyholders. To the extent the annual earnings of the with-profits fund exceed policyholder bonuses and related shareholder distributions, this excess is added to the fund for future appropriations by a charge to the profit and loss account. However, to the extent the annual earnings of the with-profits fund do not exceed policyholder bonuses and related shareholder distributions, this shortfall is transferred from the fund for future appropriations.

Under US GAAP, the impact of pre-bonus operating results within the with-profits fund is reflected in net income in the period in which it occurs. However, 90% of these results are allocated to with-profits policyholders by a charge to net income. The residual 10% interest is allocated to shareholders.

This treatment of Prudential's with-profits fund under US GAAP causes profits attributable to shareholders to be strongly influenced by annual investment returns. Annual investment returns include unrealized gains and losses and, accordingly, these returns and shareholders' profits will be subject to considerable volatility in the US GAAP figures.

Other material differences between UK GAAP and US GAAP results include the method of deferral and amortization of acquisition costs, the accounting for certain investments, revenue and claims recognition on investment type contracts, the measurement of and changes in policyholder benefit and dividend liabilities, and the accounting for deferred income tax.

Changes in Net Income on Application of US GAAP

The following table analyzes the adjustments to consolidated profit and loss in accordance with UK GAAP on application of US GAAP for the operations and periods indicated.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
Consolidated profit and loss in accordance with UK GAAP	**688**	542	880
US GAAP adjustments:			
With-profits fund	**(182)**	431	57
Other operations	**(4)**	(85)	(136)
	(186)	346	(79)
Net income in accordance with US GAAP	**502**	888	801

On a US GAAP basis, consolidated net income totalled £502 million in 2000, £888 million in 1999 and £801 million in 1998. Consolidated net income on a US GAAP basis for 2000 was £186 million less than consolidated profit under UK GAAP, for 1999 was £346 million more than consolidated profit under UK GAAP, and for 1998 was less than UK GAAP consolidated profit for the year by £79 million. The US GAAP adjustments to UK GAAP consolidated profit and loss in respect of the with-profits fund totalled a reduction of £182 million in 2000, an increase of £431 million in 1999, and an increase of £57 million in 1998. The table below analyzes the shareholders' 10% interest in the adjustments to the with-profits fund's results, as reflected above.

	Year Ended December 31,		
	2000	**1999**	**1998**
	(In £ Millions)		
US GAAP adjustments:			
Land and buildings	**(42)**	(61)	(37)
Investment securities	**4**	71	(87)
Revenue and expense recognition	**(16)**	(21)	(8)
Deferred acquisition costs	**26**	10	5
Policy liabilities	**107**	5	62
Movement in UK basis excess assets over liabilities	**(341)**	510	138
Deferred income tax	**54**	(52)	(19)
Other	**12**	5	—
Deferred tax effect of the above adjustments	**14**	(36)	3
	(182)	431	57

The decrease in the US GAAP adjustment for movement in the UK basis excess of assets over liabilities from £510 million in 1999 to a negative amount of £341 million in 2000 primarily reflects the lower investment returns in 2000 than in 1999.

The increase in the US GAAP adjustment for movement in the UK basis excess of assets over liabilities from £138 million in 1998 to £510 million in 1999 reflects the higher investment returns in 1999 than in 1998.

The main effects on the accounting for the income and expenditure of the with-profits fund on a US GAAP basis are:

- exclusion of the unrealized appreciation for land and buildings and inclusion of depreciation on buildings;
- exclusion of the unrealized appreciation/depreciation for securities classified as available for sale;
- adjustments to income recognition, deferred acquisition costs and insurance liabilities; and
- full provision of deferred income tax on unrealized investment appreciation recognized.

The following table analyzes the US GAAP adjustments for other operations.

	Year Ended December 31, 2000	1999	1998
	(In £ Millions)		
Business acquisitions and investments in associates	**(21)**	(33)	(34)
Revenue and expense recognition	**(111)**	(24)	(40)
Deferred acquisition costs	**79**	48	44
Policy liabilities	**45**	(3)	(4)
Pension plans	**21**	13	27
Deferred income tax	**(40)**	(78)	(18)
Business disposals	**—**	—	(78)
Other	**(11)**	13	(3)
Deferred tax effect of the above adjustments	**34**	(21)	(30)
	(4)	(85)	(136)

The US GAAP adjustment for business acquisitions and investments in associates primarily reflects the amortization of goodwill on acquisitions made prior to 1998. Under UK GAAP the goodwill had been charged to equity in the year of acquisition. The US GAAP adjustment to profit on business disposals of £78 million in 1998 reflects the foreign exchange translation of the net assets of Prudential's Australian operation, which was sold in 1998. The changes in the provision for deferred income tax primarily reflect deferred income tax on the unrealized appreciation of shareholder owned assets less the reinstatement from UK GAAP of deferred income tax assets for Jackson National Life.

Changes in Shareholders' Funds on Application of US GAAP

The following table shows the adjustments in shareholders' funds from UK GAAP to consolidated shareholders' equity under US GAAP for the operations and periods indicated.

	At December 31, 2000	1999
	(In £ Millions)	
Shareholders' funds in accordance with UK GAAP	**4,020**	3,424
US GAAP adjustments:		
With-profits fund	**2,039**	2,217
Other operations	**396**	405
	2,435	2,622
Shareholders' equity in accordance with US GAAP	**6,455**	6,046

Shareholders' equity was greater under US GAAP than UK GAAP in 2000 and 1999, respectively, by £2,435 million and £2,622 million. The greater equity in respect of with-profits business was £2,039 million at December 31, 2000 and £2,217 million at December 31, 1999. This difference predominantly reflects the attribution to shareholders of a 10% interest in the excess of assets over liabilities held within the fund.

The following table analyzes the shareholders' 10% interests in adjustments to the with-profits fund as reflected above.

	At December 31,	
	2000	**1999**
	(In £ Millions)	
US GAAP adjustments:		
Land and buildings	**(401)**	(361)
Revenue and expense recognition	**(102)**	(86)
Deferred acquisition costs	**96**	68
Policy liabilities	**616**	507
UK basis excess of assets over liabilities	**2,019**	2,356
Deferred income tax	**(240)**	(294)
Other	**89**	79
Deferred tax effect of the above adjustments	**(38)**	(52)
	2,039	2,217

Under UK GAAP, the excess of assets over liabilities within the with-profits fund is not allocated between policyholders and shareholders. Under US GAAP, shareholders are credited with a 10% interest in the adjusted excess of assets over liabilities.

The main effects on the accounting for the assets and liabilities in the with-profits fund are:

- writedown of land and buildings values from market value to depreciated historic cost;
- adjustments to revenue and expense recognition, deferred acquisition costs and insurance liabilities; and
- full provision of deferred income tax on unrealized investment appreciation recognized.

The following table analyzes US GAAP adjustments to shareholders' interests in other operations.

	At December 31,	
	2000	**1999**
	(In £ Millions)	
Business acquisitions	**355**	457
Investment securities	**(627)**	(651)
Revenue and expense recognition	**(396)**	(279)
Deferred acquisition costs	**586**	502
Policy liabilities	**15**	(36)
Pension plans	**178**	156
Deferred income tax	**(107)**	(83)
Shareholder dividend liability	**322**	299
Other	**(19)**	(26)
Deferred income tax of the above adjustments	**89**	66
	396	405

For other operations, shareholders' equity on a US GAAP basis exceeded that on a UK GAAP basis by £396 million in 2000 and £405 million in 1999.

The principal reasons for the increases in consolidated shareholders' equity under US GAAP compared to consolidated shareholders' funds under UK GAAP are:

- capitalization of goodwill,

- elimination of the UK basis accrual for the final dividend. The final dividend is declared each February in respect of the preceding year, and
- inclusion of Jackson National Life's fixed income security portfolio on an available for sale basis with related shadow deferred acquisition cost adjustments. Under UK GAAP the securities are carried on an amortized cost basis.

New US Accounting Pronouncements

In June 1999, the Financial Accounting Standards Board ("FASB") delayed the effective date of Statement of Financial Accounting Standard ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities." The delay in implementation was effected through the issuance of SFAS No. 137, which delays the implementation of SFAS No. 133 to fiscal years beginning after June 15, 2000.

In June 2000, the FASB issued SFAS No. 138, which amends SFAS 133. Prudential will adopt the provisions of SFAS No. 133 and SFAS No. 138 as of January 1, 2001. The impact of these statements is dependent upon Prudential's derivative positions and market conditions existing at the date of adoption. Upon adoption, a net transitional adjustment based on the aggregate fair value of Prudential's derivative instruments as of December 31, 2000 will be recorded as a cumulative effect of a change in accounting principle. Currently, Prudential is continuing its analysis of the impact of SFAS No. 133 and SFAS No. 138 on its consolidated balance sheets and statements of income on a US GAAP basis.

The impact of SFAS No. 133 and SFAS No. 138 has yet to be fully analyzed. The estimated impact as described below is therefore only broadly indicative.

It is likely that the most significant impact on net income will arise in respect of the results of Jackson National Life. Net income for Jackson National Life in 2001 and future years is likely to reflect the significantly increased volatility owing to fair value fluctuations on certain derivative instruments, particularly interest rate swaps, that are regularly used to manage risks associated with movements in interest rates. The fair value of derivative contracts will now be reflected in income while the largely offsetting change in fair value of Jackson National Life's investments will remain as an adjustment to equity in the balance sheet as unrealized gains and losses.

This accounting treatment will also subsist for the investments and derivative contracts of Prudential Annuities Limited. However, in this instance, as the company is owned by the PAC with-profit fund the impact will be ameliorated by a 90% offsetting adjustment to the undistributed policyholder allocation in the income statement.

For with-profit operations other than Prudential Annuities, market value movements in investments including most derivatives used for efficient portfolio management are already accounted for within the income statement. Subject to further consideration as to the possibility of embedded derivatives within insurance contracts, the impact of SFAS No. 133 and SFAS No. 138 is not expected to be material for the Group's with-profits funds. The impact of the two standards on the results of the banking operations is not expected to be significant to the results of the Group.

In September 2000, the FASB issued SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which supersedes SFAS No. 125 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 140 changes the circumstances under which a collateralized party must recognize certain financial assets in which it has security interest. Currently, Prudential is continuing its analysis of the effect of adoption of SFAS No. 140 on its consolidated balance sheets and statements of income on a US GAAP basis. However, the Group does not expect the adoption of SFAS No. 140 to have a material impact on its financial position.

Liquidity And Capital Resources

Prudential operates a central treasury function, which has overall responsibility for managing the group's capital funding as well as its cash and liquidity positions. Prudential arranges the financing of each of its subsidiaries, except Egg, primarily by raising external finance either at the Prudential parent company level, through finance subsidiaries whose obligations the parent company guarantees and at the operating company level. Egg has its own treasury function to manage its cash and liquidity positions.

Liquidity Requirements

The parent company's principal cash requirements are the payment of dividends to shareholders, the servicing of debt, the payment of group activity expenses and the acquisition of and investment in businesses.

Total dividends proposed by the Board for 2000, 1999 and 1998 were 24.5p, 23.0p and 21.0p per share, respectively. The final dividend in respect of the year ended December 31, 2000 of £322 million was paid on May 30, 2001. Under UK company law, dividends can only be paid if a company has distributable reserves sufficient to cover the dividend. In addition, under UK insurance legislation, a company cannot pay a dividend if any of its UK insurance subsidiaries is insolvent on a regulatory valuation basis. At December 31, 2000, Prudential plc and all of its UK insurance subsidiaries were solvent. Prudential does not believe these restrictions will limit its future ability to pay dividends to shareholders.

Debt service costs paid in 2000 were £119 million compared to £82 million for 1999 and £85 million in 1998. This increase in 2000 reflects additional funding costs following the acquisition of M&G. £114 million of the floating rate guaranteed unsecured loan notes due to mature in 2004 was repaid in 2000. Of total consolidated borrowings of £1,981 million at December 31, 2000, the parent company and finance subsidiaries had borrowings of £1,568 million outstanding. £20 million represented a bank overdraft repayable on demand, £176 million represented short-term commercial paper with a maturity of less than one year, £201 million represented US$300 million of guaranteed bonds due to mature in 2001 and £54 million represented the remaining balance of floating rate guaranteed unsecured loan notes due to mature in 2004. US$250 million of bonds are due to mature in 2005, and the remaining outstanding amounts are due to mature in more than five years.

In 2000, group activity expenses totalled £59 million compared to £52 million in 1999 and £54 million in 1998. In future periods, the parent company will fund approximately £22 million of restructuring expenses accrued at December 31, 2000.

During 2000, Prudential plc made capital contributions to Egg of £80 million. Total capital contributions made to Egg during 1999 were £370 million, of which £262 million was to maintain Egg's statutory capital requirements. Capital contributions to Egg in 1998 were £145 million. Due to the initial public offering of a minority stake in Egg in June 2000, no further contributions are anticipated from the parent company for the two years following the date of the offering.

As described in Item 4, "Information on the Company—Business of Prudential—UK Business—Compliance—Pensions Misselling", the total costs associated with the review of pensions misselling in the United Kingdom will be met from the surplus assets of Prudential Assurance's long-term fund. Management believes that charging the pensions misselling provision to the long-term fund will not have an adverse impact on the levels of bonus paid to policyholders or their reasonable expectations. In the unlikely event this proves not to be the case, an appropriate contribution to the long-term fund would be made from shareholders' funds. In view of the uncertainty, it is not practicable to estimate the level of this potential contribution.

Acquisition of Businesses

In February 2001 Prudential acquired Orico Life Insurance Co. of Japan for £133 million (¥23 billion). During 2000, Prudential invested in several new businesses. Prudential acquired an 89% interest in Core Pacific Securities Investment Trust Enterprise, a Taiwanese mutual fund provider, and increased its holding in its Taiwanese life insurance operation at a total cost of £73 million (NT$3.6 billion). Prudential's US subsidiary, Jackson National Life, acquired three branches of Fidelity Federal Bank for cash consideration of £7 million (US$10 million), Highland Bancorp for cash consideration of £75 million (US$110 million) and IFC Holdings for cash consideration of £28 million (US$42 million).

Prudential also invested in several new businesses in 1999. M&G was acquired for a cash consideration of £1,943 million and Chinfon Life Insurance Company of Taiwan was acquired for £68 million. During 1998, Prudential acquired a controlling interest in its Malaysian operation at a cost of £123 million.

Other Capital Expenditures

Prudential spent £2 million, £20 million and £5 million in 2000, 1999 and 1998, respectively, to refurbish several of its office buildings. The expenditure in 1999 related primarily to fixtures and fittings for the new Prudential head office.

Liquidity Sources

The parent company and finance subsidiaries held cash and short-term investments of £38 million and £78 million at December 31, 2000 and December 31, 1999, respectively. The principal sources of cash are dividends and loans received from operating subsidiaries, proceeds from borrowings, the sale of its businesses and recourse to the equity markets.

Dividends and Loans Received from Subsidiaries

Under UK company law, dividends can only be paid if a company has distributable reserves sufficient to cover the dividend. In Prudential Assurance, Prudential's largest operating subsidiary, distributable reserves are created mainly by the statutory long-term business profit transfer to shareholders that occurs upon the declaration of bonuses to policyholders of with-profit products and profits from Prudential's personal lines property and casualty insurance business. Prudential's insurance, banking and fund management subsidiaries' ability to pay dividends and loans to the parent company is restricted by various laws and regulations. Jackson National Life is subject to state laws that limit the dividends payable to the parent company. Dividends in excess of these limitations generally require approval of the state insurance commissioner. The table below shows the dividends and loans received by the parent company from the principal regulated operating subsidiaries during the year ended December 31, 2000. In addition, the table shows the maximum remaining dividend that could have been paid out of distributable reserves at December 31, 2000 without prior regulatory approval, although the amounts shown do not take into consideration any profit that may be generated from operations after December 31, 2000.

	Dividends and loans received in 2000	Maximum remaining dividend that could have been paid without prior regulatory approval as at December 31, 2000
	(In £ Millions)	
Prudential Assurance	**355**	**161**
Jackson National Life	**—**	**107**
Egg	**—**	**—**
M&G	**174**	**—**
Asian businesses	**18**	**73**

With the exception of Egg, each of Prudential's main operating subsidiaries generate profits sufficient to pay dividends to the parent. The amount of dividends paid by the operating subsidiaries is determined after considering the development, growth and investment requirements of the operating businesses. Prudential does not believe that the legal and regulatory restrictions constitute a material limitation on the ability of subsidiaries to meet their obligations or pay dividends to the parent company.

The parent company received total dividends and loans from subsidiaries of £593 million in 2000 compared with £655 million in 1999 and £285 million in 1998. In 1999 dividends received by the parent company included special non-recurring dividends of £190 million from M&G and £120 million from Prudential Assurance, resulting from a review of the ongoing capital requirements of all companies within the Prudential group.

In addition to the above dividends, the parent company received £39 million, £35 million and £33 million in interest on intercompany loans from Jackson National Life in 2000, 1999 and 1998, respectively.

Borrowings and Credit Facilities

Of the total consolidated borrowings of £1,981 million at December 31, 2000, the parent company and finance subsidiaries had borrowings of £1,568 million, a decrease of £192 million from December 31, 1999. In 1999, Prudential issued £250 million aggregate principal amount of 5.5% bonds due 2009 and £250 million aggregate principal amount of 5.875% bonds due 2029 to partially finance the acquisition of M&G.

Prudential also issued £168 million aggregate principal amount of guaranteed floating rate notes due 2004 to M&G shareholders as partial consideration for the acquisition of M&G. In February 2000, Prudential invited these shareholders to exchange their loan notes for units in one or more M&G unit trusts. The balance of these notes outstanding at December 31, 2000 was £54 million.

During 2000, in response to a review of its funding and liquidity requirements, Prudential replaced its existing credit facilities.

At December 31, 2000 the parent company had a £1,100 million multi-currency revolving credit facility permitting 50% of any borrowings under the facility to mature after 364 days from the establishment of the facility in June 2000 and 50% to mature in June 2005. There was no amount outstanding under the facility at December 31, 2000.

In addition, during 2000, Prudential introduced a new US$2,000 million (£1,339 million) global commercial paper program. At December 31, 2000, Prudential had amounts outstanding under the new commercial paper program amounting to £160 million with an average interest rate of 6.00% per annum. At December 31, 2000, Prudential also had amounts outstanding under previous commercial paper programs amounting to £16 million with an average interest rate of 6.46% per annum.

The parent company also maintains uncommitted standby credit facilities in the aggregate of £1,005 million. There was no amount outstanding under these facilities at December 31, 2000.

The commercial paper programs, the committed revolving credit facility and the uncommitted standby facilities are available for general corporate purposes and support the liquidity needs of the parent company. Prudential anticipates that these funding/liquidity facilities are sufficient to meet foreseeable requirements to support shareholders' existing operations.

Sale of Businesses

The initial public offering of shares in Egg on June 12, 2000 raised £239 million, of which £90 million related to the sale of shares by the parent company, after deduction of expenses, and the remainder related to new share capital issued by Egg. The transaction resulted in a profit for the Group of £119 million. Prudential does not currently anticipate any additional future public offerings of Egg shares or shares of any other subsidiary. Prudential's profits on ordinary activities before tax will continue on both the UK GAAP and US GAAP bases to include all of Egg's results. Earnings per share excludes the minority interests' share of Egg's results after tax.

On June 5, 2000, Prudential sold part of its holding in St James's Place Capital plc, an associate company listed on the London Stock Exchange, for cash proceeds of £213 million. The resulting gain on disposal was £99 million. The remaining portion of the holding in St James's Place Capital plc was sold in July 2000 for cash proceeds of £79 million. The resulting realized gain was £24 million.

On June 30, 2000, Prudential transferred part of its UK institutional equity fund management activities to Deutsche Asset Management. The activities transferred comprised management of investments of approximately £12 billion on behalf of third party institutional clients.

In 1998, Prudential completed the sale of its Australian businesses (principally Prudential Corporation Australia Limited and Prudential Assurance Company New Zealand Limited) to The Colonial Mutual Life Assurance Society Limited for net cash proceeds of £468 million.

Recourse to the Equity Markets

In July 2000, Prudential issued 17 million shares following the listing of its ADSs on the New York Stock Exchange. Proceeds raised from the issue, net of expenses, amounted to £139 million.

The cash resources of the parent company are currently sufficient to cover its obligations, interest payments and dividend payments. Prudential makes decisions to reinvest in operating businesses in order to fund growth and maximize shareholder returns. To meet all of its strategic objectives, such as the funding of potential future acquisitions, Prudential may need to raise further financing, including by recourse to the equity markets. Prudential aims to maintain an appropriate debt to equity ratio.

Other fees received

In May 2001, Prudential received a one time payment of £423 million (US$600 million) representing the full termination fee, in accordance with the merger agreement with American General Corporation.

Operating Businesses

UK Life Insurance

The liquidity sources of Prudential's UK life insurance businesses comprise premiums, deposits and charges on policies, investment income, proceeds from the sale and maturity of investments, external borrowings and capital contributions from the parent company. The liquidity requirements comprise benefits and claims, operating expenses, interest on debt, purchases of investments and dividends to the parent company.

The liquidity requirements of Prudential's UK life insurance businesses are regularly monitored to match anticipated cash inflows with cash requirements. Cash needs are forecasted and projected sources and uses of funds, as well as the asset, liability, investment and cash flow assumptions underlying these projections are reviewed periodically. Adjustments are made periodically to the investment policies with respect to, among other things, the maturity and risk characteristics of the investment assets to reflect changes in the business' cash needs and also to reflect the changing competitive and economic environment.

The primary source of short-term liquidity to support operations is a pool of highly liquid, high quality short-term instruments to provide liquidity in excess of the expected cash requirements. At December 31, 2000, the investment assets included £49,413 million of equity securities, £27,973 million of debt securities and £1,996 million of deposits.

The liquidity of Prudential's UK insurance operations is affected by the payment of guaranteed benefits and terminal bonuses on maturing policies by the UK insurance operations. In addition, the non-cash bonus declaration to policyholders results in a cash transfer to shareholders' funds. Historically and for the foreseeable future, the UK cash flows from insurance premiums and investment assets have exceeded benefit payments and operating expenses. Therefore it has not been necessary to sell investment assets or inject additional capital from shareholders to meet Prudential's obligations with respect to with-profits contracts or to pay the annual profit transfer to shareholders' funds. In addition, a large proportion of Prudential's liabilities contain discretionary surrender values or surrender charges. As indicated under "—Liquidity Requirements" in this section above, it is currently anticipated that payments in respect of the pensions misselling provision will be made out of the surplus assets of the long-term fund.

At December 31, 2000 and 1999, Prudential Assurance long-term fund's assets in excess of its required minimum solvency margin were £9,141 million and £15,631 million, respectively. The principal reason for the reduction at December 31, 2000 was the introduction on May 29, 2000 of the new, more stringent, valuation regulations, which require the establishment of reserves to cover part of the terminal bonus in respect of unitized with-profits business.

US Life Insurance

The liquidity sources of Prudential's US operations (Jackson National Life) are its cash, short-term investments and publicly traded bonds, premium income, deposits received on certain annuity and stable value products, investment income and capital contributions from the parent company.

Liquidity requirements are principally for purchases of new investments and businesses, repayment of principal and interest on intercompany debt, payments of interest on surplus notes, funding of insurance product liabilities, including payments for policy benefits, surrenders, maturities, and new policy loans, and funding of expenses, including payment of commissions, operating expenses and taxes. In addition, in 2000 Jackson National Life completed the construction of a new home office building at a total cost of US$58 million. At December 31, 2000, Jackson National Life had borrowings of US$250 million of surplus notes scheduled to mature in 2027 outstanding.

Significant increases in interest rates and disintermediation can create sudden increases in surrender and withdrawal requests by policyholders and contractholders. Other factors that are not directly related to interest rates can also give rise to disintermediation risk, including but not limited to changes in ratings from rating agencies, general policyholder concerns relating to the life insurance industry (e.g., the unexpected default of a large, unrelated life insurer in 1999), and competition from other products, including non-insurance products such as mutual funds, certificates of deposit and newly developed investment products. Most of the life insurance, annuity and stable value products Jackson National Life offers permit the policyholder or contractholder to withdraw or borrow funds or surrender cash values, although some include policy restrictions such as surrender charges and market value adjustments to discourage early withdrawal of policy and contract funds. At December 31, 2000, approximately US$8 billion of policy and contract funds had no surrender charge or market value adjustment restrictions.

Jackson National Life uses a variety of asset-liability management techniques to provide for the orderly provision of cash flow from investments and other sources as policies and contracts mature in accordance with their normal terms. Jackson National Life's principal sources of liquidity to meet unexpected cash outflows associated with sudden and severe increases in surrenders and withdrawals are its portfolio of liquid assets and its net operating cash flows. At December 31, 2000, the portfolio of cash, short-term investments and publicly traded bonds and equities amounted to US$24.6 billion. Operating net cash inflows for 2000 were US$1.8 billion. Prudential believes that these liquidity sources are sufficient to satisfy the company's liquidity needs.

At December 31, 2000, the statutory capital and surplus of Jackson National Life was US$2,222 million, which was significantly in excess of the requirements set out under Michigan insurance law. As described in Item 4, "Information on the Company—Supervision and Regulation of Prudential—US Supervision and Regulation", Jackson National Life is also subject to risk-based capital guidelines that provide a method to measure the adjusted capital that a life insurance company should have for regulatory purposes, taking into account the risk characteristics of the company's investments and products. At December 31, 2000, Jackson National Life's total risk based capital ratio under the National Association of Insurance Commissioners' definition substantially exceeded model act standards.

Egg

Egg's principal liquidity sources are deposits from customers, interest on and proceeds from sales and maturities of investments, repayments of and interest from loans and advances to customers and the issuance of equity securities. The principal liquidity requirements are customer mortgages, credit cards and personal loans, acquisition of investments and administrative expenses. At December 31, 2000, Egg had £3,693 million of cash and short-term investments.

Egg had a net cash outflow from operating activities during 2000 of £450 million, compared with £3,672 million net cash inflow for 1999. The decrease primarily reflects the reduction in new customer deposits. Egg had a net cash outflow of £31 million and £37 million in 2000 and 1999, respectively, in respect of capital expenditures due to additional investments in fixed assets to support the growth in the business.

In 2000, the parent company made capital contributions to Egg of £80 million. Total capital contributions made to Egg during 1999 were £370 million, of which £262 million was to maintain Egg's statutory capital requirements. Egg has to comply with regulatory liquidity requirements that seek to ensure that the operation has access at all times to sufficient sources of liquidity to enable it to pay both expected and unexpected demands. The regulations provide that a minimum level of liquid assets needs to be held. The calculation of these liquid assets depends on the nature of customer deposits and the time over which they can be withdrawn. Capital requirements are driven by the FSA capital regulations stipulated under the Basel Accord. Egg currently meets the target risk asset ratio set by the FSA.

At March 31, 2000, Egg entered into an agreement with Citibank, N.A., pursuant to which it completed an unfunded securitization by way of a credit default swap of approximately £900 million of its mortgage assets. The mortgages remain on Egg's balance sheet but the risk weighting on, and hence the regulatory capital that must be held by Egg in relation to, those assets is reduced.

On May 21, 2001 Egg's subsidiary, Prudential Banking plc, launched a £500 million three year floating rate note, which is expected to settle on June 4, 2001, to provide wholesale funding for its growing lending business.

Egg received net proceeds of £149 million from the initial public offering of a minority stake in the business. At the date of the offering Egg indicated that, based on current business plans and existing lines of business, it would require £300 million to £400 million in addition to the proceeds of its initial public offering to meet capital requirements for the two years following the date of the offering, to be met by the issuance of external debt by Egg.

UK Property and Casualty Insurance

The liquidity sources of Prudential's property and casualty business comprise premiums received, investment income and proceeds from the sale and maturities of investments. The liquidity requirements comprise claims, operating expenses and purchases of investments. The operating profits of the property and casualty insurance business, along with the proportion of the investment portfolio that is held in cash and highly liquid securities, have been sufficient to meet the liquidity requirements of the property and casualty insurance operations. Investments supporting the total property and casualty business were £603 million at December 31, 2000. All property and casualty business is written through Prudential Assurance, and at December 31, 2000 there were assets in excess of the required minimum solvency margin of £161 million.

Fund Management

The principal liquidity source of Prudential's fund management operations is fee income for managing retail investment funds and the investment funds of Prudential's business operations. The principal liquidity requirement is operating expenses. Amounts are distributed to the parent company as dividends after considering capital requirements. Capital requirements are driven by the regulatory stipulations based on the size of funds under management and other operating considerations. At December 31, 2000, fund management operations met the relevant regulatory requirements.

Consolidated Cash Flows

The consolidated statement of cash flows prepared under UK GAAP and included in Prudential's financial statements includes only the cash flows in respect of Prudential's property and casualty insurance business and other shareholders' businesses. Cash flows resulting from activity within the with-profits fund are excluded because UK GAAP requires that insurance companies include cash flows in respect of long-term business only to the extent that cash is transferred to shareholders and is available to meet the obligations of Prudential as a whole. In the case of UK long-term business this amount represents the profit after tax allocated to shareholders.

The discussion that follows is based on the condensed consolidated statement of cash flows prepared under US GAAP presented in note 34 of the notes to Prudential's consolidated financial statements, which includes all of the cash flows of Prudential including those of the with-profits fund.

Year Ended December 31, 2000 Compared to Year Ended December 31, 1999

Net cash provided by operating activities was £2,483 million in 2000 compared with £7,057 million in 1999. The decrease primarily reflects the reduction in Egg new customer deposits. The reduction in the change in the undistributed policyholder allocations mainly arises as a consequence of the change in investments held for trading purposes.

Net cash used for investing activities in 2000 was £2,579 million compared with £10,465 million in 1999. Cash used to purchase investments exceeded proceeds from sales and maturities by £2,652 million in 2000 compared with £8,170 million in 1999. The group had a cash outflow in respect of acquisitions of subsidiaries in 2000 of £183 million compared with £2,011 million in 1999. See "—Acquisition of Businesses" in this section above.

Net cash provided by financing activities was £639 million in 2000 compared with £3,490 million in 1999. Policyholders' deposits exceeded withdrawals by £1,415 million and £2,927 million in 2000 and 1999, respectively. Repayment of long-term borrowings in 2000 was £118 million. There was no repayment of long-term borrowings in 1999. Proceeds from long-term borrowings in 1999 were £500 million. There were no new long-term borrowings in 2000.

As at December 31, 2000 the group had cash of £1,206 million compared with £657 million at December 31, 1999, an increase of £549 million.

Other Commitments

Prudential's commitments and contingencies are discussed more fully in note 27 of the notes to Prudential's consolidated financial statements.

Introduction of the Euro

The euro was introduced on January 1, 1999 as the new currency within 11 member states of the European Union, excluding the United Kingdom, in accordance with the treaty on European Economic and Monetary Union ("EMU"). If the euro is introduced in the United Kingdom, Prudential will need to make changes in its information technology and other systems in order to accommodate the use of the euro in its products, systems and operations. Prudential currently believes it will be able to convert its information technology and other systems to the euro in the time between a definitive decision by the United Kingdom to join EMU and the actual introduction of the euro as legal tender in the United Kingdom. Prudential has spent approximately £4 million to date assessing and planning for the possibility that the United Kingdom will join EMU and introduce the euro.

Item 6. Directors, Senior Management and Employees

Directors and Senior Management

The Prudential board of directors currently consists of 11 directors and is expected to consist of 12 directors following the appointment of Mark Wood in June 2001. Set forth below are the names, ages, current positions and business experience of the 11 persons who currently serve on the board, as well as the dates of their initial election as directors.

Sir Roger Hurn (Age 63)

Sir Roger Hurn has been a non-executive director of Prudential since February 2000 and chairman since May 2000. He is also the chairman of Marconi plc (formerly The General Electric Company plc) and the deputy chairman of GlaxoSmithKline plc and previously was the deputy chairman of Glaxo Wellcome plc. He is a non-executive director of Imperial Chemical Industries PLC and was previously chairman of Smiths Industries plc and a director of SG Warburg Group. He is a chairman of the Court of Governors at the Henley Management College.

Jonathan Bloomer FCA (Age 47)

Jonathan Bloomer has been an executive director of Prudential since 1995 and group chief executive since March 2000. Previously, he was deputy group chief executive and group finance director. He is a non-executive director of Egg plc and of Railtrack Group plc. He is a member of the Urgent Issues Task Force Committee of the Accounting Standards Board.

Keith Bedell-Pearce (Age 55)

Keith Bedell-Pearce has been an executive director of Prudential since 1992, its e-commerce director since March 2000 and chairman of Prudential Europe since September 1999. Previously, he was Prudential's international development director. He joined Prudential in 1972. He is a non-executive director of Norwich & Peterborough Building Society.

Mark Tucker (Age 43)

Mark Tucker has been an executive director of Prudential since September 1999 and chief executive of Prudential Corporation Asia since 1994 and previously was general manager in Prudential, Hong Kong from 1989 to 1992. He joined Prudential in 1986.

Philip Broadley FCA (Age 40)

Philip Broadley has been an executive director of Prudential and group finance director since May 2000. Previously he was with Arthur Andersen, where he became a partner in 1993. He specialised in providing audit, risk management and regulatory advisory services to clients in the financial services industry.

Michael McLintock (Age 40)

Michael McLintock has been an executive director since September 2000. He has also been chief executive of M&G since February 1997, a position he held at the time of M&G's acquisition by Prudential in March 1999. He joined M&G in October 1992.

Ann Burdus (Age 67)

Ann Burdus has been a non-executive director of Prudential since 1996. She is also a non-executive director of Next plc and a council member of the Institute of Directors. Previously, she was a non-executive director of Safeway Group plc and a committee member of the Automobile Association.

Sandy Stewart (Age 67)

Sandy Stewart has been a non-executive director of Prudential since 1997. He is also chairman of Murray Extra Return Investment Trust plc and of the Scottish Amicable (supervisory) Board. Previously, he was a practising solicitor and Chairman of Scottish Amicable Life Assurance Society.

Sir David Barnes CBE (Age 65)

Sir David Barnes has been a non-executive director of Prudential since January 1999. He has been deputy chairman of AstraZeneca plc since April 1999 and was previously chief executive of Zeneca PLC. He has been a non-executive deputy chairman of Syngenta AG since November 2000 and non-executive chairman of Imperial Cancer Research Technology Ltd. He is a member of the Board of Trustees of the British Red Cross Society and was previously deputy chairman of Business in the Community.

Rob Rowley (Age 51)

Rob Rowley has been a non-executive director of Prudential since July 1999. He is also a director of Reuters Group PLC and chief executive of Reuterspace division. Previously, he was finance director of Reuters Group PLC.

Roberto Mendoza (Age 55)

Robert Mendoza has been a non-executive director of Prudential since May 2000. He is also a non-executive chairman of Egg plc and non-executive director of ACE Limited, Reuters Group PLC and Vitro SA. Previously, he was vice chairman and director and a member of the Corporate Office of JP Morgan & Co, Inc. and was recently a managing director of Goldman Sachs.

Other Executive Officers

The table below sets out the names of other executive officers of Prudential and their current principal positions with Prudential.

Director/Executive Officer	Job Title	Business Unit
Robert Saltzman (Age 58)	President and Chief Executive Officer	Jackson National Life
John Elbourne (Age 56)	Chief Executive	UK Insurance Operations
Rodney Baker-Bates (Age 57)	Chief Executive	Prudential Financial Services
Paul Gratton (Age 41)	Chief Executive	Egg
Kim Lerche-Thomsen (Age 48)	Chief Executive	Prudential Intermediary Business
Alan Cook (Age 47)	Chief Executive	Prudential Insurance Services
Chris Evans (Age 44)	Chief Executive	Prudential Europe

Service Contracts

The normal notice of termination which Prudential is required to give executive directors is 12 months, although for newly appointed directors there may be an initial contractual period of up to two years before the 12 months' notice period applies. The contracts of employment for all executive directors, including those appointed to the board in 2000, contain a 12 months' notice period. When considering termination of service contracts, regard will be given to the specific circumstances of each case, including mitigation. Non-executive directors do not have service contracts.

Compensation

In 2000 the aggregate compensation that Prudential paid or accrued to all Prudential directors and other executive officers as a group (26 persons) was £18,447,587, including performance-related bonuses paid to the executive directors and executive officers and including an aggregate pension contribution of £1,206,006 and provision for future benefits.

Directors' Remuneration

	Year ended December 31, 2000			
	Salary/Fees	Annual Bonus	Benefits	Total Emoluments
	(In £ Thousands)			
Executive directors				
Keith Bedell-Pearce	325	105	28	458
Jonathan Bloomer	562	224	62	848
Philip Broadley (appointed 5/11/00)	208	76	9	293
Les Cullen (resigned 2/29/00)(1)	117	—	5	122
Sir Peter Davis (resigned 2/29/00)(2)	100	—	5	105
Derek Higgs (retired 11/30/00)	368	125	18	511
Michael McLintock (appointed 9/1/00)(3)	100	350	3	453
Mark Tucker(4)	360	576	183	1,119
Total executive directors	2,140	1,456	313	3,909
Non-executive directors				
Michael Abrahams (retired 5/5/00)	23	—	—	23
Sir David Barnes	29	—	—	29
Ann Burdus	29	—	—	29
Sir Roger Hurn (appointed 2/17/00, chairman 5/5/00)	200	—	—	200
Sir Martin Jacomb (retired 5/5/00)	62	—	3	65
Bridget Macaskill (resigned 3/16/01)	29	—	—	29
Roberto Mendoza (appointed 5/25/00)	68	—	—	68
Rob Rowley	29	—	—	29
Sandy Stewart	55	—	—	55
Total non-executive directors	524	—	3	527
Overall total	2,664	1,456	316	4,436

(1) Les Cullen also received compensation for loss of office of £276,000.

(2) The highest paid director in 2000 was Sir Peter Davis whose emoluments in 2000, including the value of rights granted to him under the long-term incentive plan, were £2,476,000. Additionally in 2000 Prudential made pension contributions of £47,000 on his behalf, including contributions of £36,000 to a Funded Unapproved Retirement Benefit Scheme.

(3) Michael McLintock's bonus includes a payment of £117,000 that was included in his contractual arrangements following the purchase of M&G in 1999.

(4) Mark Tucker's bonus figure includes a cash payment of £207,000 from his 1998 Asian long-term incentive plan. His benefits include an allowance for housing and additional similar benefits paid to reflect his expatriate circumstances. For 2000, those benefits and allowances amounted to £163,000.

Annual Bonus

The annual incentive plan for directors is designed to leverage value creation over the performance period while supporting sustained long-term value creation.

Annual bonus awards are non-pensionable and in 2000 were made in cash. The awards are determined by the remuneration committee of Prudential's board of directors and are based on performance against quantitative financial and business targets in the business plans as well as personal performance.

For 2000, executive directors were eligible for awards of up to 45% of basic salary at the time of making the award, with the exception of Michael McLintock who has an annual bonus award in line with remuneration levels in the investment management industry.

Senior Executives' Long-term Incentive Plans

Prudential's primary long-term incentive plan is known as the Restricted Share Plan and is designed to provide rewards contingent upon the achievement of pre-determined returns to shareholders. Under this plan Prudential annually grants executive directors and most other executive officers a conditional award of Prudential's shares which are held in trust for three years. As group chief executive, Jonathan Bloomer received a conditional award for 2000 equivalent to 100% of his salary at the time of the award. Michael McLintock received an award equivalent to 40% of his salary. For the other executive directors, the award was equivalent to 80% of salary. The shares are valued at their average share price during the preceding calendar year. The award price used for the 2000 award was 921.7 pence.

At the end of the three-year performance period, a right to receive shares at no cost to the individual may be granted depending on Prudential's total return to shareholders relative to other companies in the FTSE 100 share index over the three years. In addition, the remuneration committee of Prudential's board of directors must be satisfied with Prudential's overall financial performance during this period. Prudential will not allocate shares if Prudential's total return ranks 60th or below other companies in the FTSE 100 share index over the three years and Prudential will award the maximum allocation only if the total shareholder return is in the top 20 of such companies. Between these points, allocations of shares will be on a straight line basis. The individual concerned may then exercise the right to receive allocations at any time during the following seven years.

As chief executive of Asian operations, Mark Tucker also participates in a cash-based long-term incentive plan that measures performance of the group's Asian operations. This plan is designed to provide reward contingent upon the rate of change in value of the Asian operations over a three-year period. The threshold performance criterion under the plan is that the growth in value must be greater than 15% per year over the period. Any payment for performance above the threshold is made in the April following the end of the performance period. The on-target payout is 100% of salary at the beginning of the period, for which an annual growth rate of 35% is required. The maximum of 150% of salary is for exceptional performance, representing 50% or higher annual growth.

As chief executive of M&G, Michael McLintock also participates in the M&G Chief Executive Long-Term Incentive Plan. The plan is designed to provide a cash reward based on the economic and investment performance of M&G over a three-year period. Awards are made under the plan through the granting of awards of phantom share options and restricted shares, vesting at the end of the performance period.

Not all executive officers participate in the Restricted Share Plan. Those who do not participate in the Restricted Share Plan participate instead in a cash-based phantom stock plan with annual awards that vest, depending on the plan in question, between four and five years after the date of grant. Awards are dependent on the performance of the business area or region over the vesting period.

Details of conditional awards of Prudential's shares under the Restricted Share Plan are shown below. These shares are held in trust and represent the conditional awards out of which allocations may be made in the allocation year:

	Conditional awards outstanding at January 1, 2000	Conditionally awarded in 2000	Rights granted in 2000	Market value of rights granted in 2000* (In £ Thousands)	Conditional awards outstanding December 31, at 2000	Release year
Keith Bedell-Pearce	39,350		39,350	383		
	36,024				36,024	2001
	28,664				28,664	2002
		28,209			28,209	2003
Subtotal	104,038	28,209	39,350	383	92,897	
Jonathan Bloomer	56,859		56,859	554		
	45,390				45,390	2001
	36,308				36,308	2002
		63,470			63,470	2003
Subtotal	138,557	63,470	56,859	554	145,168	
Philip Broadley		18,806			18,806	2003
Les Cullen(1)	16,720		4,714	46		
Sir Peter Davis(2)	101,534		101,534	1,007		
	79,417		79,417	788		
	64,494		58,045	576		
Subtotal	245,445		238,996	2,371		
Derek Higgs(3)	56,859		56,859	554		
	45,390				45,390	2001
	36,308				36,308	2002
		34,718			34,718	2003
Subtotal	138,557	34,718	56,859	554	116,416	
Michael McLintock		13,019			13,019	2003
Mark Tucker	46,931		46,931	457		
	36,024				36,024	2001
	28,664				28,664	2002
		31,247			31,247	2003
Subtotal	111,619	31,247	46,931	457	95,935	
TOTAL	754,936	189,469	438,995	4,319	482,241	

* The market value of rights granted in 2000 is based on the market value of the shares over which rights are granted on the day of the grant.

(1) In accordance with the arrangements for Les Cullen's departure, the release date applying to his 1999 RSP award was brought forward to April 2000 with shares released subject to pro rating for service in the performance period and TSR performance at February 29, 2000. The balance of the award lapsed.

(2) In accordance with the arrangements for Sir Peter Davis' departure, the release dates applying to his RSP awards were brought forward to February 2000 with shares released subject only to pro rating for TSR performance at January 31, 2000. The balance of the awards lapsed.

(3) In accordance with the arrangements for his retirement, the release dates applying to the 1999 and 2000 RSP awards for Derek Higgs have been brought forward to February 28, 2001, with pro rating and TSR performance effective December 31, 2000. The balance of the awards lapsed.

For purposes of the 1998 Restricted Share Plan, Prudential ranked 22nd out of the relevant companies on the FTSE 100 share index for the three-year period ended December 31, 2000. As a result, rights have been granted over 85% of the shares conditionally awarded to executive directors.

Senior Executives' Share Options

The Restricted Share Plan replaced the Prudential Executive Share Option Scheme in 1995 as Prudential's primary long-term incentive plan. Outstanding options under both the Prudential and M&G executive share option scheme remain in effect and are set out below under "—Share Ownership—Options to Purchase Securities from Prudential" in this section together with options under the Prudential and M&G savings-related share option scheme. The current Prudential savings-related share option scheme is open to all UK permanent employees and Prudential grants options up to UK Inland Revenue limits at a 20% discount. Optionholders cannot normally exercise such options until a minimum of three years has elapsed.

Senior Executives' Pensions

Prudential Staff Pension Scheme

All executive directors, except Michael McLintock, are eligible to participate in the Prudential Staff Pension Scheme on the same basis as other members. The scheme is non-contributory and provides members with a maximum pension of 38/60 of final pensionable earnings at the normal retirement age of 60. Final pensionable earnings are the sum of the pensionable salary for the 12 months immediately preceding retirement or termination of employment. Final pensionable earnings for entrants since May 31, 1989 are restricted to salary up to the UK Inland Revenue earnings cap.

The scheme also provides on death, whether in service, in deferment or following retirement, pensions for spouse and children. The spouse's pension on death in service is the higher of 54% of the member's prospective pension at age 60 or 25% of salary in the 12 months preceding death subject to the earnings cap. The spouse's pension on death in deferment is 50% of the member's deferred pension at the date of death. On death after retirement, the spouse's pension is 50% of the member's pension in payment ignoring any pension commuted for a lump sum at retirement. A lump sum death in service benefit of four times final pensionable earnings is also provided. Pension increases after retirement are wholly discretionary but in recent years annual increases have been awarded in line with inflation. Discretionary increases are taken into account in calculating transfer values payable in lieu of deferred pension benefits. The contract of Keith Bedell-Pearce provides that in the event of his retirement at age 55, his pension will be based on the pension he would have received at normal retirement age 60 subject to a discount rate of 3% per annum for early retirement.

M&G Group Pension Scheme

Michael McLintock is a member of the M&G Group Pension Scheme and has a normal retirement age of 60. The scheme is contributory with members currently contributing 2.4% of salary. It will provide him with a maximum pension, at the normal retirement age of 60, equal to two-thirds of the greater of his salary in the last 12 months of service and the yearly average of his salary over the last 36 months of service subject to Inland Revenue restrictions. His pension is subject to the UK Inland Revenue earnings cap because he entered the scheme after May 31, 1989.

The scheme also provides on death, whether in service, in deferment or following retirement, a spouse's pension. The spouse's pension on death in service is 50% of the pension the member would have received had they remained in service until their normal retirement age under the scheme, but based on the member's pensionable salary at the time of death. The spouse's pension on death in deferment is 50% of the member's deferred pension at the date of death. On death after retirement, the spouse's pension is 50% of the member's pension in payment ignoring any pension commuted for a lump sum at retirement. A lump sum death in service benefit of four times salary is also provided. Pensions are increased after retirement annually on October 1. In respect of any pension in excess of a member's guaranteed minimum pension under the scheme, the increases are in line with the increase in the UK Retail Prices Index over the 12 months to the preceding July, subject to a maximum increase of 5% per year.

Other Pension Arrangements

For directors subject to the earnings cap, Prudential will, on request, establish funded unapproved retirement benefit schemes and a separate life assurance scheme to provide additional retirement and life assurance benefits based on salary in excess of the earnings cap. Sir Peter Davis and Derek Higgs participated in these arrangements and Philip Broadley and Michael McLintock are participants. Jonathan Bloomer has not participated in the funded unapproved retirement benefit schemes and instead Prudential pays a salary supplement to fund arrangements for the provision of income in retirement. The Prudential Staff Pension Scheme provides a lump sum death in service benefit. Jonathan Bloomer also participates in a separate life assurance scheme that provides cover over the earnings cap. The same arrangements applied to Les Cullen.

Other officers are also eligible to join local pension arrangements, the majority of which are of the defined benefit type. Where other officers receive salary supplements or contributions to defined contribution arrangements, these have been disclosed in the Compensation of Directors and Officers above.

Board Practices

Non-executive directors of Prudential are appointed initially for a three-year term. The appointment is then reviewed towards the end of this period. All directors are required to submit themselves for re-election at regular intervals and at least every three years.

Rob Rowley is chairman, and Ann Burdus and Sandy Stewart are members, of the audit committee of the board of Prudential. The audit committee meets six times a year and assists the board in meeting its legal responsibilities to ensure an effective system of internal control and risk management. It reviews with Prudential's management and its external auditors the performance of the external auditors and auditors' fees for both statutory audit work and non-audit work.

Sir David Barnes is chairman, and Ann Burdus, Roberto Mendoza, Rob Rowley and Sandy Stewart are members, of the remuneration committee of the board of Prudential. The remuneration committee normally meets twice a year to review remuneration policy and determine the remuneration packages of the executive directors of Prudential and certain other senior executives. The remuneration committee generally consults the chairman and group chief executive about its proposals relating to remuneration. It has access to professional advice inside and outside Prudential.

Employees

The average numbers of staff employed by the Prudential group for the following periods were:

	2000	**1999**	**1998**
UK operations	**16,652**	18,885	18,818
US operations	**2,250**	1,640	1,439
Asia	**2,635**	1,535	1,328
Europe	**405**	312	272
Discontinued operations	**—**	—	977
Total	**21,942**	22,372	22,834

As at December 31, 2000, Prudential employed 22,933 persons. Of the 22,933 approximately 73% were located in the United Kingdom, 14% in Asia, 11% in the United States and 2% in Europe.

In the United Kingdom, Prudential had 2,775 employees paying union subscriptions through the payroll, mainly from the company salesforce. Following the company salesforce closure announcement in February 2001, the company is currently consulting with the union.

As at December 31, 2000, Prudential had 221 temporary employees in the United Kingdom and 52 temporary employees in Europe. Prudential did not have a significant number of temporary employees in the United States and Asia.

Share Ownership

Directors' Shareholdings

As at May 14, 2001, Prudential's directors beneficially owned the following total amount of Prudential's shares not including options and conditional awards:

Name	Holding as of May 14, 2001	Percentage of Ordinary Shares
Sir David Barnes CBE	4,119	0.0002
Keith Bedell-Pearce	175,274	0.0088
Jonathan Bloomer	152,444	0.0077
Philip Broadley	3,984	0.0002
Ann Burdus	3,086	0.0002
Sir Roger Hurn	10,000	0.0005
Michael McLintock	3,884	0.0002
Roberto Mendoza	2,913	0.0001
Rob Rowley	2,947	0.0001
Sandy Stewart	9,450	0.0005
Mark Tucker	169,407	0.0085

* Information has not been provided on Les Cullen, Sir Peter Davis, Derek Higgs, Michael Abrahams CBE DL, Sir Martin Jacomb and Bridget Macaskill because they are no longer directors of Prudential and Prudential does not maintain information on their shareholdings.

In addition, Prudential's directors and other executive officers held, as at May 14, 2001, options to purchase 910,335 shares, all of which were issued pursuant to Prudential's Executive Share Option Scheme or Prudential's Savings-Related Share Option Scheme. These options and plans are described in more detail below under "—Options to Purchase Securities from Prudential" in this section.

Prudential is not owned or controlled directly or indirectly by another corporation or by any government or by any other natural or legal person severally or jointly and Prudential does not know of any arrangements that might result in a change in Prudential's control.

Outstanding Options of Directors and Other Executive Officers

	Options outstanding at May 14, 2001	Exercise price (pence)	Earliest exercise date	Latest exercise date
Keith Bedell-Pearce[2]	189,000	201	1995	2002
	105,000	328	1996	2003
	60,500	309	1997	2004
	2,267*	344	2003	2003
	3,259*	359	2003	2004
Subtotal	360,026			
Jonathan Bloomer	196,750	315	1998	2005
	226,750	315	2000	2005
	7,677*	254	2002	2002
	2,296*	751	2005	2005
Subtotal	433,473			
Philip Broadley	1,327*	730	2003	2004
Michael McLintock	4,538*	380	2003	2003
Mark Tucker[3]	2,172*	359	2003	2004
	1,378*	751	2005	2005
Subtotal	9,415			
SUBTOTAL	802,914			
Other Executive Officers	107,421			
TOTAL[4]	910,335			

* Savings-Related Share Option Scheme.

(1) The market price of shares at December 31, 2000 was 1077 pence. The highest and lowest share prices during 2000 were 1,186 pence and 880 pence, respectively.

(2) During 1999, Keith Bedell-Pearce exercised options with an associated gain on exercise of £40,000.

(3) Mark Tucker exercised options over the 4,074 shares on March 13, 2001.

(4) Information has not been provided on Les Cullen, Sir Peter Davis and Derek Higgs because they are no longer directors of Prudential and Prudential does not maintain information on their shareholdings.

(5) None of Michael Abrahams, Sir David Barnes, Ann Burdus, Sir Roger Hurn, Sir Martin Jacomb, Bridget Macaskill, Roberto Mendoza, Rob Rowley or Sandy Stewart holds options to purchase Prudential shares.

Prudential's register of directors' interests, which is open to inspection, contains full details of the directors' shareholdings and options to subscribe for shares.

Options to Purchase Securities from Prudential

As of May 14, 2001, 22,945,328 options were outstanding, which Prudential issued under the Executive Share Option Schemes and the Savings-Related Share Option Schemes. As of May 14, 2001, directors and other executive officers held 910,335 of such outstanding options. Except as described above in "—Outstanding Options of Directors and Other Executive Officers", each option represents the right of the bearer to subscribe for one share at a particular pre-determined exercise price at a pre-set exercise date.

As of May 14, 2001, 120,663 shares were outstanding under the Share Participation Plan. Such outstanding shares held by directors are included in the shares set forth under "—Directors' Shareholdings" in this section above.

As of May 14, 2001, 31,967 shares were outstanding under the Managers Share Plan, none of which was held by a director.

As of May 14, 2001, 750,307 options were outstanding under the Restricted Share Plan. Such outstanding options held by directors are included in the shares set forth under "—Directors' Shareholdings" in this section above.

As of May 14, 2001, 2,754,299 options were outstanding under the Professional Reward Scheme, none of which was held by directors or other executive officers. The Professional Reward Scheme is a scheme open only to the UK company salesforce staff and is not open to directors and other executive officers.

As of May 14, 2001, 31,855 shares were outstanding under other awards, none of which was held by a director.

The aggregate exercise price of the outstanding options under the Executive Share Option Scheme and the Savings-Related Share Option Scheme is £121 million. The latest expiration dates for exercise or release of the securities underlying the options or awards and the number of options or shares (in millions) are set out in the table below.

Year of Expiration	Shares Outstanding Under Share Participation Plan	Shares Outstanding Under Managers Share Plan	Options Outstanding Under Restricted Share Plan	Shares and Options Outstanding Under Professional Reward Scheme	Options Outstanding Under Executive Share Option Scheme and Savings-Related Share Option Scheme	Shares Outstanding Under Other Awards	Total
	(In Millions)	(In Millions)	(In Millions)	(In Millions)	(In Millions)	(In Millions)	(In Millions)
2001	—	—	0.01	0.3	4.1	0.01	4.4
2002	0.10	0.03	—	0.2	5.0	0.02	5.4
2003	0.01	—	—	0.1	3.9	—	4.0
2004	0.01	—	—	0.1	5.5	—	5.6
2005	—	—	—	—	1.9	—	1.9
2006	—	—	0.14	—	2.0	—	2.1
2007	—	—	0.20	0.4	0.2	—	0.8
2008	—	—	0.40	0.5	0.3	—	1.2
2009	—	—	—	0.7	—	—	0.7
2010	—	—	—	0.2	—	—	0.2
2011	—	—	—	0.2	—	—	0.2
Total	0.12	0.03	0.75	2.7	22.9	0.03	26.5

Item 7. Major Shareholders and Related Party Transactions

Major Shareholders

The Companies Act 1985 provides that a person that acquires an interest of 3% or more in Prudential ordinary shares is required to notify Prudential of that interest. As at May 14, 2001 Prudential had not received any information that any shareholders own beneficially, directly or indirectly, more than 3% of its shares.

In addition, Prudential's directors and other executive officers held, as at May 14, 2001, options to purchase shares, all of which were issued pursuant to the Prudential Executive Share Option Scheme or Prudential Savings-Related Share Option Scheme. These options and plans are described in more detail under Item 6, "Directors, Senior Management and Employees—Compensation" and "—Share Ownership".

Significant Changes in Ownership

In 1997, Prudential did not receive any notification from any shareholder that it held 3% or more of its share capital. In October 1998, Legal & General Group plc notified Prudential that it held 3% of its share capital. In November 1999, Janus Capital Corporation notified Prudential that it held 3.1% of its share capital. In December 1999, Legal & General Group plc notified Prudential that it no longer held 3% of Prudential's share capital.

In April and August 2000, Janus Capital Corporation notified Prudential that it held 4.2% and 3.9% of its share capital, respectively. In September 2000, Janus Capital Corporation notified Prudential that it no longer held 3% of Prudential's share capital. Also in September 2000, CGNU notified Prudential that it held 3.07% of its share capital.

In April 2001, Barclays PLC notified Prudential that Barclays Bank PLC held 3% of its share capital in March 2001 and that, subsequently, Barclays Bank PLC ceased having a notifiable interest in Prudential. Also in April 2001, CGNU notified Prudential that it no longer held 3% of its share capital while in May 2001 it notified Prudential that it held 3.1% of its share capital.

As of May 14, 2001, there were 91,154 shareholders holding Prudential shares in the United Kingdom. These shares represented 99.64% of Prudential's issued share capital.

Related Party Transactions

In September 1997, Prudential acquired the Scottish Amicable business. Prior to the acquisition of Scottish Amicable Life Assurance Society, Sandy Stewart was a director and the chairman of that company and following the acquisition, he became one of Prudential's non-executive directors. Also, prior to the acquisition of each of M&G and Scottish Amicable, Michael McLintock was the chief executive officer of M&G and Roy Nicolson was the chief executive officer of Scottish Amicable. Following each respective acquisition, they each became executive officers in Prudential's group.

Otherwise, during the last five years Prudential has not been and is not now, a party to any other material transaction or proposed transaction in which any director, any other executive officer, any spouse or relative of any of the foregoing, or any relative of such spouse had or was to have a direct or indirect material interest.

Various executive officers and directors of Prudential may from time to time purchase insurance or annuity products marketed by Prudential companies in the ordinary course of business.

Item 8. Financial Information

See Item 18, "Financial Statements".

Item 9. The Offer and Listing

Comparative Market Price Data

The tables below set forth for the periods indicated the highest and lowest closing middle-market quotations for Prudential ordinary shares, as derived from the Daily Official List of the London Stock Exchange, and the ADS equivalent of these prices prior to June 28, 2000 or the actual ADS high and low closing sale prices on the New York Stock Exchange after that date.

	Prudential Ordinary Shares		Prudential ADS Equivalent[1]		Prudential ADS Actual[2]	
Year	**High**	**Low**	**High**	**Low**	**High**	**Low**
	(pence)		(US Dollars)		(US Dollars)	
1996	501	403	16.28	12.46	—	—
1997	757	488	24.99	16.45	—	—
1998	960	638	32.24	21.98	—	—
1999	1,220	758	39.36	24.70	—	—
2000	1,186	880	38.81	28.13	32.25	24.69

	Prudential Ordinary Shares		Prudential ADS Equivalent[1]		Prudential ADS Actual[2]	
	High	**Low**	**High**	**Low**	**High**	**Low**
	(pence)		(US Dollars)		(US Dollars)	
1999						
First quarter	1,000	758	32.86	24.70	—	—
Second quarter	934	788	29.45	25.41	—	—
Third quarter	999	845	32.05	26.86	—	—
Fourth quarter	1,220	852	39.36	28.47	—	—
2000						
First quarter	1,186	880	38.81	28.13	—	—
Second quarter	1,064	889	33.97	28.17	28.94	28.00
Third quarter	1,023	902	31.03	26.19	30.63	24.69
Fourth quarter	1,123	897	33.36	25.93	32.25	25.44
2001						
First quarter	1,095	708	32.70	20.14	32.69	20.25

	Prudential Ordinary Shares		Prudential ADS Equivalent[1]		Prudential ADS Actual[2]	
Month	**High**	**Low**	**High**	**Low**	**High**	**Low**
	(pence)		(US Dollars)		(US Dollars)	
December 2000	1,123	1,055	32.36	31.15	32.25	30.44
January 2001	1,095	985	32.70	28.86	32.69	28.63
February 2001	1,050	924	31.03	26.62	30.75	26.60
March 2001	945	708	27.51	20.14	27.50	20.25
April 2001	818	744	23.40	21.29	23.40	21.01
May 2001	873	776	24.55	22.75	24.55	22.75

(1) To obtain the ADS equivalent prices, the reported high and low prices for Prudential ordinary shares expressed in pence per Prudential ordinary share have been translated into US dollars per ADS (each evidencing two ordinary shares) by multiplying the pence per ordinary share by two and converting that amount to dollars at the noon buying rate (divided by 100 and rounded to the second decimal place) on the dates of such respective high and low prices.

(2) Prudential ADSs were listed on the New York Stock Exchange on June 28, 2000, and actual ADS prices are given from that date.

Market Data

Prudential ordinary shares are listed on the Official List of the UK Listing Authority and traded on the London Stock Exchange under the symbol "PRU". Prudential ADSs have been listed for trading on the New York Stock Exchange since June 28, 2000 under the symbol "PUK".

Item 10. Additional Information

Memorandum and Articles of Association

The following is a summary of both the rights of Prudential shareholders and certain provisions of Prudential's memorandum and articles of association. Rights of Prudential shareholders are set out in Prudential's memorandum and articles of association or are provided for by applicable English law. Because it is a summary, it does not contain all the information that may be important to you. For more complete information you should read Prudential's memorandum and articles of association. Directions on how to obtain a complete copy of Prudential's memorandum and articles of association are provided under "—Documents on Display" in this section below.

Dividends

Under English law, Prudential may pay dividends only if distributable profits are available for that purpose. Distributable profits are accumulated, realized profits not previously distributed or capitalized, less accumulated, realized losses not previously written off. Even if distributable profits are available, Prudential may only pay dividends if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves, including, for example, the share premium account and the capital redemption reserve, and the payment of the dividend does not reduce the amount of the net assets to less than that aggregate. In addition, as the parent company of UK insurance companies to which Part II of the Insurance Companies Act 1982 applies, Prudential may not declare a dividend at any time when the value of the assets representing the fund or funds maintained by any of those insurance companies in respect of its long-term insurance business (as determined in accordance with applicable valuation regulations) is less than the amount of the liabilities attributable to that business (as so determined). Subject to these restrictions, Prudential's directors have the discretion to determine whether to pay a dividend and the amount of any such dividend but must take into account Prudential's financial position.

Prudential's directors also determine the date on which Prudential pays dividends. Prudential pays dividends to the shareholders on the register on the record date that the directors determine, in proportion to the number of shares that those shareholders hold. There are no fixed dates on which entitlements to dividends arise. Interest is not payable on dividends or other amounts payable in respect of shares.

Prudential's directors have the discretion to offer shareholders the right to elect to receive additional shares (credited as fully paid) instead of all or any part of any cash dividend. The aggregate value of additional shares that a shareholder may receive under such an election is as nearly as possible equal to (but not greater than) the cash amount the shareholder would have received. Prudential does not issue fractions of shares and Prudential's directors may make such provision as they think appropriate to deal with any fractional entitlements. Prudential's directors may exclude shareholders from the right to receive shares instead of cash dividends if Prudential's directors believe that extending the election to such shareholders would violate the laws of any territory or for any other reason the directors consider in their absolute discretion appropriate.

If a shareholder does not claim a dividend within one year of becoming due for payment, Prudential's directors may invest it or otherwise use it for Prudential's benefit until such shareholder claims it. These amounts are not held on trust. If a shareholder does not claim a dividend within 12 years of becoming due for payment, such shareholder forfeits it.

Shareholder Meetings

English company law provides for shareholders to exercise their power to decide on corporate matters at general meetings. Prudential's articles of association require annual general meetings, at intervals of not longer than 15 months. At the annual general meetings, shareholders receive and consider the statutory accounts and the reports by the auditors and the directors, elect and re-elect directors, approve the appointment, and fix or determine the manner of fixing, of the remuneration of Prudential's auditors and transact any other business which ought to be transacted under the articles of association. Extraordinary general meetings to consider specific matters may be held at the discretion of Prudential's directors and must be convened following the written request of shareholders representing at least one-tenth of all the issued shares. The quorum required for a general meeting is ten shareholders present in person or by proxy.

Voting Rights

Voting at any meeting of shareholders is by show of hands unless a poll (meaning a vote by the number of shares held rather than by a show of hands) is demanded as described below. On a show of hands every shareholder who is present in person or by proxy has one vote. Proxies are not allowed to vote on a show of hands. On a poll every shareholder who is present in person or by proxy has one vote for every share held. Only the holders of fully paid shares are allowed to attend and be counted in the quorum at meetings or to vote. If more than one joint shareholder votes, only the vote of the shareholder whose name appears first in the register is counted. A shareholder whose shareholding is registered in the name of a nominee may not attend and vote at a general meeting and may only vote through his or her nominee.

Resolutions of Prudential's shareholders generally require the approval of a majority of the shareholders to be passed. Such resolutions, referred to as ordinary resolutions, require:

- on a show of hands, a majority in number of the shareholders present and voting in person or (in the case of a corporate shareholder) by an authorized corporate representative to vote in favor, or
- on a poll, more than 50% of the votes to be in favor.

Some resolutions, referred to as special resolutions, however, such as a resolution to amend the memorandum and articles of association, require a 75% majority. Such special resolutions require:

- on a show of hands, at least 75% of the shareholders present and voting in person or (in the case of a corporate shareholder) by an authorized corporate representative to vote in favor, or
- on a poll, at least 75% of the votes to be in favor.

The chairman of the general meeting has a tie-breaking vote both on a show of hands and on a poll. Any shareholder who is entitled to attend and vote at a general meeting may appoint one or more proxies to attend and vote at the meeting on his or her behalf.

The following persons may demand a poll:

- the chairman of the meeting,
- at least five shareholders present in person or by proxy having the right to vote at the meeting,
- any shareholder or shareholders present in person or by proxy and representing at least 10% of the total voting rights of all the shareholders having the right to vote at the meeting, or
- any shareholder or shareholders present in person or by proxy and holding shares conferring a right to vote at the meeting on which an aggregate sum has been paid up equal to at least 10% of the total sum paid up on all the shares conferring that right.

Transfer of Shares

Transfers of shares may be made by an instrument of transfer. An instrument of transfer must be signed by or on behalf of the transferor and, unless the share is fully paid, by or on behalf of the transferee. The transferor remains the holder of the relevant shares until the name of the transferee is entered in the share register. Transfers of shares may also be made by a computer-based system (currently the CREST system) and transferred without a written instrument in accordance with English company law. The directors may refuse to register transfers of shares, but only if such refusal does not prevent dealings in the shares from taking place on an open and proper basis. If the directors refuse to register a transfer they must send the transferee notice of the refusal within two months.

Changes in Share Capital

Increases in share capital may only take place after approval by shareholders by ordinary resolution. The class and other rights attaching to such new shares may be determined by resolution of the shareholders. Prudential's directors may issue and allot such new shares if authorized to do so by the shareholders. In addition to any increase, the following changes in share capital may only take place after approval by an ordinary resolution of the shareholders:

- share consolidations and share splits,
- subdivisions of shares, and
- cancellations of shares that have not been taken or agreed to be taken by any person.

Reductions in Prudential's share capital, capital redemption reserve and share premium account and purchases of Prudential's own shares must be approved by a special resolution of the shareholders and must be confirmed by an order of the court.

Variation of Rights

If the share capital is divided into different classes of shares, the rights of any class of shares may be changed or taken away only if such measure is approved by a special resolution passed at a separate meeting of the holders of that class. Two persons holding or representing by proxy at least one-third in nominal amount of the issued shares of the class must be present at such a meeting in person or by proxy to constitute a quorum. The issued share capital of Prudential is not currently divided into different classes of shares.

Lien

Prudential may not have a lien on fully paid shares.

Shareholders Resident Abroad

If a shareholder has not provided an address in the United Kingdom, the Channel Islands or the Isle of Man to Prudential, Prudential is not currently required to send notices to such shareholder directly. Notices to such shareholders may be posted in Prudential's registered office and are then deemed to be served on those shareholders on the day following the posting. Unless otherwise required by law or Prudential's articles of association, notices may also be given by advertisement published once in at least one leading UK daily newspaper. There are no limitations on non-resident or foreign shareholders' rights to own Prudential securities or exercise voting rights where such rights are given under English company law.

Winding-up

Prudential is subject to the general insolvency law applicable to UK companies, which is described in Item 4, "Information on the Company—Supervision and Regulation of Prudential—UK Supervision and Regulation—Insurance Regulation—Winding-up Rules".

Board of Directors

Prudential's board of directors manages Prudential's business. However, Prudential's shareholders must approve certain matters, such as changes to the share capital and the election of directors. Directors are appointed subject to Prudential's articles of association. Prudential's board of directors may fill vacancies and appoint additional directors who hold office until the next annual general meeting. The articles of association require that each director must have beneficial ownership of at least 2,500 ordinary shares. The minimum number of directors is eight and the maximum number is sixteen. Prudential may vary these limits by ordinary resolution. There are currently eleven members of Prudential's board of directors.

At every annual general meeting, directors who have been in office for three years and have not sought re-election during that time are required to retire by rotation and are eligible for re-election. Shareholders may remove any director before the end of his or her term of office by ordinary resolution and may appoint another person in his or her place by ordinary resolution. The shareholders may determine the aggregate amount of the non-executive directors' remuneration by ordinary resolution, although they are not entitled to fix the remuneration of the executive directors under their service agreements in this way.

In addition, the executive directors enter into service agreements with Prudential governing their employment relationship. The normal termination notice period under such service agreements for executive directors is twelve months. For newly appointed executive directors, there may be an initial contractual period of up to two years before the twelve-month notice period applies. Non-executive directors do not have service agreements and are not eligible for the annual bonus, membership in Prudential's Restricted Share Plan or pensions.

The directors may exercise all the powers of Prudential to borrow money and to mortgage or charge its undertaking, provided that the outstanding aggregate amount does not, when added to any amount borrowed by subsidiaries of Prudential at any time (exclusive of intra-group borrowings and borrowings by subsidiaries of Prudential that are UK-authorized banks), without the previous sanction of shareholders in a general meeting, exceed a sum equal to the aggregate of the issued capital and reserves of Prudential and of one-tenth of each of the insurance funds (including contingency funds) of each of Prudential's subsidiaries as shown in the last published balance sheets of Prudential and of each of its subsidiaries.

There is no age restriction applicable to directors in Prudential's articles of association. English company law, however, requires that if Prudential appoints or retains a director over the age of 70, special notice stating the director's age must be given in a resolution appointing or re-appointing the director. "Special notice" requires that notice of the intention to move the resolution is given to the company at least 28 days before the meeting at which the resolution is moved.

Disclosure of Interests

Section 198 of the Companies Act 1985 provides that a person (including a company and other legal entities) that acquires an interest of 3% or more in any class of shares constituting an English public company's relevant share capital (e.g., Prudential-issued share capital carrying the right to vote in all circumstances at a general meeting of Prudential) is required to notify Prudential of its interest within two business days following the day on which it acquires that interest. After the 3% level is exceeded, similar notifications must be made in respect of increases or decreases of 1% or more.

For the purposes of the notification obligation, the interest of a person in shares means any kind of interest in shares including interests in any shares:

- in which a spouse, or child or stepchild under the age of 18, is interested,
- in which a corporate body is interested and either (1) that corporate body or its directors are accustomed to act in accordance with that person's directions or instructions or (2) that person is entitled to exercise or control the exercise of one-third or more of the voting power at general meetings of that corporate body, or
- in which another party is interested and the person and that other party are parties to an agreement within the meaning of section 204 of the Companies Act 1985 (a "concert party agreement"). A concert party agreement is one that provides for one or more persons to acquire interests in shares of a particular public company. The interests of one party in shares are attributed to the other(s) if the agreement imposes obligations or restrictions on any one of the parties as to the use, retention or disposal of such interests acquired under such agreement, and any interest in the company's shares is in fact acquired by any of the parties under the agreement.

Some interests (e.g., those held by certain investment fund managers) may be disregarded for the purposes of calculating the 3% threshold, but the obligations of disclosure will still apply where those interests exceed 10% or more of any class of the company's relevant share capital and to increases or decreases of 1% or more thereafter.

Section 212 of the Companies Act 1985 provides that a public company may send a written notice to a person whom the company knows or has reasonable cause to believe to be, or to have been at any time during the three years immediately preceding the date on which the notice is issued, interested in shares constituting the company's "relevant share capital". The notice may require that person to state whether he has an interest in the shares, and in case that person holds or has held an interest in those shares, to give additional information relating to that interest and any other interest in the shares of which that person is aware.

Where a company serves notice under the provisions described above on a person who is or was interested in shares of the company and that person fails to give the company any information required by the notice within the time specified in the notice, the company may apply to an English court for an order directing that the shares in question be subject to restrictions prohibiting, among other things, any transfer of those shares, the taking up of rights in respect of those shares and, other than in liquidation, payments in respect of those shares.

In addition, under Prudential's articles of association, a shareholder may lose the right to vote his shares if he or any other person appearing to be interested in those shares fails to comply within a prescribed period of time with such a request to give the required information with respect to past or present ownership or interests in those shares, or makes a statement in response to such a request which is in the opinion of the directors false or misleading in any material manner. In the case of holders of 0.25% or more of the issued share capital of Prudential (or any class of the share capital), in addition to disenfranchisement, the sanctions that may be applied by Prudential under its articles of association include withholding the right to receive payment of dividends and other monies payable on the relevant shares, and restrictions on transfers of these relevant shares. In the case of holders of less than 0.25% of the issued share capital of Prudential, the sanction is disenfranchisement alone.

A person who fails to fulfill the obligations imposed by Sections 198 and 212 of the Companies Act 1985 described above is subject to criminal penalties.

Permitted Operations

Under clause 4 of Prudential's memorandum of association, Prudential's principal object is to carry on the business of an investment company and, for that purpose to acquire and hold (for itself or as trustee or nominee) securities in any part of the world. Further objects include providing financial, administrative and investment services for the companies in which Prudential is interested. In addition, the memorandum of association provides that each of the paragraphs setting out its objects is not limited by reference to or inference from the terms of any other paragraph but may be construed in its widest sense.

Directors' Interests

A director may not vote, and is not to be counted in the quorum present at a meeting of the board of directors, in respect of any contract or arrangement in which he has an interest that is (together with any interest of any person connected with him), to his knowledge, a material interest, other than an interest in shares or debentures of Prudential. This prohibition does not apply to:

- any contract by a director to underwrite shares or debentures of Prudential,
- any proposal concerning any other company in which a director is interested directly or indirectly, provided that neither he nor anyone connected with him is beneficially interested in 1 per cent or more of any class of the equity share capital of such company (or of any third company through which his interest is derived) or of the voting rights available to shareholders in the relevant company,
- any arrangement for the benefit of the employees of Prudential or any of its subsidiaries that only gives the director benefits also given to employees to which the arrangements relates, or
- any insurance contract that Prudential proposes to maintain or purchase for the benefit of the directors or for the benefit of persons including any of the directors.

These prohibitions may at any time be suspended or relaxed (generally or in respect of any particular contract, arrangement or transaction) by shareholders in a general meeting.

Change of Control

There is no specific provision of Prudential's articles of association that would have an effect of delaying, deferring or preventing a change in control of Prudential and that would operate only with respect to a merger, acquisition or corporate restructuring involving Prudential, or any of its subsidiaries.

Material Contracts

Prudential operates its primary long-term incentive plan, the Restricted Share Plan, to provide rewards to executive directors and most other executive officers contingent upon the achievement of pre-determined returns to shareholders. See Item 6, "Directors, Senior Management and Employees—Compensation—Senior Executives' Long-term Incentive Plans".

Exchange Controls

There are currently no UK laws, decrees or regulations that restrict the export or import of capital, including, but not limited to, foreign exchange controls, or that affect the remittance of dividends or other payments to non-UK residents or to US holders of Prudential's securities except as otherwise set forth below under "—Taxation" in this section.

Taxation

The following is a summary of the material US federal income tax and UK tax considerations related to the acquisition, ownership and disposition of Prudential ordinary shares or ADSs by US resident holders (see below). Except for the summaries below in "—UK Taxation of Capital Gains", "—UK Inheritance Tax" and "—UK Stamp Duty and Stamp Duty Reserve Tax", this discussion applies to you only if you are (1) a resident of the United States for purposes of the UK-US Income Tax Treaty (which we refer to as the "Treaty") and (2) fully eligible for benefits under the Treaty (a "US resident holder"). You generally will be a US resident holder and, therefore, will be entitled to Treaty benefits if you are:

- the beneficial owner of the Prudential ordinary shares or ADSs and of the dividends paid with respect to the Prudential ordinary shares or ADSs,
- an individual resident of the United States, a US corporation, or a partnership, estate or trust to the extent your income is subject to taxation in the United States in your hands or in the hands of your partners or beneficiaries, and
- not also a resident of the United Kingdom for UK tax purposes.

The Treaty benefits discussed below generally are not available to holders who hold Prudential ordinary shares or ADSs in connection with the conduct of business through a permanent establishment, or the performance of personal services through a fixed base, in the United Kingdom. Special rules, including a limitation of benefits provision, may apply in limited circumstances to certain investment or holding companies and tax-exempt entities. This discussion does not discuss the treatment of such holders.

This discussion does not purport to be a comprehensive description of all the tax considerations that may be relevant to any particular holder, including tax considerations that arise from rules of general application or that are generally assumed to be known by investors. In particular, the summary deals only with holders that hold Prudential ordinary shares or ADSs as capital assets and does not address the tax treatment of holders that are subject to special rules, such as US resident holders:

- that are banks, insurance companies, dealers in securities, or persons that elect mark-to-market treatment,
- that hold their Prudential ordinary shares or ADSs as a position in part of a straddle, conversion transaction or other integrated investment composed of one or more other investments,
- who own, directly or indirectly, 10% or more of Prudential's voting shares, or
- whose "functional currency" is not the US dollar.

The summary is based on laws, treaties and regulatory interpretations in effect on the date of this document, all of which are subject to change. In particular, the United States and the United Kingdom have been engaged in negotiations concerning a new income tax treaty. We cannot predict whether or when any new treaty will become effective, or how any such new treaty might affect you.

You should consult your own tax advisers regarding the tax consequences of the acquisition, ownership and disposition of Prudential ordinary shares or ADSs in light of your particular circumstances, including the effect of any state, local or other national laws.

UK Taxation of Dividends

Under current UK tax law, no tax is required to be withheld in the United Kingdom at source from cash dividends paid to US resident holders.

Under the terms of the Treaty, on payment of a dividend by Prudential a US resident holder is, in principle, entitled to receive a payment equal to the amount of the tax credit which is usually available to a UK resident individual, subject to withholding tax. That tax credit is equal to one-ninth of the amount of the dividend, that is, 10% of the aggregate of the dividend and the tax credit. However, in practice US resident holders will not receive any payment from the UK Inland Revenue in respect of the tax credit because the Treaty provides for a UK withholding tax which, although greater than the amount of the UK tax credit, is treated as fully satisfied by an amount equal to that tax credit.

UK Taxation of Capital Gains

Subject to the comments in the following paragraph, a holder of Prudential ordinary shares or ADSs who, for UK tax purposes, is not resident in the United Kingdom (and in the case of an individual also not ordinarily resident in the United Kingdom) will not be liable for UK taxation on capital gains realized on the disposal of his or her Prudential ordinary shares or ADSs unless at the time of the disposal:

- he or she carries on a trade, profession or vocation in the United Kingdom through a branch or agency, and
- the Prudential ordinary shares or ADSs are or have been used, held, or acquired for the purpose of such trade, profession, vocation, branch or agency.

A holder of Prudential ordinary shares or ADSs who (1) is an individual who has ceased to be resident or ordinarily resident for UK tax purposes in the United Kingdom on or after March 17, 1998, (2) continues not to be resident or ordinarily resident in the United Kingdom for a period of less than five tax years and (3) disposes of his or her Prudential ordinary shares or ADSs during that period may also be liable, upon returning to the United Kingdom, for UK tax on capital gains, subject to any available exemption or relief, even though he or she was not resident or ordinarily resident in the United Kingdom at the time of the disposal.

UK Inheritance Tax

Prudential ordinary shares are assets situated in the United Kingdom for the purposes of UK inheritance tax (the equivalent of US estate and gift tax). Prudential ADSs are likely to be treated in the same manner. Subject to the discussion of the UK-US estate tax treaty in the next paragraph, UK inheritance tax may apply if an individual who holds Prudential ordinary shares or ADSs gifts them or dies even if he or she is neither domiciled in the United Kingdom nor deemed to be domiciled there under UK law. For inheritance tax purposes, a transfer of Prudential ordinary shares or ADSs at less than full market value may be treated as a gift for these purposes. Special inheritance tax rules apply (1) to gifts if the donor retains some benefit, (2) to close companies and (3) to trustees of settlements.

However, as a result of the UK-US estate tax treaty, Prudential ordinary shares or ADSs held by an individual who is domiciled in the United States for the purposes of the UK-US estate tax treaty and who is not a UK national will not be subject to UK inheritance tax on that individual's death or on a gift of the Prudential ordinary shares or ADSs unless the ordinary shares or ADSs:

- are part of the business property of a permanent establishment in the United Kingdom, or
- pertain to a fixed base in the United Kingdom used for the performance of independent personal services.

The UK-US estate tax treaty provides a credit mechanism if the Prudential ordinary shares or ADSs are subject to both UK inheritance tax and to US estate and gift tax.

UK Stamp Duty and Stamp Duty Reserve Tax

UK stamp duty is payable on the transfer of Prudential ordinary shares to, and UK stamp duty reserve tax is payable upon the transfer or issue of Prudential ordinary shares to, the depositary of Prudential ordinary shares, or a nominee of the depositary, in exchange for Prudential ADRs representing ADSs. For this purpose, the current rate of stamp duty and stamp duty reserve tax is 1.5% (rounded up, in the case of stamp duty, to the nearest £5). The rate is applied, in each case, to the amount or value of the consideration given for the Prudential ordinary shares or, in some circumstances, to the value of the Prudential ordinary shares at the time of transfer or issue. To the extent that such stamp duty is paid on any such transfer of Prudential ordinary shares, no stamp duty reserve tax should be payable on that transfer.

Provided that the instrument of transfer is not executed in the United Kingdom and remains at all subsequent times outside the United Kingdom, no UK stamp duty will be required to be paid on any transfer of Prudential ADRs representing ADSs. An agreement to transfer Prudential ADRs will not give rise to a liability to stamp duty reserve tax.

The transfer for value of Prudential ordinary shares, as opposed to Prudential ADRs, will generally give rise to a charge to UK stamp duty or stamp duty reserve tax at the rate of 0.5% (rounded up, in the case of stamp duty, to the nearest £5). The rate is applied to the price payable for the relevant Prudential ordinary shares. A transfer of ordinary shares from a nominee to its beneficial owner, including the transfer of underlying Prudential ordinary shares from the depositary to an ADS holder, is subject to stamp duty at the fixed rate of £5 per transfer.

Stamp duty reserve tax is generally the liability of the purchaser and UK stamp duty is usually paid by the purchaser.

US Federal Income Tax Treatment of Prudential ADSs

For US federal income tax purposes and for purposes of the Treaty, US resident holders of Prudential ADSs will be treated as owners of the Prudential ordinary shares represented by those Prudential ADSs.

US Federal Income Tax Treatment of Distributions on Prudential Ordinary Shares or ADSs

In general, a US resident holder will be required to include distributions made with respect to Prudential ordinary shares or ADSs in its gross income. To claim credits for UK withholding tax, a US resident holder must file an election on IRS Form 8833 with its income tax return for the relevant year. A US resident holder that makes the election will be subject to US taxation on the sum of the cash dividend and the associated UK tax credit. In general, it is no longer necessary to provide information to the UK Inland Revenue to establish a holder's entitlement to Treaty benefits in respect of dividends. It is possible that treaty negotiations between the United States and the United Kingdom will affect the existence or amounts of these benefits with respect to dividends paid after a new treaty becomes effective.

If you are a US resident holder who makes the election discussed above, you will be treated as paying UK withholding tax equal to the associated UK tax credit that, subject to certain limitations, you may credit against your US federal income tax liability or take as a deduction against your federal taxable income. Dividends received with respect to the Prudential ordinary shares or ADSs will be treated as foreign source income, which may be relevant in calculating your foreign tax credit limitation. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, dividends paid with respect to the Prudential ordinary shares or ADSs generally will constitute "passive income" or, in the case of certain shareholders, "financial services income". Foreign tax credits will not be allowed for withholding taxes imposed in respect of certain short-term or hedged positions in Prudential ordinary shares or ADSs or in respect of arrangements in which a US holder's expected economic profit, after non-US taxes, is insubstantial. US resident holders should consult their own tax advisers concerning the implications of these rules in light of their particular circumstances.

Dividends paid by Prudential will not be eligible for the dividends received deduction available to some US corporate holders.

The amount of any cash distribution paid in pounds sterling will equal the US dollar value of the distribution, calculated by reference to the exchange rate in effect at the time the dividends are received by the US resident holder or, in the case of Prudential ADSs, by the depositary for the ADSs, regardless of whether the payment is in fact converted into US dollars. If dividends paid in pounds sterling are converted into US dollars on the date of receipt, US resident holders generally should not be required to recognize any foreign currency gain or loss in respect of the dividend income. If the pounds sterling are not converted into US dollars on the date received, however, gain or loss may be recognized upon a subsequent sale or other disposition of the pounds sterling. Foreign currency gain or loss, if any, will be US source ordinary income or loss for US federal income tax purposes.

US Federal Income Tax Treatment of Sales or Exchanges of Prudential Ordinary Shares or ADSs

A US resident holder will generally recognize capital gain or loss for US federal income tax purposes upon the sale or exchange of the Prudential ordinary shares or ADSs, measured by the difference between the amount received and the holder's tax basis in the Prudential ordinary shares or ADSs. Such gain or loss will be long-term capital gain or loss if the US resident holder has held the Prudential ordinary shares or ADSs for more than one year, including the holding period for any American General shares exchanged for such Prudential ordinary shares or ADSs. In the case of non-corporate US resident holders, the maximum tax rate on capital gains arising on the disposition of assets held for more than one year is 20%. In general, any capital gain or loss recognized upon the sale or exchange of Prudential ordinary shares or ADSs will be treated as US source income or loss, as the case may be, for US foreign tax credit purposes. Deduction of capital losses is subject to limitations.

Passive Foreign Investment Company

Prudential believes that it is not and will not become a passive foreign investment company ("PFIC") for US federal income tax purposes. A non-US company is a PFIC in any taxable year in which, after taking into account the income and assets of certain subsidiaries, either (i) at least 75% of its gross income is passive income or (ii) at least 50% of the average value of its assets is attributable to assets that produce or are held to produce passive income. The PFIC statute contains an exception for income "derived in the active conduct of an insurance business by a corporation which is predominantly engaged in an insurance business." This insurance exception is intended to ensure that income derived by a *bona fide* insurance company is not treated as passive income, except for any income attributable to financial reserves in excess of the reasonable needs of the insurance business. Prudential believes it is predominantly engaged in an insurance business and does not have financial reserves in excess of the reasonable needs of its insurance business.

In the event that, contrary to Prudential's belief, Prudential is classified as a PFIC in any year, a US resident holder can avoid the unfavorable rules described below by electing to mark its Prudential ordinary shares or ADSs to market. A US resident holder that makes a mark-to-market election will be required in any year in which Prudential is a PFIC to include as ordinary income the excess of the fair market value of such holder's Prudential ordinary shares or ADSs at year-end over the holder's basis in those shares. The US resident holder's tax basis in the Prudential ordinary shares or ADSs is increased by the amount of such ordinary income recognized by the US resident holder. In addition, any gain recognized upon the sale of Prudential ordinary shares or ADSs will be taxed as ordinary income in the year of sale.

If Prudential is determined to be a PFIC and a US resident holder does not make a mark-to-market election, such holder will be subject to a special tax at ordinary income tax rates on "excess distributions," including certain distributions by Prudential and gain on the sale of Prudential ordinary shares or ADSs. The amount of income tax on excess distributions will be increased by an interest charge to compensate for the tax deferral, calculated as if excess distributions were earned ratably over the period a US resident holder holds its shares. Classification as a PFIC may also have other adverse tax consequences, including in the case of individuals, the denial of a step-up in the basis of a US resident holder's shares at death. US resident holders should consult their own tax adviser regarding the US federal income tax considerations discussed above and the desirability of making a mark-to-market election.

US Information Reporting and Backup Withholding

Under the US tax code, a US resident holder of Prudential ordinary shares or ADSs, may be subject, under certain circumstances, to information reporting and possibly backup withholding at a rate of 31% with respect to dividends and proceeds from the sale or other disposition of Prudential ordinary shares or ADSs, unless the US resident holder provides proof of an applicable exemption or correct taxpayer identification number and otherwise complies with applicable requirements of the backup withholding rules. Any amount withheld under the backup withholding rules is not additional tax and may be refunded or credited against the US resident holder's federal income tax liability, so long as the required information is furnished to the IRS.

Documents on Display

Prudential is subject to the informational requirements of the Securities Exchange Act of 1934 and files information with the Commission. You may read and copy this information at the following location:

Public Reference Room
450 Fifth Street, N.W.
Room 1024
Washington, D.C. 20549

Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Copies of these materials can also be obtained by mail at prescribed rates from the Public Reference Section of the Securities and Exchange Commission, 450 Fifth Street, N.W., Room 1024, Washington, D.C. 20549. Prudential ADSs are listed on the New York Stock Exchange, and consequently, the periodic reports and other information filed by Prudential with the Commission can be inspected at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005. The primary market for Prudential ordinary shares is the London Stock Exchange. As a foreign private issuer, Prudential is not required to make filings with the Commission by electronic means, although it may do so. Any filings we make electronically will be available to the public over the internet at the Commission's web site at http://www.sec.gov.

Item 11. Quantitative and Qualitative Disclosures about Market Risk

RISK MANAGEMENT OF PRUDENTIAL

Overview

The management of exposure to risk is fundamental to Prudential's operations. Prudential's system of internal control is an essential and integral part of the risk management process. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can provide only reasonable and not absolute assurance against material misstatement or loss.

Prudential has established an ongoing process for identifying, managing and reporting risks. During the year, each business area, including group head office, prepares an assessment of its risk exposures and internal control framework. A summary of the findings is considered by the Prudential board's audit committee and the findings and conclusions are reported to the board.

Major Risks

Specific business environmental and operational risks are discussed under Item 5, "Operating and Financial Review and Prospects—Factors Affecting Results of Operations", Item 5, "Operating and Financial Review and Prospects—Introduction of the Euro" and Item 4, "Information on the Company—Business of Prudential—Competition". Risks discussed under Item 4, "Information on the Company—Business of Prudential" include "Business of Prudential—UK Business—Compliance" and "Business of Prudential—UK Business—Implications of Stakeholder Pensions".

Financial Risks

Foreign Exchange Risk

Prudential faces foreign exchange risk, primarily because its reporting currency is pounds sterling, whereas approximately 55% of Prudential's operating profits for the year ended December 31, 2000 came from Prudential's US operations. The exposure relating to the translation of reported earnings is not separately managed although its impact is reduced by interest payments on foreign currency borrowings and by the adoption of average exchange rates for the translation of foreign currency revenues.

Liquidity Risk

Liquidity risk is the risk that Prudential 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 each business seeks to ensure that, even under adverse conditions, Prudential has access to the funds necessary to cover surrenders, withdrawals and maturing liabilities.

In practice, most of Prudential's invested 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.

Credit Risk

Credit risk is the risk that a counterparty or an issuer of securities, which Prudential holds in its asset portfolio, defaults or another party fails to perform according to the terms of the contract. Some of Prudential's businesses, in particular Jackson National Life, Egg, Prudential With-Profits Life Fund and Prudential's UK pension annuity business, hold large amounts of interest rate sensitive investments that contain credit risk on which a certain level of defaults is expected. These expected losses are considered when Prudential determines the crediting rates, deposit rates and premium rates for the products that will be supported by these assets. Certain over-the-counter derivatives contain a credit risk element that is controlled through evaluation of collateral agreements and master netting agreements on interest rate and currency swaps. Prudential is exposed to credit-related losses in the event of non-performance by counterparties. However, the group does not anticipate non-performance.

Prudential provides further analysis of the credit risks in the portfolios backing its insurance business under Item 4, "Information on the Company—Business of Prudential—Investments".

Operational, Compliance and Fiscal Risk

Operational risk can result from a variety of factors, including failure to obtain proper internal authorizations or maintain internal controls, failure to document transactions properly, failure of operational and information security procedures or other procedural failures, computer system or software failures, other equipment failures, fraud, inadequate training or errors by employees. Compliance with internal rules and procedures designed to manage these risks is monitored by Prudential's local management boards.

Adherence to local regulatory requirements is monitored by internal compliance managers who report to the local management boards. The head of Prudential's group compliance function reports directly to the group legal director who submits regular reports to the board of directors. Over the last four years Prudential has upgraded the compliance function in the United Kingdom, which is discussed in Item 4, "Information on the Company—Business of Prudential—UK Business—Compliance".

Compliance risk includes the possibility that transactions may not be enforceable under applicable law or regulation as well as the cost of rectification and fines, and also the possibility that changes in law or regulation could adversely affect Prudential's position. Prudential seeks to minimize compliance risk by seeking to ensure that transactions are properly authorized and by submitting new or unusual transactions to legal advisers for review.

Prudential is exposed to certain fiscal risks arising from changes in tax laws and enforcement policies and in reviews by taxing authorities of tax positions Prudential has taken in recent years. Prudential manages this risk and risks associated with changes in other legislation and regulation through ongoing review by relevant departments of proposed changes to legislation and by membership of relevant trade and professional committees involved in commenting on draft proposals in these areas.

Market Risk

Market risk is the risk that future changes in market prices may make a financial instrument less valuable. The primary market risks Prudential faces are equity risk and interest rate risk because most of its assets are investments that are either equity type investments and subject to equity price risk, or bonds, mortgages or cash deposits, the values of which are subject to interest rate risk. The amount of risk borne by Prudential's shareholders depends on the extent to which its customers share the investment risk through the structure of Prudential's products.

The split of Prudential'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 Prudential has available. The majority of the liabilities have no guaranteed investment returns and have discretionary surrender values (for example variable annuities in the United States or with-profits contracts in the United Kingdom). This mix of liabilities allows Prudential to invest a substantial portion of its investment funds in equity and real estate investments that Prudential believes produce greater returns over the long term. On the other hand Prudential has some liabilities that contain guaranteed returns and allow instant access (for example, interest-sensitive fixed annuities, immediate annuities and fixed rate customer bank deposits), which generally will be supported by fixed income investments.

To reduce investment, interest rate and foreign exchange exposures, and to facilitate efficient investment management, Prudential uses derivative instruments. Prudential's policy is that amounts at risk through derivative contracts are covered by cash or corresponding assets.

Asset/Liability Management

Prudential manages its assets and liabilities locally, in accordance with local regulatory constraints and reflecting the differing types of liabilities Prudential has in each business. As a result of the diversity of products Prudential offers and the different regulatory environments in which it operates, Prudential employs different methods of asset/liability management. Most of Prudential's methods fall into two major categories: cash flow analysis for interest-sensitive business and stochastic modeling/ scenario testing for equity price risk sensitive business.

Stochastic modeling is a form of modeling in which probability distributions are assessed for certain claim, economic and investment-related parameters with specified inter-relationships and correlations among the various parameters. A large number of possible future outcomes are projected by the model and Prudential draws conclusions from the range of outcomes projected. The model may incorporate dynamic decision rules relating to investment policy and bonus additions on with-profits policies.

For businesses that are most sensitive to interest rate changes, such as immediate annuity business, Prudential uses cash flow analysis to create a portfolio of fixed income securities whose value changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. In the United Kingdom, the cash flow analysis is used in Prudential's annuity and banking business while, in the United States, it is used for its interest-sensitive and equity-indexed fixed annuities and stable value products. Perfect matching is not possible for interest-sensitive and equity-indexed fixed annuities because of the nature of the liabilities (which include guaranteed surrender values) and options for pre-payment contained in the assets. The US supervisory authorities require Jackson National Life to calculate projections to test Jackson National Life's ability to run-off its liabilities with assets equal to statutory reserves in a number of specified future economic scenarios. If Jackson National Life is unable to satisfy all of these tests, which are carried out quarterly, then it may be required to establish additional statutory reserves.

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

When presenting regulatory returns to the UK supervisory authorities, the calculation of the statutory liabilities for solvency purposes is required to incorporate a "resilience" reserve that is sufficient to ensure that assets equal to the statutory reserves (including the resilience reserve) remain equal to statutory reserves in the event of certain prescribed changes in equity and real estate prices combined with prescribed rises and falls in interest yields.

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

Use of Derivatives

In the United Kingdom and Asia, Prudential uses derivatives to reduce equity risk, interest rate and currency exposures, and to facilitate efficient investment management. In the United States, Prudential uses derivatives to reduce interest rate risk, to facilitate efficient portfolio management and to match liabilities under equity-indexed policies.

The most widely used derivatives are exchange traded equity and bond futures in the United Kingdom, and exchange traded and over-the-counter interest rate swaps, options to enter into interest rate swaps (referred to as "swaptions"), equity options and credit derivatives in the United States. Prudential uses futures and credit derivatives to undertake asset allocation transactions and uses interest rate swaps and interest rate swaptions to manage interest rate risk. Over-the-counter equity options are used to match liabilities under equity-indexed policies.

It is Prudential's policy that all free-standing derivatives are used to hedge exposures or facilitate efficient portfolio management. Amounts at risk are covered by cash or by corresponding assets.

World-Wide Operations

UK Business

For risk management purposes, the UK asset portfolio is divided into assets that support life and pensions business, annuity business, property and casualty insurance business and banking business. These assets are shown in the tables that appear under Item 4, "Information on the Company—Business of Prudential—Investments—Prudential's Total Investments" and Item 4, "Information on the Company—Business of Prudential—Investments—Investments Relating to UK Insurance Business".

Life and Pensions Business

Prudential's UK life and pensions business comprises both savings and protection business. The investments supporting the protection business are small in value and tend to be fixed maturities reflecting the guaranteed nature of the liabilities.

Prudential's UK insurance investments at December 31, 2000 were £105 billion, of which £ 93 billion was for life and pensions business. Of the £93 billion, £65 billion was for the with-profits business, £15 billion was for the segregated SAIF with-profits fund and £13 billion was for unit-linked business. The absence of guaranteed surrender values and the flexibility given by the operation of the bonus system means that a majority of the investments backing the with-profits business are in equities and real estate with the balance in debt and other fixed income security deposits and loans.

Pensions Annuity Business

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

At December 31, 2000, £10 billion of UK investments was for pension annuity business. These investments are in fixed income securities (including retail price index-linked bonds to match retail price index-linked annuities), loans and deposits and are duration matched with the estimated duration of the liabilities they support.

Property and Casualty Insurance

At December 31, 2000 UK investments supporting the property and casualty insurance were £603 million, of which £445 million was invested in equity securities, and £158 million was invested in fixed income securities and cash. Although the liabilities tend to be of shorter term in nature than the life and pensions business liabilities, stochastic modeling shows that given the amount of capital supporting the business, Prudential's investment policy remains prudent.

Banking Business

The assets of Prudential's UK banking business consist of retail mortgages, credit card receivables and personal loans while the liabilities comprise mostly customer deposits. To the extent that customer deposits exceed loans, mortgages and credit card receivables, the banking business purchases money market assets.

At December 31, 2000, Egg's business had £7,895 million of banking assets and £7,386 million of banking liabilities. The £7,895 million of assets consisted of £3,686 million in fixed maturity investments and £4,209 million of loans and other assets. Of the £4,209 million, £3,974 million was in respect of loans, of which £3,218 million were floating rate and £756 million were fixed rate. Of the liabilities, £7,128 million comprised floating rate retail deposits.

US Business

Jackson National Life's main exposure to market risk is through its exposure to interest rate risk because approximately 82% of its general account investments support interest-sensitive and equity-indexed fixed annuities business and 18% support stable value business. Both of these types of business contain considerable guarantee features and, consequently, require that the assets that support them are primarily fixed income or fixed maturity.

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

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

For risk management purposes, the US general account portfolio is divided substantially into assets that support the interest-sensitive fixed annuity business, the stable value business and the equity-indexed business. Prudential hedges the equity return risk on equity-indexed products by purchasing futures and options on the relevant index.

Asian Business

In Asia, Prudential sells with-profits and unit-linked policies and, although the with-profits business generally has a lower terminal bonus element than in the United Kingdom, the investment portfolios still contain a significant proportion of equities and, to a lesser extent, real estate. The small amount of non-participating business sold is largely backed by fixed income securities or deposits. Prudential does not consider the market risks inherent in its Asian business to be material because the investments of the Asian operation are less than 3% of the group total.

European Business

The investments of Prudential's European business totalled less than 0.5% of the group total at December 31, 2000. The majority of these assets were backing unit-linked liabilities. Prudential does not, therefore, consider the market risks in this business to be material.

Currency of Investments

Prudential's investments are generally held in the same currency as its liabilities and, accordingly, pound sterling liabilities will generally be supported by pound sterling assets and US dollar liabilities will generally be supported by US dollar assets. However, where Prudential believes it is appropriate, it holds some non-domestic equities in the equity portfolios in the belief that this diversifies the overall portfolio risk. As at December 31, 2000, £13 billion of Prudential's total equity securities, excluding those that support unit-linked business, were invested in non-sterling denominated equity investments.

Central Companies Exposures

Prudential is subject to interest rate risk and foreign exchange risk at a central company level because it has fixed maturity debt outstanding that is sterling and dollar denominated. At December 31, 2000, there was £1,200 million of pound sterling central company debt and £368 million, or US$550 million, of US dollar central company debt outstanding.

Sensitivity Analysis

During 2000 total equity securities decreased by £6,453 million while total debt and other fixed income securities increased by £8,511 million. This shift from equities to debt securities reflects Prudential's response to an anticipated decrease in prospective equity returns and was aimed at reducing Prudential's equity risk arising from increased market volatility.

Non-trading Activities

Foreign Exchange Rate Risk

Prudential's primary foreign exchange risk relates to the translation of Jackson National Life's profits into pounds sterling. The potential exposure to a 10% adverse fluctuation in the average US Dollar/Sterling exchange rates for the year ended December 31, 2000 and 1999 would have been a reduction in operating profit of £47 million and £45 million, respectively. Prudential believes this to be a reasonably possible near-term market change.

Interest Rate Risk—Investments

The following table quantifies the estimated reduction in fair value of investments at December 31, 2000 and 1999, resulting from a 100 basis point increase in interest rates at each date. Prudential believes this to be a reasonably possible near-term market change for both UK and US interest rates. Amounts in this table do not include investments backing unit-linked business.

	December 31, 2000		December 31, 1999	
	Fair Value	Estimated Reduction in Fair Value	Fair Value	Estimated Reduction in Fair Value
	(In £ Millions)			
United Kingdom—long-term insurance				
With-profits fund (including PAL)				
Debt and other fixed income securities	**22,941**	**1,834**	17,715	1,417
Loans and other	**1,947**	**26**	2,822	32
Sub-total	**24,888**	**1,860**	20,537	1,449
SAIF with-profits fund				
Debt and other fixed income securities	**4,678**	**329**	3,641	267
Loans and other	**570**	**9**	495	14
Sub-total	**5,248**	**338**	4,136	281
United Kingdom—other insurance				
Debt and other fixed income securities	**652**	**56**	283	7
Loans and other	**254**	**—**	138	—
Sub-total	**906**	**56**	421	7
United Kingdom—banking				
Debt and other fixed income securities	**3,698**	**27**	3,963	23
Loans and other	**3,974**	**—**	4,879	—
Sub-total	**7,672**	**27**	8,842	23
United States—insurance				
Debt and other fixed income securities	**18,242**	**646**	16,112	766
Loans and other	**5,107**	**118**	4,291	118
Sub-total	**23,349**	**764**	20,403	884
United States—banking				
Debt and other fixed income securities	**35**	**1**	15	1
Loans and other	**665**	**11**	73	2
Sub-total	**700**	**12**	88	3
Total	**62,763**	**3,057**	54,427	2,647

A 100 basis point increase in interest rates would have reduced the fair value of the total investments by £3,057 million and £2,647 million at December 31, 2000 and 1999, respectively. The change in estimated reduction in fair value relates primarily to the increase in interest sensitive assets held. The profit impact would be as follows:

- United Kingdom—with-profits fund (including PAL). The reduction in value of £1,860 million and £1,449 million at December 31, 2000 and 1999, respectively, would be borne in the first instance by the fund for future appropriations. Consequently, the impact on profit would be limited to the impact on current and future bonus declarations and the impact to shareholders would be limited to a maximum of one-ninth of the total cost of declared bonuses.

- United Kingdom—SAIF with-profits fund. The reduction of £338 million and £281 million at December 31, 2000 and 1999, respectively, would not impact profit because the profits of this business are wholly attributable to the former Scottish Amicable policyholders.
- United Kingdom—other insurance and banking. The reduction in value of £83 million and £30 million at December 31, 2000 and 1999, respectively, would be directly reflected in profit.
- United States—insurance. For Jackson National Life the profit for the year would have been affected only by the impact on realized gains because fixed income investments are held at amortized cost. Over time such an increase might make the achievement of Jackson National Life's target spread on in-force business slightly harder to achieve but an increase of this order would be unlikely to have a material impact.
- United States—banking. The reduction in value of £12 million and £3 million at December 31, 2000 and 1999, respectively, would be directly reflected in profit.

Interest Rate Risk—Long-term Debt

The table below quantifies the estimated increase in fair value of long-term borrowings at December 31, 2000 and 1999, resulting from a 100 basis point reduction in interest rates at that date. The carrying value of short-term borrowings, which approximates their fair value, would not be materially increased by a 100 basis point reduction in interest rates. Prudential believes this to be a reasonably possible near-term market change for interest rates.

	December 31, 2000			December 31, 1999		
	Carrying Value	Fair Value	Estimated Increase in Fair Value	Carrying Value	Fair Value	Estimated Increase in Fair Value
	(In £ Millions)					
Long-term borrowings						
Central companies						
Guaranteed bonds, US$300 million aggregate principal amount, 8.25% due 2001	**201**	**204**	**2**	186	189	3
Guaranteed floating rate unsecured loan notes, due 2004	**54**	**54**	**—**	168	168	—
Bonds, US$250 million aggregate principal amount, 7.125% due 2005	**167**	**172**	**7**	155	153	7
Guaranteed bonds, £150 million aggregate principal amount, 9.375% due 2007	**150**	**175**	**8**	150	171	10
Bonds, £250 million aggregate principal amount, 5.5% due 2009	**250**	**240**	**16**	250	229	16
Bonds, £300 million aggregate principal amount, 6.875% due 2023	**300**	**337**	**40**	300	316	41
Bonds, £250 million aggregate principal amount, 5.875% due 2029	**250**	**249**	**34**	250	236	35
Total central companies	**1,372**	**1,431**	**107**	1,459	1,462	112
Long-term business						
Guaranteed bonds, £100 million, principal amount, 8.5% undated subordinated	**100**	**119**	**11**	100	115	12
Surplus notes, US$250 million principal amount, 8.15% due 2027	**167**	**167**	**18**	155	154	20
Total long-term business	**267**	**286**	**29**	255	269	32
Total	**1,639**	**1,717**	**136**	1,714	1,731	144

There is no impact on profit at December 31, 2000 and 1999 as a result of this reduction in interest rates because the liabilities are recognized in the financial statements at carrying value.

Equity Market Risk

The following table quantifies the estimated reduction in fair value of investments at December 31, 2000 and 1999, resulting from a 10% decline in the value of equity and real estate values at each date. Prudential believes this to be a reasonably possible near-term market change for both UK and US equities and for both UK and US real estate. Amounts in this table do not include investments backing unit-linked business. Prudential does not hold equity investments in its UK banking portfolio.

	December 31, 2000		December 31, 1999	
	Fair Value	Estimated Reduction in Fair Value	Fair Value	Estimated Reduction in Fair Value
	(In £ Millions)			
United Kingdom—long-term insurance				
With-profits fund (including PAL)				
Equity securities	**40,936**	**4,094**	45,850	4,585
Real estate	**8,607**	**861**	7,188	719
Sub-total	**49,543**	**4,955**	53,038	5,304
SAIF with-profits fund				
Equity securities	**8,477**	**848**	10,187	1,019
Real estate	**1,505**	**150**	1,396	140
Sub-total	**9,982**	**998**	11,583	1,159
United Kingdom—other insurance				
Equity securities	**664**	**66**	672	67
Real estate	**—**	**—**	20	2
United Kingdom—banking				
Real estate	**8**	**1**	—	—
Sub-total	**672**	**67**	582	58
United States—insurance				
Equity securities	**312**	**31**	308	31
Real estate	**53**	**5**	29	—
Sub-total	**365**	**36**	337	31
United States—banking				
Equity securities	**8**	**1**	1	—
Real estate	**4**	**—**	—	—
Sub-total	**12**	**1**	1	—
Total	**60,574**	**6,057**	65,541	6,552

The profit impact at December 31, 2000 and 1999 would be similar to that described under "—Interest Rate Risk—Investments" in this section above, except that for Jackson National Life the decrease in the fair value of equities would reduce profits by the same amount because those investments are held in Prudential's financial statements at market value. The change in estimated reduction in fair value relates primarily to the decrease in equity securities held.

Derivative Contracts

At December 31, 2000 and 1999, the net market value exposure of derivatives was a loss of £2,359 million and a gain of £317 million, respectively. The tables below show the sensitivity of those derivatives, measured in terms of fair value, to equity and real estate market increases and decreases of 10% and to interest rate increases and decreases of 100 basis points. Prudential believes these increases and decreases to be reasonably possible near-term market changes. These exposures will change as a result of ongoing portfolio and risk management activities.

	December 31, 2000			December 31, 1999		
	10% Equity & Real Estate Increase Increase/(decrease) in Fair Value	Fair Value	10% Equity & Real Estate Decrease Increase/(decrease) in Fair Value	10% Equity & Real Estate Increase Increase/(decrease) in Fair Value	Fair Value	10% Equity & Real Estate Decrease Increase/(decrease) in Fair Value
	(In £ Millions)					
United Kingdom—long-term insurance						
With-profits fund (including PAL)	**(188)**	**(1,854)**	**189**	(26)	(52)	26
SAIF with-profits fund	**(54)**	**(557)**	**54**	—	88	—
United Kingdom—other insurance	**(9)**	**(93)**	**7**	(11)	(107)	11
United Kingdom—banking	**—**	**(4)**	**—**	—	14	—
United States—insurance	**93**	**149**	**(88)**	82	374	(80)
Total	**(158)**	**(2,359)**	**162**	45	317	(43)

	December 31, 2000			December 31, 1999		
	100 bp Interest Rate Increase Increase/(decrease) in Fair Value	Fair Value	100 bp Interest Rate Decrease Increase/(decrease) in Fair Value	100 bp Interest Rate Increase Increase/(decrease) in Fair Value	Fair Value	100 bp Interest Rate Decrease Increase/(decrease) in Fair Value
	(In £ Millions)					
United Kingdom—long-term insurance						
With-profits fund (including PAL)	**41**	**(1,854)**	**(49)**	(38)	(52)	38
SAIF with-profits fund	**(1)**	**(557)**	**1**	—	88	—
United Kingdom—other insurance	**—**	**(93)**	**—**	—	(107)	—
United Kingdom—banking	**1**	**(4)**	**(1)**	7	14	(7)
United States—insurance	**168**	**149**	**(159)**	76	374	(51)
Total	**209**	**(2,359)**	**(208)**	45	317	(20)

Long-term Insurance Contracts

At December 31, 2000 and 1999, the aggregate carrying value of technical provisions for long-term insurance contracts, including the technical provisions for linked liabilities, and the fund for future appropriations was £133,684 million and £131,263 million, respectively, and the fair value was £128,871 million and £126,345 million, respectively. The fair value of the technical provisions and fund for future appropriations is sensitive to changes in the fair value of investments in the with-profits fund because increases in the fair value of such investments would result in increases in future bonuses for the with-profits contracts. A 10% increase in the fair value of total investments would result in an increase in the fair value of the technical provisions and the fund for future appropriations of £12,387 million and £12,177 million at December 31, 2000 and 1999, respectively. Prudential believes this to be a reasonably possible near-term market change for the fair value of investments.

Limitations

The above analyses do not consider that assets and liabilities are actively managed and may vary at the time any actual market movement occurs. There are strategies in place to minimize the exposure to market fluctuations. For example, as market indices fluctuate, Prudential would take certain actions including selling investments, changing investment portfolio allocation, and adjusting bonuses credited to policyholders. In addition, these analyses do not consider the effect of market changes on new business generated in the future.

Other limitations on the sensitivity analyses include: the use of hypothetical market movements to demonstrate potential risk that only represent Prudential's view of reasonably possible near-term market changes and that cannot be predicted with any certainty; the assumption that interest rates in all countries move identically; the assumption that all global currencies move in tandem with the US dollar against pound sterling; and the lack of consideration of the inter-relation of interest rates, equity markets and foreign currency exchange rates.

Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

Item 14. Material Modifications to the Rights of Security Holders

None.

Item 18. Financial Statements

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Members of Prudential plc

We have audited the accompanying consolidated balance sheets of Prudential plc and its subsidiaries (the ''Group'') as of December 31, 2000 and 1999 and the related consolidated profit and loss accounts, consolidated statement of total recognized gains and losses, reconciliation of movements in consolidated shareholders' capital and reserves, and consolidated statement of cash flows from general business and shareholders' funds for the two years ended December 31, 2000. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Prudential plc and its subsidiaries at December 31, 2000 and 1999, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles in the United Kingdom.

Accounting principles generally accepted in the United Kingdom vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of accounting principles generally accepted in the United States of America would have affected the results of operations for each of the two years ended and shareholders' equity as of December 31, 2000 and 1999 to the extent summarized in Notes 33 and 34 to the consolidated financial statements.

KPMG Audit Plc
London, England
May 23, 2001

REPORT OF AUDITORS

To the Board of Directors and Members of Prudential plc

We have audited the accompanying consolidated profit and loss account, consolidated statement of total recognized gains and losses, reconciliation of movements in consolidated shareholders' capital and reserves and consolidated statement of cash flows from general business and shareholders' funds of Prudential plc and its subsidiaries (the "Group") for the year ended December 31, 1998. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We have not audited the consolidated financial statements of Prudential plc and its subsidiaries for any period subsequent to December 31, 1998.

We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated profit and loss account, consolidated statement of total recognized gains and losses, reconciliation of movements in consolidated shareholders' capital and reserves and consolidated statement of cash flows from general business and shareholders' funds present fairly, in all material respects, the results of operations and cash flows of Prudential plc and its subsidiaries for the year ended December 31, 1998, in conformity with accounting principles generally accepted in the United Kingdom.

Accounting principles generally accepted in the United Kingdom vary in certain material respects from accounting principles generally accepted in the United States. The application of the latter would have affected the determination of consolidated net income expressed in pounds sterling for the year ended December 31, 1998 to the extent summarized in Notes 33 and 34 to the consolidated financial statements.

PricewaterhouseCoopers
London, England
June 13, 2000, except as to Note 5, which is as of March 26, 2001

Prudential plc and Subsidiaries

Consolidated Profit and Loss Accounts

Years Ended December 31

	2000	1999	1998
	(In £ Millions, Except Per Share Amounts)		
Total			
Gross premiums:			
Continuing operations	**14,506**	14,898	10,950
Acquisitions	**—**	246	—
Discontinued operations	**—**	—	423
Change in unearned premiums	**(9)**	(4)	(2)
Reinsurance premiums ceded	**(121)**	(87)	(85)
Earned premiums, net of reinsurance	**14,376**	15,053	11,286
Claims incurred, net of reinsurance	**(14,213)**	(10,776)	(9,243)
Change in long-term business provision, net of reinsurance	**(6,116)**	(6,745)	(8,378)
Change in technical provisions for linked liabilities, net of reinsurance	**554**	(4,830)	(1,439)
Total change in long-term technical provisions, net of reinsurance	**(5,562)**	(11,575)	(9,817)
Investment returns	**5,046**	17,232	12,612
Investment expenses and charges	**(565)**	(431)	(407)
Net operating expenses	**(1,864)**	(1,736)	(1,422)
Shareholder and policyholder tax attributable to long-term business	**(680)**	(803)	(691)
Add back: Shareholder tax attributable to long-term business	**285**	261	232
Transfers from (to) the fund for future appropriations	**4,027**	(6,325)	(1,609)
Results of investment management and products operations	**90**	60	28
Results of US banking, broker dealer and fund management operations	**7**	(6)	—
Results of UK banking operations	**(155)**	(150)	(77)
Amortization of goodwill	**(84)**	(54)	—
Other income:			
Profit on Egg flotation	**119**	—	—
Profit on business disposals	**120**	—	249
Profit on ordinary activities before shareholder tax	**947**	750	1,141
Shareholder tax on profit on ordinary activities	**(284)**	(208)	(261)
Profit for the financial year before minority interest	**663**	542	880
Minority interest	**25**	—	—
Profit for the financial year	**688**	542	880
Dividends:			
Interim at 8.2p, 7.7p and 7.0p per share, respectively	**(162)**	(150)	(136)
Final at 16.3p, 15.3p and 14.0p per share, respectively	**(322)**	(299)	(271)
Total dividends at 24.5p, 23.0p and 21.0p per share, respectively	**(484)**	(449)	(407)
Retained profit for the financial year	**204**	93	473
Earnings per share:			
Basic (based on 1,959 million, 1,947 million and 1,942 million shares, respectively)	**35.1p**	27.8p	45.3p
Diluted (based on 1,968 million, 1,959 million and 1,955 million shares, respectively)	**35.0p**	27.7p	45.0p

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Profit and Loss Accounts

Years Ended December 31

	2000	1999	1998
	(In £ Millions, Except Per Share Amounts)		
Reconciliation of profit on ordinary activities before shareholder tax to operating profit before amortization of goodwill after tax and minority interests (based on longer term investment returns)			
Profit on ordinary activities before shareholder tax	**947**	750	1,141
Short-term fluctuations in investment returns	**48**	(28)	(24)
Profit on business disposals	**(239)**	—	(249)
Amortization of goodwill	**84**	54	—
Operating profit before amortization of goodwill and before tax based on longer term investment returns	**840**	776	868
Tax on operating profit before amortization of goodwill and before tax (based on longer term investment returns)	**(235)**	(209)	(214)
Minority interest	**12**	—	—
Operating profit before amortization of goodwill after tax and minority interests based on longer term investment returns	**617**	567	654
Earnings per share:			
Operating profit before amortization of goodwill and before tax (based on longer term investment returns) (based on 1,959 million, 1,947 million and 1,942 million shares, respectively)	**42.9p**	39.9p	44.7p
Operating profit before amortization of goodwill after tax and minority interests (based on longer term investment returns) (based on 1,959 million, 1,947 million and 1,942 million shares, respectively)	**31.5p**	29.1p	33.7p

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries
Consolidated Profit and Loss Accounts
Year ended December 31, 2000

	General Business Technical Account	Long-Term Business Technical Account	Non-Technical Account	Total
		(In £ Millions)		
Gross premiums	333	14,173		**14,506**
Change in unearned premiums	(9)			**(9)**
Reinsurance premiums ceded	(12)	(109)		**(121)**
Earned premiums, net of reinsurance	312	14,064		**14,376**
Claims incurred, net of reinsurance	(247)	(13,966)		**(14,213)**
Change in long-term business provision, net of reinsurance		(6,116)		**(6,116)**
Change in technical provisions for linked liabilities, net of reinsurance		554		**554**
Total change in long-term technical provisions, net of reinsurance		(5,562)		**(5,562)**
Investment returns		4,913	133	**5,046**
Allocated investment returns	47	57	(104)	**—**
Investment expenses and charges		(421)	(144)	**(565)**
Net operating expenses	(79)	(1,743)	(42)	**(1,864)**
Shareholder and policyholder tax attributable to long-term business		(680)		**(680)**
Transfers from the fund for future appropriations		4,027		**4,027**
Balance on the technical accounts	33	689		
Add back: Shareholder tax attributable to long-term business		285		**285**
Technical accounts subtotal	33	974		
Profit on insurance activities transferred to the non-technical account	(33)	(974)	1,007	**—**
Results of investment management and product operations			90	**90**
Results of US banking, broker dealer and fund management operations			7	**7**
Results of UK banking operations			(155)	**(155)**
Amortization of goodwill			(84)	**(84)**
Other income:				
Profit on Egg flotation			119	**119**
Profit on business disposals			120	**120**
Profit on ordinary activities before shareholder tax			947	**947**
Shareholder tax on profit on ordinary activities			(284)	**(284)**
Profit for the financial year before minority interests			663	**663**
Minority interests			25	**25**
Profit for the financial year			688	**688**
Balance on the technical accounts analyzed between:				
Continuing operations	33	689		
Discontinued operations	—	—		
Balance on the technical accounts	33	689		

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Profit and Loss Accounts

Year ended December 31, 1999

	General Business Technical Account	Long-Term Business Technical Account	Non-Technical Account	Total
		(In £ Millions)		
Gross premiums:				
Continuing operations	318	14,580		14,898
Acquisitions		246		246
Change in unearned premiums	(4)			(4)
Reinsurance premiums ceded	(12)	(75)		(87)
Earned premiums, net of reinsurance	302	14,751		15,053
Claims incurred, net of reinsurance	(200)	(10,576)		(10,776)
Change in long-term business provision, net of reinsurance		(6,745)		(6,745)
Change in technical provisions for linked liabilities, net of reinsurance		(4,830)		(4,830)
Total change in long-term business provision, net of reinsurance		(11,575)		(11,575)
Investment returns		17,056	176	17,232
Allocated investment returns	40	14	(54)	—
Investment expenses and charges		(299)	(132)	(431)
Net operating expenses	(93)	(1,603)	(40)	(1,736)
Shareholder and policyholder tax attributable to long-term business		(803)		(803)
Transfers to the fund for future appropriations		(6,325)		(6,325)
Balance on the technical accounts	49	640		
Add back: Shareholder tax attributable to long-term business		261		261
Technical accounts subtotal	49	901		
Profit on insurance activities transferred to the non-technical account	(49)	(901)	950	—
Results of investment management and product operations			60	60
Results of US banking, broker dealer and fund management operations			(6)	(6)
Results of UK banking operations			(150)	(150)
Amortization of goodwill			(54)	(54)
Profit on ordinary activities before shareholder tax			750	750
Shareholder tax on profit on ordinary activities			(208)	(208)
Profit for the financial year			542	542
Balance on the technical accounts analyzed between:				
Continuing operations	49	632		
Acquisitions	—	8		
Balance on the technical accounts	49	640		

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries
Consolidated Profit and Loss Accounts
Year Ended December 31, 1998

	General Business Technical Account	Long-Term Business Technical Account	Non-Technical Account	Total
		(In £ Millions)		
Gross premiums:				
Continuing operations	310	10,640		10,950
Discontinued operations		423		423
Change in unearned premiums	(2)			(2)
Reinsurance premiums ceded	(15)	(70)		(85)
Earned premiums, net of reinsurance	293	10,993		11,286
Claims incurred, net of reinsurance	(209)	(9,034)		(9,243)
Change in long-term business provision, net of reinsurance		(8,378)		(8,378)
Change in technical provisions for linked liabilities, net of reinsurance		(1,439)		(1,439)
Total change in long-term business provision, net of reinsurance		(9,817)		(9,817)
Investment returns		12,358	254	12,612
Allocated investment returns	41	(5)	(36)	—
Investment expenses and charges		(297)	(110)	(407)
Net operating expenses	(86)	(1,290)	(46)	(1,422)
Shareholder and policyholder tax attributable to long-term business		(691)		(691)
Transfers to the fund for future appropriations		(1,609)		(1,609)
Balance on the technical accounts	39	608		
Add back: Shareholder tax attributable to long-term business		232		232
Technical accounts subtotal	39	840		
Profit on insurance activities transferred to the non-technical account	(39)	(840)	879	—
Results of investment management and product operations			28	28
Results of UK banking operations			(77)	(77)
Profit on business disposals			249	249
Profit on ordinary activities before shareholder tax			1,141	1,141
Shareholder tax on profit on ordinary activities			(261)	(261)
Profit for the financial year			880	880
Balance on the technical accounts analyzed between:				
Continuing operations	39	601		
Discontinued operations	—	7		
Balance on the technical accounts	39	608		

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Balance Sheets

December 31

Assets	2000	1999
	(In £ Millions)	
Goodwill	**1,611**	1,582
Investments		
Land and buildings	**10,303**	8,763
Investments in associates and other participating interests	**83**	105
Other financial investments	**108,125**	105,778
Total investments	**118,511**	114,646
Assets held to cover linked liabilities	**18,323**	18,643
Reinsurers' share of technical provisions		
Long-term business provision	**353**	215
Claims outstanding and unearned premiums	**67**	61
Technical provisions for linked liabilities	**396**	400
Total reinsurers' share of technical provisions	**816**	676
Debtors		
Debtors arising out of direct insurance operations	**239**	264
Debtors arising out of reinsurance operations	**14**	30
Tax recoverable	**50**	330
Other debtors	**574**	465
Total debtors	**877**	1,089
Other assets		
Banking business assets:		
UK operations (Egg)	**7,895**	8,852
US operations	**708**	93
Tangible assets	**288**	239
Cash at bank and in hand	**1,402**	788
Ordinary shares of parent company	**31**	29
Present value of acquired in-force long-term business	**133**	170
Present value of future margins relating to advances from reinsurers	**148**	55
Total other assets	**10,605**	10,226
Prepayments and accrued income		
Accrued interest and rent	**1,150**	988
Deferred acquisition costs	**2,952**	2,741
Other prepayments and accrued income	**105**	52
Total prepayments and accrued income	**4,207**	3,781
Total assets	**154,950**	150,643

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Balance Sheets

December 31

Shareholders' funds and liabilities	**2000**	**1999**
	(In £ Millions)	
Shareholders' funds		
Ordinary share capital, 5p par value per share, 2,400 million shares authorized; 1,981 million and 1,954 million shares issued and outstanding, respectively	**99**	98
Share premium	**458**	249
Retained profit and loss reserve	**3,463**	3,077
Total shareholders' funds	**4,020**	3,424
Minority interest	**137**	—
Commitments and contingencies		
Fund for future appropriations	**23,267**	27,262
Technical provisions		
Provision for unearned premiums	**175**	164
Long-term business provision	**91,052**	84,476
Claims outstanding	**1,022**	827
Equalization provision	**38**	30
Total technical provisions	**92,287**	85,497
Technical provisions for linked liabilities	**18,719**	19,043
Provisions for other risks and charges		
Deferred tax	**332**	575
Deposits received from reinsurers	**323**	101
Creditors		
Creditors arising out of direct insurance operations	**213**	217
Creditors arising out of reinsurance operations	**21**	18
Debenture loans	**1,585**	1,546
Amounts owed to credit institutions	**909**	1,111
Banking business liabilities:		
UK operations (Egg)	**7,386**	8,436
US operations	**654**	89
Tax payable	**661**	533
Shareholders' dividends accrued	**322**	299
Other	**3,694**	2,112
Total creditors	**15,445**	14,361
Accruals and deferred income	**420**	380
Total shareholders' funds and liabilities	**154,950**	150,643

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Statement of Total Recognized Gains and Losses

Years ended December 31

	2000	1999	1998
	(In £ Millions)		
Profit for the financial year	**688**	542	880
Currency translation adjustment movements	**118**	48	(50)
Total recognized gains	**806**	590	830

Reconciliation of Movements in Consolidated Shareholders' Capital and Reserves

	Number of Ordinary Shares	Ordinary Share Capital	Share Premium	Retained Profit and Loss Reserve	Total
	(Millions)		(In £ Millions)		
January 1, 1998	1,939	97	157	2,529	2,783
Total recognized gains	—	—	—	830	830
Dividends	—	—	—	(407)	(407)
Goodwill reversed on disposals	—	—	—	28	28
New share capital subscribed	10	1	14	—	15
Charge in respect of shares issued to qualifying employee share ownership trust	—	—	50	(50)	—
December 31, 1998	1,949	98	221	2,930	3,249
Total recognized gains	—	—	—	590	590
Dividends	—	—	—	(449)	(449)
New share capital subscribed	5	—	34	—	34
Transfer for shares issued in lieu of cash dividends	—	—	(15)	15	—
Charge in respect of shares issued to qualifying employee share ownership trust	—	—	9	(9)	—
December 31, 1999	1,954	98	249	3,077	3,424
Total recognized gains	**—**	**—**	**—**	**806**	**806**
Dividends	**—**	**—**	**—**	**(484)**	**(484)**
Goodwill reversed on disposals	**—**	**—**	**—**	**90**	**90**
New share capital subscribed:					
Resulting from listing shares on New York Stock Exchange	**17**	**1**	**139**	**—**	**140**
Other	**10**	**—**	**44**	**—**	**44**
Transfer for shares issued in lieu of cash dividends	**—**	**—**	**(20)**	**20**	**—**
Charge in respect of shares issued to qualifying employee share ownership trust	**—**	**—**	**46**	**(46)**	**—**
December 31, 2000	**1,981**	**99**	**458**	**3,463**	**4,020**

The accompanying notes are an integral part of these financial statements

Prudential plc and Subsidiaries

Consolidated Statement of Cash Flows from General Business and Shareholders' Funds

Years ended December 31

	2000	1999	1998
	(In £ Millions)		
Net cash inflow from operating activities before interest and tax	**398**	42	245
Interest paid	**(119)**	(82)	(85)
Taxes recovered (paid)	**138**	62	(138)
Acquisitions and disposals			
Cash (consideration paid) proceeds received including acquisition and disposal costs	**(167)**	(1,984)	345
Proceeds received from flotation of Egg and disposal of associates	**195**	—	—
	28	(1,984)	345
Equity dividends paid	**(461)**	(421)	(382)
Financing			
Issue of debenture loan	**—**	500	300
(Redemption) issue of loan notes	**(114)**	168	—
Movement in credit facility utilized by investment subsidiaries managed by US fund management operations	**(31)**	103	—
Bank loans raised	**—**	—	98
Repayment of debenture loan	**—**	—	(84)
Issue of ordinary share capital	**184**	34	15
Net cash inflow from financing	**39**	805	329
Net cash inflow (outflow)	**23**	(1,578)	314
Net cash inflow (outflow) was invested and (financed) as follows:			
Purchases of portfolio investments:			
Equity securities	**9**	46	40
Debt and other fixed income securities	**146**	62	1,733
Total purchases of portfolio investments	**155**	108	1,773
Sales of portfolio investments:			
Equity securities	**(71)**	(82)	(22)
Debt and other fixed income securities	**(246)**	(1,701)	(1,675)
Total sales of portfolio investments	**(317)**	(1,783)	(1,697)
Net (sales) purchases of portfolio investments	**(162)**	(1,675)	76
Increase in cash and short-term deposits	**185**	97	238
Net cash inflow (outflow)	**23**	(1,578)	314

The accompanying notes are an integral part of these financial statements

1 Nature of Operations

Prudential plc (the "Company") together with its subsidiaries (collectively, the "Group" or "Prudential") is an international financial services group with its principal operations in the United Kingdom ("UK"), the United States ("US"), Asia and continental Europe. The Group operates in the UK through its subsidiaries, primarily The Prudential Assurance Company Limited ("PAC"), Prudential Annuities Limited ("PAL"), Scottish Amicable Life plc ("SAL"), M&G Investment Management Limited ("M&G"), and Egg plc ("Egg"), and in the US through Jackson National Life Insurance Company ("Jackson National Life"). The Group also has operations in Singapore, Hong Kong, Malaysia, Taiwan, Vietnam and other Asian countries. In Europe, the Group has operations in Ireland, France and Germany. Prudential offers a full range of retail financial products and services and fund management services throughout these territories. The retail financial products and services principally include life insurance, pensions, annuities and personal lines of general (property and casualty) insurance as well as collective investments and deposit and mortgage banking services.

2 Basis of Presentation

The consolidated financial statements are prepared in accordance with applicable accounting standards under UK Generally Accepted Accounting Practice ("UK GAAP"), including the Statement of Recommended Practice, "Accounting for Insurance Business", issued in December 1998 by the Association of British Insurers (the "ABI SORP") which is consistently applied for all years presented.

The consolidated financial statements of the Group include the assets, liabilities and profit and loss of the Company and material subsidiaries in which Prudential has a controlling interest. The results of subsidiaries are included in the financial statements from the date acquired to the date of disposal. All intercompany transactions are eliminated on consolidation except for investment management fees charged by M&G to the long-term business fund.

The consolidated profit and loss accounts are comprised of a general business technical account (property and casualty insurance business); a long-term business technical account (life insurance, pension, disability and sickness insurance and annuity business); and a non-technical account. The non-technical account includes the results of the Group's insurance operations. The insurance operations are presented by category of income and expenditure in each respective technical account. The balance (profit on insurance activities for the year) from each of the general and long-term business technical accounts is then included in the non-technical account and combined with the Group's other non-insurance businesses (principally banking and fund management) to determine the consolidated profit for the financial year.

In accordance with Financial Reporting Standard ("FRS") No. 1 (Revised), "Cash Flow Statements", long-term business cash flows are included in the statement of cash flows only to the extent of cash transferred to, and available to meet the obligations of, the Group. The statement of cash flows reflects only the cash flows of general business, the Group's other non-insurance businesses included in the non-technical account and amounts transferred to shareholders' funds from the Group's long-term businesses.

The consolidated financial statements do not represent Prudential's statutory accounts for the purposes of the UK Companies Act 1985. Schedule 9A of the UK Companies Act 1985 prescribes formats for the preparation of the statutory accounts of insurance companies and groups. These

2 Basis of Presentation (Continued)

financial statements are based on the prescribed formats. However, certain reclassifications and presentational changes have been made to the amounts presented for prior periods to conform these periods with the current presentation. Such reclassifications and presentational changes had no effect on the shareholders' funds, profits or cash flows. The Group's external auditors have reported on the 2000, 1999 and 1998 statutory accounts and the accounts have been delivered to the UK Registrar of Companies. The auditors' reports were unqualified and did not contain a statement under Section 237 (2) or (3) of the UK Companies Act 1985.

The consolidated financial statements have been prepared in accordance with UK GAAP and include additional disclosures required under US Generally Accepted Accounting Principles ("US GAAP"). Material differences between UK GAAP and US GAAP affecting Prudential's consolidated profits and shareholders' funds have been summarized in Note 33, "Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles". Condensed consolidated US GAAP financial statements are presented in Note 34.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

The years "2000", "1999" and "1998" refer to the years ended December 31, 2000, 1999 and 1998, respectively.

3 Significant Accounting Policies

Long-term Business

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

Premiums and claims

Premium and annuity considerations for conventional with-profits policies and other protection-type life insurance policies are recognized when due. Premium and annuity considerations for linked policies, unitized with-profits policies and other investment-type policies are recognized when received or, in the case of unitized or unit linked policies, when units are issued. Premiums exclude any taxes or duties assessed based on premiums.

Policy fees are charged to the linked, unitized with-profits and other investment-type policyholders' account balances for mortality, asset management and policy administration. These fees are recognized as revenue when charged against the policyholders' account balances.

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

3 Significant Accounting Policies (Continued)

Deferred acquisition costs

Costs of acquiring new business, principally commissions, marketing and advertising costs and certain other costs associated with policy issuance and underwriting that are not reimbursed by policy charges are specifically identified and capitalized as deferred acquisition costs ("DAC"). The DAC asset is amortized against margins in future revenues on the related insurance policies, to the extent that the amounts are recoverable out of the margins. Recoverability of the unamortized DAC asset is assessed at the time of policy issue, and reviewed if profit margins have declined.

Long-term business provision

Prudential's long-term business written in the UK and Asia is comprised predominantly of life insurance policies under which the policyholders are entitled to participate in the profit of the long-term business supporting these policies. Such policies are called "with-profits" policies. Prudential maintains with-profits funds within the Group's long-term business funds which segregate the assets and liabilities and accumulate the profit and loss activity related to that with-profits business. The amounts accumulated in these with-profits funds are available to provide for future policyholder benefit provisions and for bonuses to be distributed to with-profits policyholders. The bonuses, both annual and terminal, reflect the right of the with-profits policyholders to participate in the financial performance of the with-profits funds. Shareholders' profits with respect to bonuses declared on with-profits business correspond to the shareholders' share of the cost of bonuses as declared by the Board of Directors. The shareholders' share currently represents one-ninth of the cost of bonuses declared for with-profits policies.

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

In the UK and Asia, the future policyholder benefit provisions on conventional with-profits and other protection-type policies are calculated using the net premium method. The net premium reserves are calculated using assumptions for interest, mortality, morbidity, and expense, but without assumptions for withdrawals. These assumptions are determined as prudent best estimates at the date of valuation. Interest rates used in establishing policyholder benefit provisions for conventional with-profits policies in the consolidated financial statements range from 3.00% to 5.35%. The interest rate used in establishing policyholder benefit provisions for pension annuities in the course of payment is adjusted each year and ranged from 5.00% to 6.00%, 4.75% to 6.00% and 4.75% to 5.30% for 2000, 1999 and 1998, respectively. Mortality rates used in establishing policyholder benefit provisions are based on published mortality tables adjusted to reflect actual experience. For unitized with-profits policies, the policyholder benefit provisions are based on the policyholder account balance.

3 Significant Accounting Policies (Continued)

The future policyholder benefit provisions for Jackson National Life's conventional protection-type policies are determined using the net level premium method, with an allowance for surrenders and claims expenses. Rates of interest used in establishing the policyholder benefit provisions range from 6.00% and 9.50%. Mortality assumptions are based on published mortality tables adjusted to reflect actual experience. For investment-type products sold by Jackson National Life, the policyholder benefit provision included within technical provisions in the consolidated balance sheets is the policyholder account balance.

Segregated accounts are established for policyholder business for which policyholder benefits are wholly or partly determined by reference to specific investments or to an investment-related index. The assets and liabilities of this linked business are reported as summary totals in the consolidated balance sheets.

Fund for future appropriations

The fund for future appropriations ("FFA") represents the excess of assets over policyholder liabilities for the Group's with-profits funds. The annual excess of income over expenditures of the with-profits fund, after declaration and attribution of the cost of bonuses to policyholders and shareholders, is transferred to the FFA each year through a charge to the profit and loss account. The balance retained in the FFA represents cumulative retained earnings arising on the with-profits business that has not been allocated to policyholders or shareholders.

Overseas subsidiaries

Results of overseas subsidiaries are determined initially using local GAAP bases of accounting with subsequent adjustments where necessary to comply with the Group's accounting policies.

In the case of Jackson National Life, the US GAAP profit after tax and shareholders' funds are adjusted to comply with UK GAAP in respect of deferred tax. Under UK GAAP, Jackson National Life's fixed income securities are included in the balance sheet at amortized cost (subject to writedowns for other than temporary impairments), whereas under US GAAP, Jackson National Life holds these investments as available-for-sale and at fair value with unrealized gains and losses recorded in the equity section of the balance sheet.

In addition, certain presentational adjustments are made which have no impact on profit after tax. For the purposes of UK reporting, deposits into interest-sensitive products are recorded as premiums, withdrawals and surrenders are included in benefits and claims and the resulting net movement is recorded under other reserve movements within benefits and claims. Benefits and claims also includes interest credited to policyholders in respect of deposit products and fees charged on these policies.

General Insurance

Revenue recognition

Premiums are recognized when risks are assumed. The proportion of premiums written relating to periods of risk beyond any year-end is recorded as an unearned premium provision and subsequently

3 Significant Accounting Policies (Continued)

recognized in earnings proportional to the period of the risk. Premiums are presented gross of commission and exclude any taxes or duties assessed based on premium.

Deferred acquisition costs

Direct and indirect costs associated with the writing of new general insurance policies are deferred and amortized in a manner consistent with the method used for premium recognition described above.

Claims outstanding

Claims incurred include 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 include claims incurred up to, but not paid, at the end of the accounting period, whether or not reported.

An unexpired risks provision is established for any excess of expected claims and deferred acquisition costs over unearned premiums and investment returns. The assessment of expected claims involves consideration of claims experience up to the end of the accounting period. No specific provision is made for major events occurring after this date. In addition to the liability for outstanding claims, an equalization provision has been established in accordance with the requirements of the UK Insurance Companies (Reserves) Act 1995 to reduce the impact of claims volatility. Increases in the equalization provision are limited to certain percentages of premiums written for different lines of business as specified by statute and are charged to claims incurred.

Investment Returns

Investment returns comprise investment income, realized gains and losses and changes in unrealized gains and losses, except for changes in unrealized gains and losses on debt securities held by Jackson National Life which are carried at amortized cost. For debt and other fixed income securities held by Jackson National Life, purchase premiums and discounts are amortized based on the underlying investments' call or maturity dates and this amortization is included in investment returns. Realized gains and losses are recognized in income on the date of sale as determined on a specific identification basis for Jackson National Life and on an average cost basis elsewhere.

Investment returns in respect of long-term business, including that on assets matching solvency capital, are included in the long-term business technical account. Other investment returns are included in the non-technical account.

Investment returns are allocated from the non-technical account to the general business technical account using the longer term rate of return on assets supporting the general business technical account, liabilities and solvency capital. Investment returns are also allocated between the long-term business technical account and the non-technical account for the difference between the actual investment rate of return of the long-term business technical account and the longer term rate of return on the assets backing shareholder financed long-term business (primarily Jackson National Life). The longer term rate of return is based on historical real rates of return and current inflation expectations adjusted for consensus economic and investment forecasts.

3 Significant Accounting Policies (Continued)

Reinsurance

In the normal course of business, the Group seeks to reduce loss exposure arising primarily from catastrophes or other significant adverse events by reinsuring certain levels of risk in various areas of exposure with other insurance companies or reinsurers. An asset or liability is recorded in the consolidated balance sheets representing premiums due to or payments due from reinsurers, and the share of losses recoverable from reinsurers.

Certain reinsurance contracts include significant financing elements. For these contracts the financing liability is recorded as a deposit due to the reinsurer. An asset representing the present value of future margins on the ceded business from which the financing will be repaid is also recognized on the consolidated balance sheets to the extent the reinsurer has assumed the risk that such margins will emerge.

Tax

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

Current tax expense is charged or credited to operations based upon amounts estimated to be payable or recoverable as a result of taxable operations for the current year. To the extent that losses of an individual company are not offset in any one year they can be carried back for one year or carried forward indefinitely to be offset against profits arising from the same company. Deferred tax assets and liabilities generally are recorded based on the differences between financial statement carrying amounts and tax bases of assets and liabilities for those differences which are considered likely to reverse in the foreseeable future and for net operating losses carried forward, if any. Net deferred tax assets are not recognized, except to the extent that they are expected to be recoverable without replacement by equivalent deferred tax assets arising in the future. Deferred tax assets for tax losses carried forward can be recognized if it is assured beyond reasonable doubt that future taxable profits will be sufficient to offset the loss. Deferred tax assets and liabilities are calculated using currently enacted tax rates and laws expected to be applicable when such differences reverse.

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

3 Significant Accounting Policies (Continued)

The balance of the long-term business technical account is net of the total tax attributable to the long-term business. In order to present the profit on long-term insurance activities transferred to the non- technical account on a pre-tax basis, a tax add-back attributable to the shareholders' portion of the tax provision for long-term business, calculated at the effective tax rate of the underlying business, is recorded in the long-term business technical account. This shareholder tax add-back is then included in tax expense on the profit on ordinary activities within the non-technical account.

Stock-based Compensation

The Group offers share award and option plans for certain key employees and a Save As You Earn plan ("SAYE plan") for all UK employees. Compensation costs for non-SAYE plans are recorded over the periods during which share awards or options are earned. Compensation costs are based on the quoted market prices of the shares at the grant date less any amounts paid or payable by employees in respect of the awards. In 2000, 1999 and 1998 shares were issued to a qualifying share ownership trust and costs, representing the difference between the market price at the date of transfer to the trust and amounts payable by employees, were charged directly to shareholders' funds.

Pension Costs

Contributions to the Group's defined benefit plans are calculated and expensed on a basis that spreads the costs over the service lives of participants. Contributions in respect of defined contribution plans are accrued by the Group when incurred.

Land and Buildings

Investments in tenant and Group occupied leasehold and freehold (directly owned) properties are carried at estimated fair value, with changes in estimated fair value included in investment returns. Properties are valued annually either by the Group's qualified surveyors or professional external valuers using The Royal Institution of Chartered Surveyors ("RICS") guidelines. The RICS guidelines apply separate assumptions to the value of the land, buildings, and tenancy associated with each property. Each property is externally valued at least once every three years. The cost of additions and renovations is capitalized and considered when estimating fair value.

In accordance with Statement of Standard Accounting Practice ("SSAP") No. 19, "Accounting for Investment Properties", no depreciation is provided on investment properties as the Group's directors consider that these properties are held for investment purposes, and to depreciate them would not give a true and fair view of the Group's financial position or profit for the financial year.

Investments in Associates and Other Participating Interests

A participating interest is a beneficial equity investment where the Group exercises influence over the investee's operating and financial policies. A participating interest where the Group exercises significant influence over the investee, generally through ownership of twenty percent or more of the entity's voting rights, is considered to be an investment in associate. The Group's investments in associates are recorded at the Group's share of net assets. Goodwill, representing the difference between the consideration paid and the Group's share of net assets at the date of acquisition, relating

3 Significant Accounting Policies (Continued)

to such investments made prior to January 1, 1998, has been written off to shareholders' funds in the year of acquisition. For investments made in associates after January 1, 1998, arising goodwill is reflected as an asset on the consolidated balance sheets and is amortized through the consolidated profit and loss accounts over its estimated useful life, not exceeding 20 years. The carrying value of investments in associates is adjusted each year for the Group's share of the entities' profit or loss. This adjustment is included in investment returns. If an investment in associate is sold during the year, the Group's share of the entity's profit and loss is recorded only up to the date of disposal.

Other participating interests, where significant influence is not exercised, are carried as investments on the consolidated balance sheets at fair value.

Sales of shares by a subsidiary

Sales of previously unissued stock by a subsidiary in an initial public offering are accounted for by recognizing any gain or loss in the Group's consolidated profit and loss account. Such gains or losses are based on the difference between the parent company's carrying value and net proceeds from the initial public offering.

Other Financial Investments

Other financial investments include equity securities; debt and other fixed income securities; mortgage and other loans; loans to policyholders and deposits with credit institutions.

Equity securities and debt and other fixed income securities

Equity securities are carried at fair value. Debt and other fixed income securities are carried at fair value, except for those held by Jackson National Life, which are carried at amortized cost. Fair value is based on quoted market prices for listed securities, and on quotations provided by external fund managers, brokers, independent pricing services or values as determined by management for unlisted securities. Changes in fair value are recognized in investment returns during the year of the change. Debt and other fixed income securities held by Jackson National Life are carried at amortized cost as permitted by paragraph 24 of Schedule 9A to the Companies Act 1985. The amortized cost basis of valuation is appropriate under the provisions of the ABI SORP for Jackson National Life's redeemable fixed income securities as they are held as part of a portfolio of such securities intended to be held on an ongoing basis. Debt and other fixed income securities held by Jackson National Life are reduced to net realizable value for declines in fair value considered to be other than temporary.

Unlisted securities are carried at fair value, which is estimated by management.

Mortgage and other loans

Loans collateralized by mortgages and other unsecured loans are carried at unpaid principal balances, net of unamortized discounts and premiums and an allowance for loan losses, except for loans held by UK insurance operations which are carried at fair value. The allowance for loan losses is maintained at a level considered adequate to absorb losses inherent in the mortgage loan portfolio.

3 Significant Accounting Policies (Continued)

Loans to policyholders

Loans to policyholders are carried at unpaid principal balances and are fully collateralized by the cash value of policies.

Deposits with credit institutions

Deposits with credit institutions comprise items the withdrawal of which are subject to time constraints. These include commercial paper and certificates of deposit and are carried at fair value. Changes in fair value are included in investment returns for the year.

Derivatives

Derivative financial instruments are used to reduce or manage investment, interest rate and currency exposures, to facilitate efficient portfolio management and for investment purposes. The Group's policy is that amounts at risk through derivative transactions are covered by cash or by corresponding assets. Derivative financial instruments used to facilitate efficient portfolio management and for investment purposes are carried at fair value with changes in fair value included in investment returns. For other derivative instruments, various methods of hedge accounting are used and are more fully described in Note 21.

Securities Lending

The Group is party to various securities lending agreements under which securities are loaned to third parties on a short-term basis. The loaned securities are not removed from the Group's consolidated balance sheets, rather, they are retained within the appropriate investment classification. Management's policy is that collateral in excess of 100% of the fair value of securities loaned is required from all securities borrowers and typically consists of cash, debt securities, equity securities, or letters of credit.

In cases where the Group takes possession of the collateral under its securities lending program, the collateral is included in other financial investments in the consolidated balance sheets with a corresponding liability being recorded to recognize the obligation to return such collateral. To further minimize credit risk, the financial condition of counterparties is monitored on a regular basis.

Linked Business Funds

Certain long-term business policies are linked to specific portfolios of assets or a market related index. Such policies provide benefits to policyholders which are wholly or partly determined by reference to the value of or income from specific investments or by reference to fluctuations in the value of an index of investments. The assets supporting the linked policies are maintained in segregated accounts in conformity with applicable laws and regulations. The segregated assets are reported at fair value within assets held to cover linked liabilities on the consolidated balance sheets. The technical provisions for linked liabilities on the consolidated balance sheets are determined based on the fair value of the underlying assets supporting the policies.

3 Significant Accounting Policies (Continued)

Tangible Assets

Tangible assets, principally computer equipment, software development expenditure, and furniture and fixtures, are capitalized and depreciated on a straight-line basis over their estimated useful lives, generally 3 to 10 years. Assets held under finance leases are capitalized at their fair value.

Banking Business Assets and Liabilities

Banking business assets consist primarily of certificates of deposit and short-term deposits with credit institutions carried at fair value and mortgage loans carried at outstanding principal balances, net of allowances for loan losses, which approximates fair value. Loan provisions are recorded for the overall loan portfolio to cover bad debts which have not been separately identified but which are known from experience to be present in the portfolio. For loans in default specific loan provisions are recorded. Changes in loan provisions during the year are included in the consolidated profit and loss accounts.

Liabilities relating to the Group's banking business consist primarily of customer short-term or demand deposits, including interest accrued on the deposits.

Business Acquisitions

Business acquisitions are accounted for by applying the purchase method of accounting, which adjusts the net assets of the acquired company to fair value at the date of purchase. The difference between the fair value of the net assets of the acquired company and the fair value of the consideration given represents goodwill. Revenues and expenses of acquired entities are included in the consolidated profit and loss account from the date of acquisition for the year acquired, gross premiums of the entities are separately presented in the consolidated profit and loss account.

Effective January 1, 1998, goodwill arising from acquisitions is reflected as an asset on the consolidated balance sheets and is amortized through the consolidated profit and loss accounts on a straight-line basis over its estimated useful life, not exceeding 20 years. Prior to January 1, 1998, goodwill relating to acquisitions was charged directly to shareholders' funds. As permitted under the transitional arrangements of FRS No. 10, "Goodwill and Intangible Assets", amounts previously charged to shareholders' funds have not been reinstated as assets. Upon disposal of a business acquired prior to January 1, 1998 to which goodwill relates, the original goodwill balance is charged to the consolidated profit and loss accounts in determining the gain or loss on the sale.

For life insurance company acquisitions, the adjusted net assets include an identifiable intangible asset recorded for the present value of future profits that are expected to emerge from the acquired insurance business. The present value of future profits is calculated using best estimate actuarial assumptions for interest, mortality, persistency and expenses and is amortized over the anticipated lives of the related contracts in the portfolio.

3 Significant Accounting Policies (Continued)

Shareholders' Dividends

Shareholders' dividends are accrued in the period to which they relate regardless of when they are declared. Where scrip dividends are issued, the value of such shares, measured as the amount of the cash dividend alternative, is credited to reserves and is transferred from the share premium account.

Share Premium

Subject to adjustment for scrip dividends, share premium represents the difference between the proceeds received, net of issue costs, on issue of any shares and the nominal value of the shares issued.

Foreign Currency Translation

The profit and loss accounts of foreign subsidiaries are translated to pounds sterling at average exchange rates for the year. Assets and liabilities of foreign subsidiaries are translated at year-end exchange rates. Foreign currency borrowings that have been used to finance or provide a hedge against Group equity investments in overseas subsidiaries, are translated at year-end exchange rates. The impact of these currency translations is recorded as a component of shareholders' funds.

Assets and liabilities denominated in other than functional currencies are converted at closing exchange rates at the balance sheet date with the related foreign currency exchange gains or losses reflected in the profit and loss account for the year.

Discontinued Operations

Discontinued operations consist of all business disposals made during the year, or within three months of the year-end. Prior year amounts are restated for the current year presentation of discontinued operations. Activities of discontinued operations are separately disclosed and included in the Group's consolidated financial statements until the date of disposal.

New UK Accounting Pronouncements

During 2000, three new Accounting Standards were introduced by the Accounting Standards Board, which were pertinent to the Group's consolidated financial statements.

Financial Reporting Standard ("FRS") No. 17, "Retirement benefits" introduced in November 2000 sets out the requirements for accounting for retirement benefits. Its objective is to ensure that the financial statements reflect the fair values of assets and liabilities arising from employers' retirement benefit obligations and related funding and operating costs are recognized in the appropriate accounting period. It also provides for additional disclosure requirements. The disclosure requirements of the Standard are effective for accounting periods ending on or after June 22, 2001. Full adoption is required for accounting years ending on or after June 22, 2002. The disclosure requirements of FRS No. 17 will be adopted by the Group for the year ended December 31, 2001. Management is currently assessing the impact of fully adopting the standard's provisions.

FRS No. 18, "Accounting policies" introduced in December 2000 sets out the principles to be followed in selecting accounting policies and the disclosures needed to help users to understand the accounting policies adopted and how they have been applied. The Standard is effective for accounting

3 Significant Accounting Policies (Continued)

periods ending on or after June 22, 2001, however certain provisions may be deferred until accounting periods ending on or after December 23, 2001. Management believes it is already substantially in compliance with this standard and expects no material impact on the financial position of Prudential.

FRS No. 19, "Deferred tax" introduces a form of "full" provisioning for deferred tax, which replaces the "partial" provision method in SSAP 15. Though the standard requires full provisions for deferred taxes on all temporary differences, differences remain from the requirements of international and US accounting standards. The Standard is effective for accounting years ending on or after January 23, 2002. Management is currently assessing the impact of fully adopting the standard's provision.

4 Supplemental Earnings Information

In accordance with FRS No. 3 "Reporting financial performance" and the ABI SORP, the Group uses operating profit before amortization of goodwill and before tax based on longer term investment returns as a supplemental measure of its results. For purposes of measuring operating profit, investment returns on general business and other shareholder business are based on the expected longer term rate of return. The expected longer term rate of return is based on historical real rates of return and current inflation expectations adjusted for consensus economic and investment forecasts. The only significant general business and shareholder investments that require calculation of an expected longer term rate of return are UK equity securities. For these investments the longer term rate of return is estimated at 8.0%, 8.0% and 8.1% for 2000, 1999 and 1998, respectively. The longer term dividend yield has been assumed to be 2.75%, 2.75% and 2.6% for 2000, 1999 and 1998, respectively. For the purposes of determining the longer term investment returns, the realized gains of Jackson National Life, which invests principally in fixed income securities are averaged over five years and combined with actual interest and dividends. In addition, operating profit excludes gains on business disposals.

For the Group's continuing operations with investment portfolios that are both attributable to shareholders and subject to short-term volatility, a comparison of actual and longer term gains is as follows:

	1996 to 2000	1995 to 1999
	(In £ Millions)	
Actual gains attributable to shareholders:		
Jackson National Life	**70**	160
General business and shareholders	**264**	359
	334	519
Longer term gains credited to operating income:		
Jackson National Life	**152**	179
General business and shareholders	**158**	177
	310	356

In addition, operating profit excludes gains on business disposals and similar exceptional items.

4 Supplemental Earnings Information (Continued)

In accordance with FRS No. 3, "Reporting Financial Performance", the presentation of additional supplemental earnings per share information is permitted provided the earnings basis used is applied consistently over time and is reconciled to consolidated profit for the financial year. In determining operating profit as presented in the consolidated financial statements, the Group has used the expected longer term investment return excluding exceptional items as management believe that such presentation better reflects the Group's underlying financial performance.

The Group's supplemental measure of its results and reconciliation of operating profit before amortization of goodwill based on longer term investment results to profit on ordinary activities, including the related basic earnings per share amounts, are as follows:

	Before Tax	Tax	Minority Interest	Net	Basic Earnings Per Share
	(In £ Millions, Except Per Share Amounts)				
2000					
Operating profit before amortization of goodwill based on longer term investment returns	**840**	**(235)**	**12**	**617**	**31.5 p**
Amortization of goodwill	**(84)**	**—**	**—**	**(84)**	**(4.3)p**
Short-term fluctuations in investment returns*	**(48)**	**8**	**13**	**(27)**	**(1.4)p**
Profit on Egg flotation and business disposals	**239**	**(57)**	**—**	**182**	**9.3 p**
Profit on ordinary activities	**947**	**(284)**	**25**	**688**	**35.1 p**
1999					
Operating profit before amortization of goodwill based on longer term investment returns	776	(209)	—	567	29.1 p
Amortization of goodwill	(54)	—	—	(54)	(2.8)p
Short-term fluctuations in investment returns	28	16	—	44	2.3 p
Adjustment in respect of profit on business disposals relating to tax paid on prior year disposals	—	(15)	—	(15)	(0.8)p
Profit on ordinary activities	750	(208)	—	542	27.8 p
1998					
Operating profit based on longer term investment	868	(214)	—	654	33.7 p
Short-term fluctuations in investment returns	24	(9)	—	15	0.8 p
Profit on business disposals	249	(38)	—	211	10.8 p
Profit on ordinary activities	1,141	(261)	—	880	45.3

*The adjustment from post-tax longer term investment returns to post-tax actual investment returns includes investment return that is attributable to external equity investors in two investment funds of the US fund management operation. These two funds are consolidated as if they were subsidiaries as a result of the Group's effective control of the funds in accordance with FRS 5, "Reporting the Substance of Transactions," but have no net impact on pre-tax or post-tax operating profit. Total profit, before and after tax, incorporating the adjustment from long-term investment returns to actual investment returns, includes losses of £13 million attributable to these minority interests.

For the year ended December 31, 1998, the Group had no goodwill amortization expense.

4 Supplemental Earnings Information (Continued)

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

Number of shares	December 31 2000	1999	1998
		(Millions)	
Weighted average shares for basic earnings per share	**1,959**	1,947	1,942
Shares under option at end of year	**20**	26	28
Shares held by qualifying employee share ownership trust	**(2)**	(1)	(4)
Assumed treasury share purchases at average fair value from proceeds of assumed option exercise	**(9)**	(13)	(11)
Weighted average shares for diluted earnings per share	**1,968**	1,959	1,955

5 Segment Analysis

The Group has eight reportable business segments: Prudential Insurance Services, Prudential Financial Services, Prudential Intermediary Business, M&G and Egg, which are all located in the UK (collectively, "UK Operations"), US Operations, Asian Operations and European Operations. The business segments are determined first by the territories in which the Group conducts business, which are the United Kingdom, the United States, Asia and Europe. UK Operations are further defined by distribution networks. UK Operations include long-term life insurance business, general (property and casualty) insurance, banking and fund management activities. The Asian operations include life insurance business and fund management activities. The US and European operations are engaged principally in life insurance activities.

During 2000, Prudential restructured its UK insurance operations, which resulted in three new reportable segments: Prudential Insurance Services, Prudential Financial Services, and Prudential Intermediary Business. The new reportable segments and their relation to the previously reported segments is as follows:

- Prudential Insurance Services comprises the product manufacturing of service operations for the majority of the Prudential branded long-term and general insurance products. Previously, these activities were part of the Prudential Retail Services and Annuities business unit.
- Prudential Financial Services comprises the company's salesforce distribution channel and its group pension product manufacturing, marketing and service operations. It comprises the combination of two prior business units namely Prudential Retail, formerly part of Prudential Retail Financial Services, and Group Pensions.
- Prudential Intermediary Business, which is responsible for marketing and distribution of products via the Independent Financial Advisor channel. Prudential Intermediary Business comprises the combination of two prior business units, namely Retail IFA and Prudential Annuities.

The accounting policies of the segments are the same as those used in the Group's consolidated accounts described in Note 3, applied on a consistent basis for all periods presented, except that revenue reported by reportable segments includes deposits to unit trusts and other similar products, which are excluded from earned premiums in the consolidated profit and loss accounts.

The performance measure of reportable segments utilized by management is operating profit before amortization of goodwill and before tax. Operating profit before amortization of goodwill and

5 Segment Analysis (Continued)

before tax includes investment gains on investments attributable to shareholders based on the longer term return.

Certain amounts relating to the UK insurance operations presented in the following tables have been reclassified from the previously issued financial statements to reflect the new business units.

Analysis of Operating Profit before amortization of goodwill and before tax

The following table presents operating profit before amortization of goodwill and before tax (based on longer term investment returns) by segment:

	2000	1999	1998
	(In £ Millions)		
UK Operations			
Prudential Insurance Services	**346**	378	333
Prudential Financial Services	**28**	36	22
Prudential Intermediary Business	**127**	101	88
M&G	**125**	87	28
Egg	**(155)**	(150)	(77)
Total UK Operations	**471**	452	394
US Operations			
Jackson National Life	**459**	457	411
Banking, broker dealer and fund management	**7**	(6)	—
Total US Operations	**466**	451	411
Asian Operations			
Long-term business and investment products	**39**	27	23
Development expenses	**(17)**	(12)	(10)
Total Asian Operations	**22**	15	13
European Operations			
Long-term business	**8**	6	4
Development expenses	**(18)**	—	—
Total European Operations	**(10)**	6	4
Operating profit of reportable segments	**949**	924	822
Restructuring costs			
UK Insurance Operations	**—**	(53)	—
M&G	**—**	(17)	—
Total restructuring costs	**—**	(70)	—
Group activities	**(109)**	(78)	38
Total continuing operations	**840**	776	860
Discontinued operations	**—**	—	8
Operating profit before amortization of goodwill and before tax (based on the longer term investment returns)	**840**	776	868

5 Segment Analysis (Continued)

Analysis of Revenue by Reportable Segment and Geographical Region

The following table presents revenue by reportable segment and geographical region:

	2000	1999	1998
	(In £ Millions)		
UK Operations			
Gross premiums:			
Prudential Insurance Services:			
Long-term business	**2,321**	2,806	2,516
General business	**333**	318	310
Prudential Financial Services	**1,312**	1,281	1,137
Prudential Intermediary Business	**3,836**	5,244	3,164
M&G:			
Long-term business	**239**	223	—
Investment products	**1,328**	725	297
Total gross premiums(2)	**9,369**	10,597	7,424
Reinsurance premiums ceded	**(30)**	(11)	(18)
Change in unearned premiums	**(9)**	(4)	(2)
Investment returns(1)	**3,356**	14,895	10,693
Revenue from banking and investment management and products operations	**311**	192	80
Total UK Operations	**12,997**	25,669	18,177
US Operations			
Gross premiums	**5,223**	4,449	3,237
Reinsurance premiums ceded	**(70)**	(61)	(53)
Investment returns	**1,715**	1,609	1,470
Revenue from banking, broker-dealer and fund management operations	**169**	7	—
Total US Operations	**7,037**	6,004	4,654
Asian Operations			
Gross premiums:(2)			
Long term business	**1,076**	655	460
Investment products	**2,259**	582	72
Reinsurance premiums ceded	**(11)**	(7)	(6)
Investment returns	**(138)**	512	42
Revenue from investment management and products operations	**10**	—	—
Total Asian Operations	**3,196**	1,742	568
European Operations			
Gross premiums	**166**	168	126
Reinsurance premiums ceded	**(10)**	(8)	(5)
Investment returns	**8**	71	34
Total European Operations	**164**	231	155
Total revenue for reportable segments	**23,394**	33,646	23,554
Discontinued Operations and Other			
Gross premiums	**—**	—	456
Reinsurance premiums ceded			(3)
Investment returns	**105**	145	373
Total Discontinued Operations and Other(3)	**105**	145	826
Total revenue	**23,499**	33,791	24,380
Represented by:			
Earned premiums	**14,376**	15,053	11,286
Investment returns	**5,046**	17,232	12,612
Revenue from banking, broker-dealer, investment/fund management and product operations	**490**	199	80
Gross premiums from investment products(2)	**3,587**	1,307	402
Total revenue	**23,499**	33,791	24,380

(1) Investment returns in respect of UK insurance operations are not allocated across the UK segments.

(2) Gross premiums presented by reportable segments include deposits to unit trusts and other similar products (gross premiums from investment products), which are excluded from earned premiums in the consolidated profit and loss accounts.

(3) Discontinued operations in 2000 and 1999 relate solely to certain property and casualty business which has been run-off since 1993. Discontinued operations in 1998 also include the revenue from the disposal of the Group's Australasian businesses up to the date of disposal.

5 Segment Analysis (Continued)

Other Segment Information

Selected information is provided below on a segment basis. In cases where information is not allocated to a segment, amounts are provided by geographical region.

	2000	1999	1998
	(In £ Millions)		
Claims incurred, net of reinsurance			
UK Operations:			
Prudential Insurance Services	**3,383**	3,028	2,698
Prudential Financial Services	**1,276**	858	587
Prudential Intermediary Business	**3,102**	2,681	2,528
M&G	**1,242**	344	—
US Operations	**4,866**	3,601	2,528
Asian Operations	**309**	231	179
European Operations	**33**	26	32
Total continuing operations	**14,211**	10,769	8,552
Discontinued operations(1)	**2**	7	691
Total claims incurred, net of reinsurance	**14,213**	10,776	9,243
Change in long-term technical provision, net of reinsurance			
UK Operations:			
Prudential Insurance Services	**931**	2,575	2,526
Prudential Financial Services	**515**	1,304	1,075
Prudential Intermediary Business	**3,438**	5,049	4,611
M&G	**(1,172)**	153	—
US Operations	**1,305**	1,758	1,574
Asian Operations	**481**	579	165
European Operations	**64**	157	88
Total continuing operations	**5,562**	11,575	10,039
Discontinued operations(1)	**—**	—	(222)
Total change in long-term technical provision, net of reinsurance	**5,562**	11,575	9,817
Investment expenses and charges and net operating expenses			
UK Operations:			
Prudential Insurance Services	**868**	999	764
Prudential Financial Services	**118**	126	115
Prudential Intermediary Business	**470**	388	360
M&G	**119**	78	—
US Operations	**298**	212	212
Asian Operations	**288**	146	102
European Operations	**75**	43	31
Corporate expenditure not allocated to segments	**42**	40	46
Shareholders' interest payable	**143**	131	105
Total continuing operations	**2,421**	2,163	1,735
Discontinued operations(1)	**8**	4	94
Total investment expenses and charges and net operating expenses	**2,429**	2,167	1,829

(1) Discontinued operations in 2000 and 1999 relate solely to certain property and casualty business which has been run-off since 1993. Discontinued operations in 1998 also include amounts from the disposal of the Group's Australasian businesses up to the date of disposal.

5 Segment Analysis (Continued)

Assets

The assets of the UK Operations are managed and analyzed for UK Operations taken as a whole and are not allocated among the UK segments, except for banking business assets. An analysis of assets by geographical region is presented below:

	UK and Europe	US	Asia	Total
		(In £ Millions)		
December 31, 2000				
Insurance and investment operations:				
Investments	**91,610**	**24,136**	**2,765**	**118,511**
Deferred acquisition costs	**1,550**	**1,264**	**138**	**2,952**
Linked assets	**13,940**	**3,739**	**644**	**18,323**
Other	**5,415**	**892**	**254**	**6,561**
	112,515	**30,031**	**3,801**	**146,347**
Banking business assets	**7,895**	**708**	**—**	**8,603**
Total assets	**120,410**	**30,739**	**3,801**	**154,950**
December 31, 1999				
Insurance and investment operations:				
Investments	90,574	21,824	2,248	114,646
Deferred acquisition costs	1,607	1,043	91	2,741
Linked assets	15,256	2,806	581	18,643
Other	4,810	671	187	5,668
	112,247	26,344	3,107	141,698
Banking business assets	8,852	93	—	8,945
Total assets	121,099	26,437	3,107	150,643

5 Segment Analysis (Continued)

Analysis of the Fund for Future Appropriations ("FFA") and Net Technical Provisions

A segment analysis of the FFA and technical provisions (net of reinsurers' share) is set out below. This analysis includes liabilities and the FFA as management believes it provides a more useful indication of the assets supporting the business than would be shown through analyzing net assets.

	December 31	
	2000	**1999**
	(In £ Millions)	
Group Companies, excluding Scottish Amicable Insurance Fund (SAIF)(1)	**20,185**	23,563
SAIF(2)	**3,082**	3,699
Fund for future appropriations	**23,267**	27,262
UK Operations:		
Technical provisions (net of reinsurers' share):		
Prudential Insurance Services	**30,301**	29,220
Prudential Financial Services	**4,140**	3,437
Prudential Intermediary Business	**34,943**	31,464
M&G	**—**	81
UK technical provisions (net of reinsurers' share)	**69,384**	64,202
UK linked liabilities (net of reinsurers' share):		
Prudential Insurance Services	**318**	368
Prudential Financial Services	**4,030**	4,218
Prudential Intermediary Business	**9,011**	6,016
M&G	**—**	4,132
UK linked liabilities (net of reinsurers' share)	**13,359**	14,734
US Operations	**23,585**	21,783
Asian Operations	**3,269**	2,616
European Operations	**593**	529
Total	**133,457**	131,126

(1) Principally the with-profits fund.

(2) Closed to new business and wholly attributable, but not allocated, to policyholders.

5 Segment Analysis (Continued)

Analysis of Shareholders' Funds

An analysis of shareholders' funds by segment follows:

	December 31	
	2000	1999
	(In £ Millions)	
UK Operations*	**1,303**	1,283
US Operations (principally Jackson National Life)	**2,326**	1,911
Asian Operations	**315**	217
European Operations	**60**	53
Other Operations**	**16**	(40)
Total shareholders' funds	**4,020**	3,424

* The 1999 amount for UK Operations has been restated to £1,283 from £1,145. The restatement has been made to be consistent with a change in allocation of capital and related investments made in January 2000.

** Other Operations represent operations retained centrally and not allocated to a business segment.

6 General Business

The Group's general business is primarily written in the UK.

	Continuing Operations	Discontinued Operations	Group Total
		(In £ Millions)	
Underwriting results			
2000	**(3)**	**(11)**	**(14)**
1999:			
Excluding restructuring costs	32	(11)	21
Restructuring costs	(12)	—	(12)
Inclusive of restructuring costs	20	(11)	9
1998	12	(14)	(2)
Investment returns			
2000	**36**	**11**	**47**
1999	29	11	40
1998	27	14	41
Operating profit			
2000	**33**	**—**	**33**
1999:			
Excluding restructuring costs	61	—	61
Restructuring costs	(12)	—	(12)
Inclusive of restructuring costs	49	—	49
1998	39	—	39

6 General Business (Continued)

The general business reserves for insurance claims and claims expenses and changes thereto are as follows:

	December 31	
	2000	**1999**
	(In £ Millions)	
General business technical provision for claims outstanding and equalization provision, beginning of year	**394**	418
Less: Reinsurers' share of claims outstanding	**(44)**	(52)
Net provisions, beginning of year	**350**	366
Effect of changes in foreign currency exchange rates	**6**	2
Claims incurred:		
Attributable to the current year	**232**	186
Attributable to prior years	**7**	7
Change in equalization provision	**8**	7
Total claims incurred, net of reinsurance	**247**	200
Payments, net of reinsurance:		
Attributable to the current year	**(117)**	(117)
Attributable to prior years	**(91)**	(101)
Total payments, net of reinsurance	**(208)**	(218)
Net provisions, end of year	**395**	350
Reinsurers' share of claims outstanding	**45**	44
General business technical provision for claims outstanding and equalization provision, end of year	**440**	394
Claims outstanding on long-term business	**620**	463
Total claims outstanding and equalization provision	**1,060**	857

7 Long-Term Business Provisions, Premiums, and Policyholders' Bonuses

Long-term Business Provision and Technical Provisions for Linked Liabilities

The following table provides an analysis of technical provisions between with-profits and non-participating business:

	December 31	
	2000	**1999**
SAIF[1]	**11%**	11%
Financed by with-profits funds:		
With-profits business	**43%**	42%
Non-participating[2]	**8%**	8%
Shareholder financed business:		
Non-participating	**21%**	21%
Linked business	**17%**	18%
Total	**100%**	100%

Gross premiums

The following table provides an analysis of gross premiums between with-profits and non-participating business:

	2000	**1999**	**1998**
SAIF[1]	**4%**	4%	7%
Financed by with-profits funds:			
With-profits business	**32%**	37%	44%
Non-participating[2]	**4%**	10%	4%
Linked business	**1%**	1%	2%
Shareholder financed business:			
Non-participating	**45%**	36%	31%
Linked business	**14%**	12%	12%
Total	**100%**	100%	100%

(1) SAIF is the Scottish Amicable Insurance Fund, a separate sub-fund established within PAC's long-term business fund. This sub-fund contains all the with-profits business and all other pension businesses that were transferred to PAC from the Scottish Amicable Life Assurance Society in 1997. No new business is written in the sub-fund.

(2) Annuity business written by a subsidiary of the PAC with-profits fund, Prudential Annuities Limited, and non-participating and linked business purchased from the Scottish Amicable Life Assurance Society prior to the transfer to PAC, written in a separate sub-fund of the PAC with-profits fund.

Bonuses declared for the year in respect of the Group's with-profits business are included in the change in long-term business provision or, where the policy is no longer in-force, in claims incurred.

7 Long-Term Business Provisions, Premiums, and Policyholders' Bonuses (Continued)

The total cost of policyholders' bonuses was £3,454 million, £3,395 million and £3,056 million for the years ended December 31, 2000, 1999 and 1998, respectively.

8 Investment Returns

The sources of investment returns are as follows:

	Long-Term Business			Non-Technical Account		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
	(In £ Millions)					
Investment income from:						
Equity securities	**1,258**	1,438	1,511	**10**	13	16
Debt and other fixed income securities	**3,252**	2,689	2,541	**12**	43	104
Land and buildings	**716**	617	567	**—**	—	—
Mortgage and other loans	**266**	217	119	**—**	—	—
Linked assets	**395**	402	404	**—**	—	—
Other	**369**	368	326	**86**	44	89
Total investment income	**6,256**	5,731	5,468	**108**	100	209
Net realized gains (losses) from:						
Equity securities	**5,974**	4,304	2,314	**48**	64	17
Debt and other fixed income securities	**550**	214	464	**(17)**	(2)	(2)
Land and buildings	**143**	103	32	**—**	—	—
Linked assets	**909**	434	141	**—**	—	—
Other	**3**	31	97	**1**	—	—
Total realized gains	**7,579**	5,086	3,048	**32**	62	15
Net unrealized (losses) gains from:						
Equity securities	**(7,131)**	5,997	1,865	**(15)**	27	24
Debt and other fixed income securities	**(726)**	(1,558)	1,251	**9**	(13)	6
Land and buildings	**369**	627	253	**—**	—	—
Linked assets	**(1,522)**	1,172	410	**—**	—	—
Other	**88**	1	63	**(1)**	—	—
Total net unrealized (losses) gains	**(8,922)**	6,239	3,842	**(7)**	14	30
Total investment returns	**4,913**	17,056	12,358	**133**	176	254

9 Net Operating Expenses

A summary of operating expenses is shown below:

	Long-term Business			General Business		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
	(In £ Millions)					
Policy acquisition costs for the year	**1,126**	928	874	**31**	26	29
Change in deferred acquisition costs	**(119)**	(88)	(126)	**(1)**	—	5
Administrative expenses	**660**	719	495	**49**	68	55
Reinsurance commissions and profit participation	**11**	22	30	**—**	(1)	(3)
Amortization of present value of acquired in-force business	**65**	22	17			
Total	**1,743**	1,603	1,290	**79**	93	86

Included within net operating expenses in the consolidated profit and loss accounts are corporate expenditures relating to the non-technical account of £42 million, £40 million and £46 million for 2000, 1999 and 1998, respectively.

Administrative expenses for 1999 include £48 million (long-term business) and £12 million (general business) of restructuring costs charged to shareholders' funds. There were no restructuring charges charged to shareholders' funds in 2000. See note 31 for further information regarding the restructuring provision.

Prudential also paid fees to audit firms as follows:

	KPMG 2000	KPMG 1999	PwC 1999	Total 1999	PwC 1998
	(In £ Millions)				
Statutory audit fees	**1.9**	1.2	0.4	1.6	2.0
Audit related services:					
Regulatory returns and achieved profits basis audits	**0.4**	0.2	0.1	0.3	0.5
Tax and accounting advice	**0.3**	0.2	0.4	0.6	0.5
US GAAP work including work in connection with the listing of shares on the New York Stock Exchange	**0.7**	—	—	—	—
Acquisitions	**0.3**	—	—	—	—
Consultancy services	**18.3**	5.1	6.0	11.1	7.7
Total	**21.9**	6.7	6.9	13.6	10.7

In October 1999 KPMG Audit Plc (KPMG) replaced PricewaterhouseCoopers (PwC) as auditors of Prudential with the exception of companies managed by Egg which changed auditors in 2000. KPMG were already engaged in performing regulatory reviews prior to their appointment as auditors of the Group.

Statutory audit fees include £0.1 million for 2000, 1999 and 1998 in respect of the parent company Audit related and consultancy fees payable to KPMG include £18.8 million and £5.1 million for 2000 and 1999, respectively, for work performed in the UK. PwC audit and consultancy fees for 1998 for work performed in the UK were £8.2 million.

10 Investment Expenses and Charges

A summary of investment expenses and charges is shown below:

	Long-term Business			Non-Technical Account		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
			(In £ Millions)			
Interest on bank loans and overdrafts	**33**	29	29	**3**	2	3
Interest on other loans	**116**	26	9	**140**	129	102
Total interest expense	**149**	55	38	**143**	131	105
Investment management expenses	**272**	244	259	**1**	1	5
Total	**421**	299	297	**144**	132	110

Investment management expenses of the long-term business include management fees charged by M&G Investment Managers and fees paid to external property managers.

Long-term business interest expense includes £102 million, £18 million, and nil for 2000, 1999, and 1998, respectively, in respect of funding arrangements entered into by Jackson National Life. Interest expense in the non-technical account includes £12 million, £9 million, and £8 million for 2000, 1999, and 1998, respectively, in respect of non-recourse borrowings of investment funds of the US fund management operation, which are consolidated as if they were subsidiaries as a result fo the Group's effective control of the funds. Long-term business investment management expenses include management fees charged by M&G and fees paid to external property managers.

11 Goodwill

	December 31		
	2000	**1999**	**1998**
	(In £ Millions)		
Balance at beginning of year	**1,582**	59	—
Adjustment in respect of 1999 acquisitions	**5**	—	—
Additions:			
M&G Group plc	**—**	1,527	—
Taiwanese operations	**67**	50	—
US banking and broker dealer operations	**63**	—	—
Prudential Assurance Malaysia Berhad	**—**	—	59
Disposal of M&G institutional fund management business	**(22)**	—	—
Amortization expense charged to the profit and loss account	**(84)**	(54)	—
Balance at end of year	**1,611**	1,582	59

The cumulative goodwill charged against the Group's reserves arising on acquisitions of subsidiary undertakings prior to 1998 that are still owned by the Group amounted to £589 million at December 31, 2000 and £679 million as of both December 31, 1999 and 1998.

The adjustment in 2000 in respect of 1999 acquisitions of £5 million relates to the acquisition of banking operations by Jackson National Life.

12 Tax

The tax expense calculated on the long-term business fund is attributable to shareholders and to policyholders. The shareholders' portion of tax is determined using the effective tax rate of the underlying business applied to the profits transferred to the non-technical account. A summary of the tax expense attributable to shareholders' profits and the long-term business technical account in the consolidated profit and loss accounts is shown below:

	Attributable to Shareholders' Profits			Attributable to Long-Term Funds		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
	(In £ Millions)					
UK tax expense (benefit):						
Current	**145**	117	133	**780**	534	458
Deferred	**22**	(34)	3	**(271)**	101	73
Total UK tax expense	**167**	83	136	**509**	635	531
Foreign tax expense:						
Current	**116**	125	125	**170**	168	159
Deferred	**1**	—	—	**1**	—	1
Total foreign tax expense	**117**	125	125	**171**	168	160
Total tax expense	**284**	208	261	**680**	803	691

An analysis of the tax expense by the nature of the expense attributable to shareholders' profits and long-term funds is as follows:

	Attributable to Shareholders' Profits			Attributable to Long-Term Funds		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
	(In £ Millions)					
UK corporation tax	**6**	(48)	24	**798**	503	306
Double tax relief	**—**	—	(3)	**(12)**	(12)	(11)
Tax on franked investment income	**—**	2	3	**—**	3	166
Overseas tax	**(22)**	(15)	3	**170**	168	159
Prior year adjustments	**(8)**	42	(1)	**(6)**	40	(3)
	(24)	(19)	26	**950**	702	617
Deferred tax	**23**	(34)	3	**(270)**	101	74
	(1)	(53)	29	**680**	803	691
Shareholder tax attributable to balance on the long-term business technical account	**285**	261	232	**—**	—	—
Total shareholders' tax expense	**284**	208	261	**680**	803	691

12 Tax (Continued)

An analysis of shareholders' tax expense allocated to the various sources of profit giving rise to the taxes is as follows:

	2000	1999	1998
	(In £ Millions)		
Tax on operating profit	**235**	209	214
Tax on short-term fluctuations in investment returns	**(8)**	(16)	9
Tax on profit on Egg flotation and business disposals	**57**	15	38
Total	**284**	208	261

The sources of differences between the statutory and the effective tax rates are as follows:

	2000	1999	1998
	(In £ Millions Except Percentages)		
UK statutory tax rate	**30.0%**	30.3%	31.0%
Tax expenses at statutory rate	**284**	227	354
Non-taxable book losses (gains) on sales of subsidiaries/associates	**(44)**	28	(40)
Other capital gains	**21**	(26)	(6)
Different local basis of tax on overseas profits	**(6)**	(13)	(10)
Utilization of brought forward tax losses	**—**	(1)	(18)
UK tax basis of insurance profits	**(8)**	(2)	(17)
Non-taxable foreign exchange losses	**9**	—	—
Disallowable amortization of goodwill	**25**	16	—
Other	**3**	(21)	(2)
Tax expense	**284**	208	261
Effective tax rate	**30.0%**	27.7%	22.9%

At December 31, 2000, there are no tax losses available to carry forward to offset future taxes.

12 Tax (Continued)

The components of the net deferred income tax liability and the net liability not provided by category of timing difference are as follows:

Deferred income tax	Liability Provided (asset recognized) 2000	Liability Provided (asset recognized) 1999	Liability Not Provided (asset not recognized) 2000	Liability Not Provided (asset not recognized) 1999
	(In £ Millions)			
Unrealized gains on investments	**299**	515	**2,542**	3,189
Deferred acquisition costs	**391**	375	**—**	—
Short-term timing differences	**(335)**	(296)	**(17)**	(30)
Long-term business technical provisions and other insurance items	**9**	8	**127**	122
Capital allowances	**(32)**	(27)	**(8)**	(4)
Total	**332**	575	**2,644**	3,277

The components of the net deferred income tax liability and the net liability not provided by fund are as follows:

Deferred income tax	Liability Provided (asset recognized) 2000	Liability Provided (asset recognized) 1999	Liability Not Provided (asset not recognized) 2000	Liability Not Provided (asset not recognized) 1999
	(In £ Millions)			
Scottish Amicable Insurance Fund	**247**	434	**—**	—
PAC with-profits funds*	**16**	95	**2,543**	3,090
Jackson National Life	**—**	—	**—**	(18)
Other long-term business operations	**39**	43	**49**	57
Other operations	**30**	3	**52**	148
Total	**332**	575	**2,644**	3,277

* Includes deferred tax charges in respect of non-participating annuity business written by a subsidiary, Prudential Annuities Limited, financed by the PAC with-profits fund.

13 Acquisitions and Disposals

Acquisitions in 2000

Taiwanese operations

In September 2000, Prudential increased its holding in its subsidiary Chinfon Insurance Company of Taiwan from 74% to 81%. In October 2000, Prudential purchased an 89% interest in Core Pacific Securities Investment Trust Enterprise, a Taiwanese fund management company, which has been renamed Prudential Securities Investment Trust Enterprise.

US operations

During February 2000, Prudential's US operations acquired three branches of Fidelity Federal Bank for a cash consideration of £7 million. On September 29, 2000, Prudential's US subsidiary Jackson National Life acquired Highland Bancorp, Inc. for $110 million. Highland Bancorp, Inc. is the holding company for Highland Federal Bank, which operates seven retail branches in the state of California. On September 29, 2000 Prudential's US subsidiary Jackson National Life acquired IFC Holdings for $42 million. IFC Holdings is the holding company of Invest, a bank broker-dealer, which is a third party marketing organization.

The effect of the above transactions, which have been accounted for as acquisitions was:

	US Operations	Taiwanese Operations	Total
	(In £ Millions)		
Cash and short term investments	16	—	**16**
Banking business assets	565	—	**565**
Banking business liabilities	(535)	—	**(535)**
Other net assets	1	6	**7**
Net assets acquired	47	6	**53**
Total fair value of consideration including costs of acquisition	110	73	**183**
Goodwill recognized as an asset on the consolidated balance sheet	63	67	**130**

Goodwill is being amortized over 15 years for acquisitions by the US operations and over 20 years for acquisitions of the Taiwanese operations.

13 Acquisitions and Disposals (Continued)

Acquisitions in 1999

Acquisitions during 1999 related to the Group's purchases of the M&G Group plc, the UK's largest retail unit trust manager in April and of a majority holding in Chinfon Life Insurance Company of Taiwan in November. The effect of these transactions, which have been accounted for as acquisitions was:

	Book Value Before Acquisition	Fair Value Adjustments	Fair Value at Acquisition
		(In £ Millions)	
Investments	732	—	732
Asset held to cover linked liabilities	3,981	—	3,981
Long-term business provision	(399)	—	(399)
Technical provisions for linked liabilities	(3,981)	—	(3,981)
Other net assets	54	47	101
Net assets acquired	387	47	434
Total fair value of consideration including costs of acquisition in respect of:			
M&G Group plc			1,943
Chinfon Life Insurance Company of Taiwan			68
Total fair value of consideration including costs of acquisition			2,011
Goodwill recognized as an asset in the consolidated balance sheet			1,577

The goodwill relating to both of these acquisitions is being amortized over 20 years.

The fair value adjustment of £47 million shown above is for the present value of in force long-term business relating to M&G Group plc.

13 Acquisitions and Disposals (Continued)

The 1999 long-term business technical and non-technical accounts include the following amounts in respect of operations acquired during the year ended December 31, 1999 from the date of acquisition:

	(In £ Millions)
Long-Term Business Technical Account	
Gross premiums	246
Earned premiums, net of reinsurance	245
Investment returns	401
Claims incurred, net of reinsurance	(369)
Change in long-term business provision, net of reinsurance	(154)
Net operating expenses	(75)
Investment expenses and charges	(3)
Tax attributable to the long-term business technical account	(37)
Balance on the long-term technical account after tax	8
Non-technical account	
Balance on the long-term business technical account after tax	8
Tax credit attributable to balance on the long-term business technical account	2
Balance on the long-term business technical account before tax	10
Investment management and products result	31
Profit on ordinary activities before tax	41
Analyzed as:	
Operating profit before restructuring costs	56
Restructuring costs	(7)
Operating profit	49
Short-term fluctuations in investment returns	(8)
Profit on ordinary activities before tax	41

Acquisitions in 1998

Prudential Assurance Malaysia Berhad

In June 1998, regulatory approval was received for the purchase of a controlling interest in the Group's Malaysian operation, Prudential Assurance Malaysia Berhad. Previously, the Group's interest in the operation was accounted for as an investment in an associate.

The fair value of the consideration (including expenses) paid for the acquisition and funding of ordinary and preference shares was £123 million. The acquisition was accounted for using the purchase method of accounting resulting in a fair value adjustment of £55 million for the present value of future profits. The excess of purchase price over net assets acquired of £59 million was recorded as goodwill and is being amortized over a period of 20 years.

13 Acquisitions and Disposals (Continued)

Unaudited pro forma information

Consolidated earned premiums, revenue from banking, broker-dealer and investment management operations, profit for the financial year and related earnings per share are shown on a pro forma basis for all the acquisitions referred to for the period of acquisition and the immediately preceding period. These pro forma amounts have been derived by adding pre-acquisition revenue and other components of net profit included in the Group's consolidated profit and loss accounts post-acquisition.

	Pro Forma (Unaudited)			
	2000 and 1999 Acquisitions		1999 and 1998 Acquisitions	
	2000	1999	1999	1998
	(In £ Millions, Except Per Share Amounts)			
Earned premiums	**14,376**	15,314	15,314	11,674
Revenue from banking, broker-dealer and investment management operations	**581**	326	199	80
Consolidated net profit	**695**	521	510	935
Earnings per share	**35.5p**	26.7p	26.2p	48.1p

The presentation for 2000 and 1999 includes the acquisition of the Fidelity Bank branches, Highland Bancorp, IFC Holdings, Core Pacific Securities Investment Trust Enterprise, and additional shares in Chinfon Life Insurance Company of Taiwan as if they had been acquired as of January 1, 1999. The presentation for 1999 and 1998 acquisitions includes M&G Group plc, Chinfon Life Insurance Company of Taiwan, and Prudential Assurance Malaysia Berhad as if they had been acquired as of January 1, 1998.

Disposals in 2000

Sale of investment in associate

On June 5, 2000 Prudential sold 68% of its holding in St James's Place Capital plc, which is quoted on the London Stock Exchange, for cash proceeds of £213 million, which included £83 million attributable to the sale of the parent company's holding. After taking into account attributable net assets of £53 million and attributable goodwill of £61 million, which was charged to reserves on acquisition, the profit on disposal of this portion was £99 million. The remaining 32% of Prudential's holding in St James's Place Capital plc was sold in July 2000 for £79 million. After taking into account attributable net assets of £26 million and goodwill of £29 million, the realized gain of £24 million has been included in investment returns in the profit and loss account for the year ended December 31, 2000.

Share of exceptional gain of associate company

The profit and loss account for 2000, includes a gain of £21 million that relates to Prudential's share of the profit realized by St. James's Place Capital plc, an associate company at the time of sale, on the disposal of its interest in Global Asset Management, a Bermuda-based fund manager.

13 Acquisitions and Disposals (Continued)

Transfer of investment management activities

On June 30, 2000 Prudential transferred £12 billion of its UK institutional equity fund management activities to Deutsche Asset Management. The activities transferred comprised of management of third party institutional funds. There was no gain or loss to Prudential as a result of the transfer.

Initial Public Offering of Egg plc

On June 12, 2000 Prudential sold 73 million shares of its holding in Egg plc, a new intermediate holding company of Prudential Banking plc, in an initial public offering (IPO) and raised £90 million after deduction of expenses. At the same time, Egg issued 93 million new shares to the market with total proceeds, after deduction of expenses, of £149 million. The IPO price was £1.60 per share.

Total proceeds from the IPO, net of expenses, were £239 million, resulting in a profit for Prudential of £119 million. Taxes have been provided on the gain resulting from the Egg IPO. As a result of the IPO, the parent company's ownership percentage was reduced from 100% to 79.6%.

Disposals in 1998

In September 1998, the Group completed the sale of its Australasian businesses (principally Prudential Corporation Australia Limited and Prudential Assurance Company New Zealand Limited) to The Colonial Mutual Life Assurance Society Limited for net cash proceeds of £468 million. The Group recognized a gain on the sale of £210 million after tax of £38 million. Related goodwill of £28 million, recorded in shareholders' funds when the businesses were acquired, was charged to the consolidated profit and loss accounts in determining the gain on sale.

Summary of Disposals

The following amounts were included in the long-term business technical account in the years prior to the operations being sold.

	Long-Term Business Technical Account 1998
	(In £ Millions)
Gross written premiums	423
Earned premiums, net of reinsurance	420
Investment returns	156
Claims incurred, net of reinsurance	(691)
Change in other technical provisions, net of reinsurance	222
Net operating expenses	(70)
Investment expenses and charges	(20)
Balance on the long-term business technical account before tax	17
Tax attributable to the long-term business	(10)
Balance on the long-term business technical account	7

14 Present Value of Future Profits

The balance of the present value of future profits of acquired in-force long term business is recorded in the consolidated balance sheets as of December 31 of each year. Changes in the balance for the year are as follows:

	2000	1999	1998
	(In £ Millions)		
Balance at January 1	**170**	138	128
Exchange adjustment	**9**	—	—
Additions	**—**	47	55
Interest accrued at rates ranging from 8.25% to 10.25%*	**17**	16	9
Amortization*	**(34)**	(31)	(20)
Charge to profit and loss account arising from reinsurance transaction	**(29)**	—	—
Disposals	**—**	—	(34)
Balance at December 31	**133**	170	138

* Net of tax.

The present value of future profits relates primarily to the acquisition of M&G in 1999, the additional investment in the Malaysian operations in 1998, the acquisitions of NZI Life and SALI in 1997 and of Jackson National Life in 1986. The discount rate used for recording the present value of future profits for M&G was 8.25%, the additional investment in the Malaysian operations was 10.25%, SALI was 9.25% and Jackson National Life was between 8.5% and 9.0%. The disposal in 1988 relates to NZI Life.

On December 28, 2000, the long-term business of M&G was transferred to Scottish Amicable Life plc ("SAL"), a subsidiary company of the Group, pursuant to a Schedule 2c transfer under the Insurance Companies Act of 1982. As part of the transfer, SAL entered into a reinsurance arrangement under which the present value of acquired in force business formerly of M&G was partially written down. The present value of future margins related to advances from reinsurers is shown separately in the balance sheet.

The percentage of the present value of future profits as of December 31, 2000 that is expected to be amortized in 2001 and each of the subsequent four years is 9.9%, 10.0%, 10.2%, 10.3% and 10.6%, respectively.

15 Reinsurance

The Group cedes certain business to other insurance companies. Although the ceding of reinsurance does not relieve the Group of liability to its policyholders, the Group participates in such agreements for the purpose of limiting its loss exposure. The Group evaluates the financial condition of its reinsurers to minimize its exposure from reinsurer insolvencies. The effects of net reinsurance ceded on claims paid, change in the provision for claims incurred and change in the long-term business

15 Reinsurance (Continued)

provision, as presented in the long-term business technical account and the general business technical account, are summarized as follows:

	Long-Term Business			General Business		
	2000	**1999**	**1998**	**2000**	**1999**	**1998**
	(In £ Millions)					
Claims paid:						
Gross amount	**(13,936)**	(10,518)	(9,079)	**(215)**	(227)	(234)
Reinsurers' share	**95**	89	59	**7**	9	10
Claims paid, net of reinsurance	**(13,841)**	(10,429)	(9,020)	**(208)**	(218)	(224)
Change in the equalization provision	**—**	—	—	**(8)**	(7)	(8)
Change in the provision for claims:						
Gross amount	**(128)**	(153)	(12)	**(31)**	35	19
Reinsurers' share	**3**	6	(2)	**—**	(10)	4
Change in the provision for claims, net of reinsurance	**(125)**	(147)	(14)	**(31)**	25	23
Total claims incurred, net of reinsurance	**(13,966)**	(10,576)	(9,034)	**(247)**	(200)	(209)
Change in long-term business provision:						
Gross amount	**(6,239)**	(6,778)	(8,405)			
Reinsurers' share	**123**	33	27			
Change in long-term business provision, net of reinsurance	**(6,116)**	(6,745)	(8,378)			

The Group has reinsurance agreements with Swiss Re Group, which account for approximately 60% and 50% of the reinsurers' share of technical provisions and debtors arising out of reinsurance operations at December 31, 2000 and 1999, respectively. No other reinsurance group accounts for more than 10% at either year end.

Ceded reinsurance is treated as the risk and liability of the assuming companies. However, these reinsurance contracts do not relieve the Group from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Group; consequently, allowances are established for amounts deemed uncollectable. The Group evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurance insolvencies.

16 Land and Buildings

The carrying value of land and buildings is comprised as follows:

	December 31	
	2000	1999
	(In £ Millions)	
Fair value:		
Freehold	**6,111**	5,291
Leasehold with a term of 50 years or over	**4,033**	3,362
Leasehold with a term of less than 50 years	**159**	110
Total	**10,303**	8,763

The cost of land and buildings was £6,970 million and £5,804 million at December 31, 2000 and 1999, respectively. The fair value of land and buildings occupied by the Group was £230 million and £177 million at December 31, 2000 and 1999, respectively.

The practice in the UK for long-term leases is to pay a substantial portion of the lease obligation upon initiation of the lease with insignificant annual rental payments thereafter. As such, there are no material future minimum lease commitments for long-term leases.

Minimum future rentals to be received on non-cancelable operating leases and subleases for land and buildings for the year ended December 31, 2001 and the succeeding four years are £495 million, £485 million, £471 million, £454 million, and £434 million, respectively, and £6,709 million thereafter.

At December 31, 2000, the carrying value of properties that were non-income producing for the last twelve months preceding the consolidated balance sheet date was £154 million, primarily representing properties under development.

17 Investments in Associates and Other Participating Interests

Investments in which the Group holds a participating interest and exercises significant influence are recorded as investments in associates. Until June 2000 such investments comprised primarily St. James's Place Capital plc, an insurance holding company incorporated in England and Wales and listed on the London Stock Exchange. The proportion of ordinary shares of St. James's Place Capital plc held for the shareholders' interest was 25.0% with a related market value of £234 million at December 31, 1999. As discussed in Note 13, the Group's interest in St James's Place Capital plc was sold during 2000. Fee income received from a subsidiary of St. James's Place Capital plc, amounted to £22 million, £18 million, and £15 million in 2000, 1999, and 1998 respectively. The Group's interests in associates are included within investments in participating interests in the consolidated balance sheets.

At December 31, 2000, the investment in associates comprised IFonline plc, a company whose principal activity is mortgage intermediation. In July 2000, Egg acquired a 39.6% holding in IFonline for £15 million. The fair value of net assets acquired was £4 million, resulting in goodwill of £11 million. The goodwill arising on the acquisition is being amortized over ten years.

Interests in joint ventures relate to ventures with the Bank of China International in Hong Kong, The Industrial Credit and Investment Corporation of India (ICICI) in India, China International Trust and Investment Corporation (CITIC) in China, and Signal Iduna in Germany. The differences between

17 Investments in Associates and Other Participating Interests (Continued)

the investments on a gross and net equity basis are not material. The other participating interest is in respect of the Group's interest in Life Assurance Holding Corporation Limited, a holding company for UK life assurance companies.

The Group's investments in participating interests are as follows:

	December 31			
	Cost		Carrying Value	
	2000	1999	2000	1999
	(In £ Millions)			
Investments in associates	**15**	146	**13**	61
Interest in joint ventures	**34**	20	**34**	20
Other participating interests	**24**	24	**36**	24
Total	**73**	190	**83**	105

In addition to the participating interests shown in the table above, the Group, through its life fund venture capital activities, has investments that are accounted for as portfolio investments under FRS No. 9, "Accounting for Joint Ventures and Associates". The Company has provided loans to a number of these companies, which amounted to £160 million and £155 million at December 31, 2000 and 1999, respectively. These amounts are shown as other loans on the consolidated balance sheets.

The changes in investments in associates for 2000 and 1999 are as follows:

	Share of Capital	Share of Reserves	Goodwill	Total Share of Investment
	(In £ Millions)			
Balance at January 1, 1999	16	42	—	58
Profit for the year after tax	—	4	—	4
Dividends received	—	(1)	—	(1)
Balance at December 31, 1999	16	45	—	61
Operating profit for the year after tax	**—**	**3**	**—**	**3**
Share of exceptional gain after tax	**—**	**14**	**—**	**14**
Dividends received	**—**	**(1)**	**—**	**(1)**
Additions	**1**	**3**	**11**	**15**
Disposals	**(16)**	**(63)**	**—**	**(79)**
Balance at December 31, 2000	**1**	**1**	**11**	**13**

18 Other Financial Investments

	December 31			
	Carrying Value		Cost	
	2000	1999	2000	1999
	(In £ Millions)			
Equity securities carried at fair value:				
UK Corporate:				
Utilities, industrial and other	**9,316**	11,135	**4,089**	4,571
Financial services	**9,542**	12,268	**3,612**	4,899
Consumer goods & services	**17,449**	19,452	**7,846**	7,064
Other UK	**2,024**	2,407	**896**	481
Overseas corporate	**12,901**	12,430	**11,099**	8,635
	51,232	57,692	**27,542**	25,650
Debt and other fixed income securities—carried at fair value:				
UK government	**1,062**	2,972	**938**	2,799
US government	**1,622**	1,074	**1,460**	1,109
Local UK and foreign governments	**4,452**	2,602	**4,211**	2,519
Corporate	**22,590**	16,160	**21,380**	15,283
Other debt securities	**379**	227	**487**	270
	30,105	23,035	**28,476**	21,980
Debt and other fixed income securities—carried at amortized cost:				
US government	**3**	6	**3**	6
Corporate	**11,285**	9,679	**11,393**	9,732
Mortgage backed securities	**7,132**	6,922	**7,083**	6,865
Other debt securities	**69**	176	**69**	176
	18,489	16,783	**18,548**	16,779
Mortgage and other loans	**2,999**	2,593	**2,950**	2,530
Loans to policyholders	**758**	681	**758**	681
Deposits with credit institutions	**3,875**	4,413	**3,875**	4,413
Other investments	**667**	581	**659**	562
Total	**108,125**	105,778	**82,808**	72,595

18 Other Financial Investments (Continued)

The fair value of debt and other fixed income securities carried at amortized cost is analyzed as follows:

	December 31	
	2000	1999
	(In £ Millions)	
Debt and other fixed income securities:		
US government	**3**	6
Corporate	**10,665**	9,262
Mortgage backed securities	**7,111**	6,662
Other debt securities	**70**	182
Total	**17,849**	16,112

Gross unrealized gains on debt and other fixed income securities carried at amortized cost were £254 million and £104 million at December 31, 2000 and 1999, respectively. Gross unrealized losses on these securities were £894 million and £775 million at December 31, 2000 and 1999, respectively.

All debt securities valued at amortized cost are held by long-term business operations.

Other financial investments include investments traded on recognized investment exchanges as follows:

	December 31	
	2000	1999
	Carrying Value (In £ Millions)	
Equity securities and other variable yield securities including units in unit trusts—carried at fair value	**50,785**	56,406
Debt securities and other fixed income securities—carried at fair value	**26,516**	20,530
Debt securities and other fixed income securities—carried at amortized cost	**15,090**	14,093
Total	**92,391**	91,029

Management's determination of fair value for unlisted securities without a readily ascertainable market value is generally based on quoted market prices for similar securities. At December 31, 2000 and 1999, equity securities, debt securities and other fixed income securities, without a readily ascertainable market value having a cost of £6,576 million and £6,777 million, respectively, had an estimated fair value of £6,572 million and £7,385 million, respectively.

For those debt securities and other fixed income securities valued at amortized cost where the maturity value exceeded purchase price, the unamortized difference was £186 million and £26 million at December 31, 2000 and 1999, respectively. There were no investments valued at amortized cost where the purchase price exceeded maturity value.

18 Other Financial Investments (Continued)

The cost and fair values of debt and other fixed income securities by contractual maturity at December 31, 2000 are shown below. Fixed maturities not due at a single maturity date have been included in the table in the final year of maturity. Expected maturities may differ from contractual maturities because some borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

	Cost	Fair Value
	(In £ Millions)	
Due in one year or less	**1,012**	**987**
Due after one year through five years	**7,853**	**7,693**
Due after five years through ten years	**12,477**	**12,419**
Due after ten years	**18,483**	**19,633**
Mortgage-backed securities	**7,084**	**7,111**
Other	**115**	**111**
Total debt and other fixed income securities	**47,024**	**47,954**

Approximately 57% of the carrying value of corporate debt securities is due from UK borrowers and 33% is due from US borrowers; mortgage backed securities are due primarily from borrowers in the US.

At December 31, 2000 and 1999, the carrying value of debt and other fixed income securities and mortgage loans which were non-income producing for the twelve months preceding the consolidated balance sheet date was not significant.

At December 31, 2000 and 1999, mortgage loans on property with scheduled payments 60 days or more past their due date, comprised less than 1% of the total carrying value and cost of mortgage loans.

The payment terms of mortgage loans on property may from time to time be restructured or modified. At December 31, 2000, investments in restructured loans represent less than 1% of the carrying value of mortgage loans. At December 31, 1999 there were no investments in restructured mortgage loans. At December 31, 2000 mortgage loans which the Group believes are impaired on an individual basis represent less than 1% of the carrying value of mortgage loans. At December 31, 1999, the Group had no mortgage loans which it believes are impaired on an individual basis. Residential mortgage loans are evaluated for impairment on a collective basis. Valuation allowances on mortgage loans represented less than 1% of the carrying value of mortgage loans at December 31, 2000 and 1999. Approximately 86% of the Group's mortgage loans are collateralized by properties located in the US and Canada, with the remainder being collateralized by properties located in the UK and Asia.

In the table of Other Financial Investments, "Other investments" primarily consist of investments in limited partnerships held by Jackson National Life that invest in securities. Limited partnership income recognized by the Group was £48 million, £21 million and £6 million in 2000, 1999 and 1998, respectively. At December 31, 2000, the Group has unfunded commitments related to investments in limited partnerships totalling £401 million.

19 Assets Held to Cover Linked Liabilities

At December 31, 2000 and 1999, the fair value of assets held to cover linked liabilities was £18,323 million and £18,643 million, respectively. The fair value of managed funds included in such assets was £4,030 million and £4,246 million at December 31, 2000 and 1999, respectively. The cost of assets held to cover the linked liabilities was £16,080 million and £13,511 million at December 31, 2000 and 1999, respectively.

20 Fair Value of Financial Instruments

The Group determines fair value as the quoted market prices for those financial instruments that are actively traded in financial markets. In cases where quoted market prices are not available, fair values are estimated using quotations from independent third parties or by using present value or other valuation techniques.

The fair value estimates are made at a specific point in time, based upon available market information and judgments 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 Group's entire holdings of a particular financial instrument, nor do they consider the tax impact of the realization of unrealized gains or losses. In many cases the fair value estimates cannot be substantiated by comparison to independent markets, nor can the disclosed value be realized in immediate settlement of the financial instrument.

Fair value for mortgage loans on land and buildings are estimated by discounting future contractual cash flows using interest rates at which loans with similar characteristics and credit quality would be made.

The estimated fair value of derivative financial instruments reflect the estimated amount the Group would receive or pay if the derivative instruments were terminated. Derivative financial instruments held where the estimated fair value differs from carrying value include interest rate swaps, currency swaps, index swaps and put-swaptions. See Note 21 for further discussion of derivative financial instruments.

Fair values for long-term insurance contracts are estimated as the discounted cash flows expected to arise in the future using discount rates of 8.5% at December 31, 2000 and 1999. In determining these estimates, best estimate forecasts of future investment returns have been incorporated and account has been taken of recent economic conditions together with inherent uncertainty.

Fair values for long-term borrowings are determined using published market values, where available, or contractual cash flows discounted at market rates. The carrying value of short-term borrowings approximates their fair market value.

The difference between the carrying value and fair value of banking business assets and liabilities is not material at December 31, 2000 and 1999.

20 Fair Value of Financial Instruments (Continued)

The following table presents the carrying value and estimated fair value of all derivative financial instruments and other financial instruments for which the carrying value differs from the estimated fair value:

	December 31			
	2000		1999	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(In £ Millions)			
Financial assets:				
Debt and other fixed income securities carried at amortized cost	**18,489**	**17,849**	16,783	16,112
Mortgage loans carried at unpaid principal balances	**2,480**	**2,765**	2,123	2,110
Derivative financial instruments carried at fair value	**702**	**702**	1,396	1,396
Derivative financial instruments carried at other than fair value	**315**	**431**	216	446
Financial liabilities:				
Long-term insurance contracts	**133,684**	**128,871**	131,263	126,345
Long-term borrowings	**1,639**	**1,717**	1,714	1,731
Derivative financial instruments carried at fair value	**3,206**	**3,206**	1,466	1,466
Derivative financial instruments carried at other than fair value	**1**	**286**	19	59

The carrying value of other financial investments for which the carrying value approximates fair value is presented in Note 18.

21 Derivatives

The Group enters into a variety of exchange-traded and over-the-counter derivative financial instruments, including futures contracts; index and equity options; interest rate and currency swaps; bond and equity index swaps; and other derivative financial instruments. These derivatives are used for efficient portfolio management to obtain cost effective and efficient exposure to various markets in accordance with the Group's investment strategies and for hedging purposes to reduce and manage business risks. The Group segregates cash or securities to fund or match 100% of open derivative positions, including notional amounts plus daily changes in market value. Hedge accounting practices are supported by cash flow matching, duration matching, scenario testing and designation criteria.

Derivatives Accounted for at Fair Value

UK insurance operations use equity index futures contracts and options, equity options, forward foreign currency exchange contracts, currency swaps, equity index swaps and other derivatives for efficient portfolio management. These derivatives are carried at fair value with changes in fair value included in investment returns.

21 Derivatives (Continued)

Equity index futures contracts

Deposit margins for equity index futures contracts are included in the consolidated balance sheet as deposits with credit institutions. Subsequent changes in fair value of the contracts are reported in investment returns.

Equity index and equity options

Premiums paid or received for equity index options and equity options are recorded in the consolidated balance sheet, as other financial investments. Changes in fair value are recorded in investment returns. Upon exercise of purchased equity options, the premium paid is added to the cost basis of equities purchased, or deducted from the proceeds of equities sold; and the premium received in respect of written options is offset against the cost of underlying equity instruments. When options expire, the premium revenue or expense is recorded in investment returns.

Currency and interest rate swap agreements

Currency swap agreements involve the exchange of payments in different currencies over the life of the agreement based on a fixed or variable interest rate. Interest rate swap agreements involve the exchange of fixed and floating payments over the life of the agreement without an exchange of the underlying principal amount. These swaps are carried at fair value and any change in value is included in investment returns.

Foreign currency exchange forward contracts

Foreign currency exchange forward contracts are recorded on a net basis within cash in hand in the balance sheet with changes in market value recorded in investment returns. The contracts involve the exchange of two currencies at a specified future date and exchange ratio. The terms of the forward contracts range from two weeks to four months. There were no forward currency contracts at December 31, 2000 and 1999.

Index swap agreements

The US insurance operations held high yield bond index swaps and equity index swaps for investment purposes in 2000 and 1999. These derivatives held for investment purposes are carried at fair value with changes in fair value included in investment returns.

Derivatives Accounted for on an Accrual Basis, Hedging Assets or Liabilities Carried at Cost

Currency and interest rate swap agreements

Currency and interest rate swap agreements used for hedging purposes are accounted for on an accrual basis, consistent with the assets and liabilities hedged. Amounts paid or received on interest rate swap agreements are included in investment returns. Accrued amounts payable to or receivable from counterparties are included in other liabilities or other assets. Realised gains and losses from the settlement or termination of the interest rate swaps are deferred and amortized over the life of the specific hedged assets as an adjustment of the yield. Where a swap no longer represents a hedge,

21 Derivatives (Continued)

because the underlying asset has been sold, or the liability repaid, the swap is carried at fair value and any change in value is included in investment returns.

Foreign currency exchange forward contracts

Foreign currency exchange forward contracts used for hedging purposes are accounted for on an accrual basis consistent with the underlying assets and liabilities hedged. Accrued amounts payable or receivable from counterparties are included in other liabilities or other assets. The contracts involve the exchange of two currencies at a specified future date and exchange ratio. The terms of the forward contracts range from one month to six months. The following table summarizes, by major currency, the contractual amounts of the Group's forward currency contracts at December 31, 2000. There were no forward currency contracts used for hedging purposes at December 31, 1999.

	2000	
	Receive	Deliver
	(In £ Millions)	
US Dollars	—	472
Euro	—	58
Total	—	530

Put-swaptions

Put-swaptions are purchased to provide the US insurance operations with the right, but not the obligation, to require the counterparties to pay Jackson National Life the present value of a long duration interest rate swap at future exercise dates. Put-swaptions are purchased to hedge debt security investments.

Premiums paid for put-swaptions are included in other invested assets and are amortized to investment income over the remaining terms of the contracts with maturities up to 10 years. Realised gains and losses from the settlement or termination of the swaptions are deferred and amortized over the life of the specific hedged assets as an adjustment of the yield. Where a swaption no longer represents a hedge because the underlying asset has been sold, the swap is carried at fair value and any change in value is included in investment returns.

Credit derivatives

Credit derivatives are purchased to provide the UK banking operations with protection against default risk associated with banking business assets. The fees paid to the counterparties are included in other assets and amortized to operating expense over the term of the contract. Amounts received from the counterparties as settlement of the hedge are included in the specific hedged assets as an adjustment of the yield.

21 Derivatives (Continued)

Derivatives Accounted for on a Deferral Basis, Hedging Anticipated Transactions

Index swap agreements

Index swap agreements generally involve the exchange of payments based on a short-term interest rate index for payments based on the total return of a bond or equity index over the life of the agreement without an exchange in the underlying principal amount. Index swap agreements hedge the anticipated purchase of investment grade bonds that will be carried at amortized cost by the US insurance operations. Amounts paid or received on the swaps are deferred and adjust the basis of bonds acquired upon expiration of the swaps.

Derivatives Accounted for on a Deferral Basis, Hedging Equity Indexed Liabilities

Equity index futures contracts and equity index call options are purchased to hedge the risk related to equity index linked immediate and deferred annuities offered by Jackson National Life. The variation margin on futures contracts is deferred and recorded as an asset or liability and, upon closing of the contracts, adjusts the cost basis of index call option contracts purchased. The time premium of equity index call options acquired is amortized to investment returns over the option term. The change in intrinsic value, including amounts received on exercising the option, is deferred until the associated hedged index linked annuity liability is recognized.

Summary of Derivative Financial Instruments

The estimated fair value of a derivative contract reflects the estimated amount that the Group would receive or pay if it terminated the contract at the reporting date. Average fair value represents an average for the year of the estimated fair value of open positions of the respective derivative contracts, as calculated based on monthly estimated fair values. With respect to equity options, notional/contractual amounts represent the market value of the financial instruments underlying these derivative contracts. For all interest rate swap agreements, the notional amount represents the par value of the underlying financial instruments used to calculate interest payments. With respect to futures contracts, futures index options and other instruments, the contractual amount represents the contracted amount on date of purchase of outstanding positions.

21 Derivatives (Continued)

For derivative financial instruments which are accounted for at fair value with related unrealized gains and losses recorded in the consolidated profit and loss accounts, a summary of the aggregate notional or contractual amounts and estimated fair values for outstanding derivative financial instruments and average fair value at December 31 of such instruments is as follows:

	2000			1999		
	Notional/ Contractual Amount	Average Fair Value	Estimated Fair Value	Notional/ Contractual Amount	Average Fair Value	Estimated Fair Value
	(In £ Millions)					
Derivative Type						
Equity index futures contracts						
Asset position	**207**	**1,333**	**204**	886	444	945
Liability position	**(2,786)**	**(1,675)**	**(2,733)**	(1,195)	(702)	(1,262)
Equity index options						
Asset position	**—**	**11**	**—**	29	6	49
Liability position	**—**	**(5)**	**—**	—	(12)	—
Equity options						
Asset position	**—**	**—**	**—**	—	107	115
Liability position	**(2)**	**(1)**	**(2)**	(1)	(2)	(1)
Currency swap agreements						
Asset position	**115**	**240**	**346**	176	49	202
Liability position	**(115)**	**(214)**	**(342)**	(167)	(36)	(159)
Interest rate swap agreements						
Asset position	**200**	**47**	**58**	176	—	—
Liability position	**(200)**	**(51)**	**(46)**	(176)	(1)	(6)
Index swap agreements						
Asset position	**553**	**44**	**54**	335	8	26
Liability position	**(553)**	**(46)**	**(61)**	(335)	(8)	(23)
Property index forward contracts						
Asset position	**1,200**	**14**	**17**	—	—	—
Liability position	**(1,200)**	**(3)**	**(2)**	—	—	—
Foreign currency exchange forward contracts						
Asset position	**—**	**1**	**—**	—	—	—
Liability position	**—**	**(3)**	**—**	—	—	—
Other instruments						
Asset position	**20**	**54**	**23**	44	76	59
Liability position	**(21)**	**(16)**	**(20)**	(17)	(5)	(15)
Asset position	**2,295**	**1,744**	**702**	1,646	690	1,396
Liability position	**(4,877)**	**(2,014)**	**(3,206)**	(1,891)	(766)	(1,466)
Net asset (liability)	**(2,582)**	**(270)**	**(2,504)**	(245)	(76)	(70)

21 Derivatives (Continued)

Net recognized gains (losses) on derivatives used for efficient portfolio management and investment purposes included in investment returns are as follows:

	2000	1999	1998
	(In £ Millions)		
Financial derivative type			
Equity index futures contracts	**330**	(173)	(112)
Equity index options	**81**	32	(41)
Equity options	**—**	2	(9)
Foreign currency exchange forward contracts	**(140)**	(14)	(17)
Other instruments	**25**	42	(22)
Net recognized gains/(losses)	**296**	(111)	(201)

A summary of the aggregate notional amounts, estimated fair values and unrealized gain or (loss) for derivative financial instruments outstanding, which are accounted for as hedges, at December 31, is as follows:

	2000			1999		
	Notional Amount	Estimated Fair Value	Unrealised Gains (Losses)	Notional Amount	Estimated Fair Value	Unrealised Gains (Losses)
	(In £ Millions)					
Currency swap agreements						
Asset position	**223**	**13**	**13**	38	2	2
Liability position	**(1,173)**	**(104)**	**(104)**	(464)	(41)	(41)
Interest rate swap agreements						
Asset position	**904**	**24**	**24**	2,907	44	11
Liability position	**(6,142)**	**(182)**	**(181)**	(2,120)	(18)	1
Foreign currency exchange forward contracts						
Asset position	**530**	**8**	**—**	—	—	—
Put-swaptions						
Asset position	**15,397**	**12**	**2**	18,304	9	1
Interest rate cap agreements						
Asset position	**25**	**—**	**—**	—	—	—
Equity index options						
Asset position	**1,149**	**373**	**80**	931	391	213
Equity index futures contracts						
Asset position	**59**	**—**	**(3)**	39	—	3
Credit derivatives						
Asset position	**885**	**1**	**—**	—	—	—
Asset position	**19,172**	**431**	**116**	22,219	446	230
Liability position	**(7,315)**	**(286)**	**(285)**	(2,584)	(59)	(40)
Total	**11,857**	**145**	**(169)**	19,635	387	190

21 Derivatives (Continued)

Realized gains from derivative contracts hedging index-linked annuities that have been deferred at December 31, 2000 and 1999 were not material. There were no material realized gains or losses deferred from derivative contracts hedging anticipated purchases of investment grade bonds at December 31, 2000 or 1999.

The Group expects to hold to maturity all interest rate, index and currency swaps utilized to manage interest rate and foreign exchange risk. The term to maturity of the Group's open swap positions at December 31, was as follows:

	2000				1999			
	Notional Amount		Estimated Fair Value		Notional Amount		Estimated Fair Value	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
	(In £ Millions)							
Less than 1 year	**34**	**1,572**	**2**	**11**	584	173	11	1
1 to 5 years	**1,031**	**3,905**	**35**	**103**	2,361	2,027	35	20
Over 5 years	**930**	**2,706**	**458**	**621**	687	1,062	228	226
Total swaps held	**1,995**	**8,183**	**495**	**735**	3,632	3,262	274	247

Credit Risk

Exchange-traded futures

Exchange-traded futures comprise a significant part of the UK insurance operation's financial derivatives activity. All margin accounts are guaranteed against default by the clearing facility on each applicable exchange, which enforces a system of margining to ensure that all market traders are fully capable of meeting their obligations on a daily basis. Management feels that these exchange level controls substantially mitigate counterparty credit risk related to their investment in futures contracts.

Over-the-counter derivatives

Over-the-counter derivative positions, primarily interest rate swaps and put-swaptions, are only held with approved counterparties who are subject to careful evaluation of credit standing, and which must possess high short-term deposit ratings with a major rating agency. The Group assigns exposure limits to all counterparties according to the size of their capital base and credit rating. All exposure limits are subject to regular credit monitoring procedures. The Group also manages the potential credit exposure through evaluation of collateral agreements and master netting agreements on interest rate and currency swaps. The Group is exposed to credit-related losses in the event of non-performance by counterparties, however, the Group does not anticipate non-performance.

22 Securities Lending

At December 31, 2000 and 1999, the estimated fair value of loaned securities was £6,498 million and £6,415 million, respectively, consisting of equity and debt securities. These securities remain recorded in the consolidated balance sheets. Cash collateral received of £454 million and £179 million at December 31, 2000 and 1999, respectively, was invested in a pooled fund, and is included in the

22 Securities Lending (Continued)

consolidated balance sheets. A related payable for the return of the cash collateral received is included in liabilities. Pledged collateral in respect of securities loaned was £6,428 million and £6,535 million at December 31, 2000 and 1999, respectively. Such pledged collateral, consisting principally of cash, securities and letters of credit, is not recorded in the consolidated balance sheets of the Group.

23 Investments in Subsidiaries

The principal subsidiaries of the Company at December 31, 2000 were:

	Main Activity	Country of Incorporation
Jackson National Life Insurance Company*	Insurance	United States of America
Prudential Annuities Limited*	Insurance	England and Wales
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore
Prudential Banking plc*	Banking	England and Wales
M&G Investment Management Limited*	Investment management	England and Wales
Scottish Amicable Life plc*	Insurance	Scotland

* Owned by a subsidiary of the Company.

Each subsidiary operates mainly in its country of incorporation, and has only one class of ordinary shares, all of which are held by the Company or a subsidiary of the Company.

Prudential Banking plc is a subsidiary of Egg plc, a subsidiary of the Company that is listed on the London Stock Exchange. The ordinary shares of Egg plc, of which there is only one class, are owned 79% by the Company. The remaining 21% of ordinary shares are owned by shareholders external to the Prudential Group.

24 Tangible Assets

Tangible assets are principally computer equipment, software development expenditure and fixtures and fittings.

	December 31	
	2000	**1999**
	(In £ Millions)	
Cost		
Balance at beginning of year	**395**	266
Additions	**122**	144
Arising on acquisition of subsidiaries	**6**	44
Disposals	**(44)**	(59)
Balance at end of year	**479**	395
Depreciation		
Balance at beginning of year	**(156)**	(125)
Depreciation	**(62)**	(47)
Arising on acquisition of subsidiaries	**(5)**	(30)
Disposals	**32**	46
Balance at end of year	**(191)**	(156)
Net book value at beginning of year	**239**	141
Net book value at end of year	**288**	239

25 Borrowings

Borrowings of the Group were as follows:

	December 31	
	2000	**1999**
	(In £ Millions)	
Parent company and finance subsidiaries:		
Guaranteed Bonds, US $300 million principal amount, 8.25%, due 2001	**201**	186
Bonds, US $250 million principal amount, 7.125%, due 2005*	**167**	155
Guaranteed Bonds, £150 million principal amount, 9.375%, due 2007	**150**	150
Bonds, £250 million principal amount, 5.5%, due 2009*	**250**	250
Bonds, £300 million principal amount, 6.875%, due 2023*	**300**	300
Bonds, £250 million principal amount, 5.875%, due 2029*	**250**	250
Long-term business operations:		
Surplus Notes, US $250 million principal amount, 8.15%, scheduled to mature 2027	**167**	155
Guaranteed Bonds, £100 million principal amount, 8.5%, undated subordinated	**100**	100
Total debenture loans	**1,585**	1,546
Parent company and finance subsidiaries:		
Floating Rate Guaranteed unsecured Loan Notes 2004	**54**	168
Short-term commercial paper	**176**	301
Borrowings of investment subsidiaries managed by US fund management operations:		
Collateralized senior and subordinated debt	**47**	44
Senior collateralized revolving credit line	**79**	103
Bank loans and overdrafts repayable on demand:		
General Insurance and shareholders' funds	**20**	58
Parent company and finance subsidiaries	**20**	—
Total borrowings	**1,981**	2,220
Borrowings are repayable as follows:		
Within one year or on demand	**417**	359
Between one year and two years	**—**	186
Between two years and three years	**28**	—
Between three and four years	**135**	—
Between four years and five years	**184**	299
After five years	**1,217**	1,376
Total borrowings	**1,981**	2,220

* Debenture loans issued by the Parent Company.

Non-debenture borrowings are classified in the consolidated balance sheets depending on the nature of the borrowing. Commercial paper and floating rate loan notes are classified within other creditors and the remaining non-debenture borrowings are classified in the consolidated balance sheets within amounts owed to credit institutions.

25 Borrowings (Continued)

Amounts owed to credit institutions were as follows:

	December 31	
	2000	**1999**
	(In £ Millions)	
Borrowings:		
Bank loans and overdrafts repayable on demand	**40**	58
Senior collateralized revolving credit	**126**	103
Other senior and subordinated debt	**—**	44
Other:		
Jackson National Life reverse repurchase and dollar-roll agreements	**733**	893
Other	**10**	13
Total	**909**	1,111

Short-term borrowings

The Group maintains uncommitted standby credit facilities in the aggregate amount of £1,005 million that are available to support short-term borrowings. These credit facilities consist of a number of credit lines with interest rates that are floating and are based on the drawing bank's short-term borrowing rate. There was no amount outstanding under these facilities at December 31, 2000.

The Group has a £1,100 million multi-currency revolving committed credit facility available to support the issuance of commercial paper and other short-term borrowings. The interest rates are floating and are calculated with reference to the London InterBank Offering Rate or the US Prime rate or Federal Funds rate, depending on the borrowing currency. There was no amount outstanding under these facilities at December 31, 2000. Commitment fees are payable on these facilities.

Additionally, the Group has a US$2,000 million (£1,339 million) global commercial paper program. At December 31, 2000, Prudential had amounts outstanding under this program of £160 million with an average interest rate of 6.00% per annum. The Group also had amounts outstanding under its multi currency Euro commercial paper program, which was closed in 2000. Amounts outstanding under this program at December 31, 2000 were £16 million with an average interest rate of 6.46% per annum. The commercial paper programs are available for general corporate purposes and to support the liquidity needs of the Group.

Other short-term borrowings are primarily bank loans and overdrafts repayable on demand. Under the terms of the Group's banking arrangements, the lender has a right of offset between credit balances (other than those of long-term funds) and all overdrawn balances of those Group undertakings under similar arrangements.

Repurchase Agreements

During 2000 and 1999, Jackson National Life entered into reverse repurchase and dollar-roll repurchase agreements whereby Jackson National Life agreed to sell and repurchase securities. These

25 Borrowings (Continued)

activities have been accounted for as financing transactions, with the assets sold remaining in the consolidated balance sheets and liabilities recorded for the sales proceeds. Short-term liabilities under such agreements averaged £449 million and £613 million during 2000 and 1999, at weighted average interest rates of 6.52% and 5.39%, respectively. Interest expense on such agreements was £29 million and £33 million in 2000 and 1999, respectively. The highest level of short-term liabilities at any month end was approximately £792 million in 2000 and £931 million in 1999.

Long-term Borrowings

In May 1999, the Company issued £250 million principal amount 5.5% Bonds, due 2009, and £250 million principal amount 5.875% Bonds, due 2029. The combined proceeds of these debt issues along with net cash held were used to finance the acquisition of M&G and a £262 million injection of regulatory capital in Egg.

In January 1998, the Company issued £300 million principal amount 6.875% Bonds, due 2023, the proceeds of which were used to repay the Swiss Franc 200 million principal amount Guaranteed Bonds at maturity, settle a related swap transaction which matured that month, and repay certain short-term borrowings.

In March 1997, Jackson National Life issued 8.15% unsecured surplus notes in the principal amount of US $250 million (£167 million), which are scheduled to mature in March 2027. The surplus notes are subordinate to all present and future indebtedness, policy claims and other creditor claims. Payments of interest or principal may be made only with prior regulatory approval, and only out of surplus earnings that the regulators determine to be available for payment. The surplus notes may not be redeemed at the option of Jackson National Life or any holder prior to maturity.

The £100 million principal amount undated guaranteed subordinated bonds issued by Scottish Amicable Finance plc bear a fixed interest rate of 8.5% until June 2018 at which time the notes can either be redeemed or extended for five year periods, each time at a rate of interest based on the market rate at the applicable date. The interests of the holders of these bonds are subordinate to the entitlements of the policyholders of SAIF. PAC has guaranteed this obligation.

The senior debt represents debt issued by investment subsidiaries managed by PPM America, the US fund management operation, which is collateralized by the investments held by the relevant investment subsidiaries. Interest rates on the senior debt are variable based on a market interest rate and range from 7.38% to 8.63% at December 31, 2000. The interests of the holders of the subordinated debt issued by these subsidiaries are subordinate to the entitlements of the holders of the senior debt. Interest rates on the subordinated debt are fixed and range from 7.80% to 8.36% at December 31, 2000. The term of the revolving credit facility drawn on by these subsidiaries includes a cross default provision with the subordinated notes. In addition to the debt of these subsidiaries, the US fund management operation manages investment funds with liabilities of £1,030 million pertaining to debt instruments issued to external parties. In all instances the holders of the debt instruments issued by these subsidiaries do not have recourse beyond the assets of these subsidiaries.

Several of the long-term borrowing agreements have restrictive covenants. The Group is in compliance with all debt covenants.

26 Dividend Restrictions and Minimum Capital Requirements

Certain Group subsidiaries are subject to restrictions on the amount of funds they may transfer in the form of cash dividends or otherwise to the Company. At December 31, 2000 the Company had £1,434 million of retained profit that is wholly available for distribution to shareholders.

Jackson National Life can pay dividends on its capital stock only out of earned surplus. Dividends which exceed the greater of 10% of Jackson National Life's statutory surplus or statutory net gain from operations for the prior year require prior regulatory approval. At December 31, 2000, the maximum amount of dividends that could be paid by Jackson National Life without prior regulatory approval was approximately US $160 million (£107 million).

The Group's Asian subsidiaries, mainly the Singapore and Malaysia businesses, may remit dividends to the Group, in general, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations. At December 31, 2000, the maximum amount of dividends that could be paid by the Asian subsidiaries was £73 million.

In accordance with the UK Insurance Companies Act 1982, UK insurance companies are required to maintain solvency margins which must be supported by capital reserves and other resources, including unrealized gains and losses on investments. The Group's insurance businesses in other countries, mainly in the United States, Singapore and Malaysia, are also subject to capital adequacy and solvency margin regulations. Management believes that the Group's subsidiaries are in compliance with all applicable solvency and capital adequacy requirements.

Jackson National Life and PAC are the two principal insurance subsidiaries of the Group which together comprise in excess of 76% of total Group assets. At December 31, 2000, the statutory capital and surplus of Jackson National Life was £1,487 million. At December 31, 2000 the PAC long-term fund's excess of assets over its required minimum solvency margin was approximately £9,041 million. At December 31, 2000 the PAC general business and shareholders' funds had assets in excess of the required minimum solvency margin of approximately £161 million.

27 Commitments and Contingencies

Commitments

Prudential has provided, from time to time, certain guarantees and commitments to third parties. These arrangements include commitments and guarantees by Prudential to fund the purchase or development of land and buildings and other commitments related to the Group's investments in land and buildings. At December 31, 2000, the aggregate amount of commitments and guarantees in respect of land and buildings was approximately £168 million.

Contingencies

Pension misselling

In 1988, the UK government introduced new pensions legislation intended to encourage more individuals to make their own arrangements for their pensions. During the period from April 1988 to June 1994, many individuals were advised by insurance companies, IFAs and other intermediaries to not join, to transfer from or to opt out of their occupational pension schemes in favor of private pension products introduced under the UK Income and Corporation Taxes Act 1988. The UK

27 Commitments and Contingencies (Continued)

insurance regulator (previously the Personal Investment Authority, now the Financial Services Authority) subsequently determined that many individuals were incorrectly advised and would have been better off not purchasing the private pension product sold to them. Industry participants are responsible for compensating the persons to whom private pensions were missold. As a result, the UK regulator required that all UK life insurance companies review their potential cases of pension misselling arising and pay compensation to policyholders where necessary and as a consequence record a provision for the estimated benefits entitled.

The UK regulator has divided the review into two phases. Phase 1 cases, originally referred to as priority cases, consisted primarily of cases where the investor was close to retirement or had died or retired since purchasing the pension product. Phase 2 cases, originally referred to as non-priority cases, are primarily younger investors who have retirement dates which are not near term. The regulator initially established deadlines for reviewing Phase 1 cases and had the power to impose sanctions where companies failed to meet the deadlines or otherwise did not comply with the regulator's guidelines for the resolution of cases of pensions misselling. In 1998, the regulator established the procedures and deadlines for reviewing Phase 2 cases.

In relation to this pension misselling review, a provision has been established, which has been charged as a change in the long-term technical provisions in the Group's profit and loss accounts. Within the long-term business technical account the transfer to FFA has been determined after taking account of charges to long-term business technical provisions for changes in the pension misselling liability. The following provides a summary of the changes in the pension misselling liability including internal and external legal and administrative costs for each of the years ended December 31:

	2000	1999	1998
	(In £ Millions)		
Balance at January 1	**1,700**	1,100	450
Cases added due to expanded scope of the review	**—**	202	759
Change in actuarial assumptions and method of calculation	**(117)**	261	—
Increase in provision for administrative expenses	**50**	190	—
Discount accretion	**102**	66	27
Redress to policyholders	**(134)**	(73)	(110)
Payments of administrative costs	**(126)**	(46)	(26)
Balance at December 31	**1,475**	1,700	1,100

In 1998 and 1999 the scope of the pension misselling review was expanded by the UK regulator to include Phase 2 cases and as a result the Group increased the provision to reflect the increase in the number of cases to be reviewed and the possible increase in the amount to be paid to policyholders. The increase in the provision as a result of this expansion in scope amounted to £759 million in 1998 and £202 million in 1999.

The UK regulator updates the actuarial assumptions to be used in calculating the provision including interest rates and mortality assumptions every six months. In addition in 1999 the UK regulator also changed the method of calculation of the provision. These changes resulted in a decrease in the provision in 2000 of £117 million and and an increase in 1999 of £261 million.

27 Commitments and Contingencies (Continued)

In 2000 the provision for administrative expenses was increased by £50 million reflecting the additional cost the Group expects to incur settling Phase 2 cases. The increase in the provision for administrative expenses of £190 million in 1999 reflected the additional administrative costs the Group expects to incur predominantly due to the shortening of the deadline for completing the Phase 2 cases by the UK regulator from December 2004 to June 2002.

The pension misselling liability represents the discounted value of future expected payments, including benefit payments and all internal and external legal and administrative costs of adjudicating, processing and settling these claims and as a consequence, to the extent that amounts have not been paid, the provision increases each year reflecting the accretion of the discount.

Management believes that, based on current information, the pension misselling provision, together with future investment return on the assets backing the provision, will be adequate to cover the costs of pension misselling as well as the costs and expenses of the Group's pension review unit established to identify and settle such cases. Such provision represents the best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased. The Group has estimated, based on current FSA guidelines, that the discounted present value of reasonably possible losses might range up to an additional £160 million over that provided at December 31, 2000. This potential additional provision has been determined using more stringent assumptions in respect of customer responses to mailings and redress in comparison to external occupational schemes, applied to those cases identified at December 31, 2000.

The calculation of the pension misselling provision is dependent upon a number of assumptions and requirements provided by the UK regulator. Following a visit from the UK regulator concerns have been raised over the Group's proper completion of certain aspects of Phase 1. The outcome of this review is currently uncertain and as a result additional corrective action may be initiated.

Throughout the pension misselling review process the UK regulator has made changes to its requirements and therefore it is not possible to predict any additional changes to the requirements and any resultant changes to the provision that might be made in the future.

As approved by the UK regulator, the pensions misselling provision is funded from the PAC with-profits fund. Given the strength of the with-profits fund, management believes that the pensions misselling provision will not have an adverse impact on the levels of bonuses paid to policyholders or their reasonable expectations. In the unlikely event that this proves not to be the case, an appropriate contribution to the with-profits fund would be made from the shareholders' funds. In view of this uncertainty, it is not practicable to estimate the level of this potential contribution.

Free Standing Additional Voluntary Contribution business

In February 2000, the UK regulator ordered a review of Free Standing Additional Voluntary Contribution business, which constitutes sales of personal pensions to members of company pension schemes. Individuals who have purchased these pensions instead of the Additional Voluntary Contributions (AVC) scheme connected to their company's pension scheme may have been in a better financial position investing their money, and any matching contributions from their employers, in their company's AVC scheme. The UK regulator's review is to ensure that any employees disadvantaged due

27 Commitments and Contingencies (Continued)

to not being properly informed of the benefits foregone from not investing in their AVC scheme are compensated.

The review requires companies to identify relevant investors and contact them offering to review their individual case. As a result of the work completed to date, Prudential has established a liability of £68 million as of December 31, 2000, which has been charged as a change in the long-term business technical provisions in Prudential's profit and loss accounts. Within the long-term business technical account, the transfer to FFA has been determined after taking account of changes to long-term business technical provisions. The deadline for completing the reviews is June 30, 2002.

Management believes 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 reviewing Free Standing Additional Contribution business as well as the costs and expenses of the review unit established to identify and settle such cases. The provision represents Prudential's best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

Litigation

The Company and its subsidiaries are involved in litigation arising in the ordinary course of business. Some of the actions and proceedings have been brought on behalf of various alleged classes of claimants and certain of these claimants seek damages of unspecified amounts. While the outcome of such matters cannot be predicted with certainty, it is the opinion of management that the ultimate outcome of such litigation will not have a material adverse effect on Prudential's financial condition, results of operations or cash flows.

On December 14, 2000, proceedings were issued against Prudential Assurance by a policyholder. These proceedings, which relate to the assets represented by the FFA in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers (''excess assets'') in Prudential Assurance's long-term fund, ask the court to decide whether and, if so, to what extent the excess assets should be paid out to or applied for the benefit of stockholders and/or shareholders. Prudential is considering the proceedings and the issues raised by them with its legal advisers.

The amount and timing of any attribution to shareholders is sufficiently uncertain that it is not possible to accurately estimate any potential attribution. In addition, it is likely that if any excess assets are attributed to shareholders, they will remain in Prudential Assurance's long-term fund to support the long-term business, and accordingly, they are unlikely to be distributed to shareholders for some considerable period of time, if at all.

Jackson National Life has been named in civil proceedings, which appear to be substantially similar to other class action litigation brought against many life insurers alleging misconduct in the sale of insurance products. At this time, it is not possible to make a meaningful estimate of the amount or range of loss, if any, that could result from an unfavorable outcome in such actions. In addition, Jackson National Life is a defendant in several individual actions that involve similar issues, including an August 1999 verdict against Jackson National Life for $33 million (£22 million) in punitive damages. Jackson National Life has appealed the verdict on the basis that it is not supported by the facts or the law. No amount has been accrued with regard to the above proceedings.

27 Commitments and Contingencies (Continued)

Other Matters

Long-term business fund

The long-term business funds retain the annual profit and loss activity of with-profits business in excess of bonus distributions and associated shareholders' distributions for the year within the fund for future appropriations. The balance of the long-term business fund has accumulated over many years and has come from a variety of sources. Management believes that the balance of the long-term business fund is greater than amounts anticipated to be distributed as benefits and future annual and terminal bonuses on policies currently in-force. Prudential is currently discussing the attribution of unallocated assets in the PAC long-term business fund with the Financial Services Authority, the UK insurance regulator. These discussions may or may not result in an additional portion of the long-term business fund being attributed to shareholders at some future date. Due to the uncertainty, no amount in respect of any attribution to shareholders has been reflected in the consolidated financial statements.

Shareholder support of long-term business funds

As a proprietary insurance company, the Group 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 FFA in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers ("excess assets") in the long-term funds could be materially depleted over time, by, for example, a significant or sustained equity market downturn, significant fundamental strategic change costs, or material increases in the pensions misselling provision. In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the Group's ability to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations to the policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency. As of December 31, 2000 and 1999, the excess of SAIF assets over guaranteed benefits was £3,082 million and £3,699 million, respectively. Due to the quality and diversity of the assets in SAIF, the aforementioned amounts of the excess of assets over guaranteed benefits and the ability of the Group to revise guaranteed benefits in case of an asset shortfall, the Group believes that the probability of either the PAC long-term fund or the Group shareholders' funds having to contribute to SAIF is less than remote.

Guarantee funds

Guarantee funds in both the UK and US provide payments to policyholders on behalf of insolvent life insurance companies. These guarantee funds are financed by payments assessed on solvent insurance companies based on location, volume, and types of business. The Group has estimated its reserve for future guarantee fund assessments for Jackson National Life to be £38 million at December 31, 2000. Similar assessments for UK and Asian businesses were not significant. Management believes the reserves are adequate for all anticipated payments for known insolvencies.

27 Commitments and Contingencies (Continued)

Synthetic guaranteed investment contracts

Jackson National Life offers synthetic guaranteed investment contracts to Group customers including pension funds and other institutional organizations. These contracts represent an off-balance sheet fee-based product where the customer retains ownership of the assets related to these contracts and Jackson National Life guarantees each contractholder's obligations to its own members in respect of these assets. The values of off-balance sheet guarantees were £31 million and £29 million at December 31, 2000 and 1999, respectively.

Management believes the risk under these contracts is mitigated by careful underwriting of the contractholder and a number of features associated with these contracts, including controls on the plan's investments, requirements for "buffer funds" to absorb unexpected fluctuations in member withdrawals and, for most contracts, experience rating of the crediting rates granted to plan members.

Mortgage Endowment Products

The UK regulator announced in November 2000 that as part of its review of the sale of endowment policies, it would look into instances where it considered policyholders had not been treated fairly due to "product flaws".

Prudential's primary exposure in this area is in connection with Scottish Amicable Insurance Fund with regard to policies written by Scottish Amicable prior to its acquisition by Prudential. The UK regulator has notified a number of companies, including Scottish Amicable, of their concerns about the basis of premium calculation. This matter is under discussion with the UK regulator.

The UK regulator issued a report in March 2001 raising concerns regarding Scottish Amicable's conduct of sales of mortgage endowments since 1999. Scottish Amicable is considering its response and will work with the regulator to resolve the concerns raised.

In April 2001, Prudential announced that, due to the shift within the marketplace towards repayment mortgages over the past two years, and the consequent significant fall in demand for endowment products, Scottish Amicable would withdraw from the mortgage endowment sales market.

28 Supplemental Information

Cash flows

The following supplemental cash flows information provides details of amounts in the consolidated statement of cash flows from general business and shareholders' funds and reconciles the cash amounts to the consolidated balance sheets:

Reconciliation of operating profit to net cash inflow from operations	**2000**	**1999**	**1998**
	(In £ Millions)		
Operating profit before amortization of goodwill and before tax (based on longer term investment returns)	**840**	776	868
Add back: interest charged to operating profit	**143**	131	105
Adjustments for non-cash items:			
Tax on long-term business profits and franked investment income	**(285)**	(263)	(235)
General business and shareholder longer term investment gains	**(28)**	(33)	(23)
Increase (decrease) in general business technical provisions	**71**	(33)	(39)
Amounts retained and invested in long-term business operations	**(449)**	(332)	(309)
Decrease (increase) in banking business assets (net of liabilities)	**76**	(286)	(69)
Other*	**30**	82	(53)
Net cash inflow from operations as shown on the consolidated statements of cash flows from general business and shareholders' funds	**398**	42	245

* The 1999 amount of £82 million for other adjustments of non-cash items includes the effects of restructuring costs that had not been paid at December 31, 1999.

28 Supplemental Information (Continued)

Changes in investments net of financing	2000	1999	1998
		(In £ Millions)	
Movements arising from cash flows:			
Increase in cash and short-term deposits as shown on the consolidated statements of cash flows	**185**	97	238
Net purchases (sales) of portfolio investments	**(162)**	(1,675)	76
Decrease (increase) in loans	**114**	(668)	(314)
Movement on credit facility by investment subsidiaries managed by US fund management operations	**31**	(103)	—
Share capital issued	**(184)**	(34)	(15)
Total movements arising from cash flows	**(16)**	(2,383)	(15)
Investment appreciation	**22**	76	42
Investments and cash acquired with purchase of M&G	**16**	214	—
Foreign exchange translation and other	**9**	37	(15)
Transfer to retained profit in respect of shares issued in lieu of cash dividends	**20**	15	—
Portfolio investments, net of financing, beginning of year	**(1,025)**	1,016	1,004
Portfolio investments, net of financing, end of year	**(974)**	(1,025)	1,016
Represented by:			
Investments (including short-term deposits)	**983**	1,078	2,339
Cash at bank and in hand	**209**	150	270
Borrowings	**(1,714)**	(1,965)	(1,324)
Cumulative charge to Group profit and loss account reserve in respect of shares issued to qualifying employee share ownership trust	**105**	59	50
Share capital and share premium	**(557)**	(347)	(319)
Portfolio investments, net of financing, end of year	**(974)**	(1,025)	1,016
Reconciliation of investments to the consolidated balance sheets			
General business and shareholder investments (as above)	**983**	1,078	2,339
Long-term business	**117,445**	113,463	97,973
Total portfolio investments in the consolidated balance sheets	**118,428**	114,541	100,312
Reconciliation of cash to the consolidated balance sheets			
General business and shareholders (as above)	**209**	150	270
Long-term business	**1,193**	638	414
Total cash at bank and in hand in the consolidated balance sheets	**1,402**	788	684
Reconciliation of borrowings to the consolidated balance sheets			
General business and shareholders (as above)	**1,714**	1,965	1,324
Long-term business	**267**	255	255
Total borrowings in the consolidated balance sheets	**1,981**	2,220	1,579

28 Supplemental Information (Continued)

The following table provides a summary of the items comprising the net cash flows relating to acquisitions and disposals of subsidiaries:

Acquisitions and disposals of subsidiaries	2000 Acquisitions	2000 Flotation of Egg and Disposals of Businesses	2000 Total	1999	1998
	(In £ Millions)				
Net assets acquired (disposed of):					
Investment in associates	**—**	**(79)**	**(79)**	—	—
Other investments	**—**	**—**	**—**	187	—
Goodwill asset	**130**	**(22)**	**108**	1,577	59
Net assets held in long-term business operations	**—**	**184**	**184**	213	(127)
Net banking assets	**30**	**149**	**179**	—	—
Minority interest in Egg	**—**	**(120)**	**(120)**	—	—
Tax payable	**—**	**—**	**—**	(9)	(39)
Cash	**16**	**—**	**16**	27	—
Other net assets	**7**	**(31)**	**(24)**	16	—
Total net assets acquired (disposed of)	**183**	**81**	**264**	2,011	(107)
Cash (consideration paid) proceeds received including acquisition and disposal costs	**(183)**	**195**	**12**	(2,011)	345
Net impact on shareholders' funds	**—**	**276**	**276**	—	238
Represented by:					
Short-term fluctuations in investment returns after tax	**—**	**19**	**19**	—	—
Goodwill credited to shareholders' funds	**—**	**90**	**90**	—	28
Profit after tax on disposal	**—**	**167**	**167**	—	210
Total	**—**	**276**	**276**	—	238

Net banking assets of £149 million in regards to the flotation of Egg and disposal of businesses represents cash received and retained by Egg from the flotation of its shares.

28 Supplemental Information (Continued)

Scottish Amicable Insurance Fund

Assets and liabilities included in the consolidated balance sheets with respect to SAIF are as follows:

	December 31	
	2000	1999
	(In £ Millions)	
Assets		
Investments:		
Land and buildings	**1,505**	1,396
Other financial investments	**13,726**	14,323
Total investments	**15,231**	15,719
Reinsurers' share of technical provisions for linked liabilities	**1,809**	1,835
Reinsurers' share of long-term business technical provision	**7**	7
Debtors	**59**	96
Cash at bank and in hand	**207**	133
Accrued interest and rent	**116**	80
Deferred acquisition costs	**148**	175
Other prepayments and accrued income	**6**	6
Total assets	**17,583**	18,051
Liabilities		
Fund for future appropriations*	**3,082**	3,699
Long-term business technical provision	**12,192**	11,819
Technical provisions for linked liabilities	**1,809**	1,835
Deferred tax	**247**	434
Debenture loans	**100**	100
Other creditors	**149**	119
Accruals and deferred income	**4**	45
Total liabilities	**17,583**	18,051

* Wholly attributable, but not allocated to policyholders.

28 Supplemental Information (Continued)

Revenues and expenses included in the consolidated long-term business technical accounts with respect to SAIF are as follows:

	2000	1999	1998
	(In £ Millions)		
Gross premiums	**517**	572	581
Reinsurance premiums ceded	**(70)**	(72)	(67)
Earned premiums, net of reinsurance	**447**	500	514
Claims incurred, net of reinsurance	**(956)**	(862)	(855)
Change in long-term technical provisions, net of reinsurance	**(454)**	(588)	(891)
Investment returns	**441**	2,445	1,682
Net operating expenses	**(116)**	(68)	(85)
Tax attributable to long-term business	**21**	(205)	(137)
Transfers from/(to) the SAIF fund for future appropriations	**617**	(1,222)	(228)
Balance on long-term technical accounts	**—**	—	—

UK Banking Operations

Net operating loss before tax included in the consolidated profit and loss accounts in respect of UK banking operations are as follows

	2000	1999	1998
	(In £ Millions)		
Interest income:			
Loans and advances to banks	**79**	159	14
Loans and advances to customers	**211**	84	34
Debt securities	**249**	142	39
Other	**118**	79	22
	657	464	109
Interest expense:			
Customer accounts	**(451)**	(362)	(75)
Other	**(126)**	(78)	(23)
	(577)	(440)	(98)
Net interest income	**80**	24	11
Administrative expenses	**(193)**	(150)	(77)
Provision for bad and doubtful debts	**(37)**	(9)	(2)
Other	**(5)**	(15)	(9)
Net operating loss before tax	**(155)**	(150)	(77)

28 Supplemental Information (Continued)

Assets, liabilities and shareholders' funds included in the consolidated balance sheets with respect to the UK banking operations are as follows:

	December 31	
	2000	**1999**
	(In £ Millions)	
Assets		
Loans and advances to banks	**238**	2,613
Loans and advances to customers	**3,736**	2,046
Debt securities	**3,686**	3,971
Other banking assets	**235**	222
Total banking assets	**7,895**	8,852
Intragroup balances	**—**	58
Other assets, including tax	**39**	26
Total	**7,934**	8,936
Liabilities		
Customer accounts	**7,128**	8,157
Other banking liabilities	**258**	279
Total banking liabilities	**7,386**	8,436
Intragroup liabilities	**1**	4
Tax balances	**23**	29
	7,410	8,469
Shareholders' funds		
Group share	**417**	467
Minority interests	**107**	—
Total	**7,934**	8,936

29 Pension Plans and Information on Staff

The Group operates a variety of pension benefit plans around the world covering the majority of Group employees. The specific features of these plans vary in accordance with the regulations of the country in which employees are located, although they are, in general, funded wholly by the Group and based either on a cash balance formula or on years of service and salary earned in the last year or years of employment. The Group's principal UK defined benefit plan, the Prudential Staff Pension Scheme, covers approximately 57% of all the Group's employees.

The projected accrued benefits method was used to value the Prudential Staff Pension Scheme defined benefit plan. The principal actuarial assumptions adopted were investment return at 7.1% per annum, earnings that qualify for pension benefits growth of 5.0% per annum, increases to pensions in payment of 3.0% per annum and dividend growth of 3.5% per annum.

Plan assets are held in a separate trustee administered fund. The market value of plan assets at the valuation date was approximately £4,504 million with the actuarial value of the assets being

29 Pension Plans and Information on Staff (Continued)

sufficient to cover 116% of the benefits that had accrued to members. As a result of the actuarial valuation, the employer's contribution rate became the minimum prescribed under the plan rules, currently equivalent to 10.6% of earnings that qualify for pension benefits.

The plan was last valued for UK purposes as at April 5, 1999 by a qualified actuary as required under the triennial valuation.

The Group also sponsors various defined contribution plans. The most significant of these plans covers Jackson National Life employees. To be eligible for the Jackson National Life plan, an employee must have attained the age of 21 and completed at least 1,000 hours of service in a 12 month period. Annual contributions to the plan are based on a percentage of eligible compensation paid to participating employees during the year.

Following is an analysis of the Group's Pension expenses:

	2000	1999	1998
	(In £ Millions)		
Defined benefit plans	**37**	41	36
Defined contribution plans	**9**	6	5
Total pension expense[(1)]	**46**	47	41

(1) Total pension expense includes £7 million, £4 million and £4 million for 2000, 1999, and 1998, respectively, relating to pension plan expense outside of the UK.

The average numbers of staff employed by the Group during the year were:

	2000	1999
UK Operations	**16,652**	18,885
US Operations	**2,250**	1,640
Asian Operations	**2,635**	1,535
European Operations	**405**	312
Group total	**21,942**	22,372

The costs of employment were:

	2000	1999	1998
	(In £ Millions)		
Wages and salaries	**656**	637	576
Social security costs	**55**	51	44
Other pension costs	**46**	47	41
Group total	**757**	735	661

30 Stock-based Compensation

The Group maintains five active stock award and stock option plans: the Restricted Share Plan; the Share Participation Plan; the Managers' Share Plan; the Professional Reward Scheme; and the Savings-Related Share Option Scheme. The Group has established various trusts to facilitate the delivery of shares under the stock-based compensation plans.

The Restricted Share Plan is the Group's long-term incentive plan for executive directors and other senior executives. Each year participants are granted a conditional option to receive a number of shares. There is a deferment period, currently three years, at the end of which the award vests to an extent that depends on the performance of the Group's stock including notional reinvested dividends. After vesting, the award may then be exercised at zero cost at any time, subject to closed period rules, in the balance of a ten year period. Shares are purchased in the open market by a trust for the benefit of qualifying employees. Currently, the trust holds at least the maximum number of shares conditionally awarded and not yet forfeited or exercised. The Restricted Share Plan replaced the Executive Share Option Scheme in 1995 and options remain outstanding under this prior plan for exercise no later than 2005.

The Share Participation Plan is designed to encourage share ownership amongst senior executives and to provide rewards based upon various performance factors of the Group. Each year, participants may be offered the choice of a cash award, a matching share award if cash or shares to the value of the cash award are lodged, or a combination of 50% of each. Share awards vest after five years for executive directors of Prudential plc and three years (formerly five years) for all other eligible employees and are transferred to the participants at no additional cost. Ordinary shares for share awards are purchased in the open market by a trust, which holds them during the vesting period for the benefit of qualifying employees.

The Managers' Share Plan is offered to a selected group of managers of the Group in order to acknowledge their contribution and to promote alignment with the interests of the Group's shareholders. The size of the awards is based on an assessment of overall Group performance. Participants receive annual share awards that vest after a three-year period. After vesting, awards are transferred to participants at no cost. Ordinary shares for share awards are purchased in the open market by a trust which holds them during the vesting period for the benefit of qualifying employees. No new awards under the Managers' Share Plan were made after the year ended December 31, 1998.

The Professional Reward Scheme is designed to reward certain high performing members of the salesforce with both share options and share awards. Based on specified sales level criteria participants are granted both share options and share awards annually that vest after a three-year period. After vesting, participants receive immediate title to share awards and are able to exercise their stock options at any time over the next seven years. Ordinary shares for share awards and grant of options are purchased in the open market by a trust, which holds them during the vesting period for the benefit of qualifying employees.

The Savings-Related Share Option Scheme is designed to foster share ownership among UK employees. Permanent employees are eligible for this plan if they have been employed by the Group for the previous six months. At the outset participants choose an option period (three, five or seven years, or a combination of these periods) and the amount of monthly contributions to be made from their earnings during the option period, which determines the number of options granted. The option

30 Stock-based Compensation (Continued)

price is fixed at the start and is based on a discount of 20% to the market price. Participants may exercise their options within six months of the end of the option period. If options are not exercised, participants are entitled to receive a refund of their cash contributions plus interest. The maximum number of shares that may be issued on exercise of options under this plan is 367.7 million.

During 2000, Egg initiated two stock-based compensation plans, the Egg Restricted Share Plan and the Egg Employee Share Options Plan. Both plans are based on shares in Egg, not Prudential plc. At December 31, 2000, 12.1 million share awards relating to these plans were outstanding. Any compensation expense relating to these plans is included in the Group totals.

At December 31, 2000, 7.2 million of the Company's shares, with a market value of £78 million, were held in various trusts relating to incentive plans and ownership trusts. Shares held in these trusts are conditionally gifted to employees. The employees' entitlements to dividends and eventual distribution depend upon the particular terms of each incentive plan.

At December 31, 2000, 5.2 million of the 7.2 million shares held by trusts under employee incentive plans have been accounted for in the consolidated balance sheet as own shares. The carrying value of the shares is £24 million, which represents the cost of purchase less the cumulative amounts charged to the profit and loss account. In addition, at December 31, 2000, 2 million shares were held by a qualifying employee share ownership trust. These shares are expected to be fully distributed shortly after June 1, 2001 on current maturities of the savings-related share option plan. The exercise price of options outstanding in respect of these shares is £3.44 per share. The shares are valued at the amount of expected proceeds and are carried at £7 million as an asset on the consolidated balance sheets. Share options outstanding under the Group's share-based compensation plans during 2000, 1999 and 1998 were as follows:

	2000		1999		1998	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
	(Millions)	£	(Millions)	£	(Millions)	£
Options outstanding:						
Beginning of year	**32.0**	**4.31**	33.5	3.50	39.2	3.18
Granted	**4.1**	**6.29**	9.2	5.82	3.6	6.13
Exercised	**(8.8)**	**3.51**	(8.2)	2.46	(5.7)	2.60
Cancelled	**(2.1)**	**5.34**	(2.5)	4.83	(3.6)	3.98
End of year	**25.2**	**4.84**	32.0	4.31	33.5	3.50
Options immediately exercisable, end of year	**3.9**	**3.66**	4.6	3.08	4.8	2.92

30 Stock-based Compensation (Continued)

Share awards outstanding under the Group's share-based compensation plans at December 31, 2000, 1999 and 1998 are as follows:

	Number of Awards		
	2000	**1999**	**1998**
	(Millions)		
Share awards outstanding:			
Beginning of year	**1.9**	2.4	2.0
Granted	**0.1**	0.5	0.8
Exercised	**(0.8)**	(0.8)	(0.3)
Cancelled	**(0.2)**	(0.2)	(0.1)
Share awards outstanding, end of year	**1.0**	1.9	2.4

At December 31, 2000, the weighted average contractual life of outstanding awards was 0.7 years. The following table provides a summary of the range of exercise prices for options outstanding at December 31, 2000:

	Options Outstanding			Options Exercisable	
	Number Outstanding	**Weighted Average Remaining Contractual Life**	**Weighted Average Exercise Prices**	**Number Exercisable**	**Weighted Average Exercise Prices**
	(Millions)	(years)	(£)	(Millions)	(£)
Range of exercise prices					
Between £0 and £1	**2.2**	**7.6**	**—**	**0.4**	**—**
Between £1 and £2	**0.1**	**—**	**1.93**	**0.1**	**1.93**
Between £2 and £3	**1.9**	**1.6**	**2.48**	**0.8**	**2.43**
Between £3 and £4	**6.7**	**2.1**	**3.44**	**1.7**	**3.18**
Between £4 and £5	**1.7**	**0.6**	**4.34**	**—**	**—**
Between £5 and £6	**2.0**	**3.3**	**5.12**	**0.4**	**5.37**
Between £6 and £7	**3.3**	**3.2**	**6.19**	**—**	**—**
Between £7 and £8	**6.7**	**4.0**	**7.44**	**0.2**	**7.72**
Between £8 and £9	**—**	**—**	**—**	**—**	**—**
Between £9 and £10	**0.6**	**7.7**	**9.47**	**0.3**	**9.48**
	25.2	**3.5**	**4.84**	**3.9**	**3.66**

(1) Less than 100,000 options exercisable.

There were options outstanding under share option schemes to subscribe for 19.8 million shares, at prices ranging from £2.01 to £7.59 at December 31, 2000. At December 31, 1999, there were options to subscribe for 26 million shares at prices ranging from £1.93 to £7.59. All share options outstanding at December 31, 2000 and 1999 were exercisable no later than 2007.

31 Restructuring provision

Restructuring costs are charged within operating expenses in the long-term business technical account, the general business technical account and the non-technical account.

UK Retail insurance operations

During 1999 the Group made a commitment and announced a plan to restructure its UK work force for the Retail Financial Services, General Insurance and Retail IFA business units. The restructuring plan was substantially completed by December 31, 2000. As a result of this plan a provision of £131 million was established, of which £78 million was borne by the PAC with-profits fund and £53 million was borne by the shareholders' fund. In connection with this plan, the Group decided to reduce its direct salesforce, branch networks and administrative functions that support the salesforce. The components of the aforementioned restructuring cost of £131 million include a provision in respect of termination benefits and redundancy costs of £64 million, branch closures and other property related charges of £56 million and other transition and systems-related costs of £11 million. The total number of staff being made redundant is 3,467 people.

As of December 31, 2000 all affected employees had been notified that they will be terminated. The number of employees made redundant who were still employed at December 31, 2000 was 344. As of December 31, 2000, the amount paid and charged against the provision was £97 million. The remaining costs, with the exception of certain property related charges which will be incurred over future years, will be paid by the end of 2001.

M&G

During 1999 Prudential established a provision of £17 million relating to the integration in the UK of Prudential Portfolio Managers and M&G following the M&G acquisition. The provision was borne by the shareholders' fund.

As part of the integration, Prudential reduced its M&G life/pension and institutional administrative force and eliminated some departments. Prudential also reduced its management force. The provision was comprised of redundancy costs of £9 million, department closures of £2 million, and other collective integration costs of £6 million.

The total number of employees made redundant was 124. The plans were substantially completed by the end of 2000. The amount paid and charged against the provision through December 31, 2000 was £12 million. All remaining amounts will be paid by the end of 2001.

32 Post Balance Sheet Events

Acquisition of Orico Life

On January 23, 2001, Prudential announced an agreement to acquire Orico Life Insurance Co. Ltd. for £133 million (¥23 billion) from Orient Corporation, one of Japan's major consumer credit providers. The deal was completed in February 2001.

Restructuring of UK direct salesforce and customer service channels

On February 13, 2001, Prudential announced its plans to restructure its direct sales channels and customer service operations in the UK. As a result of the restructuring, Prudential expects to incur a restructuring charge of £110 million, of which £13 million will be borne by the shareholders' funds in 2001. Prudential anticipates that the restructuring will result in 2,000 jobs being made redundant.

Proposed acquisition of American General Corporation

On March 12, 2001, Prudential announced an agreement to merge with American General Corporation, a US investment, life, and insurance and consumer finance group in an all share transaction in which each American General Corporation share would have been exchanged for 3.6622 new ordinary shares of Prudential. On completion of the merger, Prudential shareholders would have owned approximately 50.5% and American General shareholders would have owned approximately 49.5% of the combined group on a fully diluted basis.

On May 11, 2001, the merger agreement between Prudential and American General was terminated. In accordance with the merger agreement, Prudential received the full termination fee of £423 million (US$600 million) from American General.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles

The Group's consolidated financial statements are prepared in accordance with UK GAAP. These accounting practices differ in certain material respects from generally accepted accounting principles in the US ("US GAAP"). The material differences between UK GAAP and US GAAP affecting the Group's consolidated profit and loss and shareholders' funds are set forth in the following tables with descriptions of the differences thereafter. The reconciliation tables present an analysis of the material differences affecting both the with-profits funds and other operations. See Note 34 for presentation of condensed consolidated US GAAP financial statements.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

Reconciliation to US GAAP

The approximate effects on consolidated profit and loss of the differences between UK GAAP and US GAAP, including a breakdown of the US GAAP adjustments between with-profits funds and other operations, are as follows:

	2000			1999			1998		
	With-Profits Funds	Other	Total	With-Profits Funds	Other	Total	With-Profits Funds	Other	Total
					(In £ Millions)				
Consolidated profit for the financial year in accordance with UK GAAP			**688**			542			880
US GAAP adjustments:									
Business acquisitions and investments in associates	**36**	**(21)**	**15**	(71)	(33)	(104)	(49)	(34)	(83)
Restructuring charges	**(11)**	**(10)**	**(21)**	11	17	28	—	—	—
Investments:									
Real estate	**(424)**	**—**	**(424)**	(615)	—	(615)	(369)	—	(369)
Securities	**36**	**—**	**36**	711	—	711	(865)	—	(865)
Mortgage and other loans	**10**	**—**	**10**	53	—	53	(52)	—	(52)
Long-term business:									
Revenue and expense recognition	**(157)**	**(111)**	**(268)**	(213)	(24)	(237)	(82)	(40)	(122)
Deferred acquisition costs	**260**	**79**	**339**	103	48	151	51	44	95
Policy liabilities	**1,073**	**45**	**1,118**	52	(3)	49	621	(4)	617
Reversal of transfer (from) to FFA	**(3,409)**	**—**	**(3,409)**	5,103	—	5,103	1,381	—	1,381
Provision for policyholders' share of earnings on with-profits business in excess of cost of policyholder bonuses declared	**1,636**	**—**	**1,636**	(3,876)	—	(3,876)	(509)	—	(509)
Equalization provision	**—**	**8**	**8**	—	7	7	—	8	8
Pension plans	**89**	**21**	**110**	54	13	67	101	27	128
Stock-based compensation	**—**	**(9)**	**(9)**	(1)	(11)	(12)	(4)	(11)	(15)
Deferred income tax	**537**	**(40)**	**497**	(522)	(78)	(600)	(195)	(18)	(213)
Business disposals	**—**	**—**	**—**	—	—	—	—	(78)	(78)
Deferred tax effect of the above adjustments	**142**	**34**	**176**	(358)	(21)	(379)	28	(30)	(2)
Total US GAAP adjustments	**(182)**	**(4)**	**(186)**	431	(85)	346	57	(136)	(79)
Consolidated net income in accordance with US GAAP			**502**			888			801

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The approximate effects on consolidated shareholders' funds of the differences between UK GAAP and US GAAP, including a breakdown of the US GAAP adjustments between with-profits funds and other operations as of December 31 are as follows:

	2000			1999		
	With-Profits Funds	Other Operations	Total	With-Profits Funds	Other Operations	Total
			(In £ Millions)			
Consolidated shareholders' funds in accordance with UK GAAP			**4,020**			3,424
US GAAP adjustments:						
Business acquisitions and investments in associates	**362**	**355**	**717**	327	457	784
Restructuring charges	**—**	**2**	**2**	11	17	28
Investments:						
Real estate	**(4,006)**	**—**	**(4,006)**	(3,607)	—	(3,607)
Securities	**(5)**	**(627)**	**(632)**	(8)	(651)	(659)
Mortgage and other loans	**(47)**	**—**	**(47)**	(57)	—	(57)
Long-term business:						
Revenue and expense recognition	**(1,021)**	**(396)**	**(1,417)**	(855)	(279)	(1,134)
Deferred acquisition costs	**957**	**586**	**1,543**	675	502	1,177
Policy liabilities	**6,156**	**15**	**6,171**	5,068	(36)	5,032
Reversal of FFA	**20,185**	**—**	**20,185**	23,563	—	23,563
Undistributed policyholder allocations	**(18,354)**	**—**	**(18,354)**	(19,950)	—	(19,950)
Equalization provision	**—**	**38**	**38**	—	30	30
Pension plans	**597**	**178**	**775**	508	156	664
Stock-based compensation	**(1)**	**(59)**	**(60)**	—	(73)	(73)
Deferred income tax	**(2,404)**	**(107)**	**(2,511)**	(2,936)	(83)	(3,019)
Shareholder dividend liability	**—**	**322**	**322**	—	299	299
Deferred tax effect of the above adjustments	**(380)**	**89**	**(291)**	(522)	66	(456)
Total US GAAP adjustments	**2,039**	**396**	**2,435**	2,217	405	2,622
Consolidated shareholders' equity in accordance with US GAAP			**6,455**			6,046

The following descriptions of differences between UK and US GAAP include tables summarizing the effects on the condensed consolidated US GAAP balance sheets and income statement lines of the US GAAP adjustments for each reconciling item. For adjustments in respect of with-profits funds, the net effect of a particular US GAAP adjustment on US GAAP consolidated net income or shareholders' equity would be the amounts shown in the table, net of related policyholders' share of the adjustment. The policyholders' share is included in the adjustment for undistributed policyholder allocations.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

Business Acquisitions and Investments in Associates

Business acquisitions are generally accounted for using the purchase method under both UK GAAP and US GAAP. Under UK GAAP, goodwill arising on acquisitions prior to 1998 was charged against shareholders' funds when acquired. Upon disposal of subsidiaries acquired prior to 1998, the entire goodwill recorded at acquisition is credited to shareholders' funds, and charged against the gain or loss on the sale.

Under US GAAP, and UK GAAP for acquisitions subsequent to 1997, goodwill is recorded as an asset and amortized in the consolidated profit and loss account on a straight-line basis over its estimated useful life, generally not exceeding 20 years. Upon disposal, any remaining unamortized goodwill is charged against the gain or loss on the sale.

Under UK GAAP, the Group's interests in associates, principally St. James's Place Capital plc, which was primarily acquired in 1997 as part of the Scottish Amicable transaction and sold in 2000 at a total realized gain of £123 million, and IFonline, which was acquired in 2000, are carried at the Group's share of underlying net assets at the date of acquisition, adjusted each year for the Group's share of increases or decreases in shareholders' funds of the associate. In 1997 and prior periods, the difference between the purchase price of an investment in an associate and the Group's share of net assets was written off to shareholders' funds in the year of acquisition. For investments in associates subsequent to 1997, goodwill is recorded as an asset and amortized in the consolidated profit and loss account on a straight-line basis over its estimated useful life, generally not exceeding 20 years.

Under US GAAP, interests in associates are recorded using the equity method of accounting. Equity method investments are recorded at the purchase price in the year of acquisition including related goodwill. The carrying values of investments in associates are adjusted each year for the Group's share of US GAAP profits or losses, with such adjustments being included in the income statement. Dividends received from associates are recorded as a decrease in the carrying value of the investment. Related goodwill is amortized in the consolidated statement of income on a straight-line basis over its estimated useful life, generally not exceeding 20 years. Investments in other participating interests where the Group does not exercise significant influence are carried at fair value with changes in fair value recognized as unrealized gains and losses and reported, net of applicable income taxes, in other comprehensive income.

In June 2000, the Group sold 68% of its 25% holding in St. James's Place Capital plc (SJPC) for cash proceeds of £213 million. Under UK GAAP, the resulting gain was £99 million. The remaining 32% of the Group's holding in SJPC was sold in July 2000 at a gain of £24 million. These gains were determined after taking into account the investment balance under equity accounting and goodwill written off to reserves recorded upon acquisition. In total, the gain on disposal under UK GAAP was £123 million.

Under US GAAP, the goodwill upon the acquisition of SJPC was capitalized and amortized over 20 years. The resulting aggregate gain, after taking into account the unamortized balance of goodwill and the investment balance under equity accounting, was £136 million.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for business acquisitions and investments in associates had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Investment results	**126**	(45)	—
Underwriting, acquisition and other operating expenses	**(64)**	—	—
Other charges (amortization expense)	**(47)**	(59)	(83)
Total US GAAP adjustments	**15**	(104)	(83)
Condensed consolidated US GAAP balance sheets:			
Fixed maturities	**(79)**	—	
Equity securities	**(44)**	58	
Other investments	**47**	79	
Intangible assets	**801**	750	
Other assets	**254**	—	
Debt	**(201)**	—	
Other liabilities	**(61)**	(103)	
Total US GAAP adjustments	**717**	784	

Restructuring Charges

Under UK GAAP, restructuring charges can be provided as a liability on the basis that the entity has a constructive obligation. A constructive obligation has arisen when the entity has a detailed formal plan and raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or by making a public commitment. The establishment of a restructuring liability is charged to the profit and loss account for both restructurings of existing and newly acquired operations.

Under US GAAP, restructuring charges arising from business combinations and relating to involuntary termination/relocation of the acquired entity's employees or costs relating to exiting an activity of the acquired company are recognized as liabilities assumed in the business combination and included in the accounting for the acquisition. Restructuring charges related to involuntary employee terminations or other costs to exit existing activities are accrued with a charge to income when a formal plan is approved by management and specific information regarding termination benefits is communicated to affected employees.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for restructuring charges had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Underwriting, acquisition and other operating expenses	**(21)**	28	—
Total US GAAP adjustments	**(21)**	28	—
Condensed consolidated balance sheets:			
Intangible assets	**—**	5	
Other liabilities	**2**	23	
Total US GAAP adjustments	**2**	28	

Under US GAAP, the 1999 provision for restructuring the UK Retail insurance operations to reduce the direct salesforce, branch networks and administrative function was for termination benefits and redundancy costs of £53 million, branch closures and other property related charges of £53 million and other transition and systems related costs of £11 million. In 2000, additional redundancy costs of £11 million were provided for US GAAP purposes, which were provided in 1999 under UK GAAP. The total number of staff being made redundant is 3,467. As of December 31, 2000 all affected employees had been notified that they will be terminated. The number of employees made redundant who were still employed at December 31, 2000 was 344.

Under US GAAP, in 1999 £5 million of the provision for the reduction of Prudential M&G Asset Management life and pension and institutional administrative force, elimination of some departments and the reduction of the management force has been accounted for as part of the M&G purchase price. Termination benefits of a further £2 million had been charged as restructuring costs and an additional £1 million was provided for employee retention bonuses. The remaining costs recorded under UK GAAP did not qualify for inclusion under US GAAP. In 2000, additional redundancy, integration and closure costs of £7 million were paid and accounted for under US GAAP. These costs were provided in 1999 under UK GAAP. The total number of people made redundant and terminated by December 31, 2000 was 124.

Investments

Real estate

Under UK GAAP, investments in tenant and Group occupied freehold and leasehold properties are carried at fair value as defined by The Royal Institution of Chartered Surveyors guidelines. The costs of additions and renovations are capitalized and considered when estimating fair value.

Under US GAAP, investments in tenant and Group occupied freehold and leasehold properties are carried at depreciated cost. Depreciation is calculated using the straight-line method over the properties' estimated useful lives, generally 30 to 50 years. The costs of additions and renovations are capitalized and depreciated using the straight-line method over the estimated useful lives, generally 7 to

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

25 years, or the remaining useful life of the property if shorter. Property is considered to be impaired when its carrying value exceeds the future undiscounted estimated cash flow of the property. Impaired property is written down to fair value, through a charge to the statement of income. Rental income and rental expense are recognized on a straight line basis over the term of the lease.

The US GAAP adjustments for real estate had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Investment results	**(418)**	(607)	(363)
Other charges (depreciation on Group occupied properties)	**(6)**	(8)	(6)
Total US GAAP adjustments	**(424)**	(615)	(369)
Condensed consolidated US GAAP balance sheets:			
Real estate	**(4,051)**	(3,677)	
Other assets (Group occupied properties)	**45**	70	
Total US GAAP adjustments	**(4,006)**	(3,607)	

Securities

Under UK GAAP, equity securities and unit trusts are carried at fair value. Debt and other fixed income securities are carried at fair value, except for those held by Jackson National Life, which are carried at amortized cost. Changes in fair value are recorded in the consolidated profit and loss account.

Under US GAAP, investments in debt and equity securities are carried at fair value. Changes in fair value of securities classified as trading are recognized in the statement of income. Changes in fair value of securities classified as available-for-sale are recorded as a component of other comprehensive income in shareholders' equity, net of related deferred acquisition cost amortization, change in policyholder benefit liabilities and deferred taxes. When impairment of available-for-sale securities is deemed to be other than temporary, the decrease in value is included in the statement of income as a realized loss and a new cost basis is established.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for securities had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Investment results	**36**	711	(865)
Total US GAAP adjustments	**36**	711	(865)
Condensed consolidated US GAAP balance sheets:			
Fixed maturities	**(642)**	(685)	
Equity securities	**10**	26	
Total US GAAP adjustments	**(632)**	(659)	

Mortgage and other loans

In the UK financial statements, loans collateralized by mortgages held by Egg and Jackson National Life are carried at outstanding principal balances less allowances for loan losses. Loans collateralized by mortgages and other unsecured loans held by UK insurance operations are carried at fair value with changes in fair value recorded in the consolidated profit and loss account.

Under US GAAP, all loans are carried at their outstanding principal balances, less allowances for loan losses.

The US GAAP adjustments for mortgage and other loans had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Investment results	**10**	53	(52)
Total US GAAP adjustments	**10**	53	(52)
Condensed consolidated US GAAP balance sheets:			
Mortgage loans	**(41)**	(45)	
Other loans	**(6)**	(12)	
Total US GAAP adjustments	**(47)**	(57)	

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

Long-term Business

Revenue and expense recognition

Under UK GAAP, for long-term insurance contracts, all premium and annuity considerations and related expenses, investment returns, and increases in policyholder accounts and other long-term business liabilities are, on recognition, recorded within the profit and loss account.

Under US GAAP, premiums from conventional with-profits policies and other protection-type life insurance policies are recognized as revenue when due from the policyholder. Premiums from unitized with-profits life insurance policies and investment contracts, which have minimal mortality risk, are reported as increases in policyholder account balances when received. Revenues derived from these policies consist of mortality charges, policy administration charges, investment management fees and surrender charges that are deducted from policyholders' accounts.

Under US GAAP, premiums and policy charges received that relate to future periods are recorded as a deferred income liability. For limited payment annuities, the excess of the gross premium over the US GAAP net benefit premium is deferred and amortized in relation to the expected future benefit payments. For investment contracts, policy charges that benefit future periods are deferred and amortized in relation to expected gross profits.

Under US GAAP, investment results of separate account assets offset the increase in separate account liabilities.

Some long-term reinsurance contracts are structured to provide a form of financing as well as the transfer of risk. Under UK GAAP, where it is not practicable to separate out the financing components, such long-term reinsurance contracts are accounted for in the long-term technical account as reinsurance transactions. Where an amount received from a reinsurer is to be repaid in future accounting periods together with interest (or equivalent charge), the amount outstanding is included in the consolidated balance sheets as a liability. Where the repayment is contingent upon the emergence of margins, the present value of that part of the future margins which are expected to finance the repayment, is recognized as an asset in the consolidated balance sheets. Where appropriate, the carrying value of acquired in-force business, to which reinsurance contracts of this nature are in place, is reduced.

Under US GAAP, the financing element of reinsurance contracts is estimated and accounted for as a loan transaction.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for differences in revenue and expense recognition had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Insurance policy revenues	**(9,921)**	(9,928)	(7,511)
Investment results	**207**	(1,899)	(849)
Benefits and claims	**9,406**	11,590	8,238
Other charges	**40**	—	—
Total US GAAP adjustments	**(268)**	(237)	(122)
Condensed consolidated US GAAP balance sheets:			
Intangible assets	**40**	—	
Other assets	**(148)**	(55)	
Policyholder benefit liabilities	**(1,309)**	(1,079)	
Total US GAAP adjustments	**(1,417)**	(1,134)	

Deferred acquisition costs

Under UK GAAP, costs of acquiring new insurance policies, principally commissions, marketing and advertising costs and certain other costs associated with policy issue and underwriting that are not reimbursed by specific policy charges are capitalized as an asset and amortized in relation to profit margins. Recoverability is assessed at the time of policy issue, and reviewed if profit margins decline.

Under US GAAP, commissions, salesforce direct costs and costs associated with policy issue and underwriting that vary with and are primarily related to the production of new and renewal contracts are deferred. Deferred acquisition costs are regularly evaluated for recoverability and amounts determined not to be recoverable are charged to income. Deferred acquisition costs for conventional with-profits life insurance and other protection-type insurance policies are amortized in relation to premium income using assumptions consistent with those used in computing policyholder benefit provisions. Deferred acquisition costs for unitized with-profits life insurance and investment-type policies are amortized in relation to expected gross profits. Expected gross profits are evaluated regularly against actual experience and revised estimates of future gross profits and amortization are adjusted for the effect of any changes. Deferred acquisition costs associated with internally replaced policies are written off in the year replacement occurs and the incremental commissions and selling costs of the replacement contract are capitalized and amortized over the life of the replacement policy.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for deferred acquisition costs had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Underwriting, acquisition and other operating expenses	**339**	151	95
Total US GAAP adjustments	**339**	151	95
Condensed consolidated US GAAP balance sheets:			
Deferred acquisition costs	**1,543**	1,177	
Total US GAAP adjustments	**1,543**	1,177	

Policy liabilities

Under UK GAAP, future policyholder benefit provisions are based on fund value for unitized with-profits insurance policies and investment-type policies and are calculated using net premium methods for conventional with-profits life insurance and other protection-type insurance policies. The net premium reserves are calculated using assumptions for interest, mortality, morbidity and expenses, but without assumptions for withdrawals. These assumptions are determined as prudent best estimates at the date of valuation. Terminal bonuses expected to be paid on with-profits policies within the declaration period for the next financial year are recorded as part of the technical provision; liabilities for future annual and terminal bonus declarations are not provided.

Under US GAAP, for unitized with-profits life insurance and other investment-type policies, the liability is represented by the policyholders' account balances before any applicable surrender charges. Policyholder benefit liabilities for conventional with-profits life insurance and other protection-type insurance policies are developed using the net level premium method, with assumptions for interest, mortality, morbidity, withdrawals and expenses using best estimates at date of policy issue plus provisions for adverse deviation based on Group experience. Interest assumptions range from 3.7% to 12.0%. When the policyholder benefit liability plus the present value of expected future gross premiums are insufficient to provide for expected future policy benefits and expenses, using current best estimate assumptions, deferred acquisition costs are written down and/or a deficiency liability is established by a charge to earnings.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for policy liabilities had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Benefits and claims	**1,118**	49	617
Total US GAAP adjustments	**1,118**	49	617
Condensed consolidated US GAAP balance sheets:			
Policyholder benefit liabilities	**6,171**	5,032	
Total US GAAP adjustments	**6,171**	5,032	

Other With-Profits Policyholders' Funds and the FFA

Under UK GAAP, the long-term business technical provisions include provision for declared annual and terminal bonuses. The charge for the cost of bonuses declared in the year is recognized in the movement in the long-term business provision in the long-term business technical account. No technical provisions are made for bonuses beyond that covered in the current bonus declaration period. All amounts of the with-profits funds not yet allocated to policyholders or shareholders are recorded in the FFA. Changes in the FFA are charged or credited to the profit and loss account.

For US GAAP purposes, the FFA recorded under UK GAAP is reversed and a liability is established for undistributed policyholder allocations. The liability for undistributed policyholder allocations is established in the balance sheets because under the Articles of Association of PAC, and overseas operations having with-profits funds, the allocation and distribution of profits from the with-profits funds to shareholders is limited to up to one-ninth of the amount allocated to policyholders as bonuses. This is also the current basis of allocation and distribution. The liability for policyholder allocations represents an accumulation of 90% of the cumulative pre-bonus undistributed earnings of the with-profits business, measured on a US GAAP basis, less the cumulative cost of policyholders' benefits and claims. The provision for the policyholders' share of earnings on with-profits business charged to income represents 90% of the current year's pre-bonus earnings, before income taxes. Under US GAAP, the charge for the cost of bonuses recognized in the income statement for UK GAAP purposes is reversed and deducted from the balance of the undistributed policyholder allocations and included in policyholder benefit liabilities. The total US GAAP income adjustment represents the increase in the total allocation over the cost of policyholder bonuses declared.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for undistributed policyholder allocations had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Benefits and claims (cost of bonuses declared)	**2,704**	2,734	2,418
Provision for policyholders' share of earnings on with-profits business	**(966)**	(7,777)	(3,458)
Income tax attributable to the policyholders' share of earnings on with-profits business	**(102)**	1,167	531
Total US GAAP adjustments	**1,636**	(3,876)	(509)
Condensed consolidated US GAAP balance sheets:			
Undistributed policyholder allocations	**(18,354)**	(19,950)	
Total US GAAP adjustments	**(18,354)**	(19,950)	

The UK GAAP FFA and related profit and loss account transfer have been reversed for US GAAP. The reduction in liabilities increased shareholders' equity in the condensed consolidated US GAAP balance sheets by £20,185 million and £23,563 million in 2000 and 1999, respectively. The reversal of the related UK GAAP profit and loss account transfer reduced net income in the condensed consolidated US GAAP income statement by £3,409 million in 2000, and increased net income by £5,103 million and £1,381 million in 1999 and 1998, respectively.

As set out in Note 27 to the consolidated financial statements Prudential is currently discussing the attribution of certain assets within the PAC long-term fund with the UK insurance regulator. These discussions may or may not result in an additional portion of the long-term business funds being attributed to shareholders at some future date. Accordingly, these discussions may or may not affect the undistributed policyholder allocations recorded for US GAAP purposes.

Equalization Provision

Under UK GAAP, an equalization provision is recorded to mitigate claims volatility. The annual change in the equalization provision is recorded in the profit and loss accounts for the year.

Under US GAAP, provisions for losses not yet incurred are not permitted, therefore, the equalization provision is eliminated.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for the equalization provision had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Benefits and claims	**8**	7	8
Total US GAAP adjustments	**8**	7	8
Condensed consolidated US GAAP balance sheets:			
Policyholder benefit liabilities	**38**	30	
Total US GAAP adjustments	**38**	30	

Pension Plans

Under UK GAAP, employer contributions to defined benefit plans are calculated and expensed on a basis that spreads the costs over the service lives of participants.

Under US GAAP, Statement of Financial Accounting Standards ("SFAS") No. 87, "Employers' Accounting for Pensions", a transition asset has been recognized in the condensed consolidated balance sheet reflecting the overfunded status of the Group's primary UK staff pension plan at January 1, 1997. This transition asset is being amortized on a straight-line basis over a 15-year period beginning January 1, 1989, the effective date of SFAS No. 87.

The US GAAP adjustments for pension plans had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Underwriting, acquisition and other operating expenses	**110**	67	128
Total US GAAP adjustments	**110**	67	128
Condensed consolidated US GAAP balance sheets:			
Other assets	**775**	664	
Total US GAAP adjustments	**775**	664	

Stock-based Compensation

Under UK GAAP, compensation costs for stock compensation plans, other than the Savings Related Share Option Scheme, are recorded based on the quoted market price of the shares at the grant date less the amounts, if any, that employees are required to pay. For these plans, these costs are recognized in the profit and loss accounts over the period for which the share awards or options are earned. Prior to 1998, shares under the Savings Related Share Option Scheme were issued directly to qualifying employees. No compensation cost was recorded and the increase in share premium reflected the difference between proceeds received for qualifying employees and the nominal value of the shares

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

being issued. Beginning in 1998 shares were issued to a qualifying share ownership trust and costs, representing the difference between the market price at the date of transfer to the trust and amounts payable by employees, were charged directly to retained profit and loss reserve. An equal and opposite amount is recorded as an increase in the share premium. Any shares held by a qualifying share ownership trust are included in "ordinary shares of parent company" in the UK GAAP consolidated balance sheets.

Under US GAAP, compensation costs for all stock-based compensation plans are determined based on the quoted market price of the stock at the measurement date less the amounts, if any, that employees are required to pay. These costs are recognized in net income over the plans' respective vesting periods. The measurement date is the date upon which are known both the number of shares or options the employee is entitled to and the employee's cost per share. For plans with variable terms the measurement date may be after the balance sheet reporting date. If so, the market price used to estimate compensation cost is the price at the balance sheet date. Compensation costs previously recorded are adjusted for changes in the market price of the stock occurring before the measurement date. Under US GAAP, any Prudential shares purchased in the open market by a qualifying share ownership trust are recorded at historical cost and classified as treasury stock. At December 31, 2000 and 1999, 5.2 million and 7.5 million shares, respectively, were held as treasury stock.

The US GAAP adjustments for stock-based compensation had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Underwriting, acquisition and other operating expenses	**(9)**	(12)	(15)
Total US GAAP adjustments	**(9)**	(12)	(15)
Condensed consolidated US GAAP balance sheets:			
Other assets	**(34)**	(24)	
Other liabilities	**(26)**	(49)	
Total US GAAP adjustments	**(60)**	(73)	

Deferred Income Tax

Under UK GAAP, deferred tax assets and liabilities are provided for temporary differences between financial and taxable income when it is probable that a liability will be realized in the foreseeable future or an asset will be realized in the near term. Under this policy, a liability for a significant proportion of deferred tax on the unrealized gains on investment assets of the long-term business fund and on earnings retained overseas is not provided. In addition, deferred tax assets on losses carried forward are not recognized unless it is assured beyond reasonable doubt that future taxable profits will be sufficient to offset current losses.

Under US GAAP, deferred taxes are provided under the liability method for all temporary differences except for undistributed earnings of foreign subsidiaries that are not expected to be remitted for an indefinite period. Deferred tax assets are recognized subject to adjustment for valuation allowances when it is more likely than not that the underlying tax benefit will not be realized.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustments for deferred income tax had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Income tax expense	**673**	(979)	(215)
Total US GAAP adjustments	**673**	(979)	(215)
Reconciliation line items for consolidated net income:			
Deferred income tax	**497**	(600)	(213)
Deferred tax effect of other US GAAP adjustments	**176**	(379)	(2)
Total US GAAP adjustments	**673**	(979)	(215)
Condensed consolidated US GAAP balance sheets:			
Net deferred income tax liability	**(2,802)**	(3,475)	
Total US GAAP adjustments	**(2,802)**	(3,475)	
Reconciliation line items for consolidated shareholders' equity:			
Deferred income tax	**(2,511)**	(3,019)	
Deferred tax effect of other US GAAP adjustments	**(291)**	(456)	
Total US GAAP adjustments	**(2,802)**	(3,475)	

Shareholder Dividend Liability

Under UK GAAP, shareholders' dividends are accrued in the period to which they relate regardless of when they are declared. Under US GAAP, shareholders' dividends are accrued when declared.

The US GAAP adjustments for the shareholders' dividends resulted in a decrease in other liabilities on the condensed consolidated US GAAP balance sheets of £322 million and £299 million at December 31, 2000 and 1999, respectively. There were no effects of this item on US GAAP net income.

Business Disposals

Under UK GAAP, cumulative foreign currency translation gains and losses on foreign subsidiaries charged to shareholders' funds are not reversed upon the sale of a subsidiary.

Under US GAAP, cumulative foreign currency translation gains and losses realized upon sale of a subsidiary are reversed from shareholders' equity and included in net income as part of the gain or loss on the sale. In August 1998, upon sale of the Group's Australian and New Zealand operations, cumulative foreign currency translation losses of £68 million were realized, and netted against the gain on sale in the income statement.

33 Summary of Material Differences between UK Generally Accepted Accounting Practice and US Generally Accepted Accounting Principles (Continued)

The US GAAP adjustment for business disposals includes the above £68 million foreign currency translation adjustment and £10 million of change in gain on the sale of Australia and New Zealand operations.

Sale of Egg shares

Under US GAAP Prudential has chosen to account for the difference between the parent company's carrying value and net proceeds from the initial public offering of Egg shares as a gain in Prudential's consolidated profit and loss account. This treatment is similar to the UK GAAP treatment and therefore there is no UK to US GAAP adjustment.

Earnings per share under US GAAP

No adjustments were required from net income to net income available to common shareholders used in either the basic or diluted earnings per share calculation under US GAAP. The only dilutive potential shares outstanding affecting the diluted earnings per share calculation relate to employee stock options, which increased average weighted shares outstanding by 9 million shares, 12 million shares and 18 million shares in 2000, 1999 and 1998, respectively.

New Accounting Pronouncements

In June 1999, the Financial Accounting Standards Board ("FASB") delayed the effective date of Statement of Financial Accounting Standard ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities." The delay in implementation was effected through the issuance of SFAS No. 137, which delays the implementation of SFAS No. 133 to fiscal years beginning after June 15, 2000.

In June 2000, the FASB issued SFAS No. 138, which amends SFAS 133. Prudential will adopt the provisions of SFAS No. 133 and SFAS No. 138 as of January 1, 2001. The impact of these statements is dependent upon Prudential's derivative positions and market conditions existing at the date of adoption. Upon adoption, a net transitional adjustment based on the aggregate fair value of Prudential's derivative instruments as of December 31, 2000 will be recorded as a cumulative effect of a change in accounting principle. Currently, Prudential is continuing its analysis of the impact of SFAS No. 133 and SFAS No. 138 on its consolidated balance sheets and statements of income on a US GAAP basis. Net income in 2001 and future years are likely to reflect increased volatility owing to fair value fluctuations on certain derivative instruments, particularly interest rate swaps, that are regularly used to manage risks associated with movements in interest rates.

In September 2000, the FASB issued SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which supersedes SFAS No. 125 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 140 changes the circumstances under which a collateralized party must recognize certain financial assets in which it has security interest. Currently, Prudential is continuing its analysis of the effect of adoption of SFAS No. 140 on its consolidated balance sheets and statements of income on a US GAAP basis. However, the Group does not expect the adoption of SFAS No. 140 to have a material impact on its financial position.

34 Condensed Consolidated US GAAP Financial Statements

The following condensed consolidated US GAAP financial statements reflect the material differences between UK GAAP and US GAAP on consolidated profit and loss and consolidated shareholders' funds described in Note 33. In addition to these material differences that have an effect on the consolidated profit and loss accounts and/or consolidated shareholders' funds, there are material differences in classification between specific line items in the UK GAAP and condensed consolidated US GAAP financial statements as described in the notes to the condensed consolidated US GAAP financial statements.

Condensed consolidated US GAAP statement of income and comprehensive income	**2000**	**1999**	**1998**
		(In £ Millions)	
Insurance policy revenues	**3,926**	4,899	3,592
Investment results	**4,669**	12,793	8,599
Non-operating income: Profit on Egg flotation	**119**	—	—
Other income	**620**	600	165
Total revenue	**9,334**	18,292	12,356
Benefits and claims	**(5,057)**	(6,479)	(6,122)
Provision for policyholders' share of earnings on with-profits business	**(966)**	(7,777)	(3,458)
Underwriting, acquisition and other operating expenses	**(2,562)**	(2,436)	(1,468)
Other charges	**(157)**	(144)	(106)
Net income before income taxes	**592**	1,456	1,202
Income tax expense	**(13)**	(1,735)	(932)
Income tax attributable to the policyholders' share of earnings on with-profits business	**(102)**	1,167	531
Income tax attributable to shareholders	**(115)**	(568)	(401)
Net income before minority interest	**477**	888	801
Minority interest	**25**	—	—
Net income	**502**	888	801
Other comprehensive income (loss)	**171**	(457)	(40)
Total comprehensive income	**673**	431	761
Earnings per share under US GAAP:			
Basic (based on 1,959 million, 1,947 million and 1,935 million shares, respectively)	**25.6p**	45.6p	41.4p
Diluted (based on 1,968 million, 1,959 million and 1,953 million shares, respectively)	**25.5p**	45.3p	41.0p

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Condensed Consolidated US GAAP balance sheets	December 31 2000	December 31 1999
	(In £ Millions)	
Assets		
Investments:		
Fixed maturities	**47,590**	41,393
Equity securities	**43,030**	47,467
Short term investments	**3,569**	5,951
Real estate	**4,522**	3,541
Mortgage loans	**5,888**	4,106
Policy loans	**729**	649
Other loans	**1,830**	561
Other investments	**891**	889
Total investments	**108,049**	104,557
Cash	**1,206**	657
Deferred acquisition costs	**4,348**	3,743
Intangible assets	**2,581**	2,524
Other assets	**4,503**	3,964
Separate account assets	**32,337**	33,477
Total assets	**153,024**	148,922
Liabilities		
Policyholder benefit liabilities	**76,711**	71,179
Undistributed policyholder allocations	**18,354**	19,950
Debt	**4,899**	3,642
Net deferred income tax liability	**2,904**	3,614
Other liabilities	**11,227**	11,014
Separate account liabilities	**32,337**	33,477
Total liabilities	**146,432**	142,876
Minority interest	**137**	—
Shareholders' equity		
Common stock	**99**	98
Additional paid-in capital	**502**	309
Less treasury stock	**(55)**	(58)
Retained earnings	**6,124**	6,083
Accumulated other comprehensive income	**(215)**	(386)
Total shareholders' equity	**6,455**	6,046
Total liabilities and shareholders' equity	**153,024**	148,922

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Condensed Consolidated US GAAP statement of cash flows	December 31 2000	1999	1998
	(In £ Millions)		
Cash flows from operating activities:			
Consolidated net income	**502**	888	801
Adjustments to reconcile consolidated net income to net cash provided by operating activities:			
Depreciation and amortization	**271**	283	187
Realized investment gains	**(621)**	(219)	(436)
Interest credited to policyholders	**2,760**	2,492	2,409
Policy fees charged to policyholders	**(418)**	(576)	(377)
Bonuses paid to policyholders	**(1,281)**	(1,132)	(882)
Change in:			
Investments held for trading purposes	**1,604**	(9,855)	(4,616)
Deferred policy acquisition costs	**(602)**	(372)	(221)
Other assets	**(326)**	(722)	(395)
Policy benefit liabilities	**1,561**	3,562	2,720
Undistributed policyholder allocations	**(321)**	5,049	1,267
Other liabilities	**(682)**	7,702	1,554
Other, net	**36**	(43)	(8)
Net cash provided by operating activities	**2,483**	7,057	2,003
Cash flows from investing activities:			
Proceeds from sale or maturity of:			
Real estate	**286**	180	108
Available for sale securities sold	**5,354**	6,034	5,706
Available for sale securities matured	**5,045**	4,341	709
Mortgage and other loans	**1,791**	371	190
Purchases of:			
Real estate	**(1,361)**	(704)	(837)
Available for sale securities	**(11,911)**	(16,867)	(8,028)
Mortgage and other loans	**(4,341)**	(2,356)	(1,176)
Change in short-term investments, net	**2,485**	831	(646)
Net increases in other investments	**(103)**	(143)	(114)
Acquisitions of subsidiaries	**(183)**	(2,011)	(123)
Proceeds from flotation of Egg and other business disposals	**474**	—	468
Purchase of property and equipment	**(122)**	(144)	(67)
Proceeds from disposal of property and equipment	**7**	3	7
Net cash used in investing activities	**(2,579)**	(10,465)	(3,803)
Cash flows from financing activities:			
Policyholders' deposits	**7,608**	7,990	6,375
Policyholders' withdrawals	**(6,193)**	(5,063)	(3,825)
Proceeds from long-term borrowings	**—**	500	300
Repayment of long-term borrowings	**(118)**	—	(89)
Net change in short-term debt	**(381)**	450	(299)
Dividends paid to shareholders	**(461)**	(421)	(382)
Proceeds from issuance of stock	**184**	34	15
Net cash provided by financing activities	**639**	3,490	2,095
Net impact of foreign exchange fluctuations	**6**	1	—
Net increase in cash	**549**	83	295
Cash, beginning of year	**657**	574	279
Cash, end of year	**1,206**	657	574

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Results of Operations

Under UK GAAP, results of operations are presented in three separate consolidated profit and loss accounts, which segregate the results of operations of general, long-term and other shareholder business results of operations. Under US GAAP, all of the Group's activity is presented in one consolidated statement of income, and no distinction is made between general business, long-term business, or non-technical account financial results.

The US GAAP condensed consolidated financial statements include the assets, liabilities and profit and loss of subsidiaries in which Prudential has a majority voting interest. All intercompany transactions are eliminated on consolidation.

Cash Flows

Under UK GAAP, the consolidated statement of cash flows presents only the cash flows of general business and shareholders' funds. Cash flows of the long-term business technical account, other than amounts transferred to the non-technical account, are not included in the consolidated statement of cash flows. Under US GAAP, the consolidated statement of cash flows consists of all cash flows of the Group in its entirety, including cash flows related to policyholders' funds in the long-term business technical account. Unrealized gains or losses on securities classified as available-for-sale and related amortization of DAC, loss recognition, and deferred income taxes, which have been included as direct increases or decreases in shareholders' equity, are non-cash items.

Unitized With-Profits

Under US GAAP, premiums from unitized with-profits life insurance and other investment-type policies are not recorded as revenue within the consolidated profit and loss account as done under UK GAAP. Premium payments are directly credited to the liability for future benefits, with no resulting impact on the consolidated income statement. Revenues under these policies consist only of policy fees and charges, and investment earnings from assets backing policy account values. Expenses consist of amounts credited to policyholders, and any benefit payments in excess of related policy liabilities.

Income Taxes

Under UK GAAP, the balance on the long-term business technical account is determined net of total income taxes and then the shareholders' portion of tax attributable to long-term business, calculated at the effective tax rate of the underlying business, is added back and the resulting pre-tax profit on long- term business insurance activities is transferred to the non-technical account. The shareholder tax add-back is then included in tax on profit on ordinary activities of the non-technical account.

Under US GAAP, income before income taxes is determined after deducting the provision for policyholders' share of earnings on with-profits business before income taxes. Income tax expense includes income taxes that will be charged to undistributed policyholder allocations. The income tax attributable to the policyholders' share of earnings on with-profits business, calculated as 90% of the total income tax on with-profits business, is deducted from income tax expense to arrive at income tax attributable to shareholders.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Separate account assets and liabilities

In the Group's UK financial statements, segregated accounts are established for policyholder business for which policyholder benefits are wholly or partly determined by reference to specific investments or to an investment-related index. The assets and liabilities of this linked business are reported as summary totals in the consolidated balance sheets. In addition, the assets and liabilities of SAIF, the fund acquired in 1997 that is closed to new business, are included in the consolidated balance sheets within the classifications to which they relate.

Under US GAAP, the assets and related liabilities of UK segregated accounts established for policyholder business in which substantially all underlying investment risk is assumed by policyholders are reported as separate account assets and liabilities in the condensed consolidated balance sheets. Under US GAAP, separate account assets are stated at fair value. Such separate account balances also include the assets and liabilities of SAIF. However, assets and liabilities relating to index-linked business for which the Group bears investment risk are not reported as separate account balances.

The US GAAP reclassifications for separate account assets and liabilities relating to index-linked products had the following effects on the condensed consolidated US GAAP financial statements:

	December 31	
	2000	1999
	(In £ Millions)	
Condensed consolidated US GAAP balance sheets:		
Fixed maturities	**1,681**	1,614
Short-term investment	**4**	6
Separate account assets	**(1,685)**	(1,620)
Policyholder benefit liabilities	**(1,685)**	(1,620)
Separate account liabilities	**1,685**	1,620
Total US GAAP adjustments	**—**	—

34 Condensed Consolidated US GAAP Financial Statements (Continued)

The US GAAP reclassifications for separate account assets and liabilities relating to SAIF had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
	(In £ Millions)		
Condensed consolidated US GAAP statement of income:			
Insurance policy revenues	**(468)**	(295)	(377)
Investment results	**(423)**	(2,431)	(1,667)
Other income	**(4)**	(14)	(15)
Benefits and claims	**1,410**	1,450	1,746
Provision for policyholders' share of earnings on with-profits business	**(617)**	1,222	228
Underwriting, acquisition and other operating expenses	**102**	68	85
Total US GAAP adjustments	**—**	—	—
Condensed consolidated US GAAP balance sheets:			
Fixed maturities	**(4,669)**	(3,633)	
Equity securities	**(8,477)**	(10,187)	
Short-term investments	**(387)**	(299)	
Real estate	**(1,505)**	(1,396)	
Policy loans	**(29)**	(33)	
Other loans	**(95)**	(106)	
Other investments	**(69)**	(65)	
Cash	**(207)**	(133)	
Deferred acquisition costs	**(148)**	(175)	
Other assets	**(1,997)**	(2,024)	
Separate account assets	**17,428**	17,870	
Policyholder benefit liabilities	**14,001**	13,654	
Undistributed policyholder allocations	**3,082**	3,699	
Debt	**100**	100	
Other liabilities	**400**	598	
Separate account liabilities	**(17,428)**	(17,870)	
Total US GAAP adjustments	**—**	—	

Banking Business

In the Group's UK financial statements the financial position related to the banking business is recorded in single consolidated asset and liability line items. The net results of banking and investment management activities are each recorded in separate lines in the consolidated profit and loss accounts. Under US GAAP, the banking business assets and liabilities are recorded in the condensed consolidated balance sheets within the classifications to which they relate while the banking and investment management activities are recorded in the condensed consolidated statements of income within corresponding revenue and expense items.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

The US GAAP reclassifications to present banking business within the classifications to which they relate had the following effects on the condensed consolidated US GAAP financial statements:

	2000	1999	1998
		(In £ Millions)	
Condensed consolidated US GAAP statement of income:			
Investment results	**554**	386	88
Other income	**244**	214	104
Underwriting, acquisition and other operating expenses	**(798)**	(600)	(192)
Total US GAAP adjustments	**—**	—	—
Condensed consolidated US GAAP balance sheets:			
Fixed maturities	**3,636**	3,591	
Equity securities	**9**	—	
Short-term investments	**315**	2,993	
Mortgage loans	**3,042**	1,620	
Other loans	**1,334**	426	
Cash	**18**	—	
Other assets	**(8,354)**	(8,630)	
Debt	**(163)**	(10)	
Other liabilities	**163**	10	
Total US GAAP adjustments	**—**	—	

Discontinued Operations

Under UK GAAP, discontinued operations consist of all business disposals made during the year, or within three months after the year-end. Under US GAAP, discontinued operations consist only of the sale or disposal of a business whose activities comprise a distinct line of business or class of policyholder. The Group has not sold any portion of its business that meets the US GAAP criterion for discontinued operations.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Other Comprehensive Income

An analysis of accumulated other comprehensive income follows:

	2000	1999	1998
		(In £ Millions)	
Foreign currency translation adjustments:			
Foreign currency translation adjustments arising during the year	**146**	49	(49)
Less reclassification adjustment for losses included in net income	**—**	—	68
Foreign currency translation adjustments	**146**	49	19
Unrealized investment gains (losses) on available-for-sale securities:			
Unrealized holding gains (losses) arising during the year	**170**	(1,465)	802
Less reclassification adjustment for gains included in net income	**(172)**	(286)	(119)
Unrealized investment gains (losses), net	**(2)**	(1,751)	683
Related amortization of deferred acquisition costs	**3**	345	86
Related loss recognition	**33**	467	(696)
Policyholders' share of with-profits business	**(3)**	119	(121)
Related deferred taxes	**(6)**	314	(11)
Net unrealized gains (losses) on available-for-sale securities	**25**	(506)	(59)
Other comprehensive income (loss)	**171**	(457)	(40)
Accumulated other comprehensive income (loss), beginning of year	**(386)**	71	111
Accumulated other comprehensive income (loss), end of year	**(215)**	(386)	71
Components of accumulated other comprehensive income:			
Foreign currency translation adjustments	**59**	(87)	
Net unrealized gains on available-for-sale securities:			
Unrealized investment gains, net	**386**	388	
Related amortization of deferred acquisition costs	**191**	188	
Related loss recognition	**(947)**	(980)	
Policyholders' share on with-profits business	**14**	17	
Related deferred taxes	**82**	88	
Net unrealized losses on available-for-sale securities	**(274)**	(299)	
Accumulated other comprehensive income (loss), end of year	**(215)**	(386)	

Securities supporting UK payout annuities written by PAL and securities owned by Jackson National Life are classified as available-for-sale securities and are carried at fair value with unrealized investment gains and losses, and changes therein, reflected as separate components of accumulated other comprehensive income and other comprehensive income, respectively. These unrealized investment gains and losses, and changes therein, are presented net of the following items to the extent that they would be reflected in net income had unrealized gains and losses been realized: (a) related deferred acquisition costs amortization for products that amortize deferred acquisition costs in relation to expected gross profits and are supported by available-for-sale securities; (b) loss recognition for

34 Condensed Consolidated US GAAP Financial Statements (Continued)

limited payment contracts supported by available-for-sale securities if use of market yields in computing loss recognition would result in a premium deficiency; (c) with-profits policyholders' share of the increase in net equity of with-profits fund subsidiaries that hold available for sale securities; and (d) deferred income taxes on unrealized gains and losses, net of other items described above.

Underwriting, acquisition and other operating expenses

	2000	1999	1998
	(In £ Millions)		
Acquisition costs incurred	**953**	816	603
Acquisition expenses deferred	**(807)**	(688)	(486)
Amortization of deferred acquisition costs	**320**	424	231
Operating costs	**2,085**	1,884	1,120
Total underwriting, acquisition and other operating expenses	**2,551**	2,436	1,468

Investments

For US GAAP purposes, the Group has classified certain debt, other fixed income and equity securities principally in relation to Jackson National Life and the UK annuity business as available-for-sale. Securities classified as available-for-sale are carried at fair value and changes in unrealized gains and losses are reflected in accumulated other comprehensive income in shareholders' equity. All securities not classified as available-for-sale, principally in relation to the Group's with-profits business (excluding UK annuity business), are classified as trading, including securities included in deposits with credit institutions. Trading securities are carried at fair value with the changes in unrealized gains and losses recorded in the statement of income for the period. Bank time deposits included in deposits with credit institutions have maturities of less than 90 days and are carried at fair

34 Condensed Consolidated US GAAP Financial Statements (Continued)

value which approximates cost. Deposits with credit institutions are included in short term investments in the condensed consolidated US GAAP balance sheets.

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value
		(In £ Millions)		
December 31, 2000				
Fixed maturities—available-for-sale				
US Government and other Governments	**945**	**77**	**(4)**	**1,018**
UK Government securities	**822**	**83**	**—**	**905**
Local government securities	**354**	**92**	**(1)**	**445**
Corporate securities	**19,764**	**1,018**	**(880)**	**19,902**
Mortgage-backed securities	**7,631**	**88**	**(108)**	**7,611**
Other debt securities	**2,918**	**13**	**(9)**	**2,922**
Total fixed maturities—available-for-sale	**32,434**	**1,371**	**(1,002)**	**32,803**
Fixed maturities—trading				**14,787**
Total fixed maturities				**47,590**
Equity securities—available-for-sale	**603**	**63**	**(46)**	**620**
Equity securities—trading				**42,410**
Total equity securities				**43,030**

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value
		(In £ Millions)		
December 31, 1999				
Fixed maturities—available-for-sale				
US Government and other Governments	182	8	(2)	188
UK Government securities	979	104	(1)	1,082
Local government securities	525	140	—	665
Corporate securities	20,269	953	(580)	20,642
Mortgage-backed securities	6,937	14	(275)	6,676
Other debt securities	340	3	(16)	327
Total fixed maturities—available-for-sale	29,232	1,222	(874)	29,580
Fixed maturities—trading				11,813
Total fixed maturities				41,393
Equity securities—available-for-sale	294	59	(19)	334
Equity securities—trading				47,133
Total equity securities				47,467

34 Condensed Consolidated US GAAP Financial Statements (Continued)

The following table sets out certain additional information relating to sales of available-for-sale securities:

	2000	1999	1998
	(In £ Millions)		
Sales proceeds	**5,354**	7,025	5,706
Gross realized gains	**228**	223	213
Gross realized losses	**(38)**	(44)	(18)
Net realized gains	**190**	179	195

The change in net unrealized gains on trading securities included in income was a reduction of £6,225 million for 2000, and an increase of £3,800 million, and £1,618 million for 1999 and 1998, respectively.

Real Estate

The following table sets out certain information concerning the Group's real estate holdings as of December 31:

	Group Occupied		Held for Investment	
	2000	1999	2000	1999
	(In £ Millions)			
Cost	**312**	283	**5,418**	4,336
Accumulated depreciation	**(44)**	(43)	**(896)**	(795)
Depreciated cost	**268**	240	**4,522**	3,541

Real estate held for sale was £10 million and nil at December 31, 2000 and 1999, respectively. There were no impairment losses recorded on real estate at December 31, 2000 or 1999. Depreciation expense for group occupied real estate was £6 million, £8 million, and £6 million and for investment real estate was £114 million, £116 million, and £100 million for the years ended December 31, 2000, 1999, and 1998, respectively. Group occupied real estate is classified as "Other assets" in the condensed consolidated US GAAP balance sheets.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Policyholder Benefit Liabilities

The following table shows the components of policyholder benefit liabilities:

	December 31	
	2000	**1999**
	(In £ Millions)	
Future policy benefits and losses (policy reserves)	**25,696**	24,582
Policy account values	**48,745**	44,775
Unearned revenue reserve	**1,309**	1,079
Other policy claims and benefits payable	**961**	743
Policyholder benefit liabilities	**76,711**	71,179

Debt

In addition to the borrowings described in Note 25, for US GAAP debt includes £733 million and £893 million at December 31, 2000 and 1999, respectively, for the obligation of Jackson National Life to repurchase securities sold under reverse repurchase and dollar roll agreements. Under UK GAAP, these liabilities are shown as amounts owed to credit institutions. Jackson National Life has entered into a program of funding arrangements, the liabilities for which amounted to £1,920 million in 2000 and £619 million in 1999, and have been included in debt under US GAAP but other creditors under UK GAAP. Additionally, £163 million and £10 million at December 31, 2000 and 1999, respectively, of banking operations' bank loans and overdrafts repayable on demand are included in debt for US GAAP. The £100 million principal amount 8.5% subordinated collateralized bonds issued by Scottish Amicable Finance plc, which is owned by SAIF, are included in separate account liabilities for US GAAP. For US GAAP, debt at December 31, 2000 also includes £201 million, which represents debt obligations of certain entities which are consolidated for US GAAP purposes and are carried at market value under UK GAAP.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Undistributed Policyholder Allocations

A reconciliation of movements in the undistributed policyholder allocations included in the condensed consolidated US GAAP balance sheets as of December 31 is as follows:

	2000	1999	1998
	(In £ Millions)		
Balance at January 1	**19,950**	16,155	15,646
Provision for policyholders' share of earnings on with with-profits business:			
Before income tax	**966**	7,777	3,458
Income tax	**102**	(1,167)	(531)
Net of income tax	**1,068**	6,610	2,927
Cost of policyholders' bonuses declared	**(2,704)**	(2,734)	(2,418)
Policyholders' share of unrealized investment gains on available-for-sale securities	**3**	(119)	120
Disposal of subsidiary	**—**	—	(95)
Foreign exchange adjustment	**37**	38	(25)
Balance at December 31	**18,354**	19,950	16,155

Taxes

Components of the US GAAP net deferred income tax liability, which is included in other liabilities on the condensed consolidated balance sheets at December 31, 2000 and 1999 are as follows:

	2000	1999
	(In £ Millions)	
Asset:		
Short-term temporary differences	**(43)**	(67)
Long-term business technical provisions and other insurance items	**(543)**	(484)
Capital allowances	**(50)**	(33)
Total	**(636)**	(584)
Liability:		
Deferred acquisition costs	**554**	491
Short-term temporary differences	**228**	213
Long-term business technical provisions and other insurance items	**309**	291
Unrealized gains on investments	**2,449**	3,203
Total	**3,540**	4,198
Net deferred income tax liability	**2,904**	3,614

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Pension Plans

Prudential's UK staff pension plan and Scottish Amicable's staff pension plan are the two primary defined benefits plans that cover substantially all UK-based employees. These plans are non-contributory, with benefits based on employee retirement age, years of service and compensation near retirement. The plans' assets include UK and overseas equity and fixed income securities, index-linked gilts, unauthorized unit trusts, venture capital investments, property and cash.

The status of defined benefit plans under US GAAP at December 31 was as follows:

	2000	1999	1998
	(In £ Millions)		
Change in benefit obligation:			
Benefit obligation, beginning of year	**3,799**	3,667	3,077
Acquisitions during the year	**—**	79	—
Service cost	**117**	82	65
Interest cost	**223**	203	227
Actuarial loss	**(165)**	(38)	456
Benefit payments	**(185)**	(194)	(158)
Benefit obligation, end of year	**3,789**	3,799	3,667
Change in plan assets:			
Fair value of plan assets, beginning of year	**5,416**	4,434	4,073
Acquisitions during the year	**—**	107	—
Actual return on plan assets	**(265)**	1,030	485
Employer contributions	**41**	39	34
Benefit payments	**(185)**	(194)	(158)
Fair value of plan assets, end of year	**5,007**	5,416	4,434
Funded status end of year:			
Plan assets in excess of benefit obligation	**1,218**	1,617	767
Unrecognized transition obligation asset	**(138)**	(184)	(231)
Unrecognized net actuarial (gains) losses	**(194)**	(657)	145
Prepaid benefit cost (included in other assets)	**886**	776	681
Components of net periodic pension cost:			
Service cost	**117**	82	65
Interest cost	**223**	203	227
Expected return on assets	**(348)**	(267)	(341)
Recognized net actuarial gains	**(15)**	—	—
Amortization of transition obligation	**(46)**	(46)	(46)
Net periodic pension cost (included in underwriting, acquisition and other operating expenses)	**(69)**	(28)	(95)

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Assumed discount rates, rates of increase in future compensation levels and rates of pension increases used in calculating the projected benefit obligations together with long-term rates of return on plan assets are updated annually to reflect changing economic conditions in the UK where the pension plans are situated.

The actuarial assumptions used in determining benefit obligations at December 31, were as follows:

	2000	1999
	%	%
Discount rate	**6.0**	6.0
Rate of increase in future compensation levels	**5.0**	5.0
Rate of increase in pension payments for inflation	**3.0**	3.0
Expected long-term return on plan assets	**6.5**	6.5

Goodwill

The following table provides an analysis of goodwill under US GAAP:

	2000	1999	1998
	(In £ Millions)		
Goodwill, beginning of year	**2,019**	549	536
Acquisitions during the year	**218**	1,555	59
Disposal of subsidiary undertaking	**(23)**	—	(21)
Amortization charge for the year	**(114)**	(85)	(25)
Goodwill, end of year	**2,100**	2,019	549

Business Acquisitions

On April 28, 1999 Prudential acquired M&G Group plc (M&G). As a result of the acquisition, Prudential accrued a liability of £3 million for employee termination benefits, affecting 117 employees comprising primarily the institutional and life and pension administrative departments of M&G. Prudential also accrued a liability of £2 million for exiting some activities of M&G. The total liability of £5 million, was reflected in other liabilities in the condensed consolidated US GAAP balance sheet at December 31, 1999, and was considered part of the M&G purchase price. Termination benefits paid and charged against the liability during 1999 were £0.2 million and the number of employees terminated was 4. During 2000, an additional £2 million has been paid against the liability. Substantially all employees were terminated by December 31, 2000.

Prudential also accrued a liability of £2 million for employee termination benefits affecting 3 employees from Prudential and an additional £1 million for employee retention bonuses. An additional £2 million was paid in 2000 for termination benefits affecting an additional 4 employees. All affected employees have been terminated by December 31, 2000.

34 Condensed Consolidated US GAAP Financial Statements (Continued)

Pension Misselling Liability

The components of the pension misselling liability at December 31, 2000 relating to future benefit payments were discounted at 6% in accordance with guidelines issued by the UK Government Actuaries Department. The undiscounted amounts, including expected internal and external legal and administrative costs of adjudicating, processing and settling these claims, at December 31, 2000 expected to be paid in each of the years ended December 31 are as follows:

	(In £ Millions)
2001	740
2002	447
2003	43
2004	31
2005	31
Thereafter	639
Total undiscounted amount	1,931
Aggregate discount	(456)
Pension misselling liability	1,475

Stock-based Compensation

Compensation expense for stock option plans is recorded if the market price of the underlying shares on the measurement date exceeds the option exercise price. Compensation expense recorded under US GAAP for stock option plans during 2000, 1999, and 1998 was £8 million, £19 million, and £21 million, respectively.

If the Group had determined compensation expense based on the fair value of the options at the grant date for its share options and awards granted after December 15, 1994 under SFAS No. 123, "Accounting for Stock-Based Compensation", the Group's pro forma earnings would have been as follows:

	2000	1999	1998
	(In £ Millions, Except Per Share Amounts)		
Net income:			
As reported	**502**	888	801
Pro forma	**495**	894	804
Basic earnings per share:			
As reported	**25.6p**	45.6p	41.4p
Pro forma	**25.3p**	45.9p	41.6p
Diluted earnings per share:			
As reported	**25.5p**	45.3p	41.0p
Pro forma	**25.2p**	45.6p	41.2p

34 Condensed Consolidated US GAAP Financial Statements (Continued)

In accordance with SFAS No. 123, the pro forma amounts include only the effects of share options and awards granted since December 15, 1994 and are not necessarily indicative of future pro forma net income.

The weighted average exercise prices and fair values of options granted during 2000, 1999 and 1998 were as follows:

	2000		1999		1998	
	Weighted Average Fair Value £	Weighted Average Exercise Price £	Weighted Average Fair Value £	Weighted Average Exercise Price £	Weighted Average Fair Value £	Weighted Average Exercise Price £
Stock options granted with exercise prices:						
Greater than or equal to grant-date market value	**1.74**	**9.45**	1.45	7.72	2.26	9.48
Less than grant-date market value	**3.87**	**6.15**	3.28	5.57	4.51	4.95

The fair value amounts above were determined using the Black-Scholes option-pricing using the following assumptions:

	2000	1999	1998
Dividend yield	**2.27%**	2.73%	2.56%
Expected volatility	**20.00%**	20.00%	20.00%
Risk free interest rate	**6.12%**	6.05%	6.35%
Expected life	**3.92 years**	3.93 years	4.28 years

INDEX TO CONDENSED FINANCIAL INFORMATION OF REGISTRANT

INDEPENDENT AUDITORS REPORT ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors and Members of Prudential plc

Under date of May 23, 2001, we reported on the consolidated balance sheets of Prudential plc and its subsidiaries as of December 31, 2000 and 1999 and the related consolidated profit and loss accounts, consolidated statement of total recognized gains and losses, reconciliation of movements in consolidated shareholders' capital and reserves, and consolidated statements of cash flows from general business and shareholders' funds for the two years ended December 31, 2000, which are included herein. In connection with our audit of the aforementioned consolidated financial statements, we also audited the related condensed financial statement schedule included herein and appearing on pages S-4 to S-9. This condensed financial statement schedule is the responsibility of the Group's management. Our responsibility is to express an opinion on this schedule based on our audits.

In our opinion, such condensed financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

Accounting principles generally accepted in the United Kingdom vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of accounting principles generally accepted in the United States of America would have affected net income for each of the two years ended December 31, 2000 and shareholders' equity as of December 31, 2000 and 1999 to the extent summarized in Notes 33 and 34 to the consolidated financial statements and Note 3 to the condensed financial statement schedule.

KPMG Audit Plc
London, England
May 23, 2001

REPORT OF THE AUDITORS ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors and Members of Prudential plc

Our audit of the consolidated profit and loss account, consolidated statement of total recognized gains and losses, reconciliation of movements in consolidated shareholders' capital and reserves and consolidated statement of cash flows from general business and shareholders' funds of Prudential plc and its subsidiaries, referred to in our report dated June 13, 2000, except as to Note 5, which is as of March 26, 2001, appearing in this Form 20-F on page F-3 also included an audit of the profit and loss account, reconciliation of movements in shareholders' capital and reserves and statement of cash flows for the year ended December 31, 1998 included in the financial statement schedule, as listed in Item 18 of this Form 20-F. In our opinion, the profit and loss account, reconciliation of movements in shareholders' capital and reserves and statement of cash flows for the year ended December 31, 1998, present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

PricewaterhouseCoopers
London, England
June 13, 2000, except as to Note 5 of the consolidated financial statements, which is as of
March 26, 2001.

SCHEDULE II

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

PRUDENTIAL plc

PROFIT AND LOSS ACCOUNTS

Years ended December 31

	2000	1999	1998
	(In £ Millions)		
Investment income	**508**	794	640
Investment expenses and charges	**(225)**	(207)	(155)
Other charges:			
Corporate expenditure	**(60)**	(52)	(54)
Exchange gains (losses)	**32**	(45)	(4)
Charge in respect of shares issued to qualifying employee share ownership trust	**(46)**	(9)	(50)
Profit on ordinary activities before tax	**209**	481	377
Tax on profit on ordinary activities	**47**	49	(1)
Profit for the financial year	**256**	530	376
Dividends:			
Interim at 8.2p, 7.7p and 7.0p per share, respectively	**(162)**	(150)	(136)
Final at 16.3p, 15.3p and 14.0p per share, respectively	**(322)**	(299)	(271)
Total dividends at 24.5p, 23.0p and 21.0p per share, respectively	**(484)**	(449)	(407)
Retained (loss) profit for the financial year	**(228)**	81	(31)

The accompanying notes are integral part of this condensed financial information

SCHEDULE II

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

PRUDENTIAL plc

BALANCE SHEETS

December 31

	2000	1999
	(In £ Millions)	
Fixed assets		
Investments:		
Shares in subsidiary undertakings	**4,972**	5,023
Loans to subsidiary undertakings	**1,673**	1,531
	6,645	6,554
Current assets		
Debtors:		
Amounts owed by subsidiary undertakings	**307**	295
Tax recoverable	**—**	95
Other debtors	**6**	14
Other investments	**—**	81
Cash at bank and in hand	**35**	29
	348	514
Less liabilities: amounts falling due within one year		
Bank loans and overdrafts	**(20)**	—
Commercial paper	**(160)**	—
Amounts owed to subsidiary undertakings	**(260)**	(527)
Tax payable	**(20)**	—
Final dividend payable	**(322)**	(299)
Accruals and deferred income	**(47)**	(46)
	(829)	(872)
Net current liabilities	**(481)**	(358)
Total assets less current liabilities	**6,164**	6,196
Less liabilities: amounts falling due after more than one year		
Debenture loans	**(967)**	(955)
Amounts owed to subsidiary undertakings	**(3,206)**	(3,252)
Total net assets	**1,991**	1,989
Capital and reserves		
Share capital	**99**	98
Share premium	**458**	249
Profit and loss account	**1,434**	1,642
Shareholders' funds	**1,991**	1,989

The accompanying notes are an integral part of this condensed financial information

SCHEDULE II

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

PRUDENTIAL plc

RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' CAPITAL AND RESERVES

	Number of Ordinary Shares	Ordinary Share Capital	Share Premium	Retained Profit and Loss Reserve	Total
	(Millions)		(In £ Millions)		
January 1, 1998	1,939	97	157	1,577	1,831
Profit for the financial year	—	—	—	376	376
Dividends	—	—	—	(407)	(407)
New share capital subscribed	10	1	14	—	15
Charge in respect of shares issued to qualifying employee share ownership trust	—	—	50	—	50
December 31, 1998	1,949	98	221	1,546	1,865
Profit for the financial year	—	—	—	530	530
Dividends	—	—		(449)	(449)
New share capital subscribed	5	—	34	—	34
Transfer for shares issued in lieu of cash dividends	—	—	(15)	15	—
Charge in respect of shares issued to qualifying employee share ownership trust	—	—	9	—	9
December 31, 1999	**1,954**	**98**	**249**	**1,642**	**1,989**
Profit for the financial year	**—**	**—**	**—**	**256**	**256**
Dividends	**—**	**—**	**—**	**(484)**	**(484)**
New share capital subscribed:					
Resulting from listing on New York Stock Exchange	**17**	**1**	**139**	**—**	**140**
Other	**10**	**—**	**44**	**—**	**44**
Transfer for shares issued in lieu of cash dividends	**—**	**—**	**(20)**	**20**	**—**
Charge in respect of shares issued to qualifying employee share ownership trust	**—**	**—**	**46**	**—**	**46**
December 31, 2000	**1,981**	**99**	**458**	**1,434**	**1,991**

The accompanying notes are an integral part of this condensed financial information

SCHEDULE II

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

PRUDENTIAL plc

STATEMENT OF CASH FLOWS

December 31

	2000	1999	1998
		(In £ Millions)	
Operations			
Net cash inflow from operations before interest and tax	**457**	726	557
Interest paid	**(120)**	(82)	(76)
Taxes recovered (paid)	**162**	48	(37)
Acquisitions and disposals			
Disposals of (investment in) shares in subsidiary undertakings	**51**	(2,229)	(152)
Disposals of (investment in) other investments	**81**	(72)	(9)
	631	(2,301)	(161)
Equity dividends paid	**(461)**	(421)	(382)
Financing			
Issue of ordinary share capital (net of related transfer to share ownership transfer)	**184**	34	15
Issue of debenture loans	**—**	500	300
Net loans (to) from subsidiary undertakings	**(528)**	1,370	205
Net cash (outflow) inflow from financing	**(344)**	1,904	520
Net cash (outflow) inflow in the year	**(174)**	(126)	421
Reconciliation of operating profit to net cash inflow from operations			
Operating profit	**209**	481	377
Add back: interest charged	**225**	207	155
Exchange movements	**(32)**	45	4
Charge in respect of transfer to share ownership trust	**46**	9	50
Decrease (increase) in debtors	**8**	(15)	(29)
Increase (decrease) in creditors	**1**	(1)	—
Net cash inflow from operations	**457**	726	557

The accompanying notes are an integral part of this condensed financial information

SCHEDULE II

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

PRUDENTIAL plc

NOTES TO THE CONDENSED FINANCIAL STATEMENT SCHEDULE

December 31, 2000

1 Accounting Policies

The UK GAAP accounting policies as described in Note 3 of the notes to the consolidated financial statements have been used in the preparation of these parent company financial statements, except for the accounting policy described below.

Investments in shares in subsidiary undertakings

Shares in subsidiary undertakings in the balance sheet of the parent company are shown at the lower of cost and net realizable value. Any dividend income arising from these subsidiary undertakings is included within investment income on the parent company profit and loss account.

2 Dividends from subsidiaries

	2000	1999	1998
	(In £ Millions)		
Prudential Assurance Company Ltd	**330**	350	605
Prudential Corporation Holdings Ltd	**78**	—	—
Prudential M&G Ltd	**—**	141	—
M&G Group plc	**72**	50	—
Prudential Portfolio Managers Ltd	**—**	24	26
Prudential Mustang Ltd	**—**	—	1
Prudential Financial Services Ltd	**—**	—	3
Holborn Finance Holding Company Ltd	**—**	190	—
Total dividends	**480**	755	635

3 Reconciliation from UK GAAP to US GAAP

	2000	1999	1998
	(In £ Millions)		
Net Income			
Profit for the financial year in accordance with UK GAAP	**256**	530	376
Share in profit of the Group	**432**	12	504
US GAAP adjustments	**(186)**	346	(79)
Net Income in accordance with US GAAP	**502**	888	801
Net Equity			
Shareholders' funds in accordance with UK GAAP	**1,991**	1,989	
Shareholder dividend liability	**322**	299	
Share in net equity of the Group	**1,707**	1,435	
US GAAP adjustments (less dividends)	**2,435**	2,323	
Shareholders' equity in accordance with US GAAP	**6,455**	6,046	

3 Reconciliation from UK GAAP to US GAAP (Continued)

The parent company financial statements are prepared in accordance with UK GAAP. The above table provides a reconciliation between UK GAAP and US GAAP. Note 33 to the notes of the consolidated financial statements describes the material differences between UK GAAP and US GAAP.

"US GAAP adjustments" in the above table represent the total of material differences between UK GAAP and US GAAP as presented in Note 33 to the notes of the consolidated financial statements, except that the adjustment to shareholders' equity for shareholder dividend liability is shown separately above.

The share in profit/net equity of the Group represents the parent company's equity in the earnings and net assets of subsidiaries and associates. As stated in Note 1 to these financial statements, the parent company accounts for its investments in shares in subsidiary undertakings on a cost basis for UK GAAP whilst for US GAAP, these investments are accounted for under the equity method of accounting.

4 Guarantees provided by the parent company

The parent company provides guarantees for all of the commercial paper of the Group disclosed in Note 27 of the consolidated financial statements. This commercial paper is issued by two of the parent company's finance subsidiaries. Additionally, the parent company provides guarantees for the US $300 million principal amount, 8.25% guaranteed bonds due 2001 and the £150 million principal amount, 9.375% guaranteed bonds due 2007 as disclosed in Note 27 of the consolidated financial statements and issued by one of its finance subsidiaries.

Item 19. Exhibits

Documents filed as exhibits to this Form 20-F:

*1. Memorandum and Articles of Association of Prudential.

*2. Form of Deposit Agreement among Prudential, Morgan Guaranty Trust Company of New York, as depositary, and holders and beneficial owners from time to time of ADRs issued thereunder, including the form of ADR.

*4(a). Restricted Share Plan.

6. Statement re computation of per share earnings (set forth in Note 4 and Note 33 to the consolidated financial statements included in this Form 20-F).

8. Subsidiaries of Prudential (set forth in Note 23 to the consolidated financial statements included in this Form 20-F).

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* Previously filed.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

PRUDENTIAL PLC

By: /s/ JONATHAN BLOOMER

Name: Jonathan Bloomer
Title: Group Chief Executive

Date: June 1, 2001

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