Registered No 992726

PRUDENTIAL PENSIONS LIMITED

Annual Report and Financial Statements for the year ended 31 December 2012

PRUDENTIAL PENSIONS LIMITED

Incorporated and registered in England and Wales. Registered No. 992726.
Registered Office: Laurence Pountney Hill, London EC4R 0HH.

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PRUDENTIAL PENSIONS LIMITED

Directors

D J Belsham (Chairman)
J Betteridge
K Nunn

Secretary

Prudential Group Secretarial Services Limited

Auditor

KPMG Audit Plc, London

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DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2012

Principal activity

The principal activity of Prudential Pensions Limited (the Company) in the course of 2012 was the writing of long-term insurance business in the United Kingdom. This activity will continue in 2013.

Business review

Market review and strategy

The Company accepts reassurance from The Prudential Assurance Company Limited in respect of corporate pension schemes. In addition the Company sells direct investment only business to group pension schemes. Most of the Company's products are unit-linked products. The Company has a small book of annuities reassured to another group company. The profits from the Company's business accrue solely to shareholders.

The operations of the Company are managed as part of the UK Insurance Operations (UKIO) of the Prudential plc Group and M&G.

UKIO's long-term products consist of life insurance, pension products and pension annuities. The Company remains focused on maximising value from the opportunity afforded by the fast growing need for retirement solutions.

The M&G side of the business largely invests money on behalf of defined benefit pension schemes. The key determinant of success and retention is delivery of good investment performance relative to the benchmark. Performance generally in 2012 was favourable. The Company is further exposed to changes in the marketplace, particularly in relation to its traditional defined benefit book, and actively monitors those changes.

Performance and measurement

The following table sets out the key performance indicators for the Company. These are considered to be the key metrics for the Company.

Key Performance Indicators	**2012**	**2011**	**Change**
	£000	**£000**	**%**
Profit on ordinary activities before tax	11,438	9,181	24.6%
Shareholder funds	46,756	37,200	25.7%
Funds under management	12,344,136	11,585,758	6.5%

Accounts

The state of affairs of the Company at 31 December 2012 is shown in the balance sheet on page 16. The profit and loss account appears on pages 13 to 14.

Share Capital

There were no changes in the Company's share capital during 2012.

Dividend

No dividend is proposed for the year (2011: Nil).

Risks & uncertainties

As a provider of insurance services, the Company's business is the managed acceptance of risk. The Company is a wholly owned subsidiary of the Prudential Group and is subject to the Group's internal control and risk management processes as detailed in the Group Governance Manual and Group Risk Framework. The control procedures and systems established within the Group are designed to manage, rather than eliminate, the risk of failure to meet business objectives. They can only provide reasonable and not absolute assurance against material misstatement or loss, and focus on aligning the levels of risk-taking with the achievement of business objectives.

The Group's risk and governance framework requires all businesses and functions within the Group, including the Company, to establish processes for identifying, evaluating and managing key risks. The risk governance framework is based on the concept of three lines of defence: risk management, risk oversight and independent assurance.

The Company is exposed to risks from its business. A number of risk factors (both financial and non-financial) affect the Company's results and financial condition. The risk factors of the Company, mentioned below, should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

Financial risks

The Company's exposure to financial risk is limited due to the matching of policyholder liabilities to attaching asset value movements for unit linked business. The key financial risk factors affecting the Company include market risk, persistency risk and expense risk. Further information on the financial risk management objectives and policies of the Company and the exposure of the Company to the financial risk factors is given in note 7.

The current uncertainty in local and international economic and investment climates has increased financial risks and this could adversely affect the Company's business and profitability. Since 2008 the Company has had to operate against a challenging background of periods of unprecedented volatility in global capital and equity markets, interest rates, liquidity, and the broader economic environment. Government interest rates have also fallen to historic lows in the US and the UK.

In recent times, the global financial markets have experienced further volatility brought on, in particular, by concerns over European sovereign debt, as well as concerns about a general slowing of global demand reflecting an increasing lack of confidence among consumers, companies and governments. Upheavals in the financial markets may affect general levels of economic activity, employment and customer behaviour. For example, insurers may experience an elevated incidence of claims, lapses, or surrenders of policies, and some policyholders may choose to defer or stop paying insurance premiums. The demand for insurance products may also be adversely affected. If sustained, this environment is likely to have a negative impact on the insurance sector over time and may consequently have a negative impact on the Company's business and profitability. New challenges related to market fluctuations and general economic conditions may continue to emerge.

(a) Expense risk

Expense risk is the risk of loss or of adverse change in the profitability or financial situation of the Company resulting from changes in the level of expenses incurred.

Expense risk is the risk of the actual expenses exceeding the assumptions in pricing and reserving and is relevant to all lines of business. The Company makes assumptions about future expected levels of expenses for each line of business and uses these in pricing and calculating reserves. If the actual expenses exceed these assumptions, the Company's operating results could be adversely impacted. Expense risk is a significant risk for the Company.

(b) Persistency risk

Persistency risk is the risk of loss or of adverse change in the profitability of the Company resulting from changes in the level of lapses or surrenders.

Persistency is the assumption that the Company makes about future expected levels of the rates of early termination of products by its customers. The Company's persistency assumptions reflect the recent past experience for each relevant line of business including any expected trends in future persistency rates. If the actual levels of future persistency are significantly lower than assumed (that is, policy termination rates are significantly higher than assumed), the Company's results could be adversely affected.

(c) Market risk

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

The current uncertainty in local and international economic and investment climates has increased market risk and this could adversely affect the Company's business and profitability, principally through a fall in the Company's assets under management due to reduced investment returns, adverse movements in foreign currency exchange rates (for overseas investment funds) and/or reduced new business. This is because a large proportion of the Company's income is earned via fund management charges that are expressed as a percentage of funds under management. A fall in funds under management as a result of market risk would therefore adversely affect the Company's profitability.

In common with other industry participants, the profitability of the Company's business ultimately depends on a mix of factors including investment performance, impairments and unit costs of administration and expenses

Non-financial risk

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

(a) Business environment risk

Business environment risk is the exposure to forces in the external environment that could significantly change the fundamentals that drive the Company's overall strategy.

The Company conducts its business subject to regulation and is therefore exposed to changes in laws, and regulations that affect the products and markets in which it operates. Changes in government policy, legislation (including tax), regulatory interpretation and accounting standards applying to UK insurance companies may be applied retrospectively, may adversely affect the Company's product range, distribution channels, capital requirements and, consequently, reported results and financing requirements.

The material regulatory and legal change risks currently faced by the Company are:

- Solvency II - The EU is harmonising the solvency framework for insurance companies across Europe based on the concept of three pillars - minimum capital requirements, supervisory review of firms' risk management system, and enhanced disclosure requirements. This will cover valuations, the treatment of insurance groups and companies, the definition of capital and the level of capital required. A key aspect of Solvency II is that the assessment of risks and capital requirements will be aligned more closely with economic capital methodologies, and may allow the Company to make use of its internal economic capital models, if approved by the relevant supervisory authority. Although the Solvency II Directive was formally approved by the Economic and Financial Affairs Council in November 2009 the Solvency II implementation date has been postponed from 1st January 2014 and the new date is yet to be confirmed. Discussions are on-going within the European Parliament to agree the Omnibus II Directive and to develop the detailed rules that will complement the high-level principles of the Directive, referred to as 'implementing measures'. Agreement to the Omnibus II Directive is now expected to be finalised during 2013 with the implementing measures expected to be finalised later in 2013 or 2014. There is significant uncertainty regarding the final outcome of this process. As a result there is a risk that the effect of the measures finally adopted could be adverse for the Company, including potentially a significant increase in capital required to support its business and that the Company may be placed at a competitive disadvantage to other European and non-European financial services groups.

- The split of regulation in the UK in 2013 between the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) may give rise to new requirements and regulatory expectations for the Company.

- Any further changes or modification to Financial Reporting Standards, or adoption of International Financial Reporting Standards (IFRS) may require a change in the reporting basis of future results, or a restatement of reported results.

- Changes in tax legislation could affect the Company's financial condition and results of operations.

The corporate market for UK financial services is highly competitive with several factors affecting the Company's ability to sell its products and its continued profitability. These include; the range of products offered, price and yields offered, financial strength and ratings, product quality, brand strength and name recognition, and investment management performance. Responding appropriately to changes in the business environment both short and longer term is a key risk for the Company.

(b) Strategic and Group risk

Strategic risk is the risk of ineffective, inefficient or inadequate senior management processes for the development and implementation of business strategy in relation to the business environment and the Company's capabilities. Group risk is the risk associated with being part of a group, particularly as a result of contagion.

Being a member of the Prudential group can provide significant advantages for the Company in terms of the brand, financial strength, technical expertise and management experience. It can also give rise to risks; if a change in strategy or support given by the parent or another member of the group on which the Company relies, were removed. The independent capitalisation of the Company as well as the strategic planning and risk management processes within the Company ensures any strategic or group risk is appropriately managed.

(c) Operational risk

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

The Company is exposed to operational risk in the ordinary course of its business and as a result may be subject to unplanned costs, reputational damage, regulatory or legal actions and disputes.

The Company's activities and target market relies on the investment management performance and expertise within M&G and external partners to attract and retain corporate clients, resulting in the potential for key person risk for certain funds. Also, the Company needs to maintain good relationships with Employment Benefit Consultants to manage the retention of a small number of schemes which contribute significant funds under management and profit.

The Company operates in a mature and highly regulated environment where the pace of regulatory change has intensified making regulatory compliance a key risk. In addition to the level of regulatory change experienced, regulatory relationships have become more intrusive particularly around product development, distribution processes, complaint handling and breach management. There has been an increase in fines and regulatory sanctions imposed on firms.

The Company's unit linked business requires timely and accurate processing of a large number of complex transactions to minimise the risk of fund and pricing errors. In addition, the Company outsources several operations intra-group and externally, including investment management, pricing and IT. The Company is therefore reliant upon the operational processing performance of its outsourcing partners, and their performance is monitored carefully. The Company's systems and processes incorporate controls which are designed to manage and mitigate the operational risks associated with its activities as any weakness in the administration systems, finance systems and processes or actuarial reserving process could have an impact on its results during the affected period.

Further, because of the long-term nature of much of the Company's business, accurate records have to be maintained for significant periods.

Corporate responsibility

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

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

As a business that provides savings, income, investment and protection products and services the Group creates social value through its day-to-day operations. First, the Group provides customers with ways to help manage uncertainty and build a more secure future. Second, by playing a key role in financial markets, the Group provides long-term capital that finances businesses, builds infrastructure and fosters growth in both developed and developing countries.

The Group aims to be sustainable in the broadest sense – financially, socially and environmentally. Sustainability is integral to the way it does business. Prudential has long-term liabilities and investments, and its commitments to its customers and its employees, as well as its support for communities and its responsibility towards the environment, are rooted in its aim of continuing to deliver strong financial performance sustainably.

The Group believes that CR is best managed on the ground by those closest to the customer and local stakeholders. Underpinning this approach are the Group's four global CR themes:

1. Customers: Using the Group's financial strength, knowledge and skills to provide fair and transparent products, which meet customers' needs;
2. People: Recruiting, developing and retaining the best people for the best-performing business;
3. The environment: Increasing the efficiency of the Group's business by reducing the direct impact of the properties it occupies and the properties it manages as part of its investment portfolio;
4. Communities: Supporting its communities through donations, employee volunteering and long-term partnerships with charitable organisations that make a real difference.

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

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

Solvency II and other global regulatory developments

The European Union (EU) is developing a new solvency framework for insurance companies, referred to as 'Solvency II'. The Solvency II Directive, which sets out the new framework, was formally approved by the Economic and Financial Affairs Council in November 2009. The new approach is based on the concept of three pillars – minimum capital requirements, supervisory review of firms' assessments of risk, and enhanced disclosure requirements.

Specifically, Pillar 1 covers the quantitative requirements around own funds, valuation rules for assets and liabilities and capital requirements. Pillar 2 provides the qualitative requirements for risk management, governance and controls, including the requirement for insurers to submit an Own Risk and Solvency Assessment which will be used by the regulator as part of the supervisory review process. Pillar 3 deals with the enhanced requirements for supervisory reporting and public disclosure.

A key aspect of Solvency II is that the assessment of risks and capital requirements are intended to be aligned more closely with economic capital methodologies and may allow Prudential to make use of internal economic capital models if approved by the FSA or other relevant supervisory authority.

Representatives from the European Parliament, the European Commission and the Council of the European Union are currently discussing the Omnibus II Directive which, once approved, will amend certain aspects of the original Solvency II Directive. In addition the European Commission is continuing to develop, in consultation with stakeholders including industry, the detailed rules that will complement the high-level principles in the Solvency II Directive, referred to as 'implementing measures'. The Omnibus II Directive is not currently scheduled to be finalised until late 2013, while the implementing measures cannot be finalised until after Omnibus II.

There is a significant uncertainty regarding the final outcome from this process. In particular, the Solvency II rules relating to the determination of the liability discount rate remain unclear and the capital position of the Prudential Group, of which the Company is a part, is sensitive to these outcomes. With reference to the liability discount rate, solutions to remove artificial volatility from the balance sheet have been suggested by policymakers as the regulations continue to evolve. These solutions are continuing to be considered by policymakers as part of the process to reach agreement on the Omnibus II Directive. There is a risk that the effect of the measures finally adopted could be adverse for the Prudential Group and the Company, including potentially that a significant increase in capital may be required to support its business and that the Prudential Group and the Company may be placed at a competitive disadvantage to other European and non-European financial services groups. The Prudential Group is actively participating in shaping the outcome through its involvement in industry bodies and trade associations, including the Chief Risk Officer and Chief Financial Officer Forums, together with the Association of British Insurers and Insurance Europe (formerly known as the Comité Européen des Assurances).

The delays in finalising the Omnibus II Directive and implementing measures are expected to result in a deferral of the Solvency II implementation date for firms beyond the previously anticipated date of 1 January 2014. At this stage, it remains unclear exactly when Solvency II will come into force, although a deferral until 1 January 2016 or beyond appears likely.

Having assessed the requirements of Solvency II, an implementation programme was initiated with dedicated teams to manage the required work across the Group. The activity of the local Solvency II teams is being coordinated centrally to achieve consistency in the understanding and application of the requirements. The Prudential Group is continuing its preparations to adopt the regime when it eventually arrives and is undertaking in parallel an evaluation of the possible actions to mitigate its effects. The Prudential Group regularly reviews its range of options to maximise the strategic flexibility of the Group. This includes consideration of optimising the Group's domicile as a possible response to an adverse outcome on Solvency II.

Over the coming months the Prudential Group will be progressing its implementation plans and remain in regular contact with the FSA as it continues to engage in the 'pre-application' stage of the approval process for the internal model.

Currently there are also a number of other prospective global regulatory developments which could impact the way in which the Prudential Group and the Company is supervised. These include the work of the Financial Stability Board (FSB) on Globally Systemically Important Financial Institutions (G-SIFIs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) being developed by the International Association of Insurance Supervisors (IAIS).

As part of a global initiative to identify G-SIFIs, in May 2012, the IAIS published proposed assessment methodology for designating Globally Systematically Important Insurers (G-SIIs). For those groups that are designated by the FSB as G-SII then additional policy measures including enhanced supervision and higher loss absorbency requirements could be proposed. Further detail of the proposals is expected during 2013 and implementation is likely to be over a period of years. Furthermore, the FSA is considering the designation of Domestically Systemically Important Insurer (DSII) for those UK insurers that are significant in UK terms. It is not yet clear what the impact of this designation may be.

ComFrame is also being developed by the IAIS to provide common global requirements for supervision of insurance groups. The framework is designed to develop common principles for supervision and so may increase the focus of regulators in some jurisdictions. It is also possible that some prescriptive requirements, including group capital, could be proposed. Further clarity on ComFrame is expected during the second half of 2013.

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2012 (continued)

Payment policy

The Company does not have any trade creditors and therefore codes or standards on payment practice and disclosure of trade creditor days are not applicable.

Disclosure of information to auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

Auditor

In accordance with Section 487(2) of the Companies Act 2006, KPMG Audit Plc will be deemed to be re-appointed auditor of the Company for the current financial year.

Directors' and Officers' Protection

Prudential plc has arranged appropriate insurance cover in respect of legal action against directors and senior managers of companies within the Prudential Group. In addition, the Articles of Association of the Company permit the directors, officers and employees of the Company to be indemnified in respect of liabilities incurred as a result of their office.

On behalf of the Board of directors.

S D Windridge
On behalf of Prudential Group Secretarial Services Limited
Company Secretary

25th March 2013

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

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

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

• select suitable accounting policies and then apply them consistently;

• make judgments and estimates that are reasonable and prudent;

• state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and

• prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

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

D J Bell

D J Belsham
Director

25th March 2013

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PRUDENTIAL PENSIONS LIMITED

We have audited the financial statements of Prudential Pensions Limited for the year ended 31 December 2012 set out on pages 13 to 35. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

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

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 11, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements:
- give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

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

MWilliams

Marie Williams (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
15 Canada Square
Canary Wharf
London
E14 5GL

25th March 2013

PRUDENTIAL PENSIONS LIMITED

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2012

Long-term Business Technical Account	Notes	2012 £000	2011 £000
Investment income	3	713,335	633,076
Unrealised gains / (losses) on investment	3	450,580	(132,044)
Other technical income		30,471	29,777
		1,194,386	**530,809**
Change in other technical provisions, net of reinsurance			
Long term business provision, net of reinsurance			
- gross amount		4,461	643
- reinsurers' share		(4,461)	(643)
	10	-	-
Change in technical provisions for linked liabilities, net of reinsurance	10	(1,127,500)	(497,560)
		(1,127,500)	**(497,560)**
Net Operating Expenses			
- Acquisition costs		(495)	(576)
- Administrative expenses		(2,463)	(2,776)
Investment expenses and charges	3	(13,917)	(18,669)
Foreign exchange (losses) / gains	3	(36,575)	805
Interest payable	3	(123)	(358)
Tax attributable to long term business	4	(3,796)	(4,111)
		(57,369)	**(25,685)**
Balance on the long-term business technical account		**9,517**	**7,564**

All of the amounts above are in respect of continuing operations.

The accounting policies and notes on pages 17 to 35 form an integral part of these financial statements.

PRUDENTIAL PENSIONS LIMITED

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2012 (continued)

Non-Technical Account	Notes	2012 £000	2011 £000
Balance on the long-term business technical account		**9,517**	**7,564**
Tax attributable to the balance on the long-term business technical account	4	1,870	1,539
Balance on the long term business technical account before tax		11,387	9,103
Investment income	3	50	76
Bank interest receivable	3	1	2
Operating profit on ordinary activities before tax		**11,438**	**9,181**
Tax on profit on ordinary activities	4	(1,882)	(1,560)
Profit for the financial year		**9,556**	**7,621**

The Company has no recognised gains or losses other than those reported in the profit and loss account.

In accordance with the amendment to Financial Reporting Standard 3 (FRS 3) published in June 1999 no note of historical cost profits has been prepared as the Company's only material gains and losses on assets relate to the holding and disposal of investments.

All of the amounts above are in respect of continuing operations.

The accounting policies and notes on pages 17 to 35 form an integral part of these financial statements.

PRUDENTIAL PENSIONS LIMITED

RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUND FOR THE YEAR ENDED 31 DECEMBER 2012

	2012 £000	2011 £000
Shareholders' fund at the beginning of the year	37,200	29,579
Profit for the financial year	9,556	7,621
Shareholders' fund at the end of the year	**46,756**	**37,200**

The accounting policies and notes on pages 17 to 35 form an integral part of these financial statements.

PRUDENTIAL PENSIONS LIMITED

BALANCE SHEET AS AT 31 DECEMBER 2012

	Notes	2012 £000	2011 £000
ASSETS			
Investments			
Other financial investments	7	60,350	62,798
Assets held to cover linked liabilities	7,9	10,652,995	10,090,022
Reinsurers' share of technical provisions			
Long term business provision	10,11	71,881	76,342
Technical provision for linked liabilities	10	1,691,141	1,495,736
Debtors			
Other debtors	13	3,311	1,784
Other assets			
Cash at bank and in hand	14	7,779	4,699
Prepayments and accrued income		39	48
Total assets		**12,487,496**	**11,731,429**
LIABILITIES			
Capital and reserves			
Called up share capital	16	6,000	6,000
Capital redemption reserve	10	4,088	4,088
Profit and loss account	10	36,668	27,112
Total shareholders' funds attributable to equity interests		**46,756**	**37,200**
Technical provisions			
Long term business provision	10, 11	72,081	76,542
Technical provisions for linked liabilities	10	12,344,136	11,585,758
Provisions for other risks and charges			
Deferred taxation	4	4,830	4,943
Creditors			
Other creditors including taxation and social security	12	19,693	26,986
Total liabilities		**12,487,496**	**11,731,429**

The accounts on pages 13 to 35 were approved by the board of directors on 25th March 2013.

D J Belsham

D J Belsham
Director

NOTES ON THE FINANCIAL STATEMENTS

1. Accounting Policies

(a) Change in accounting policies

The Company has implemented the following changes in preparing its results for the year ended 31 December 2012. These standards closely reflect the requirements of International Financial Reporting Standards (IFRS) and form part of the continuing convergence of UKGAAP to IFRS requirements in the UK.

In 2012, the Company adopted the "Amendments to FRS29 (IFRS7) – Financial Instruments: Disclosures – Disclosures – Transfers of Financial Assets" which had no material impact on the financial statements of the Company.

(b) Basis of presentation

The financial statements are prepared in accordance with Part 15 of the Companies Act 2006 and Schedule 3 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. The financial statements comply with applicable accounting standards and the 2005 ABI SORP, updated on 21 December 2006, and have been prepared under the historical cost accounting rules, modified to include the revaluation of investments.

The Company has taken advantage of the exemption under FRS1 (Revised) from preparing a cash flow statement. The Company has not presented a capital position statement with supporting disclosures under FRS 27 on the basis that the Company is more than 90 per cent owned within a group and the Company is included in the publicly available Prudential group financial statements which provide information on a group basis complying with this requirement.

Going concern

The directors have a reasonable expectation that the Company will be able to continue in operational existence for the foreseeable future and thus continue to adopt the going concern basis of accounting in preparing the financial statements. This conclusion has been based upon the following: the Company is a subsidiary within the Prudential Group and it, its parent company and the ultimate parent company are continuing to trade and there are no plans for liquidation, the Company has a healthy solvency margin, well in excess of the regulatory capital resource requirement (Note 8 on page 31), generates positive cashflows and has very low debt-financing. In addition consideration has also been given to the Company's performance, the market in which it operates, its strategy and risks and uncertainties, as set out in the Directors' Report on pages 4 to 10, the management of financial risk as set out in Note 7, including its exposure to liquidity risk and credit risk.

(c) Long term business

Under FRS 26, the measurement basis of assets and liabilities of long term business contracts is dependent upon the classification of the contracts as either insurance contracts, if the level of insurance risk is significant, or investment contracts if the risk is insignificant. A further distinction is made between investment contracts with and without discretionary participation features. Discretionary participation features represent the contractual right to receive additional benefits as a supplement to guaranteed benefits. The Company has no investment contracts with discretionary participating features. The Company's contracts are mainly unit-linked contracts which are investment contracts without discretionary participating features. Insurance contracts are accounted for under previously applied UK GAAP, as set out in the ABI SORP.

Investment contracts without discretionary participation features are accounted for as financial liabilities under FRS 26 and, where relevant the provisions of the ABI SORP in respect of the attaching investment management features of the contracts. FRS 26 applies a different accounting treatment to these contracts than the previously applied UK GAAP primarily in respect of deferred acquisition costs, deferred income reserves, and provisions for future expenses commonly called "sterling reserves" (see below).

A further feature is that investment contracts without discretionary participation features are closer in nature to a deposit style arrangement between the investors and the Company. Premiums and withdrawals for these contracts are recorded within the balance sheet as a movement on the investors' liability and the long-term business technical account reflects the fee income, expenses, and taxation on the contract. The provisions for investment contracts without discretionary participation features are included in Technical Provisions for Linked Liabilities in the balance sheet.

1. Accounting Policies (continued)

(c) Long term business (continued)

Technical account treatment

For unit linked business, premiums are accounted for when the liabilities arising from the premiums are created. Premiums exclude any taxes or duties based on premiums. Pensions annuity contracts that vest during the year are included in claims incurred and premium income at the annuity purchase price.

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

Under FRS26, the accounting treatment for investment contracts without discretionary participation features reflects the deposit nature of the arrangement with premiums and claims reflected as deposits and withdrawals taken directly to the balance sheet as a movement on the investors liability with the long-term technical account reflecting fee income, expense, and taxation on these contracts.

Sterling reserves are not permitted to be recognised under FRS26 for investment contracts.

(d) Investments

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

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

Under FRS26, upon initial recognition financial investments are recognised at fair value. Subsequently, the Company is permitted, subject to specific criteria, to designate its investments as either financial investments at fair value through profit and loss, financial investments held on an available-for-sale basis, financial investments held to maturity, or loans and receivables. The Company holds financial investments on the following bases:

(i) Financial investments at fair value through profit and loss – this comprises assets designated by management as fair value through profit and loss on inception and derivatives which deemed to be held for trading. These investments are valued at fair value with all changes thereon being recognised in the profit and loss account.

The Company uses bid prices to value its quoted financial investments. Actively traded investments without quoted prices are valued using external broker bid prices. If there is no active established market for an investment, the Company applies an appropriate valuation technique such as discounted cash flow technique.

(ii) Loans and receivables – this comprises investments that have fixed or determinable payments and are not designated as fair value through profit and loss or available-for-sale. These investments include loans secured by mortgages, deposits and loans to policyholders and other unsecured loans and receivables. These investments are carried at amortised cost using the effective interest method and subject to impairment reviews. The Company measures the amount of the impairment loss by comparing the amortised cost with the present value of its estimated future cash flows discounted at the original effective interest rate.

Properties are valued annually by professional external valuers at market value as defined in the Appraisal and Valuation Manual issued by the Royal Institute of Chartered Surveyors in particular Practice statement 3.2. In accordance with SSAP 19, no depreciation is provided on investment properties as the directors consider that to depreciate them would not give a true and fair view.

1. Accounting Policies (continued)

(e) Long term business provision

The long term business provision is determined by the Company's directors based on advice from the Company's actuarial function holder, who determined the provision using recognised actuarial methods, with due regard to the actuarial principles laid down in Directive 2002/83/EC. It is calculated initially on a statutory solvency basis to comply with the reporting requirements under the Financial Services and Markets Act 2000. The valuation is then modified to remove certain resilience, contingency and other reserves required by the Prudential Sourcebook for Insurers and the General Prudential Sourcebook issued by the Financial Services Authority.

(f) Reinsurance

The Company uses reassurance to gain policyholder access to third party unit linked funds. The Company also seeks to reduce loss exposure by reinsuring certain levels of risk in various areas of exposure with other insurance companies or reinsurers. An asset or liability is recognised in the balance sheet representing premiums due to or payments due from reinsurers and the share of benefits and claims recoverable from reinsurers. The measurement of reinsurance assets is consistent with the measurement of the underlying direct insurance contracts.

(g) Allocation of surpluses

Surpluses arising from linked long term business, as a result of the annual investigation of the long term business, are carried forward to the profit and loss account.

(h) Tax

Tax is charged on all taxable profits arising in the accounting period.

The UK Government has made substantial changes to the rules relating to the taxation of life insurance companies, effective from 1 January 2013. Until the end of 2012, shareholders' taxable profits are calculated using regulatory surplus as a starting point, with appropriate deferred tax adjustment for UK GAAP. Beginning in 2013, under new life tax rules, taxable profits will be calculated using accounting profit or loss as a starting point.

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

(i) Cash flow statement

The Company has taken advantage of the exemption under FRS 1 (Revised) from preparing a cash flow statement.

(j) Foreign currencies

Foreign currency assets and liabilities are translated at year end exchange rates. Foreign currency revenue transactions are translated at rates ruling at the transaction dates, except for accrued revenue items that are translated at year end exchange rates.

2. Segmental analysis

(a) Gross Premiums

Premiums comprise corporate pension business. For premiums in respect of corporate pension business investment risk is borne by policyholders and transacted within the UK. All direct single and regular premiums are group pension business. Premiums for 2012 and 2011 are nil as all business is investment contracts without discretionary participation features and are deposit accounted, as described in the accounting policies part (c).

	2012 £000	2011 £000
New Business		
Single premiums		
- direct:		
pensions	678,548	727,730
external reinsurance	24,775	28,686
- intragroup reassurance accepted, pensions	634,114	576,997
	1,337,437	1,333,413

New business premiums include those contracts excluded from premium income in the technical account under FRS26 and the ABI SORP (as amended in December 2006). These are investment contracts without discretionary participation features and carry no significant insurance risk.

All new business premiums are in respect of investment linked contracts.

(b) Assets attributable to the long term business fund

Of the total amount of assets shown on page 16, £12,468,483,000 (2011: £11,717,457,000) is attributable to the long term business fund.

NOTES ON THE FINANCIAL STATEMENTS (continued)

3. Investment return

	Long-term business Technical account		Non-Technical account	
	2012	2011	2012	2011
	£000	£000	£000	£000
Investment Income				
Income from land and buildings	30,941	30,331	-	-
Income from listed investments	358,201	346,719	-	-
Income from other investments	18,852	16,880	50	76
Profit on the realisation of investments	305,341	239,146	-	-
	713,335	633,076	50	76
Investment expenses and charges				
Investment managers' expenses	(13,917)	(18,669)	-	-
Unrealised gains / (losses) on investments				
Debt securities	52	2,016	-	-
Linked assets	450,528	(134,060)	-	-
Exchange (losses) / gains on investments	(36,575)	805	-	-
Bank interest (payable) /receivable	(51)	(65)	1	2
Intragroup interest (payable)	(72)	(293)	-	-
Total investment return	**1,113,300**	**482,810**	**51**	**78**

4. Tax on profit on ordinary activities

(a) Analysis of charge in the period

	Long-term business technical account		Non technical account	
	2012	2011	2012	2011
	£000	£000	£000	£000
Current tax				
UK Corporation tax on profits of the period	2,009	4,114	12	21
Adjustments in respect of previous years	(26)	1,123	-	-
	1,983	5,237	12	21
Foreign tax	1,926	2,572	-	-
Total current tax	3,909	7,809	12	21
Deferred tax				
Adjustment in respect of previous years	(12)	(258)	-	-
Origination and reversal of timing difference	319	(3,045)	-	-
Effect of changes in tax rate	(420)	(395)	-	-
Tax charge on profit on ordinary activities	**3,796**	**4,111**	**12**	**21**
Shareholder tax attributable on the balance on the long term business technical account:				
Current tax			1,983	5,237
Deferred tax			(113)	(3,698)
			1,870	1,539
Total			**1,882**	**1,560**

PRUDENTIAL PENSIONS LIMITED

NOTES ON THE FINANCIAL STATEMENTS (continued)

4. Tax on profit on ordinary activities (continued)

(b) Factors affecting tax charge for period

From April 2012, the standard corporation tax rate for the UK changed from 26% to 24%. A further reduction in the standard corporation tax rate to 23% from April 2013 has also been enacted. Deferred tax at the end of 2012 has been provided wholly at the rate of 23% on the basis that all of the temporary differences will reverse at the new rate. The effect of this change on the deferred tax liabilities at 31 December 2012 is £420,000.

The Chancellor has proposed a further reduction to the UK corporation tax rate to 20% by 2015 however this is not reflected in the financial statements for the year ended 31 December 2012 as it has not been substantively enacted.

	2012 £000	2011 £000
Profit on ordinary activities before tax	11,438	9,181
Profit on ordinary activities multiplied by effective rate of corporation tax in the UK of 24.5% (2011: 26.5%)	2,802	2,433
Effects of		
Permanent differences	3	1
Depreciation lower than capital allowances	(8)	(9)
Utilisation of losses	-	(208)
Double tax relief claimed	(472)	(1,286)
Movement in reserves	(304)	3,204
Adjustments to current tax in respect of previous periods	(26)	1,123
Current tax charge for the period	**1,995**	**5,258**

(c) Balance sheet

	2012 £000	2011 £000
Provision for Deferred Tax		
Policy reserves (Life Tax Transitional Arrangements)	4,830	4,943
Undiscounted provision for deferred tax liability	**4,830**	**4,943**
Deferred tax liability at start of the period	4,943	8,641
Deferred tax (credited) / charged in technical/non-technical account for the period	(113)	(3,698)
Deferred tax liability at the end of period	**4,830**	**4,943**

The UK Government has made substantial changes to the rules relating to the taxation of life insurance companies, effective from 1 January 2013. Until the end of 2012, shareholders' taxable profits are calculated using the regulatory surplus as a starting point, with appropriate deferred tax adjustments for UK GAAP. Beginning in 2013, under new life tax rules, taxable profits will be calculated using accounting profit or loss as a starting point.

At the end of 2012, a deferred tax liability is recognised for the transitional adjustment that arises from the difference in retained UK GAAP profits and tax surplus which is required to be spread and taxed over a 10 year period.

The effect of these changes is reflected in the financial statements for the year ended 31 December 2012 but has no material impact on the Company's net assets.

NOTES ON THE FINANCIAL STATEMENTS (continued)

5. Auditors' remuneration

The remuneration of the auditors in respect of the audit of the Company's accounts and the Company's reporting pack for the Parent's consolidated accounts amounted to £54,000 (2011 total audit fee: £54,000). The remuneration of the auditors in respect of other services pursuant to legislation, including the audit of the regulatory return amounted to £8,000 (2011: £8,000).

6. Directors' emoluments and staff costs

During the year the directors of the Company received the following emoluments in respect of work on behalf of the Company:

	2012 £000	2011 £000
Aggregate emoluments and benefits	77	82

Retirement benefits are accruing for the directors under the Group's defined benefit scheme. The Company has no employees (2011: Nil). Included within net operating expenses are amounts paid in return for management services provided to the Company by other group companies.

7. Investments

	Current value		Cost	
	2012 £000	2011 £000	2012 £000	2011 £000
Debt securities and other fixed income securities	14,350	14,298	11,633	11,633
Deposits with credit institutions	46,000	48,500	46,000	48,500
	60,350	**62,798**	**57,633**	**60,133**

All debt securities and other fixed income securities are listed on a recognised UK investment exchange.

A. Financial instruments

(i) Designation and fair values

All financial assets are designated as either fair value through profit and loss or loans and receivables. Financial liabilities are designated as either fair value through profit and loss or amortised cost (in both years).

2012	Fair value through profit and loss £000	Loans and receivables £000	Total carrying value £000	Fair value £000
Financial Assets				
Deposits with credit institutions	-	46,000	46,000	46,000
Debt securities	14,350	-	14,350	14,350
Accrued investment income	-	39	39	39
Other debtors	-	3,311	3,311	3,311
Cash at bank and in hand	-	7,779	7,779	7,779
Assets held to cover linked liabilities	10,652,995	-	10,652,995	10,652,995
Total	**10,667,345**	**57,129**	**10,724,474**	**10,724,474**

7. Investments (continued)

(i) Designation and fair values (continued)

2012	**Fair value through profit and loss**	**Amortised Cost**	**Total carrying value**	**Fair value**
	£000	**£000**	**£000**	**£000**
Financial Liabilities				
Creditors arising out of direct insurance operations		185	185	185
Other creditors	-	19,508	19,508	19,508
Investment contracts without discretionary participating features	12,344,136	-	12,344,136	12,344,136
Total	**12,344,136**	**19,693**	**12,363,829**	**12,363,829**

2011	**Fair value through profit and loss**	**Loans and receivables**	**Total carrying value**	**Fair value**
	£000	**£000**	**£000**	**£000**
Financial Assets				
Deposits with credit institutions	-	48,500	48,500	48,500
Debt securities	14,298	-	14,298	14,298
Accrued investment income	-	48	48	48
Other debtors	-	1,784	1,784	1,784
Cash at bank and in hand	-	4,699	4,699	4,699
Assets held to cover linked liabilities	10,090,022	-	10,090,022	10,090,022
Total	**10,104,320**	**55,031**	**10,159,351**	**10,159,351**

2011	**Fair value through profit and loss**	**Amortised Cost**	**Total carrying value**	**Fair value**
	£000	**£000**	**£000**	**£000**
Financial Liabilities				
Creditors arising out of reinsurance operations	-	5,929	5,929	5,929
Creditors arising out of direct insurance operations	-	89	89	89
Other creditors	-	18,711	18,711	18,711
Investment contracts without discretionary participating features	11,585,758	-	11,585,758	11,585,758
Total	**11,585,758**	**24,729**	**11,610,487**	**11,610,487**

(ii) Determination of fair value

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

The fair values of the financial instruments for which fair valuation is required under UK GAAP are determined by the use of current market bid prices for quoted investments, or by using quotations from independent third-parties, such as brokers and pricing services or by using appropriate valuation techniques. Investments valued using valuation techniques include financial investments which by their nature do not have an externally quoted price based on regular trades and financial investments for which markets are no longer active as a result of market conditions e.g. market illiquidity. The valuation techniques used include comparison to recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation. These techniques may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments. When determining the inputs into the valuation techniques used priority is

7. **Investments (continued)**

(ii) Determination of fair value - continued

given to publicly available prices from independent sources, when available but overall, the source of pricing is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date.

The fair value estimates are made at a specific point in time, based upon available market information and judgements about the financial instruments, including estimates of the timing and amount of expected future cash flows and the credit standing of counterparties. Such estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument, nor do they consider the tax impact of the realisation of unrealised gains or losses from selling the financial instrument being fair valued. In some cases the fair value estimates cannot be substantiated by comparison to independent markets, nor can the disclosed value be realised in immediate settlement of the financial instrument.

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

The estimated fair value of derivative financial instruments reflects the estimated amount the Group would receive or pay in an arm's length transaction. This amount is determined using quoted prices if exchange listed, quotations from independent third-parties or valued internally using standard market practices.

The fair value of borrowings is based on quoted market prices, where available.

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

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

The classification criteria and its application to the Company can be summarised as follows:

Level 1 – quoted prices (unadjusted) in active markets for identical assets and liabilities

Level 1 principally includes exchange listed equities, mutual funds with quoted prices, exchange traded derivatives such as futures and options, and national government bonds unless there is evidence that trading in a given instrument is so infrequent that the market could not possibly be considered active. It also includes other financial instruments where there is clear evidence that the year end valuation is based on a traded price in an active market.

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

Level 2 principally includes corporate bonds and other non-national government debt securities which are valued using observable inputs, together with over-the-counter derivatives such as forward exchange contracts and non-quoted investment fund valued with observable inputs. It also includes investment contract liabilities that are valued using observable inputs.

In addition level 2 can include debt securities that are valued internally using standard market practices. None of the level 2 debt securities are valued internally in the current year. The Company's usual policy for valuing such securities is to use matrix pricing, which is based on assessing the credit quality of the underlying borrower to derive a suitable discount rate relative to government securities. Under matrix pricing, the debt securities are priced taking the credit spreads on comparable quoted public debt securities and applying these to the equivalent debt instruments factoring a specified liquidity premium. The significance of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

7. **Investments (continued)**

(ii) Determination of fair value (continued)

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

Level 3 principally includes investments in private equity funds, investments in property funds which are exposed to bespoke properties or risks, investments which are internally valued or subject to a significant number of unobservable assumptions and certain derivatives which are bespoke or long dated. It also includes debt securities which are rarely traded or traded only in privately negotiated transactions and hence where it is difficult to assert that these have been based on observable market data. The inherent nature of the vast majority of these assets means that, in normal market conditions, there is unlikely to be significant change in the specific underlying assets classified as level 3.

	31 December 2012			
	Level 1	**Level 2**	**Level 3**	**Total**
	£000	**£000**	**£000**	**£000**
Unit-linked				
Equity securities	3,227,293	-	-	3,227,293
Debt securities	1,388,285	4,819,360	-	6,207,645
Other investments (including derivative assets)	3,111	5,566	-	8,677
Derivative liabilities	(338)	(977)	-	(1,315)
Total financial investments, net of derivative liabilities:	**4,618,351**	**4,823,949**	-	**9,442,300**
Investment contracts without discretionary participation features held at fair value	-	(12,344,136)	-	(12,344,136)
Total	**4,618,351**	**(7,520,187)**	-	**(2,901,836)**
Percentage of total	(159%)	259%	-	100%
Non-linked				
Debt securities	**14,350**	-	-	**14,350**
Percentage of total	100%	-	-	100%
Company total				
Equity securities	3,227,293	-	-	3,227,293
Debt securities	1,402,635	4,819,360	-	6,221,995
Other investments (including derivative assets)	3,111	5,566	-	8,677
Derivative liabilities	(338)	(977)	-	(1,315)
Total financial investments, net of derivative liabilities	**4,632,701**	**4,823,949**	-	**9,456,650**
Investment contracts without discretionary participation features held at fair value	-	(12,344,136)	-	(12,344,136)
Total	**4,632,701**	**(7,520,187)**	-	**(2,887,486)**
Percentage total	(160%)	260%	-	100%

NOTES ON THE FINANCIAL STATEMENTS (continued)

7. Investments (continued)

(ii) Determination of fair value (continued)

	31 December 2011			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Unit-linked				
Equity securities	3,076,674	-	16	3,076,690
Debt securities	1,880,183	4,093,139	-	5,973,322
Other investments (including derivative assets)	1,242	22,011	-	23,253
Derivative liabilities	(1,067)	(2,499)	-	(3,566)
Total financial investments	**4,957,032**	**4,112,651**	**16**	**9,069,699**
Investment contracts without discretionary participation features held at fair value	-	(11,585,758)	-	(11,585,758)
Total	**4,957,032**	**(7,473,107)**	**16**	**(2,516,059)**
Percentage of total	(197%)	297%	-	100%
Non-linked				
Debt securities	**14,298**	-	-	**14,298**
Percentage of total	100%	-	-	100%
Company total				
Equity securities	3,076,674	-	16	3,076,690
Debt securities	1,894,481	4,093,139	-	5,987,620
Other investments (including derivative assets)	1,242	22,011	-	23,253
Derivative liabilities	(1,067)	(2,499)	-	(3,566)
Total financial investments	**4,971,330**	**4,112,651**	**16**	**9,083,997**
Investment contracts without discretionary participation features held at fair value	-	(11,585,758)	-	(11,585,758)
Total	**4,971,330**	**(7,473,107)**	**16**	**(2,501,761)**
	(199%)	299%	-	100%

Reconciliation of movements in level 3 financial instruments measured at fair value

The following table reconciles the value of level 3 financial instruments at 1 January 2012 to that presented at 31 December 2012. Total gains and losses recorded in the long-term technical account in the period represents realised gains and losses, including interest and dividend income, unrealised gains and losses on financial instruments classified at fair value through profit and loss and foreign exchange movements on overseas investments. All these amounts are included within "investment income" and "unrealised gains/(losses)" in the long-term technical account.

2012	**At 1 Jan 2012**	**Total gains or (losses) in long-term technical account**	**Purchases**	**Sales**	**Transfers into level 3**	**Transfers out of level 3**	**At 31 Dec 2012**
Unit-linked	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**
Equity securities	16	(16)	-	-	-	-	-

2011	**At 1 Jan 2011**	**Total gains or (losses) in long-term technical account**	**Purchases**	**Sales**	**Transfers into level 3**	**Transfers out of level 3**	**At 31 Dec 2011**
Unit-linked	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**
Equity securities	-	(38)	-	-	54	-	16

7. Investments (continued)

(ii) Determination of fair value (continued)

Transfers between level 1 and level 2

During 2012, transfers from level 1 to level 2 amounted to £19m (2011: level 2 to level 1 £54m) in respect of certain unit linked investments held by the Company which arose due to a reclassification of investment type.

B. Market Risk

The financial assets and liabilities attaching to the Company's life assurance business are, to varying degrees, subject to market risk that may have a material effect on the profit or loss and shareholders' funds.

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

Market risk comprises four types of risk, namely:

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

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

(i) Interest rate risk

The following table shows an analysis of the classes of financial assets with direct exposure to interest rate risk. Each applicable class of the Company's assets are analysed between those exposed to fair value interest rate risk, cash-flow interest rate risk and those with no direct interest rate risk exposure. Interest rate risk is minimal for the shareholder assets as the deposits are all less than one month, whereas for the unit-linked assets the risk is borne by the policyholders.

2012	**Fair value interest rate risk**	**Cash flow interest rate risk**	**Total**
	£000	**£000**	**£000**
Financial Assets			
Deposits with credit institutions	-	46,000	46,000
Debt securities	14,350	-	14,350
Cash at bank and in hand	-	7,779	7,779
	14,350	**53,779**	**68,129**

2011	**Fair value interest rate risk**	**Cash flow interest rate risk**	**Total**
	£000	**£000**	**£000**
Financial Assets			
Deposits with credit institutions	-	48,500	48,500
Debt securities	14,298	-	14,298
Cash at bank and in hand	-	4,699	4,699
	14,298	**53,199**	**67,497**

7. **Investments (continued)**

Effective interest rates

2012	Balance of financial instruments not at fair value in profit and loss £000	Range of effective interest rate applicable as at 31st December 2012 %
Financial Assets		
Deposits with credit institutions	46,000	0.25 % - 0.43%
Cash at bank and in hand	7,779	0.4%
	53,779	

2011	Balance of financial instruments not at fair value in profit and loss £000	Range of effective interest rate applicable as at 31st December 2011 %
Financial Assets		
Deposits with credit institutions	48,500	0.55 % - 0.72%
Cash at bank and in hand	4,699	0.3%
	53,199	

Liquidity Analysis

(ii) Contractual maturities

Maturity profile for investment contracts and durations of long-term business contracts on an undiscounted basis

The majority of the in force business consists of pooled investment vehicles used for Pension Scheme business which by nature do not have any contractual repricing or maturity dates, as the benefits are the realisation values of the units held in the internal linked funds and may be surrendered at any time.

(iii) Sensitivity to interest rate movement

The estimated sensitivity of the Company to a movement in interest rates (including assumed investment returns for all asset classes, market values of debt securities and all risk discount rates) of 1% and 2% is as follows:

	31 December 2012			
	Fall of 1%	Fall of 2%	Rise of 1%	Rise of 2%
	£000	£000	£000	£000
Carrying value of debt securities	1,654	3,308	(1,654)	(3,308)
Interest on deposits with credit institutions	(156)	(156)	538	1,076
Related tax effects	(345)	(725)	257	513
Net sensitivity of profit after tax and shareholders' funds	**1,153**	**2,427**	**(859)**	**(1,719)**

	31 December 2011			
	Fall of 1%	Fall of 2%	Rise of 1%	Rise of 2%
	£000	£000	£000	£000
Carrying value of debt securities	1,279	3,135	(1,279)	(3,135)
Interest on deposits with credit institutions	(319)	(319)	531	1,064
Related tax effects	(240)	(704)	187	518
Net sensitivity of profit after tax and shareholders' funds	**720**	**2,112**	**(561)**	**(1,553)**

7. **Investments (continued)**

C. Credit Risk

(i) Concentration of credit risk

The following table summarises by rating the securities held by the Company as at 31 December 2012 and 2011.

	2012 £000	2011 £000
AAA	60,350	14,298
AA	7,779	-
AA-	-	4,699
A+	-	5,000
A-	-	43,500
	68,129	67,497
Unit-linked	10,652,995	10,090,022
Total assets bearing credit risk	10,721,124	10,157,519

Due to the matching of policyholders liabilities to attaching asset value movements there is minimal credit risk for the Company on the Unit linked contracts as the risks are borne by the policyholders.

Reverse repurchase agreements

At 31 December 2012, the Company had entered into reverse repurchase transactions under which it purchased securities and had taken on the obligation to resell the securities for the purchase price of £624m (2011: £214m), together with accrued interest.

D. Risk management

The Company's business involves the acceptance and management of risk. The Company has in place a risk management process, which is undertaken in accordance with the Group Risk Framework adopted by the Prudential Group.

A number of risk factors affect the Company's operating results and financial condition. The financial risk factors affecting the Company include the effects of market risk, credit risk and liquidity risk on the financial instruments of the Company.

The Company's investment guidelines allow the use of derivatives to facilitate efficient portfolio management or to reduce investment risk.

It is the Company's policy that cash or corresponding assets cover amounts at risk through derivative transactions. 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 the profit and loss account. The Company does not apply hedge accounting to its derivatives.

For unit linked insurance and investment contracts, the liability to policyholders is determined by the value of the assets in the unit-linked portfolios. There is therefore minimal net equity price, currency, interest rate or credit risk exposure to the Company for these contracts as the risks are borne by the policyholders.

(i) Market risk

Market risk is the risk that future changes in market prices may make a financial instrument less valuable. Due to the matching of policyholder liabilities to attaching asset value movements the UK unit-linked business is not directly affected by market or credit risk.

NOTES ON THE FINANCIAL STATEMENTS (continued)

7. Investments (continued)

(ii) Credit risk

Credit risk is the risk that a counterparty or an issuer of securities, which the Company holds in its asset portfolio, defaults or another party fails to perform according to the terms of the contract. Due to the matching of policyholder liabilities to attaching asset value movements the UK unit-linked business is not directly affected by credit risk. The Company is also exposed to credit-related losses in the event of non-performance by counterparties.

(iii) Liquidity risk

Liquidity risk is the risk that the Company may be unable to meet payment of obligations in a timely manner at a reasonable cost or the risk of unexpected increases in the cost of funding the portfolio at appropriate maturities or rates. Liquidity management in the Company seeks to ensure that, even under adverse conditions, the Company has access to the funds necessary to cover surrenders, withdrawals and maturing liabilities.

For the unit-linked funds, there is a risk that significant policyholder outflows could exceed the short-term liquidity within the funds. The Company has the power to defer settlement to policyholders in certain circumstances by between one and six months, depending on the fund.

8. Capital requirements and management

The available capital of £30.4m (2011: £22.2m) reflects the excess of regulatory basis assets over liabilities of the Company before deduction of the regulatory capital resources requirement of £13.2m (2011: £12.2m). This excess of available capital over capital resources requirement is monitored during the year. In addition, a realistic assessment of available capital and capital requirements sufficient to cover a 1 in 200 year event is undertaken. Additional capital is sought from the parent company as necessary.

	2012 £000	2011 £000
Shareholders' equity		
Held outside long-term funds	17,238	11,716
Held in long-term funds	29,518	25,484
Total shareholders' equity	46,756	37,200
Adjustments to regulatory basis		
Other adjustments to restate these amounts to a regulatory basis	(16,326)	(14,969)
Total available capital resources on FSA regulatory basis	30,430	22,231

9. Assets held to cover linked liabilities - at current value

	2012 £000	2011 £000
Freehold land and buildings	424,285	436,047
Leasehold land and buildings	76,429	90,800
Shares and other variable yield securities	3,227,293	3,076,690
British government securities - fixed income	534,450	900,215
British government securities - index linked	476,014	800,758
Debentures and loan stocks	5,082,506	4,184,371
Provincial & municipal stocks	114,675	87,978
Deposits with credit institutions	188,722	167,055
Other investments	7,363	-
Other assets	521,258	346,108
	10,652,995	**10,090,022**
Assets held to cover linked liabilities - at cost	9,676,683	9,485,663

Included in the carrying values above are amounts in respect of listed investments as follows:

	2012 £000	2011 £000
Shares and other variable yield securities	3,227,293	3,076,690
British government securities - fixed income	534,450	900,215
British government securities - index linked	476,014	800,758
Debentures and loan stocks	5,082,506	4,184,371
Provincial & municipal stocks	114,675	87,978
Other investments	7,363	-
	9,442,301	**9,050,012**

10. Reserves and policyholder liabilities

	Long-term business provision net of reassurance £000	Provision for linked liabilities net of reassurance £000	Profit and Loss account £000	Capital Redemption Reserve £000
Balance at 1 January 2012	**200**	**10,090,022**	**27,112**	**4,088**
Movement in technical provisions for year	-	1,127,500	-	-
Movement in profit & loss account for year	-	-	9,556	-
Deposits received from policyholders under investment contracts	-	1,033,452	-	-
Payments made to policyholders of investment contracts	-	(1,597,979)	-	-
Balance at 31 December 2012	**200**	**10,652,995**	**36,668**	**4,088**

Of the reinsurer's share of technical provisions for linked liabilities of £1,691.1m at 31 December 2012 (2011: £1,495.7m), the entire balance relates to companies outside of the Prudential Group and of this 98% (2011: 99%) was from reinsurers with S&P's rating of A and above.

The entire reinsurer's share of technical provisions for long term business of £71.9m at 31 December 2012 (2011: £76.3m) relates to reinsurance agreements with other Prudential Group companies.

11. Long term business provision

The long term business provision comprises a provision for annuity business and an additional provision for data integrity.

For annuity business, the provisions are the present value of the annuity payments and expenses. The calculation of the provisions requires a number of actuarial assumptions regarding future experience to be made. The assumptions are set by the Directors having regard to actuarial advice and based on analysis of relevant past and current data and information on anticipated future trends.

Valuation interest rates have been amended, where necessary, in line with changes in market yields.

There have been no other significant changes in the bases or assumptions adopted for the calculation of the long term business provision during the year.

The reinsurers' share of the long term business provision relates mainly to cessions to Prudential Annuities Limited, a fellow subsidiary company.

The provisions have been calculated on the following bases:

	2012	**2011**
Discount Rate	3.741% for annuities	4.381% for annuities
Fund Growth	N/A for annuities	N/A for annuities
Expense Inflation	3.50% gross	3.75% gross
Renewal expenses:		
Reassured annuity business	£21.57 p.a per policy	£19.84 p.a per policy
Annuity mortality	Male: 99% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long term improvement rate of 2.25% p.a.	Male: 98% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 2.25% p.a.
	Female: 89% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long term improvement rate of 1.50% p.a.	Female: 88% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 1.25% p.a.

12. Creditors

All creditors are payable within a period of five years.

	2012	2011
	£000	£000
Creditors arising from reinsurance operations	-	5,929
Creditors arising from direct insurance operations	185	89
Due to group undertakings	1,372	15,161
Sundry creditors	16,361	3,550
Tax payable	1,775	2,257
	19,693	**26,986**

The amounts due to related undertakings are intercompany balances which are cleared regularly and not interest bearing. At the end of 2011, amounts due to group undertakings included an amount of £14.0m which represented a contingent loan (including interest at 3 month LIBOR plus 1% cumulative) repayable to The Prudential Assurance Company Limited. This loan was repaid during 2012.

Sundry creditors are payable on demand and are not interest bearing.

13. Other debtors

All debtors are due within one year.

	2012	2011
	£000	£000
Debtors arising from reinsurance operations	2,360	-
Amounts owed by group undertakings	755	877
Other debtors	196	907
	3,311	**1,784**

14. Bank accounts

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

15. Charges

In the normal course of business certain reinsurance liabilities were secured by a floating charge, ranking these liabilities equally with amounts due under unsecured direct (non-reassurance) policies, over the long term insurance assets of the Company. Amounts secured by charges of this nature were £4,058.3m, £70.3m, £36.1m, £10.8m, £8.4m and £0.6m, representing liabilities to six different customers.

NOTES ON THE FINANCIAL STATEMENTS (continued)

16. Share capital

	2012 £000	2011 £000
Allotted and fully paid		
6 million ordinary shares (2011: 6 million) of £1 each	6,000	6,000

17. Related party transactions

The Company has taken advantage of the exemption under paragraph 3(c) of Financial Reporting Standard 8 (FRS 8) from disclosing transactions with other subsidiary undertakings of the Prudential Group. There were no other transactions with related parties.

18. Ultimate and immediate parent companies

The immediate parent company is The Prudential Assurance Company Limited. The ultimate parent company is Prudential plc which is the only parent company which prepares group accounts. Copies of these accounts can be obtained from the Company Secretary, Laurence Pountney Hill, London EC4R OHH.