The Prudential Assurance Company Limited

Solvency and Financial Condition Report

31 December 2018

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This report has been prepared in compliance with the Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009|138|EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) ('Delegated Regulation'). The structure of this report follows the structure set out in Annex XX and discloses the information referred to in Articles 292 to 298 of the Delegated Regulation. The report also contains narrative information in quantitative and qualitative form supplemented, where appropriate, with quantitative templates.

Summary

Company background

The Prudential Assurance Company Limited (‘PAC’, ‘the Company’) was founded in the United Kingdom ('UK') in 1848, and is a leading provider of savings and retirement income products. Our biggest strength comes from providing investments that help our customers meet their long-term goals, whilst also protecting them against short-term market fluctuations.

Throughout 2018 the Company owned insurance subsidiary undertakings including Prudential Pensions Limited ('PPL'), Prudential International Assurance plc ('PIA') and a branch in Poland. These transacted insurance business in the United Kingdom and overseas.

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

The Company consists of the With-Profits Fund and the Shareholder Fund. The With-Profits Fund is made up of the With-Profits Sub-Fund ('WPSF'), the Scottish Amicable Insurance Fund ('SAIF') and Defined Charge Participating Sub-Fund ('DCPSF') as shown in the table below.

The Prudential Assurance Company Limited (PAC)			
With-Profits Fund			Shareholder Fund "0:100"
With-Profits Sub-Fund (WPSF) "90:10"	Scottish Amicable Insurance Fund (SAIF) "100:0"	Defined Charge Participating Sub-Fund (DCPSF) "100:0"	

The proportion of divisible profit attributable to with-profits policyholders in the WPSF is defined by the Articles of Association as being at least 90 per cent. Most of the With-Profits Fund business is written in WPSF and is 90:10.

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

The whole of the profit arising in SAIF, including profits or losses on its non-profit business, will be allocated to with-profits policyholders in SAIF (i.e. SAIF is a "100:0" sub-fund). SAIF is a sub-fund closed to new business that contains the bulk of the business originally written by the Scottish Amicable Life Assurance Society acquired by the Company in 1997. The profit in the DCPSF which forms part of the Company's long term fund arises solely from investment performance and is entirely attributable to DCPSF policyholders (i.e. the DCPSF is a "100:0" sub-fund).

All the profit of the Shareholder Fund is attributable to shareholders (i.e. the Shareholder Fund is a "0:100" sub-fund).

The Company's core strengths in with-profits and financial products for retirement are underpinned by expertise in areas such as understanding life expectancy, managing investment risk and a range of investment assets. The Company is also financially strong enabling it to withstand major market volatility and ensure it meets all commitments.

The Company's products are typically long-term, consisting of life insurance, pensions, pension annuities, investment and savings products. In common with other UK long-term insurance companies, the Company's products are structured as either with-profits (or participating) products written in the with-profits funds, or non-participating products including annuities in payment and unit-linked products written in the shareholder fund.

Business and performance

The fundamentals underpinning the UK’s retirement market continue to change. Risk and responsibility for retirement provision continues to transfer away from the state and corporates to individuals. As customers adjust to the reforms introduced by Pensions Freedom in 2015, the new flexible arrangements to control their own pensions have been accompanied by significant complexity which is adding to the burden of personal responsibility to secure an income in retirement. Investment risk, longevity risk and inflation risk are to be mitigated by today’s retirement saver.

To support its customers in this changing environment, the Company’s product and distribution profile has evolved by increasing the range of product options to mirror the flexibilities of the pensions freedom era. There has been a shift away from a reliance on annuity business to a focus on more flexible bond, ISA, pension and income drawdown products across a range of tax efficient solutions. The Company launched the Prudential Retirement Account in 2016, an online account based plan, that provides customers with the flexibility to save for their retirement, benefit from an income in retirement and facilitate access to their fund as they save. The Retirement Account allows customers to invest in PruFund, the Company’s customer proposition managed by Prudential Portfolio Management Group, the Company’s market leading multi-asset management team. In 2018 Prufund reached £43 billion (2017: £36 billion) in customer assets under management ('AUM'), up 19 per cent. This included the Prudential Retirement Account, which experienced a successful year accumulating AUM of £12 billion (2017: £7.2 billion).

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

In March 2018 Prudential plc announced its intention to demerge the newly formed M&GPrudential from Prudential plc, resulting in two separately-listed companies, with different investment characteristics and opportunities. In preparation for the demerger, the legal ownership of the Company's Hong Kong Insurance subsidiaries (as had been stated in the 2017 Solvency and Financial Condition Report post balance sheet events) was transferred to Prudential Corporation Asia Limited ('PCAL') on 19 December for £33 million. See section A.1.4 for further details.

The Company reinsured £12 billion of the Company's shareholder annuity portfolio to Rothesay Life in March 2018, which is expected to be followed by a Part VII transfer of most of the portfolio by 30 June 2019. M&GPrudential as a standalone group will continue to drive its transformation into a more capital-efficient and customer-focused business, targeting growing customer demand for comprehensive financial solutions in the retirement and savings markets.

The Company announced a major investment programme in the new combined business’s infrastructure to improve customer service, accelerate product development, and widen customer choice. The MyPru online servicing portal, which allows customers to enjoy ease and convenience of accessing policies online, and dramatically reducing the time it takes to withdraw money from bonds are just two of the ways that a digitisation of the business is making customers’ lives easier. As part of M&GPrudential, the Company has the opportunity to offer its customers a wider set of solutions as their needs evolve.

In January 2018, the Company announced a new partnership with Tata Consultancy Services ('TCS'), a global leader in IT, business process and digital services, to enhance its service for UK savings and investment customers. Over four million life and pensions contracts have moved to Diligenta, the FCA-regulated subsidiary of TCS. This involved the transfer of 2,500 people, including 650 Prudential colleagues.

The performance of the Company for the year-ended 31 December 2018, as provided in Section A, is described using the Company's results as presented in its UK GAAP financial statements.

The Company's total operating profit of £1,089 million in 2018 was 37 per cent (£292 million) higher than the 2017 operating profit of £797 million. The increase is primarily due to an increase of £391 million in relation to the Thematic Review of Annuities Sales Practices ('TRASP'). A charge of £225 million was made in 2017 in relation to TRASP, whereas income of £166 million in relation to insurance recoveries has been recognised for 2018. See section A.1.4.5 for further details.

Changes in longevity assumption basis contributed £441 million to operating profit, an increase of £237 million on 2017 reflecting changes to annuitant mortality assumptions to reflect current mortality, as well as the adoption of the Continuous Mortality Investigation ('CMI') 2016 model and some refinements to the Company's expectations for mortality for its portfolio.

This was partially offset by a £187 million decrease in other management actions to improve solvency because of reduced opportunity for this activity in 2018 and a £75 million decrease on shareholder business primarily due to the partial sale of the shareholder annuity portfolio which means there is a smaller portfolio remaining on which profits may be earned. Recent court cases have also confirmed that there is a requirement for guaranteed minimum pensions (GMPs) to be equalised between male and female members / policyholders. £55 million is included within the long term business provision to cover the expected costs of equalisation.

The Company's total non-operating result has decreased by £1,532 million to a profit of £263 million in 2018 from a profit of £1,795 million in 2017. This is primarily due to revaluation on the Hong Kong subsidiaries which has decreased by £987 million. In 2018 there was a gain of £599 million prior to the transfer, which represents the estimated fair value of the business at the date of transfer of £9,450 million less the opening amount at 1 January 2018 of £8,851 million. In 2017 the Hong Kong subsidiaries contributed a revaluation gain of £1,586 million.

In 2018, the Company announced the partial sale of the Company's shareholder annuity portfolio to Rothesay Life. The non-operating loss arising from the transaction was £508 million.

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

The UK GAAP profit before tax has decreased by £1,240 million from a profit of £2,592 million in 2017 to a £1,352 million profit in 2018 as a result of these movements in operating and non-operating profits.

System of governance

The Board of The Prudential Assurance Company Limited is collectively responsible for the long-term success of the Company and for providing leadership within a framework of effective controls. The control environment enables the Board to identify significant risks and apply appropriate measures to manage and mitigate them.

The Company's governance structures are kept under constant review to ensure they suit the needs of the business and stakeholders. In 2018 the Company became a wholly owned subsidiary of M&G Prudential Limited which is a newly formed subsidiary of Prudential plc, the parent company of the Prudential group. This resulted in changes to the board governance as detailed in section B.1.1.

There were further changes made to the internal structure of the Company, as well as the delegation of responsibilities, reporting lines and allocation of functions to meet requirements of the ongoing demerger and transformation activity. The Company's Fit and Proper Policy was updated to align with the introduction of the Senior Managers and Certification Regime ('SMCR') in December 2018. There have been no other material changes to the system of governance at the date of this report.

Further information on the Company’s system of governance including information on the composition of its Board, key functions, risk management and internal control system is provided in Section B.

Risk profile

The Company's Risk Management Framework is designed to ensure the business remains strong through stress events so it can continue to deliver on long term commitments to both customers and shareholders. Markets were relatively stable during the first half of 2018. However, the second half of the year saw a fall in markets due to concerns over adverse impacts from a potential hard Brexit, an uncertain political and economic outlook and rising international trade tensions. The Company continues to carefully monitor and manage such risks and the financial strength of the Company remained robust throughout 2018.

The Company generates value for shareholders by selectively taking exposure to risks that are adequately rewarded and that can be appropriately quantified and managed. The Company retains risks within a clearly defined risk appetite, which contributes to value creation and provides the ability to withstand the impact of an adverse stressed outcome.

The Company defines ‘risk’ as the uncertainty that it faces in successfully implementing its strategies and objectives. This includes all internal or external events, acts or omissions that have the potential to threaten the success and survival of the Company. As such, material risks will be retained selectively if there is value in doing so, and where it is consistent with the Company's risk appetite and philosophy towards risk-taking.

For retained risks, the Company ensures that it has the necessary capabilities, expertise, processes and controls to appropriately manage the exposure.

Further information on the main risks inherent in the business (namely market risk, credit risk, insurance or underwriting risk, liquidity risk, operational risk, business environment risk, reputational risk, conduct risk, group risk, strategic risk and technology risk) and how these risks are managed, and details of how the Company maintains an appropriate risk profile are provided in Section C.

Valuation for solvency purposes

For the purposes of Solvency II reporting, the Company applies the Solvency II valuation rules to value the assets and liabilities of the Company:

(i) As a general principle, technical provisions under Solvency II are valued at the amount for which they could theoretically be transferred immediately to a third party in an arm's length transaction. The technical provisions consist of the best estimate liability and the risk margin, reduced by the “transitional measures on technical provisions” where relevant.

(ii) The assets and other liabilities are valued under Solvency II at the amount for which they could be exchanged between knowledgeable and willing parties in arm's length transactions. The assets and other liabilities are valued separately using methods that are consistent with this principle in accordance with the valuation approaches set out in the Solvency II Directive.

The own funds and capital for the Company’s non-insurance subsidiary Prudential Lifetime Mortgages Limited which carries out financial activities are included using sectoral rules.

The legal ownership of the Hong Kong insurance subsidiaries was transferred to another Group company on 19th December 2018 as detailed in A.1.4.2. Until this date, the own funds and Solvency Capital Requirement for the Company included amounts in relation to the Hong Kong subsidiaries.

Further information on the valuation of assets, technical provisions and other liabilities of the Company for solvency purposes is provided in Section D, including a discussion of the differences between Solvency II and the UK GAAP valuation bases.

Capital management

The Company has been granted approval by the Prudential Regulation Authority ('PRA') to calculate its solvency capital requirement ('SCR') based on its internal model. At 31 December 2018, the SCR was £9,309 million (2017: £14,397 million). The minimum capital requirement ('MCR') is currently 25 per cent (2017: 25 per cent) of the SCR, £2,327 million at 31 December 2018 (2017: £3,599 million). The Company's SCR and MCR have been met at all times throughout 2018. At 31 December 2018, the Company's Solvency II surplus was £3,691 million (2017: £6,115 million). The majority of the reduction in surplus is as a result of the transfer of the Hong Kong subsidiaries to PCAL and further detail is provided in section E.

A summary of the reconciliation of the Company's shareholder Solvency II position published in the Company's 2018 financial statements to the Solvency II position, incorporating the Company's ring-fenced funds, included in the quantitative reporting templates attached to this document, is provided in Section E. Additional information on the components of the Company's own funds and solvency capital requirement is also provided in Section E.

A Business and performance

(Unaudited)

A.1 Business

A.1.1 Overview

Name and legal form

The Prudential Assurance Company Limited ('the Company') is a company limited by shares incorporated and registered in England and Wales.

The Company is a wholly owned subsidiary of M&G Prudential Limited which is a wholly owned subsidiary of Prudential plc, the ultimate parent company. Prudential plc is a public limited company, limited by shares, incorporated and registered in England and Wales and is the parent company of the Prudential group ('the Prudential Group' or 'the Group'). The Group is an international financial services group, with significant operations in Asia, the United States and the United Kingdom. Prudential plc has dual primary listings in London (premium listing) and Hong Kong and has therefore adopted a governance structure based on the UK and Hong Kong Corporate Governance Codes. Prudential plc also maintains listings on the New York Stock Exchange and the Singapore Stock Exchange.

During 2018, the address of the registered office of the Company, M&G Prudential Limited and Prudential plc was:

Laurence Pountney Hill
London
EC4R 0HH

On 12 April 2019 the address of the registered office of the Company and M&G Prudential Limited changed to:

10 Fenchurch Avenue
London
EC3M 5AG

On 12 April 2019 the address of the registered office of Prudential plc changed to:

1 Angel Court
London
EC2R 7AG

This Solvency and Financial Condition Report ('SFCR') covers PAC on a solo entity basis.

Supervisory authority and Group supervisory authority

The Company and the Group are supervised by the Prudential Regulation Authority ('PRA'), the Company's lead supervisor in accordance with the Financial Services and Markets Act 2000 ('FSMA'). The contact details are:

Prudential Regulation Authority
Bank of England
Threadneedle Street
London
EC2R 8AH
United Kingdom

The Company is authorised by the PRA to provide regulated products and services, including: carrying out contracts of insurance, accepting deposits, providing credit to consumers, giving investment advice, arranging deals in investments, safeguarding and administration of assets and establishing, operating or winding up a personal or stakeholder pension scheme.

External auditor

The Company is audited by KPMG LLP. The contact details are:

KPMG LLP
15 Canada Square
London
E14 5GL
United Kingdom

Holders of qualifying holdings

As at 31 December 2018, M&G Prudential Ltd, incorporated and registered in England and Wales, is the only holder of qualifying holdings in the Company (being holdings of 10 per cent or more of the capital or voting rights) following the sale of the Company from Prudential plc to M&G Prudential Ltd during the year.

A.1.2 Company structure

Material subsidiaries of the Company

The Company's material trading subsidiaries at 31 December 2018 are set out below:

	Main activity	**Country of incorporation**
Prudential Pensions Limited	Insurance	England and Wales
Prudential International Assurance plc	Insurance	Ireland

The Company has 100 per cent of the voting rights of the subsidiaries listed above. The percentage of equity owned is the same as the percentage of the voting rights held.

In preparation for the demerger of M&GPrudential from Prudential plc, the beneficial interests in the Company's Hong Kong insurance subsidiaries were transferred from the Company to Prudential Corporation Asia Limited ('PCAL') on 14 December 2018, with the legal ownership transferring on 19 December 2018. See Section A.1.4 for further details.

Particulars of the subsidiaries are shown in Section D.1. A complete list of the Company's related undertakings is provided in Appendix A.

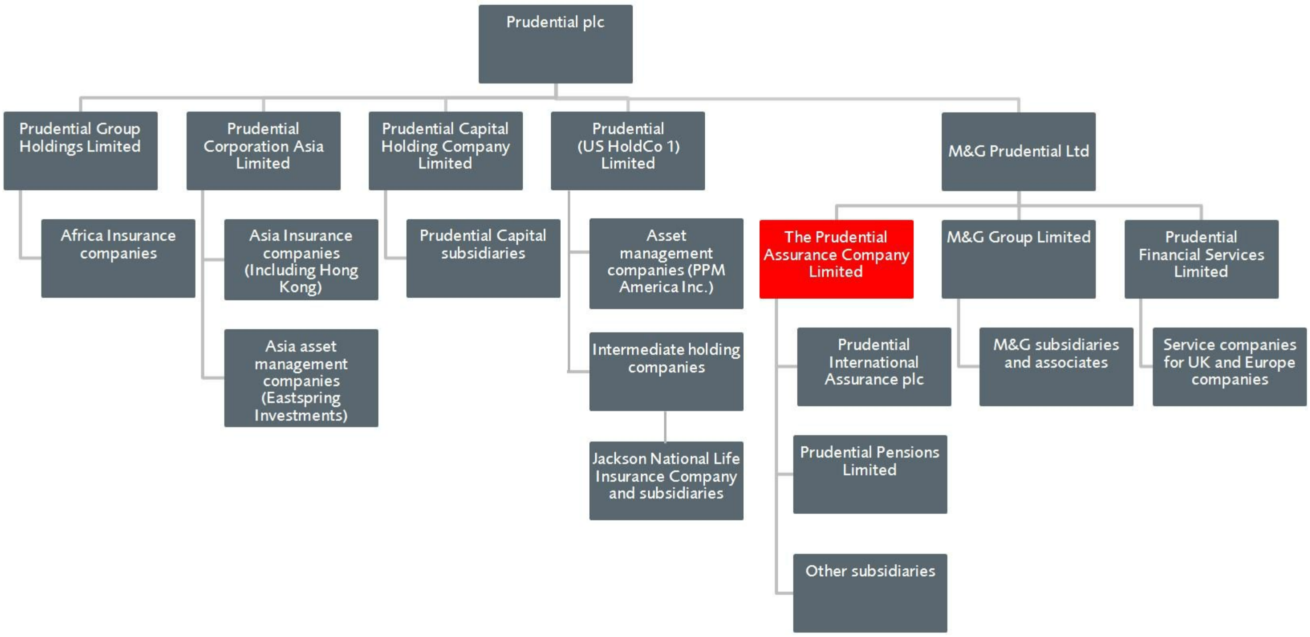
Legal structure of the Group and related undertakings

As noted above, the Company is part of the Prudential plc Group. The Prudential plc Group is structured around three main business units: Prudential Corporation Asia (incorporating the asset management business, Eastspring Investments), North America Business Unit and M&GPrudential in the UK and Europe. In addition, in recent years, the Group has expanded into Africa. The Company forms the major part of the M&GPrudential business unit's insurance operations.

On 26 November 2018 in preparation for the expected demerger the Company's legal ownership was transferred from its previous parent company Prudential plc to a new holding company M&G Prudential Limited. M&G Prudential Limited is a subsidiary of Prudential plc. The ultimate parent of the Company at 31 December 2018 therefore remains Prudential plc.

Figure 1 below shows, in a simplified form, the direct subsidiary undertakings of the ultimate parent company, Prudential plc (shares held directly or via nominees) and Prudential's significant subsidiaries as at 31 December 2018.

Figure 1: Simplified structure of Prudential plc as at 31 December 2018



A.1.3 Business and performance

Material lines of business and material geographical areas

The Company transacts long-term insurance business in the United Kingdom ('UK'). Throughout 2018 the Company also owned insurance subsidiary undertakings in the UK and in the Republic of Ireland, and a branch in Poland.

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

The Company's UK insurance subsidiary, Prudential Pensions Limited mainly sells unit-linked products.

The Company's Irish subsidiary, Prudential International Assurance plc ('PIA'), is a leading insurer in the offshore bond market while also providing risk insurance for its UK policyholders. PIA sells to both UK and non-UK nationals. Its focus in 2018 has been the sale of multi-asset solutions to UK nationals resident in the UK and selected countries in continental Europe.

The core business of the Company's Polish branch is a life insurance product, Premiopolisa. This is an individual protection product offering guarantees with significant growth potential at maturity. In addition the Polish branch offer some protection products. In January 2019 there was a Part VII transfer of the Polish branch to PIA as detailed in section A.5.3.1.

The Company's Hong Kong subsidiaries were transferred to PCAL, as detailed in section A.1.4 below.

A.1.4 Significant business or other events that have a material impact on the Company over the reporting period

A.1.4.1 M&GPrudential Demerger

In March 2018, Prudential plc announced its intention to demerge its UK & Europe business ('M&GPrudential') from Prudential plc, resulting in two separately-listed companies. The Company forms a major part of M&GPrudential.

A1.4.2 Transfer of Hong Kong Subsidiaries

On 14 December 2018, the Company's Hong Kong subsidiaries, Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited were transferred to PCAL, with the legal ownership transferring on 19 December 2018. The Hong Kong companies offer both participating and non-participating term, whole life endowment and unit-linked policies. These were previously included as participations in the Company's Solvency II balance sheet.

Based on values at 1 January 2018 the transfer resulted in a decrease of £6.9 billion in the value of own funds. The Solvency Capital Requirement ('SCR') decreased by £2.7 billion. These changes resulted overall in a decrease in surplus of £4.2 billion. Refer to section E.1.3 for a reconciliation of this £6.9 billion decrease in own funds to the £7,761 million own funds impact at the transfer date.

A.1.4.3 Partial sale of annuity portfolio

In March 2018, the Company announced the partial sale of the Company’s shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, the Company reinsured £12 billion of liabilities (valued as at 31 December 2017) to Rothesay Life. This resulted in a £1.1 billion decrease in SCR and £0.2 billion decrease in own funds. This is expected to be followed by a Part VII transfer of most of the portfolio by 30 June 2019 which will have a further SCR benefit. The UK GAAP loss arising from the transaction was £508 million.

The UK GAAP liabilities relating to the Company’s total UK shareholder annuity portfolio as at 31 December 2018 were £33 billion, of which £11 billion is reinsured by Rothesay Life.

A.1.4.4 Other events with material impact

A number of management actions were taken in 2018 to improve the Solvency II position of the UK insurance operations and further mitigate market risk, which have generated a combined surplus of £237 million (2017: £401 million). This consists of optimisation actions resulting in asset trading profits for 2018. The 2017 amount also included a benefit in respect of a longevity reinsurance transactions which was not repeated in 2018.

Changes to longevity assumption basis in 2018 result in a £378 million benefit (2017: £212 million) arising from changes to annuitant mortality assumptions to reflect current mortality, as well as the adoption of the Continuous Mortality Investigation ('CMI') 2016 model and some refinements to the Company's expectations for mortality for its portfolio. For 2017, the £212 million benefit arose from the adoption of the CMI 2015 model.

A.1.4.5 Thematic Review of Annuities Sales Practices ('TRASP')

The Company holds a provision at 31 December 2018 for review of past annuity sales after utilisation during the year of £324 million (31 December 2017: £369 million). The Company has agreed with the Financial Conduct Authority (FCA) to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. The review is examining whether customers were given sufficient information about their potential eligibility to purchase an enhanced annuity, either from Prudential or another pension provider. A gross provision of £400 million, before costs incurred, was established at 31 December 2017 to cover the costs of undertaking the review and any related redress and following a reassessment, no change has been made to the amount provided, although £45 million has been utilised in 2018.

The expectation is that the majority of the provision will be utilised in 2019. The ultimate amount that will be expended by the Company on the review will remain uncertain until the project is completed.

If the population subject to redress increased or decreased by 10 per cent, then the provision would be expected to increase or decrease by circa 7 per cent accordingly.

Additionally, in 2018, the Company agreed with its professional indemnity insurers that they will meet £166 million of claims costs, which will be paid as the Company incurs costs/redress. This income has been recognised as other operating income in the UK GAAP income statement and on the balance sheet within ‘Other debtors’ at 31 December 2018. For Solvency II this is included in receivables (trade,not insurance) in the S.02.01 balance sheet template.

A.2 Underwriting performance

Operating profit is management's primary measure of profitability and provides an underlying operating result based on longer-term investment returns, which gives a more relevant measure of the performance of the business. Other items are excluded from operating profit to allow more relevant period on period comparisons of the trading operations of the Company, e.g. the effects of material corporate transactions such as the partial sale of the annuity portfolio and the transfer of the Hong Kong subsidiaries.

The Company uses UK GAAP to prepare its solo entity statutory financial statements, and IFRS to report the results of the Company to Prudential plc for inclusion in the Group results. The accounting policies between UK GAAP and IFRS are aligned where possible and as such there are no material differences in operating profit between these two bases. The performance results set out in Section A are on a UK GAAP basis, consistent with the Company's solo entity statutory financial statements.

Operating profit broadly equates to premiums less claims (including change in technical provision) and expenses together with assumed longer-term investment returns. Given the linkage between the movement of technical provisions and the movement in investments backing those liabilities (e.g. for unit-linked funds, investment return (where positive or negative) results in a corresponding change in unit-linked technical provisions), the Company has defined operating profit as its underwriting performance as discussed in this section. Similarly, the core discussion of the investment performance of the Company in Section A.3 is by reference to short-term fluctuations in investment returns.

An analysis of premiums, claims, expenses and investment return is given in Section A.5.2 below.

A.2.1 Operating profit overview

Figure 2: Shareholder profit for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	2018 £m	2017 £m	Change %
Operating profit based on longer-term investment returns	**1,089**	**797**	**37**
Short-term fluctuations in investment returns	6	40	(85)
Revaluation of Hong Kong Subsidiaries	599	1,586	(62)
Revaluation of shareholder subsidiaries	(17)	81	(121)
Dividends from subsidiaries	183	88	108
Partial sale of annuity portfolio	(508)	—	—
Profit before tax attributable to shareholders	**1,352**	**2,592**	**(48)**

The Company's total operating profit of £1,089 million in 2018 was 37 per cent (£292 million) higher than the 2017 operating profit of £797 million.

The with-profits shareholder transfer of £320 million (2017: £288 million) is £32 million higher than 2017 due to growth of the with-profits funds under management.

Operating profit for shareholder-backed business includes an increase of £391 million in relation to TRASP, from a charge of £225 million in 2017 to income of £166 million in relation to insurance recoveries which has been recognised for 2018.

In 2018 changes in longevity assumption basis of £441 million (2017: £204 million) reflected changes to annuitant mortality assumptions to reflect current mortality, as well as the adoption of the Continuous Mortality Investigation ('CMI') 2016 model and some refinements to the Company's expectations for mortality for its portfolio. The £204 million benefit for 2017 arose from the adoption of the CMI 2015 model.

Operating profit for 2017 included £31 million in respect of longevity reinsurance transactions which were not repeated in 2018. Other management actions in 2017 included the impact of repositioning the fixed income portfolio to improve the trade off between yield and credit risk. Following significant trading in 2017, there was reduced opportunity for this activity in 2018.

Further detail on non-operating profit items include short-term fluctuations as set out in Section A. 3.1, details on investments in subsidiaries (including the revaluation of the Hong Kong subsidiaries prior to transfer), dividends in Section A.4.1 and partial sale of the annuity portfolio in A.4.2. Investments in subsidiaries are carried at fair value through profit and loss.

A.2.2 UK GAAP operating profit analysed by Solvency II lines of business

UK GAAP operating profit, as discussed above, is allocated by material Solvency II lines of business as follows:

Figure 3: Operating profit before tax for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	2018 £m	2017 £m	Change %
Insurance with-profits participation[1]	320	288	11
Other (comprising index-linked and unit-linked insurance, other life insurance and life reinsurance)[2]	769	509	51
Operating profit before tax	1,089	797	37

[1] Insurance with-profits participation comprises the shareholders' transfer from the with-profits funds of the Company.
[2] Other comprises mainly profits relating to the shareholder annuity business.

A.3 Investment performance

A.3.1 Short-term fluctuations

As explained in Section A.2 Underwriting Performance, the Company describes its UK GAAP performance by reference to operating profit and non-operating profit.

UK GAAP operating profit is based on longer-term investment return assumptions. The difference between actual investment returns recorded in the income statement and assumed longer-term returns is reported within short-term fluctuations in investment returns.

Included in non-operating results are gains of £6 million as a result of short-term fluctuations (2017: gain of £40 million). During 2013 the Company entered into a partial equity hedge of the shareholder transfers expected to emerge from the Company's with-profits sub-fund, which has been extended in 2017 and 2018. The non-operating profit includes gains on the partial hedge of the shareholder transfers in respect of future years of £216 million (2017: loss of £124 million).

Also there is favourable credit experience of £49 million (2017: £87 million) partially offset by capital losses on surplus assets of £233 million (2017: gain of £124 million), unrealised losses of £15 million (2017: £46 million unrealised gain) on certain equity release mortgages, losses on surplus assets from credit events of £10 million (2017: £60 million) and losses on swaption contracts of £1 million (2017: £33 million).

A.3.2 Investment management expenses

The total investment management expenses incurred by the Company's insurance operations, including those that were paid to the Company's asset management operations totalled £330 million (2017: £389 million).

An analysis of investment return in the income statement by asset class is given in Section A.5.2.4.

A.3.3 Investments in securitisations

Certain of the securities classified as asset-backed securities meet the definition of securitisation under Solvency II for the purpose of the Solvency II capital requirements calculation. Investments in securitisations are subject to specific spread stresses in the calculation in order to ensure that risks arising from securitisation positions are reflected appropriately.

Of the £5,739 million of asset-backed securities at 31 December 2018 (2017: £5,541 million), £5,396 million (2017: £4,518 million) meet the definition of investments in securitisations.

A.4 Performance of other activities

A.4.1 Investments in subsidiaries and dividends

The contribution to non-operating profit by the Company's subsidiaries as shown in the shareholder profit table in Section A.2.1, includes the revaluation of the Hong Kong subsidiaries prior to transfer (as described in section A.1.4.2) which resulted in a revaluation gain of £599 million. This represents the estimated fair value of the business at the date of sale of £9,450 million less the opening amount at 1 January 2018 of £8,851 million. In 2017 the Hong Kong subsidiaries contributed a revaluation gain of £1,586m.

In 2018 there was also a further revaluation loss of £17 million on other shareholder subsidiaries.

Dividends totalling £183 million (2017: £88 million) were received from shareholder subsidiaries during the year. All amounts for 2018 were in respect of the Hong Kong subsidiaries prior to their sale.

A.4.2 Leasing

The Company's operating and finance lease arrangements relate principally to properties.

The Company holds investment properties which are leased out to earn a return. Further information on the Company's leasing arrangements is provided below.

The Company does not hold any individually material leasing arrangements.

Office accommodation for the majority of employees in the UK is leased by another group company, Prudential Distribution Limited.

A.4.2.1 Operating leases

The Company as a lessor

Investment properties principally relate to the Company's with-profits funds and are carried at fair value. The Company's policy is to let investment properties to tenants through operating leases.

The 2018 income statement includes rental income from investment properties of £466 million (2017: £496 million) and direct operating expenses including repairs and maintenance arising from these properties of £50 million (2017: £74 million).

The Company as a lessee

The Company leases two properties under non-cancellable operating lease arrangements to provide office space for employees. One lease commenced in September 2002 and expires in September

2022; the other lease commenced in December 2013 and expires in December 2025. The total operating lease expense in 2018 was £4 mllion.

A.4.2.2 Finance leases

The Company as a lessor
As at 31 December 2018, investment properties of £33 million (2017: £33 million) are held under finance lease assets.

The 2018 income statement includes rental income from investment properties of £2 million (2017: £2 million).

The Company as a lessee
The Company's portfolio of investment properties comprise both freehold and leasehold properties. As at 31 December 2018, investment properties of £3,959 million (2017: £4,258 million) are held under finance leases. These finance leases are arrangements which grant very long leases with a large payment made upfront with minimal ground rent payable on an annual basis.

The 2018 income statement includes £8 million in respect of finance lease charges (2017: £7 million).

A.5 Any other information

A.5.1 Additional analysis of profits before tax by nature of revenue and charges

Total profit before tax attributable to shareholders for the year-ended 2018 was £1,352 million (2017: £2,592 million), representing operating profit of £1,089 million (2017: £797 million), as set out in Figure 2 and discussed in Section A.2.1, and non-operating profit of £263 million (2017: loss of £1,795 million). Analysis of profit before tax is shown in Figure 4 below by nature of revenue and charges, on a UK GAAP basis.

Figure 4: Total revenue and charges for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	2018 £m	2017 £m
Gross premiums written	13,002	13,077
Outward reinsurance premiums	(13,117)	(1,030)
Earned premiums, net of reinsurance	**(115)**	**12,047**
Other income	**19**	**17**
Investment income	20,684	11,043
Unrealised (losses) gains on investments	(22,958)	2,961
Investment return	**(2,274)**	**14,004**
Total revenue, net of reinsurance	**(2,370)**	**26,068**
Claims paid – gross amount	(12,163)	(12,019)
Claims paid – reinsurers' share	1,435	1,085
Change in provision for claims - gross amount	(34)	(29)
Change in long-term business provision - gross amount	2,417	(9,283)
Change in long-term business provision - reinsurers' share	9,074	318
Change in technical provision for linked liabilities	3,721	(54)
Claims incurred and changes in other long-term business and technical provisions – Net of reinsurance	**4,450**	**(19,982)**
Net operating expenses	(949)	(1,011)
Investment expenses and charges	(343)	(408)
Other charges	(20)	(14)
Tax attributable to the long-term business	371	(686)
Actuarial and other gains on pension schemes	46	94
Transfer to the fund of future appropriations	93	(1,649)
Profit before tax (being tax attributable to shareholders' and policyholders' returns)	**1,278**	**2,412**
Tax credit attributable to the balance on the long-term business technical account	74	180
Profit on ordinary activities before tax	**1,352**	**2,592**

A.5.2 Premiums, claims and expenses

A.5.2.1 Comparison of earned premiums with the prior period

Figure 5: Premiums by Solvency II line of business for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	Health insurance £m	Insurance with profit participation £m	Index-linked and unit-linked insurance £m	Other life insurance £m	Accepted life insurance £m	Total 2018 £m	Total 2017 £m
Premiums earned - gross	18	11,452	580	443	885	13,378	13,439
Outward reinsurance premiums	(2)	(1)	(355)	(13,102)	—	(13,460)	(1,386)
Earned premiums, net of reinsurance	16	11,451	225	(12,659)	885	(82)	12,053

Gross premiums for the Company decreased from £13,439 million in 2017 to £13,378 million in 2018, driven by reductions in conventional annuities, with profit corporate pensions and individual pensions, offset by increases in the retirement accounts and PruFund ISAs.

The gross earned premiums of £13,002 million for 2018 in Figure 4 above on UK GAAP basis excludes £376 million of premiums for investment contracts without discretionary participation features (as defined by FRS 103 insurance contracts) reflecting the deposit nature of these contracts. The premiums for these investment contracts without discretionary participation features are included in premiums written and earned under Solvency II. The gross premiums amount of £13,378 million, including these investment contracts, as analysed in Figure 5.

The increase in outward reinsurance premiums from £1,386 million in 2017 to £13,460 million includes £12,149 million relating to the reinsurance of part of the annuity portfolio to Rothesay Life.

Premiums classified above as 'Insurance with-profits participation' principally relate to PruFund business. On-going demand for the Company's PruFund multi-asset funds remains strong as customers continue to be attracted by its performance track record, the benefits of a smoothed return in managing market volatility and its ability to reduce customer investment risk in the current market conditions. In total across all products, PruFund APE sales of £1,221 million increased by 3 per cent from 2017, with total AUM having increased 19 per cent since the start of the year to £43 billion. The largest contribution to PruFund APE Sales come from Retirement Account products, followed by Bonds and ISAs. Annual premium equivalent sales ('APE') comprise regular premium sales plus one-tenth of single premium insurance sales.

A.5.2.2 Comparison of benefits and claims with the prior period

Figure 6: Benefits and claims by Solvency II line of business for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	Health insurance £m	Insurance with profit participation £m	Index-linked and unit-linked insurance £m	Other life insurance £m	Accepted life insurance £m	Total 2018 £m	Total 2017 £m
Claims incurred and changes in other long-term business and technical provisions, gross of reinsurance	(13)	(4,795)	(772)	(1,459)	(888)	(7,927)	(21,946)
Reinsurers share of claims incurred and changes in other long-term business and technical provisions	5	(11)	77	12,238	1	12,310	1,933
Claims incurred and changes in other long-term business and technical provisions, net of reinsurance	(8)	(4,806)	(695)	10,779	(887)	4,383	(20,013)

Claims incurred and changes in other long-term business and technical provisions (net of reinsurance) totalling £4,450 million in 2018 (as noted in Figure 4 above on a UK GAAP basis) includes £20 million (2017: £19 million) of claims handling expenses, £34 million (2017: £7 million) deposit accounting and an adjustment for other charges of £13 million (2017: £43 million). These amounts are not included in the benefits and claims net of reinsurance (£4,383 million) analysed above in figure 6 on a Solvency II basis.

Claims incurred and changes in other long-term business and technical provisions (gross of reinsurance) have decreased by 64 per cent from £21,946 million in 2017 to £7,927 million in 2018. The £14,019 million decrease in claims incurred and changes in other long term business provisions gross of reinsurance consists of a reduction of £11,027 million for insurance with profit participation mainly due to negative investment returns in 2018 in contrast to positive investment returns in 2017. The total of other life insurance and accepted life insurance of £2,347 million has reduced by £1,325 million since 2017 due to market movements, as well as decreases due to assumption changes. The remaining £1,667 million movement is mainly related to index-linked and unit-linked insurance and is caused by negative investment returns.

The difference between the net and gross of reinsurance claims incurred totals in 2018 includes £11,219 million within other life insurance due to the reinsurance of part of the annuity portfolio to Rothesay Life.

A.5.2.3 Acquisition costs and other expenditure

Net operating expenses consist of acquisition costs £183 million (2017: £218 million) and administration expenditure £766 million (2017: £793 million). Investment expenses and charges are comprised of investment management expenses £330 million (2017: £389 million), plus interest on bank borrowings of £13 million (2017: £19 million).

Acquisition expenses have decreased mainly due to lower project costs in 2018.

Administration expenditure has decreased by £27 million from £793 million in 2017 to £766 million in 2018. Although there were no TRASP expenses in 2018 (2017: £225 million), there were several increases in other expense categories including restructuring costs attributable to both shareholders and policyholders of £140 million (caused by higher transformation costs), pension costs £26 million and a number of other smaller items.

The decrease in investment management expenses was caused by lower investment fees in line with the decrease in the value of the investments. There was also lower interest on bank borrowings reflecting partial repayments of Vitality contingent loans.

A.5.2.4 Investment return by asset class

Figure 7: Investment return for the year-ended 31 December 2018 (with 31 December 2017 comparison)

	2018 £m	2017 £m
Income		
Investment properties	466	496
Loans	144	145
Equity securities and portfolio holdings in unit trusts	1,756	1,665
Debt securities	2,473	2,851
Other investments (including deposits)	709	697
Total income	**5,548**	**5,854**
Investment (depreciation) appreciation and other investment return		
Investment properties	50	516
Loans	4	(5)
Equity securities and portfolio holdings in unit trusts	(5,593)	5,393
Debt securities	(2,090)	(66)
Other investments (including deposits)	(193)	2,312
Total investment (depreciation) appreciation and other investment return	**(7,822)**	**8,150**
Total investment return	**(2,274)**	**14,004**

Investment return principally comprises interest income, dividends, and investment appreciation/depreciation (realised and unrealised gains and losses) on investments designated as fair value through profit and loss. It also includes impairment losses relating to assets held at amortised cost.

Total income has decreased by £306 million from £5,854 million in 2017 to £5,548 million in 2018. Debt securities contributed a decrease of £378 million mainly as a result of reduced holdings following the reinsurance of annuity liabilities to Rothesay life.

Investment income from equity securities and portfolio holdings in unit trusts has decreased from a gain of £5,393 million to a loss of £5,593 million due to negative investment return in 2018 and positive investment return in 2017. Debt securities have also decreased due to negative investment return in 2018.

Other investments are carried at fair value through profit and loss and consist mainly of revaluation in subsidiaries and derivative movements.The reduction of £2,505 million compared to 2017 is a result of a £1,116 million decrease in the revaluation of subsidiaries, of which £1,036 million relates to Hong Kong subsidiaries. There was also a £2,082 million decrease in the value of derivatives which had losses in 2018 and gains in 2017 and a £145 million decrease in mortgage loans. These were offset by an increase of £217 million in exchange gains and a £621 million higher return on other investments including limited partnerships.

A.5.3 Post balance sheet events

A.5.3.1 Part VII transfer of EU business to PIA

M&GPrudential has been reviewing its operations across Europe since the UK voted to leave the European Union. In January 2019 there was a Part VII transfer of all of the Company’s long term European business (excluding the UK) into its subsidiary Prudential International Assurance plc ('PIA'), which is based in the EU.

The with-profits element of the business will be reinsured back into the Company ensuring continuation of the economic substance of the current situation. The shareholder business will remain in PIA following the Part VII transfer.

B System of governance

(Unaudited)

B.1 General information on the system of governance

B.1.1 Board governance

As noted in Section A.1.1, the Company is a wholly owned subsidiary of M&G Prudential Limited which is a subsidiary of Prudential plc, the parent company of the Prudential group ('the Group').

The Group consists of a number of material Business Units ('BUs'). These BUs include M&GPrudential which incorporates Prudential UK. Prudential UK provides the management structure for the Company, along with its subsidiaries and associated entities. In March 2018, Prudential plc announced the intention to demerge the combined M&GPrudential business from Prudential plc.

During the year, the Prudential UK Chief Executive Officer ('Prudential UK CEO') reported to the Board of Directors of the Company ('the Board') and to the Chief Executive Officer, M&GPrudential ('CEO M&GPrudential'), who in turn reported to the Prudential Group Chief Executive.

The M&GPrudential Chief Financial Officer (Prudential UK CEO until 18 January 2019) held the Senior Management Function 1 ('SMF1'), Chief Executive role for the Company and had delegated responsibility for the operational management of the Company. The Prudential UK business is managed through the executive operating structure including an Executive Committee ('EXCOM') and other committees to implement the three lines of defence model in operation across the Company and the wider Prudential Group.

The Company's Board has an independent non-executive Chairman. In addition, two other independent non-executive Board directors hold roles of Chair of the Board Risk and Capital Committee ('BRCC') and Board Audit Committee ('BAC'). At least half of the Board's directors (including the Chairman) are independent Non-Executive Directors ('NEDs'). The NEDs are responsible for both supporting and overseeing executive management whilst, as members of a unitary Board, sharing in the wider duty to promote the success of the Company and to ensure the Company continues to meet its Threshold Conditions (minimum conditions requiring to be met to undertake its regulated activities). Whilst forming part of the Prudential Group, the appointment of independent NEDs on the Board recognises the need for the Company to maintain local entity integrity distinct from the Group.

The membership of the Board as at 31 December 2018 is detailed in Figure 8 below.

Figure 8: Membership of the PAC Board as at 31 December 2018

PAC Board Members	Role
Paul Spencer	Chairman and Independent Non-Executive Director (SMF 9)
Clive Adamson	Independent Non-Executive Director and Chairman of the BRCC (SMF 10)
Richard Bennison	Independent Non-Executive Director and Chairman of the BAC (SMF 11)
Clare Bousfield	Director, CEO Prudential UK (SMF 1) and CFO M&GPrudential
Michael Evans	Independent Non-Executive Director (SMF 7) and Chairman of M&GPrudential
Ian Owen	Independent Non-Executive Director (Notified NED)
Joanne Dawson	Independent Non-Executive Director (SMF12)
John Foley	Director and CEO M&GPrudential (SMF 7)
Mark FitzPatrick	Director and Group CFO (SMF 7)

This is correct as at 31 December 2018. However, John Foley was approved as SMF1 for PAC with effect from 18 January 2019.

The Board is authorised to exercise all the powers of the Company within any applicable legislation and the provisions of the Articles of Association subject to the limits imposed, approvals required and policy set by Prudential plc, including the Prudential Group Governance Manual ('GGM').

The terms of reference for the Board are reviewed on an annual basis and an annual effectiveness review of the Board is also undertaken.

Material changes to the system of governance

At the date of this report there have been no material changes to the Company's system of governance which is considered appropriate for the nature, scale and complexity of the risks inherent in the Company's current business. This will continue to be considered as merger, transformation and demerger activity progresses.

B.1.2 Board committees and decision making

The Board has established a number of committees comprising independent NEDs to provide oversight, challenge and to assist the Board in discharging its responsibilities effectively. The responsibilities of the principal committees are a key component of the governance framework, and are listed below.

The Board is responsible for:

1. Strategy, Budgets and Business Plans
   - approving the Company's strategy, long-term objectives, annual budgets and business plan prior to their submission to Prudential plc;
   - monitoring the implementation of the Company's strategy and long-term objectives, annual budgets and business plan as approved by the Prudential plc Board, and overseeing any corrective action taken by the Company.

2. Structure and Capital
   - approving, subject to the GGM, the following matters;
     - material changes to the Company's corporate structure, including decisions to cease operations in parts of the Company or to extend activities into new business or geographic areas;
     - material changes to the Company's capital structure, including reduction of capital, share issues and the re-organisation or restructuring of capital;
     - the raising of, or committing to, external finance and financing programmes;
     - material transactions and certain other matters.

3. Financial Reporting and Dividends
   - approving the Company's Annual Report and Accounts;
   - approving the payment of dividends;
   - monitoring whether the Company adopts the Group's accounting policies;
   - endorsing the proposed appointment, reappointment or removal of the Group's external auditor;
   - regularly reviewing the overall financial condition of the Company and its subsidiaries, any relevant credit ratings and regulatory capital requirements.

4. Internal Control and Risk Management
   - overseeing that an effective system of internal control and risk management is in place, maintained and reviewed annually;
   - monitoring whether the overall risk appetite and tolerance of the Prudential UK business adheres to the Group Risk Framework ('GRF'), policies and limits;
   - approving the Company's risk appetite and risk framework and policies within the limits;
   - overseeing and approving where applicable, material disclosures to, and regular reporting required by, regulators.

5. Board and other appointments
   - taking the following actions, each in accordance with the Group Material Subsidiaries Corporate Governance Manual;
     - implementing changes to the structure, size and composition of the Board and membership, including the chairmanship of its committees and;
     - approving the appointment and removal of Directors;
   - overseeing, in conjunction with the Prudential UK CEO, that there is a succession planning process in place for executive directors and senior management;

- overseeing that there is an effective process for the ongoing refreshment of non-executive directors.

6. Governance
   - overseeing that the Company adheres to the Group's governance policies;
   - overseeing that an evaluation of the Board's own performance, that of its committees and of all directors is undertaken in accordance with the Material Subsidiaries Corporate Governance Manual and that an appropriate plan of action is adopted to address matters identified in the evaluation;
   - authorising any actual or potential conflict of interest situation applying to any director;
   - authorising the Company Secretary to arrange for all directors to obtain, at the Company's expense, appropriate external professional advice where necessary.

7. Delegation of Authorities
   - delegating authority to a number of standing and ad hoc committees of the Board and regularly reviewing the terms of reference for, and reports from, the committees, in adherence with the Material Subsidiaries Corporate Governance Manual;
   - The Prudential UK CEO has responsibility for the operational management of the Company and its subsidiaries and may sub-delegate authority as they determine.

8. With-Profits
   - overseeing that the interests of the with-profits policyholders are appropriately considered in relation to matters affecting with-profits policyholders as a whole or as separately identifiable groups of policyholders;
   - receiving advice from the With-Profits Committee to ensure compliance with the Company's Principles and Practices of Financial Management ('PPFM').

9. Investment Strategy
   - inputting into the development of, and approving, the Company's investment strategy in the context of Company's business strategy; and
   - monitoring the implementation of the Company's investment strategy, and overseeing any corrective action taken by the Company.

Board Committees

The BAC, BRCC, With-Profits Committee, Independent Governance Committee and the Scottish Amicable Board are the principal standing committees of the Board.

The role of each Committee together with details of the current Chairman is summarised in Figure 9 below.

Figure 9: Summary of the role of each Board Committee and Chairman as at 31 December 2018

Board Committees	Role
PAC Board Audit Committee	**Chair : Richard Bennison** The BAC is accountable to the Board and assists the Board in meeting its responsibility for the integrity of the Company's financial statements, for the effectiveness of the Company's internal control and risk management systems and for monitoring the effectiveness and objectivity of the internal and external auditors.
PAC Board Risk and Capital Committee	**Chair : Clive Adamson** The BRCC is accountable to the Board and assists the Board in meeting its responsibility for overseeing the effectiveness of risk and capital management frameworks for all financial and non-financial risks faced by the Company. The Committee also oversees compliance with the GRF, related Group Risk Policies and Group Approved Limits.
With-Profits Committee	**Chair: Ronnie Bowie** The With-Profits Committee is an independent committee which acts in an advisory capacity to inform the decision-making of the Company to ensure that the interests of its with-profits policyholders are appropriately considered and to consider issues affecting with-profits policyholders as a whole or as separately identifiable groups of policyholders.
Independent Governance Committee	**Chair: Lawrence Churchill** The role of the Independent Governance Committee is to act solely in the interest of the pension scheme members, to assess, raise concerns and report on the value for money of the Company's contract-based defined contribution workplace pension schemes and to focus on the quality of their schemes and ongoing review of regulatory and legislative requirements.
Scottish Amicable Board	**Chair: Bernard Solomons** The role of the Scottish Amicable Board is to observe and perform the terms of the Scottish Amicable Scheme of Transfer. It has regard solely to the interests and reasonable expectations of the holders of policies allocated to the Scottish Amicable Insurance Fund.

During the year, and up to the date of transfer, oversight of the Company's Hong Kong subsidiaries was through the Hong Kong Oversight Committee. Oversight was achieved principally through enhancing the seniority and functional mix of attendees at this Committee as well as expanding the financial, risk and operational reporting to it. A report was made after each meeting to the next BRCC, ensuring Non Executive scrutiny of the business. The Prudential UK CEO was a director of PHKL until 14 December 2018. The Hong Kong Oversight Committee was disbanded following the transfer of the Company's Hong Kong subsidiaries on 14 December 2018 to PCAL.

The key functional control areas of Risk, Internal Audit, Compliance and Actuarial report to Board Committees in accordance with each Committee's terms of reference. It is the responsibility of the BAC to review the resources of Internal Audit and Compliance through its review of annual plans and progress of their delivery during the year.

Further information of the key functions, e.g. Risk, Compliance, Group-wide Internal Audit ('GwIA') and Actuarial is given in Sections B.3.2, B.4.2, B.5 and B.6, respectively.

B.1.3 Remuneration Committee and policy

The Group Remuneration Committee is responsible for overseeing that BUs across the Group (including Prudential UK) comply with the Group Remuneration Policy and with applicable regulations.

The Solvency II requirement for the Company to have an independent remuneration committee is met by the M&GPrudential Remuneration Committee which reports into the Group Remuneration Committee. Whilst an executive committee, further independence of the M&GPrudential Remuneration Committee is achieved through having membership comprised of non-M&GPrudential personnel and an independent NED from the Company's Board. The M&GPrudential Remuneration

Committee covers the Company and other constituents of Prudential UK and M&G with a remit to implement the remuneration policy and structures established by the Group Remuneration Committee.

Prudential Group's Remuneration Policy and practices ensure that the BUs and the Group Head Office have an effective approach in place to reward employees in an appropriate way that:

- aligns incentives to business objectives in order to support the delivery of Group and BU business plans and strategies;
- enables the recruitment and retention of high calibre employees and incentivises them to achieve success for their BU and the Group; and
- is consistent with the organisation's risk framework and appetite.

Remuneration practices within the Company follow the Prudential Group Remuneration Policy and there is no separate remuneration policy at the BU level.

The principles of the Remuneration Policy, implemented within the Company are:

- pay for performance;
- tailored to the relevant market;
- interest in Prudential shares;
- BU and Group focus;
- shareholder value creation;
- fair and transparent system for all;
- designed to minimise regulatory and operational risk; and
- safeguards to avoid conflicts of interest.

Remuneration architecture

Both fixed and variable remuneration is assessed against market data and internal benchmarks on an annual basis and balanced so that the fixed component represents a sufficiently high proportion of the total remuneration. This avoids employees being overly dependent on the variable components and helps to mitigate unintended consequences and inappropriate behaviours to the detriment of customer outcome.

Variable remuneration available to employees includes short-term incentives (i.e. annual bonus, quarterly sales incentives for sales staff) and long-term incentive plan ('LTIP') awards.

Annual bonus measures include various combinations of BU financial and / or strategic targets, Group financial targets, functional targets and individual performance reflecting the level, nature and scope of the role and the practice in the market in which the Company operates. This allows the Group and BUs to operate a fully flexible bonus policy, including the possibility of not paying an annual bonus based on financial and non-financial criteria. All share awards are subject to malus during the vesting period.

Any awards made under the Group's LTIPs are based on Group and BU financial metrics and other non-financial metrics, such as the new Sustainability Scorecard which incorporates a conduct measure to be applied to all staff. The LTIP awards to senior executives are made under the Prudential LTIP and include a Group target to ensure their remuneration includes a link to the overall results of the Group.

Prudential does not operate any supplementary pension or early retirement schemes at Group or UK level. The defined benefit schemes are closed to new members.

Governance processes deliver robust oversight of reward, effective management of conflicts of interest and reflect the need to link remuneration decisions with risk appetite and business strategy.

The Chief Risk and Compliance Officer ('CRCO') for M&GPrudential is actively involved in ensuring that remuneration across Prudential UK reflects the extent to which decisions were made within the organisation's risk appetite. The CRCO reports to the M&GPrudential Remuneration Committee, in writing, at least once a year which:

- provides context on the risk environment during the period;
- assesses risk performance and the overall effectiveness of the control environment;

- identifies any significant risk issues that should be considered by the Remuneration Committee: and
- assesses the degree to which performance plans are appropriate in the context of risk appetite, including whether a risk modifier should be considered by the Committee.

B.1.4 Material transactions with directors and shareholders

Transactions with directors

In addition to remuneration for their role on the Board, executive officers and directors of the Company may from time to time purchase insurance, asset management or annuity products marketed by the Group's companies in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with other persons.

In accordance with the Companies Act 2006, directors are required to disclose any transactions that may represent a conflict of interest to their roles.

In 2018, other transactions with directors were not deemed to be sufficient both by virtue of their size and in the context of the directors' financial position to constitute a conflict of interest. All such 2018 transactions were on terms broadly equivalent to those that prevail in arm's length transactions with other persons.

Transactions with shareholders

In 2018 there were no loan repayments (2017: £30 million) from Prudential plc (the holding company until 26th November 2018) to the Company. M&G Prudential Limited became the holding company from 26th November 2018.

There were no other material transactions with shareholders outside the normal course of business.

B.2 Fit and proper requirements

The Company ensures that senior managers are fit and proper through the implementation of a Fit and Proper Policy, which has been updated to reflect the implementation of the Senior Managers and Certification Regime ('SMCR') in December 2018, having previously addressed the requirements of the Senior Insurance Managers Regime.

The Policy applies to:

- all persons approved by PRA and/or FCA as holding Senior Management Functions ('SMFs') including approved NEDs;
- all persons defined as Key Function Holders and notified to the regulator;
- all persons defined as Standard NEDs and notified to the regulator; and
- all persons defined as holding a Certification function.

Each BU and the Group Head Office undertakes an annual certification programme to demonstrate compliance with the GGM, which includes the Fit and Proper policy and the systems of control.

B.2.1 Fit and proper criteria

All individuals to whom the Fit and Proper Policy applies have been verified to fulfil the following requirements:

- honesty, integrity and reputation, i.e. that they will be open and honest in their dealings and able to comply with the requirements imposed on them;
- competence and capability, i.e. that they have the necessary skills to carry on the function they are to perform; and
- financial soundness.

B.2.2 Processes for assessments

The Company has processes in place for assessing the initial fitness and propriety of persons covered under the Fit and Proper Policy. These processes are described below;

- during the recruitment process and before any regulatory application is made, an assessment of the person's fitness is conducted including:
  - the person's professional and formal qualifications;
  - knowledge and relevant experience within the insurance sector, other financial sectors or other businesses;
  - where relevant, the insurance, financial, accounting, actuarial and management skills of the person;
- during the recruitment process and before any regulatory application is made, an assessment of the person's propriety is conducted including integrity, honesty, and financial soundness, based on evidence regarding their character, personal behaviour and business conduct, including any criminal, financial and supervisory checks; and
- in relation to outsourced key functions, an individual who is responsible for assessing the fitness and propriety of the service provider is identified.

Ongoing assessment fitness and propriety

The Company has processes for assessing the ongoing fitness and propriety of persons covered under the Fit and Proper Policy, in order that:

- sufficient evidence is gathered at least annually, to assess the ongoing Fitness and Propriety of individuals captured by the SMCR, including Key Function Holders and notified NEDs. This includes:
  - an assessment of whether the individuals are adhering to the relevant PRA/FCA Conduct Standards and Rules;
  - credit and criminality checks;
  - self-certification of regulatory Fitness & Propriety questions;
  - confirmation that role profile remains up to date and is an accurate reflection of current responsibilities.
- for individuals in scope, a specific Approved Persons / Key Function Holder and Performers objective is a requirement of the Performance Management process, against which individuals are appraised on an annual basis. This objective is tailored to the specific FCA and PRA conduct standards for the role being performed.

The activity above is supported by the following processes;

- the Compliance Function is notified where there is a change in the fit and proper status of any SMFs or Key Function Holders;
- the PRA and FCA are notified of any change to the fit and proper status of SMFs or Key Function Holders, including instances of where these individuals have been replaced because they are no longer fit and proper;
- the PRA and FCA are notified as soon as reasonably practicable when a breach has occurred in the Conduct Standards and Rules that has a material impact on the assessment of an individual's fitness and propriety; and
- the Compliance Function is notified as soon as reasonably practicable in the event of a breach of the Fit and Proper Policy requirements.

B.3 Risk management system including the Own Risk and Solvency Assessment

B.3.1 Risk governance, culture and our risk management cycle

Risk is defined as the uncertainty the Company faces in successfully implementing its strategies and objectives. This includes all internal and external events, acts or omissions that have the potential to threaten the success and survival of the Company. Material risks will be retained selectively where there is value to do so, and where it is consistent with the Company's risk appetite and philosophy towards risk-taking.

The following section provides more detail on the Company's risk governance, culture and risk management processes.

Risk governance

The Company's risk governance comprises the organisational structures, reporting relationships, delegations of authority, roles and responsibilities, and risk policies that have been established to influence and oversee decisions and control activities on risk-related matters. This encompasses individuals, key functions and committees involved in the management of risk.

(i) Risk committees and governance structure

The Company's risk governance structure is led by the BRCC, the members of which are independent NEDs. The BRCC assists the Board in providing leadership and oversight of the Company's overall risk appetite in addition to guidance on risk tolerance and strategy. The Committee oversees and advises the Board on the current and potential future risk exposures of the Company, reviewing and approving the Prudential UK Risk Management Framework ('RMF'), monitoring its effectiveness and adherence to the various risk policies. The BRCC also supports the Board and management in embedding and maintaining a supportive culture in relation to the management of risk.

In addition, there are various executive risk forums to ensure risk issues are considered and escalated appropriately. These are led by the Executive Risk Committee ('ERC') which is supported by a number of technical sub-committees that have members with the specialist skills required.

(ii) Risk management framework

The RMF describes the approach to risk management, and the key arrangements and standards for risk management and internal control that support compliance with GGM and regulatory requirements. It provides a disciplined and structured process for the taking and management of risk in compliance with the Prudential Group Code of Business Conduct and GRF, plus the statutory and regulatory requirements under Solvency II. This includes:

- outlining the governance structure and apportionment of accountabilities by which Prudential UK operates;
- providing a reference point when considering risks, by defining the risk management principles, strategy, policies and the risk management cycle;
- providing a common language and framework for managing all types of risk which is important for consistency and enables understanding of the overall risk exposure;
- promoting a responsible risk culture supported through the recruitment and training of the capabilities and behaviours needed to develop and control the business; and
- outlining the key processes for risk management and internal control that support compliance with statutory and regulatory requirements; including UK Corporate Governance Code compliance, GGM, Solvency II, and the relevant rules of the PRA Rulebook and principles of the FCA Handbook.

(iii) Risk appetite, limits and triggers

The Company's risk appetite and tolerance to take on risk is specified through risk appetite statements and limits that are aligned to the business model and subject to regular review. Risk appetite defines the amount of each type of risk an organisation is willing to accept in pursuit of its business objectives.

The Board maintains risk appetite statements and limits that inform decision making, reflect the business model and are compatible with Group-wide risk limits which are defined within the GRF and which apply in aggregate for earnings volatility, liquidity and capital requirements. The

GRF sets out three types of measure (limits, triggers and indicators) that are used in applying the Group's stated appetite towards individual risk types.

The Company uses the Group Risk Appetite Statements as a basis for developing its own risk appetite statements, triggers and limits for each of the group risk categories. The appetite statements for the Company are approved annually by the ERC, BRCC and PAC Board. Regular monitoring of such triggers and indicators facilitates the early identification, escalation and management of potential breaches.

The framework of risk appetite statements, limits and triggers are designed to adequately manage risk within agreed limits and tolerances, rather than eliminate it, although there may exist some risks for which Prudential has no tolerance and which are actively avoided - e.g. Compliance risk and losses from ineffective anti-money laundering and counter-terrorist financing processes and controls.

(iv) Risk policies

Risk policies set out the principles by which the Company conducts its business in the area covered by the policy, usually by the setting of specific requirements. Policy requirements are typically brief and principles based and seek to address fundamental concepts rather than operational procedures. This allows business users to determine how best to comply with requirements based on their expertise.

There are core risk policies for each of the key risk categories, with supporting policies to help define the internal control framework.

(v) Risk standards

The Company adopts and complies with Group-wide Operating Standards which provide supporting detail to the higher level risk policies and provide more detail on minimum standards for certain key practices and procedures. In many cases they define minimum requirements for compliance with Solvency II regulations which in some areas are highly prescriptive.

Risk culture

Culture is a strategic priority of the Board who recognise the importance of good culture in the way that the Company does business. Risk culture is a perspective of broader organisational culture, which shapes the organisation-wide values that are used to prioritise risk management behaviours and practices.

The RMF sets out the standards for an effective risk culture within the Company, including:

- articulation by the Board and Senior Management, which is visibly supported by the decisions they take, on the need for good risk management as a way to realise long-term value; and
- promoting employee understanding of their role in managing risk including their awareness and open discussion of risk as part of the way they perform their role.

Key aspects of risk culture are reflected in the values and behaviours displayed within the Company, and captured by the Prudential Code of Business Conduct. The Company's performance management and reward structure balances risk with profitability and growth, in the performance evaluation of key individuals, including both senior management and those directly responsible for risk management. In addition, every member of staff has a risk management objective to be achieved each year.

The risk management cycle

The Prudential UK risk management cycle consists of procedures to identify, measure and assess, manage and control, and monitor and report risks on a continuous basis.

(i) Risk identification and Risk Analysis / Measurement

Risk identification and measurement is derived through a number of processes, in particular the annual top-down and bottom-up risk identification processes, quarterly emerging risk process, and an annual exercise of stress and scenario testing in line with regulatory and Group requirements. Each of these is designed to identify and assess risk from a different perspective to form an overall understanding of the business' risk profile and how it has and is expected to evolve.

(ii) Risk Evaluation and Risk Treatment

Risks are evaluated against the defined risk appetite limits, triggers and indicators in order to establish whether the business is operating within risk appetite. Where risk appetite is exceeded, or in some cases the limit is close to being exceeded, management are expected to take action in the form of risk treatment.

Risk treatment is the process of selecting and implementing measures to manage the risk once evaluated. There are four options available:

- mitigate the risk by improving or adding to the internal controls in place;
- transfer the risk through risk transfer activities (e.g. insurance, reinsurance, hedging);
- avoid the risk through divestment or termination of activities which contravene company policy or the risk strategy (e.g. political risk); and
- formal acceptance of the risk, subject to appropriate governance.

(iii) Risk monitoring and oversight

Risk monitoring is an ongoing process to track the status of risks and is undertaken throughout the risk management cycle by both the risk owners and through oversight and assurance by the Risk, Compliance and Internal Audit Functions. Risk owners monitor risks against operating limits derived from the risk appetite statements and tolerance limits, monitoring the effectiveness of controls against policy standards and identifying, responding to and learning from incidents and loss events that occur.

(iv) Risk Communication and Reporting

To ensure timely and appropriate decision making, the Board, its committees and senior management are provided with accurate and timely risk reports and management information, including:

- regular management information, prepared by the Risk Function on behalf of the CRCO, which is presented to the ERC and BRCC to enable oversight of risks on an ongoing basis; and
- Own Risk and Solvency Assessment ('ORSA') reporting, further details of which are contained in Section B.3.4.

B.3.2 The risk function

Risk management system

The Company's risk governance arrangements, which support the Board, the BRCC and the BAC, are based on the principles of the 'Three Lines of Defence' model: risk taking and management, risk control and oversight, and independent assurance.

Within this model, the Risk Function is structurally independent of the first Line of Defence ('1st Line') and is responsible for risk oversight. While the 1st Line has responsibility for risk-taking, which is constrained within clear parameters, the Risk Function assists the Board to formulate and implement the approved Risk Appetite and Limit Framework, risk management plans, risk policies, risk reporting and risk identification processes. The Risk Function also monitors and assesses the risk taking activities of the 1st Line, challenging, where appropriate, the actions taken to manage and control risks and approving any significant changes to the controls.

The Risk Function’s responsibilities include, but are not limited to:

- coordinating the identification and assessment of key risks to establish the risk profile used as a basis for setting qualitative risk appetite statements and quantitative limits, the management information received by risk committees and the Board;
- the assessment of solvency needs, and stress and scenario testing;
- providing overall coordination and control of the effectiveness and efficiency of risk management processes and systems;
- supporting the Board and management in embedding and maintaining a supportive culture in relation to risk management;
- overseeing that development of the Internal Model is within the framework of model governance and remains fit for purpose;
- monitoring and reporting risks on an ongoing basis, including reporting on material exposures against risk appetite and the Company’s top risks;
- providing input and review of public and regulatory disclosures, such as the annual Solvency and Financial Condition Report;
- performing the ORSA, undertaking stress and scenario testing including Reverse Stress Testing, and informing the key areas of risk based decision making; and
- considering material findings from regulatory reviews and interactions with regulators which impact on risk governance or risk management processes.

In order to fulfil these responsibilities, the Risk Function liaises with other functions (e.g. Actuarial and Compliance), to provide technical expertise and advice throughout the risk management cycle.

B.3.3 Internal model

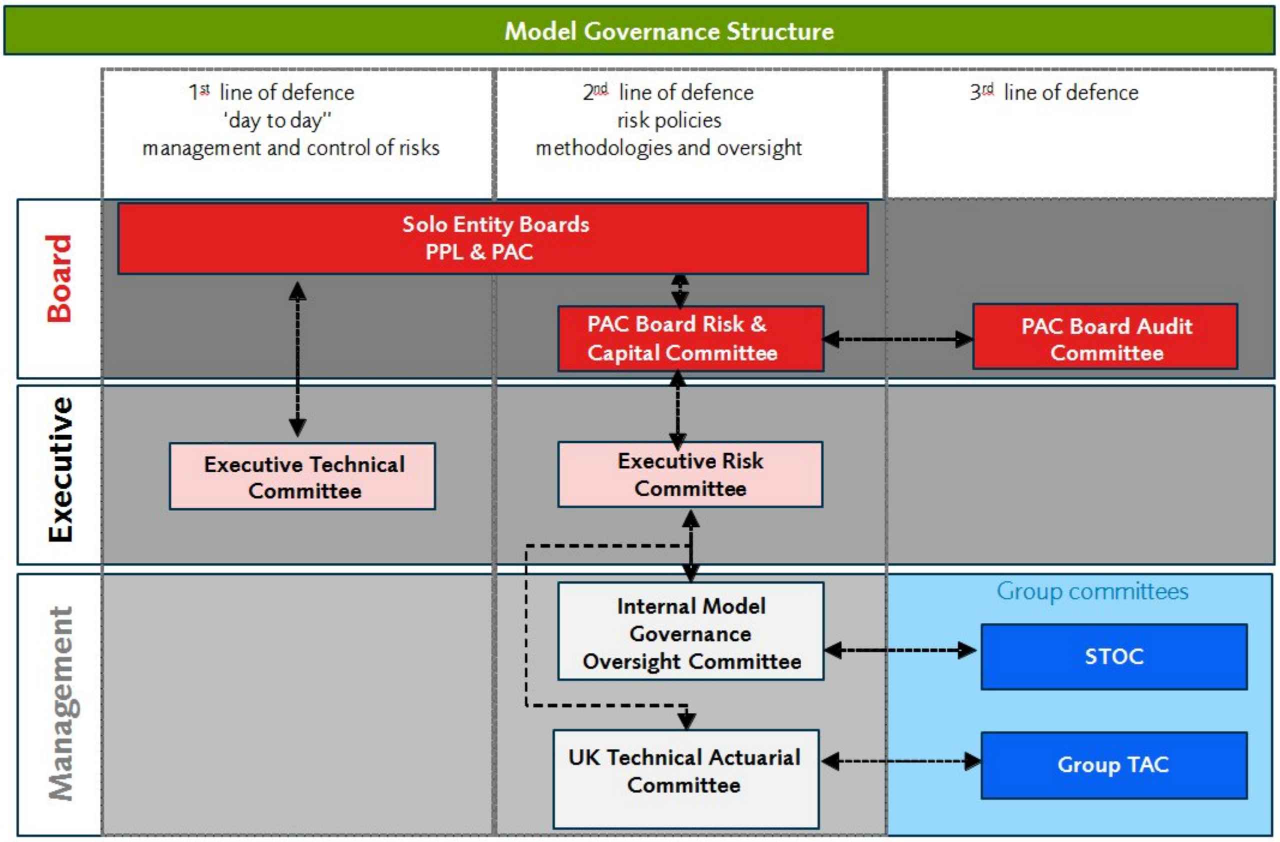
The Solvency II Internal Model is a key risk management tool and refers to the systems and processes used to identify, monitor and quantify risks for the purpose of calculating the Solvency II capital requirement (‘SCR’, ‘Pillar I’) and management's own assessment of economic capital (‘ECap’, ‘Pillar II’) requirements.

To ensure that the Internal Model is, and continues to be, suitable to support this assessment of risk and capital, the Company has implemented a governance and control framework in relation to:

- model use: to provide assurance that the model is widely used in the business, playing an important role in the system of governance and decision-making processes;
- model change: where changes to the Internal Model are required (e.g. adjustments, enhancements), these are implemented in a consistent and controlled manner with consideration of any potential implications;
- model limitations, assumptions and judgements: to note the circumstances under which the Internal Model does not work effectively, including where assumptions and judgements are made, making sure these are reasonable and understood by those who may rely upon any model output; and
- model validation: to confirm that the capital requirements resulting from the Internal Model remain appropriate through an annual schedule of rigorous and independent testing.

This model governance framework is implemented in accordance with the Prudential UK Internal Model Risk Policy which, in turn, is aligned with the Prudential Group Internal Model Risk Policy and relevant requirements of the Solvency II Directive. Further Policies and Operational Standards support the application of the Internal Model Risk Policy, with a committee structure in place to manage and oversee the framework as set out in Figure 10 below.

Figure 10: Committee Structure to oversee the Internal Model Governance



Prudential International Assurance ('PIA') conducts its own model governance with reports approved either by the PIA Risk & Compliance Management Committee, PIA Risk Committee or PIA Board as appropriate.

Validation process

The Internal Model Governance Oversight Committee ('IMGOC') and the UK Technical Actuarial Committee ('UK TAC') have responsibility for ensuring that the Internal Model is, and continues to be, suitable to support the assessment of risk and capital and that it complies with all regulatory requirements. The IMGOC is responsible for overseeing use of the Internal Model within the Company and its subsidiaries, including independent validation of the model. The UK TAC is responsible for reviewing and approving the methodology, and assumptions for the Internal Model, including any changes to the model. The IMGOC and UK TAC report to the UK ERC, which is chaired by the CRCO. The CRCO reports to the Board(s) as necessary on matters relating to the Internal Model.

As noted above, the model oversight and governance is supported by the implementation of the Prudential UK Internal Model Risk policy which forms part of the RMF. The policy defines:

- minimum standards for effective model risk management;
- processes for the Risk Function and relevant management bodies to monitor and manage model risk and ensure the Internal Model is fit for purpose ('model governance'); and
- flows of management information required to manage model risk and to meet the needs of external stakeholders and, in doing so, fulfil relevant legislation and supervisory requirements and rating agency requests.

The policy also gives rise to the following key requirements with respect to governance of the Internal Model:

- establish controls for the Internal Model;
- ensure appropriate documentation of the model, methodology, assumptions and inputs, which should include identification of the Internal Model's limitations and weaknesses;

- ensure the users of the model have an adequate understanding of the Internal Model;
- establish and maintain a system for making and managing changes to the Internal Model; and
- establish and maintain a system for validation for the Internal Model.

Compliance with the policy is attested to, and overseen by the ERC, on an annual basis.

Material changes to the Internal Model governance

There were no material changes to Internal Model governance in 2018.

B.3.4 Own Risk and Solvency Assessment

The Company defines the ORSA as the ongoing process of identifying, assessing, controlling, monitoring and reporting the risks to which the business is exposed, and of assessing the own funds necessary to ensure that the Company's solvency needs are met at all times. Risk appetite and limits are the key controls that apply on the current and future risk profile, as a result of the Company's strategy and business plan, and ensure that the company complies with its solvency requirements on a continuous basis under a reasonable range of scenarios. This process is documented and evidenced through an ORSA report. The ORSA is performed annually, or more frequently if there is a significant change in the Company's risk profile following any internal actions or a change in the external environment.

The ORSA report includes a current and forward looking assessment of both the capital and solvency position as well as the risk profile of the business. It combines the analysis performed by, and the outcomes of, the ongoing risk and capital management processes that are embedded and which have been reviewed by various Committees such as the ERC and BRCC. It also provides a quantitative and qualitative assessment of the Company's risk profile and solvency needs on a forward looking basis incorporating the Company's strategy and business plan.

The scope of the ORSA report covers all the known risks of the Company.

Figure 11 below sets out the key responsibilities of the ORSA stakeholders in the production of the ORSA report.

Figure 11: High level overview of ORSA responsibilities

Stakeholder	Roles
PAC Board	Steer and challenge throughout the ORSA process, approving the ORSA report.
PAC Board Risk and Capital Committee	Review of the ORSA and recommendation to the Board for approval.
Executive Risk Committee	Review and comment upon the ORSA prior to submission to BRCC and the Board.
Prudential UK Chief Risk Officer, who is also M&GPrudential Chief Risk and Compliance Officer	Ownership of the ORSA report.
M&GPrudential Risk & Compliance	Preparation of the ORSA report, collaborating with functional areas as needed.
M&GPrudential Finance	Preparation of quantitative inputs to ORSA report.

The RMF is designed to ensure adequate protection of policyholder and other stakeholder interests. The ORSA is recognised as a valuable component of this, providing the means to understand the links between strategy, risk and capital. The Company holds capital with the objective of ensuring that the aggregate risk of not being able to meet liabilities as they fall due is kept to an acceptably low level. Embedding of the ORSA within the business drives top-down understanding of risks to the company and ensures the centrality of the Internal Model in business decision making.

B.4 Internal control system

B.4.1 Overview

The internal control system consists of policies, processes, structures and other arrangements used across the three lines of defence to give effect to and provide assurance over the agreed approach to risk management. The internal control framework is a central part of the risk management system with a key role in the management of risks that are significant to the fulfilment of business objectives and maintaining positions within agreed risk appetite and tolerance.

The purpose of the internal control system is to set the parameters and procedures that ensure the effectiveness and efficiency of operations, the reliability of reporting (both internal and external) and compliance with regulatory and other requirements.

The Board has delegated authority to the BAC to review the framework and effectiveness of the systems of internal control. The BAC is supported in this responsibility by the assurance work carried out by GwIA.

B.4.2 Compliance function

The Compliance Function provides dedicated support for regulatory interactions, including coordinating regulatory activity across the business, and provision of support and advice to the business on regulatory matters as well as future policy developments. The Compliance Function also provides guidance, advice and feedback on regulation, as well as setting and advising on, compliance standards. Routine monitoring and deep dive activities are carried out, to assess compliance with regulatory rules and legislation. The Compliance Function reports to the CRCO with its annual plan and required resources agreed by the BAC.

The Group and UK Compliance Policies set out the principles and minimum requirement by which the Company conducts its business and controls the scope covered by the policy. The policy includes requirements to:

- treat customers fairly, openly and honestly;
- provide and promote a range of products and services that meet customer needs, are easy to understand and that deliver real value;
- maintain honest, constructive and open relationships with governments and regulators to ensure mutual trust, respect and understanding;
- comply with all Group Policies, as well as applicable laws, rules and regulations in every country in which the Group operates;
- accept responsibility in all its activities for compliance with the spirit as well as the letter of all applicable laws, rules and regulations;
- act with due skill, care and diligence;
- ensure that an effective compliance culture thrives and operates at all levels of the business; and
- maintain appropriate means of identifying, assessing, managing and reporting regulatory compliance risks within BUs and on an aggregated basis across the Group.

B.5 Internal Audit function

Internal Audit is implemented through a Group-wide Function, therefore, references to GwIA are relevant to the Company's Internal Audit Function.

How the Company's Internal Audit Function is implemented

The work of GwIA is part of the overall Internal Control Framework of the Prudential Group. It operates as a third line of defence, providing independent and objective internal control assurance.

GwIA's primary objective is to assist the Board, Group Executive Committee, Group Audit Committee and Group Risk Committee in protecting the assets, reputation and sustainability of the organisation through the assessment and reporting of the overall effectiveness of risk management, control and governance processes across the Group; and by appropriately challenging Executive Management to improve the effectiveness of those processes.

GwIA activity is not restricted in scope in any way, is empowered by the Prudential Group Audit Committee to audit all parts of the Prudential Group and has full access to any of the organisation's records, physical properties and personnel. All employees are required to assist GwIA in fulfilling its roles and responsibilities. In executing its responsibilities, GwIA adheres to:

- the Institute of Internal Auditors requirements as set out in the Institute of Internal Audit's 'Code of Ethics' and 'International Standards for the Professional Practice of Internal Auditing', and the Chartered Institute of Internal Auditor's revised guidance, 'Effective Internal Audit in the Financial Services Sector';
- the requirements for internal audit functions set out in the Solvency II Directive 2009/138/EC (Level 1 text) Article 47 and Delegated Regulation (EU) 2015/35 (Level 2 text) Article 271;
- the requirements of the SMCR and the Group's Fit and Proper Policy.

How the Company's Internal Audit Function maintains its independence and objectivity from the activities it reviews

GwIA maintains independence and objectivity in the discharge of responsibilities and appropriate reporting lines are in place to support this goal:

- In accordance with the GwIA Charter, Prudential UK has an internal audit team, led by the Prudential UK Audit Director who reports to the GwIA Director as functional head, with direct access to the Chair of the BAC. The GwIA Director will consider the independence, objectivity and tenure of the Prudential UK Audit Director when performing their appraisals. For administrative purposes (excluding strictly all audit related matters) the Prudential UK Audit Director reports directly to the Prudential UK CEO;
- The Prudential UK Audit Director reports audit related matters to the BAC and communicates directly with the BAC through attendance at its meetings. In addition, the Prudential UK Audit Director is invited to private sessions with the BAC members on a regular basis to discuss coverage and any restrictions on GwIA's work, as well as engaging in regular dialogue with the BAC Chair outside of the formal Committees to discuss upcoming meetings and the risk and control landscape;
- The Prudential UK Audit Director, in consultation with the Prudential UK CEO, is empowered to attend and observe all or part of EXCOM and Board meetings and any other key management decision making committees and activities as appropriate;
- The function also has an autonomous Quality Assurance Director, whose primary role is to monitor and evaluate adherence to industry practice guidelines and GwIA's own standards and methodology and to undertake external reviews on a 3-year cycle;
- The assessment of the adequacy and effectiveness of the Risk, Compliance and Finance Functions is within the scope of GwIA and as such GwIA is independent of these functions and is neither responsible for, nor part of, them;
- GwIA staff are expected to exhibit the highest level of professional objectivity in carrying out their duties; make a balanced assessment of all relevant circumstances; remain impartial; and seek to avoid any professional or personal conflict of interest;

GwIA has a Conflicts of Interest register. Potential conflicts are recorded and monitored by the GwIA Quality Assurance Director, including a quarterly review of reported conflicts to assess appropriate management oversight. Where deemed necessary, the Quality Assurance team will review audits where a potential conflict has been identified to ensure conformance with the GwIA charter.

B.6 Actuarial function

The Actuarial Function is defined as the Chief Actuary, their team within the Risk Function, and specified individuals within the wider business who are responsible for carrying out the tasks of the Actuarial Function. The role of the Chief Actuary is a PRA SMF under the new SMCR and has responsibility for all of the activities of the Actuarial Function. The Actuarial Function forms part of Prudential Group's Actuarial Function.

The need for, and the scope of, the Actuarial Function is defined in Article 48 of the Solvency II Directive. This sets out the tasks that the Actuarial Function is responsible for. In addition to the tasks defined in Article 48 of the Solvency II Directive, the CRCO as the head of the Risk Function has delegated a number of the Risk Management responsibilities to the Chief Actuary, in particular oversight of the calibration and calculation of the SCR. This ensures that the Actuarial Function is embedded in the key stages of the risk management system in relation to the calculation of the capital requirements.

The key activities undertaken by the Actuarial Function to meet its responsibilities are summarised below:

Valuation of technical provisions

The Finance Function propose the valuation methodology and assumptions, and calculate the technical provisions. The Chief Actuary reviews the valuation methodology and assumptions, the models and data used in the calculation of the technical provisions and the resulting technical provisions and advises the Board accordingly. The report to the Board constitutes a component report of the overall Actuarial Function Report.

Underwriting Policy

The Chief Actuary reviews and advises on all aspects of the underwriting policy on an ongoing basis. In addition, they carry out an annual review of the policy focussing on different aspects each year, depending on previous reviews, recent business activities and any particular issues that the Chief Actuary wishes to review further. The Chief Actuary provides an annual report to the Board expressing an opinion on the underwriting policy, identifying any deficiencies and providing recommendations. This constitutes a component report of the overall Actuarial Function Report.

Reinsurance arrangements

The Chief Actuary reviews and advises on all aspects of the reinsurance arrangements on an ongoing basis. In addition, they carry out an annual review of the reinsurance policy, focussing on different aspects each year, depending on previous reviews, recent business activities and any particular issues that the Chief Actuary wishes to review further. The Chief Actuary provides an annual report to the Board expressing an opinion on the adequacy of the reinsurance arrangements, identifying any deficiencies and providing recommendations. This constitutes a component report of the overall Actuarial Function Report.

Capital requirements

The Finance Function propose the valuation methodology and assumptions and calculate the SCR. The Chief Actuary reviews the valuation methodology and assumptions and the resulting SCR and advises the Board accordingly. The Chief Actuary also chairs the UK TAC the internal management committee with responsibility for internal capital model methodology and assumptions.

Actuarial Function Report

The Actuarial Function provides a written report to the Board, at least annually, to document the tasks that have been undertaken by the Actuarial Function and their results, to identify any deficiencies and provide recommendations as to how such deficiencies should be remedied. This report summarises the tasks described above and highlights the key areas of focus following the Actuarial Function's activities each year.

B.7 Outsourcing

The Company uses outsourcing and third party solution providers to allow focus on its core business strengths, reduce costs and manage its delivery risks. The Company recognises that the use of outsourcing and third party solution providers can impact its risk profile, for example, the service may fail, resulting in significant business interruptions, liability for losses and costs, reputational damage and regulatory breaches. The Company retains ultimate responsibility for any activity that is supplied or outsourced.

The Company has material external and intra-group outsource providers. The external providers supply customer servicing, policy administration, new business processing, claims activity and related IT support services located in the UK and India, and back office administration for pension schemes and annuities located in the UK. The intra-group outsourcers provide various support services including investment strategy and portfolio management services located in the UK.

On 16 January 2018 the Company announced a new 10-year partnership with Tata Consultancy Services ('TCS'), a global player in IT, business processes and digital services, to enhance service for its UK savings and retirement customers. This included, the administration of over four million life and pensions contracts being moved from Capita to Diligenta, the FCA-regulated subsidiary of TCS, on 1 August 2018, with a contractual commitment of full transfer by 2022. In addition, further services primarily related to the Company's annuities business, transferred from the Company to Diligenta on 1 October 2018. Responsibility for the operation of some of the Company's IT infrastructure transferred from PGDS to Diligenta on 1 May 2018.

The Company has a Third Party Supply Policy in place which forms part of the overall RMF and is aligned with the three lines of defence governance model. The policy sets out the requirements for the management of all outsourcing and third party supply arrangements across the Company and is aligned to relevant policies, which address specific outsourcing topics, e.g. data security, information risk, and business continuity. The policy was refreshed in 2018 and is compliant with regulatory requirements for outsourcing, covering the full lifecycle of managing outsourcers and third parties, from procurement to management and oversight, relationship management and contract termination. The Third Party Supply Policy provides definitions of types of outsourcer (e.g. external, intra-group) and criticality of arrangements, along with minimum requirements to manage them. Attestation of compliance with the Third Party Supply Policy is completed on an annual basis by the Chief Operating Officer ('COO') and is overseen by the Risk Function.

B.8 Any other information

The effectiveness of the system of internal control and risk management is reviewed regularly and the outcomes are considered by the Board and its sub-committees. As part of the evaluation, the Prudential UK CEO and CFO report on compliance with the Group's governance policies and the internal control and risk management requirements. The Risk Function facilitates a review of the matters identified by this certification process. This includes the assessment of any risk and control issues reported during the year, and the findings from the reviews undertaken by GwIA. Issues arising from any external regulatory engagement are also taken into account. The Company continues to address issues raised following the FCA's thematic reviews of annuity sales and the fair treatment of long-standing customers in the life insurance sector.

The Board has reviewed the effectiveness and performance of the system of risk management and internal control during 2018. This review covered all material controls, including financial, operational and compliance controls and risk management systems. The review identified a number of areas for improvement, particularly in respect of the general IT control environment, and the necessary actions that have been or are being taken. The BAC monitors outstanding actions regularly and whether sufficient resource and focus is in place to resolve them within a reasonable time frame.

C Risk profile
(Unaudited)

Under the Solvency II regime, companies are required to manage their solvency position in line with the Solvency II regulatory SCR. Companies are also required to form their own views of the capital needed to ensure that they can meet liabilities as they fall due, allowing for the risks that they retain (Solvency II Pillar II or Economic Capital requirements). For the Company, the Solvency II Pillar 1 regulatory requirement remains the biting constraint. Consequently, the regulatory basis is the focus for the purposes of the capital assessment contained in this report.

The charts below show the undiversified SCR risks in relation to the Company at 31 December 2018 for shareholder-backed and policyholder-backed business. Detailed information on how the SCR allocation has changed during 2018 is set out in Section E.2.

Figure 12: Undiversified SCR for Shareholder business as at 31 December 2018

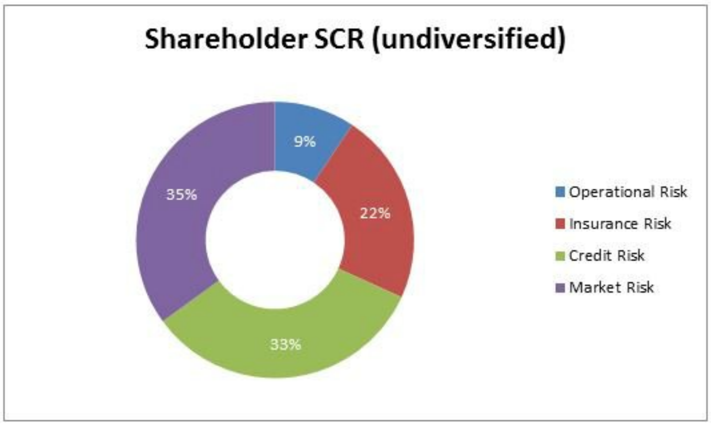
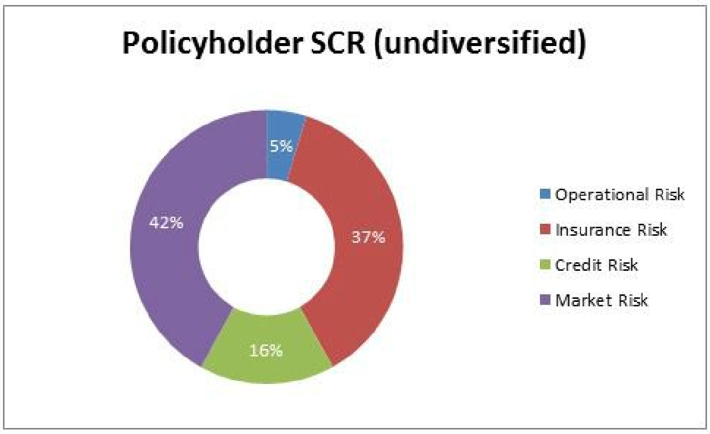


Figure 13: Undiversified SCR for Policyholder business as at 31 December 2018



The charts above show that the shareholder business has a proportionately greater exposure to credit risk, arising from the holdings in fixed income investments held to back the shareholder annuity business. The policyholder business has a higher proportionate exposure to investment risk arising from the investments held in the with-profits business including a significant allocation to equities and property. The key risk exposures are discussed in the following sections:

- Underwriting risk, or insurance risk, which includes persistency, longevity and expense (refer to Section C.1).
- Market risk, which includes equity, interest rate and currency risks (refer to Section C.2).
- Credit risk (refer to Section C.3).
- Liquidity risks (refer to Section C.4).
- Operational risk (refer to Section C.5).

- Other material risks (refer to Section C.6).

There have been no material changes to the measures used to assess the risk exposure or the material risks over the reporting period. However, the risk profile of the Company changed materially with the transfer of the Hong Kong business to PCAL on 14 December 2018. Persistency, equity, interest rate and currency risk exposures have all reduced considerably following the transfer of the Hong Kong Business to PCAL.

C.1 Underwriting risk

C.1.1 Risk exposure and mitigation

The Company's shareholder business is exposed to material levels of underwriting risk (or insurance risk) as a result of its insurance business operations. Given the large in-force annuity book, longevity remains a material risk for shareholder business, although the reinsurance of c.£12 billion of UK shareholder annuity liabilities to Rothesay Life during 2018 significantly reduced longevity exposures. The policyholder funds' exposure to longevity risk is also material and also arises from annuity business.

Longevity risk for both shareholder-backed business and policyholder-backed business has been predominantly managed through:

- annual reviews of best estimate assumptions, supported by detailed assessments of actual mortality experience versus best estimate assumptions;
- longevity research;
- longevity risk transfer transactions, assessed against principles and guidance provided in the Reinsurance Appraisal Framework; and
- annual oversight of actual versus expected SCR run-off for shareholder annuities by the ERC.

Other insurance risks, such as persistency risk, expense risk and non-annuitant mortality risk are subject to similar regular reviews, with frequency and intensity proportionate to the materiality of the risk.

C.2 Market risk

C.2.1 Risk exposure and mitigation

Equity and property risk

The Company is materially exposed to risk arising from the mismatch between guarantees embedded in the liabilities and the assets backing them, primarily equity assets. The key share-holder backed areas impacted are the present value of expected shareholder transfers from the with-profits business and the lifetime mortgage book. Equity risk remains material to the Company in absolute terms and proportionally to other risks.

The with-profits business of the Company is exposed to equity and property risk as a result of underlying guarantees built into certain products. This risk is largely borne by the with-profits fund itself, though shareholder support may be required in extreme circumstances where the fund has insufficient resources to support the risk.

Current Brexit uncertainties heighten such equity and property risks. A hard Brexit may result in increased market volatility, reduced economic activity and a fall in property values.

Interest rate risk

The Company's exposure to interest rate risk primarily arises from the need to match cash payments to meet annuity obligations with cash received from investments. The Company aims to match the duration (a measure of interest rate sensitivity) of assets and liabilities as closely as possible, with regular monitoring and managing of the exposures. The Solvency II regime and its impact on the way the balance sheet is constructed, such as the requirement to include a risk margin in our capital reserves, creates additional interest rate risk for the Company.

The with-profits business of the Company is exposed to interest rate risk as a result of underlying guarantees built into certain products. As noted above, the risk is largely borne by the with-profits fund itself, though shareholder support may be required in extreme circumstances where the fund has insufficient resources to support the risk.

As the solvency position remains sensitive to interest rates, the Company continues to closely monitor and manage its interest rate exposures.

Currency risk

The Company has currency risk exposure arising from investment in non-currency assets. The Company has limited appetite for currency risks and where appropriate, has limits and controls in place to monitor and manage the risk. Where currency risk arises outside risk appetite, currency borrowings, swaps and other derivatives are used to manage the exposure.

Risk mitigation

The methods used to manage and mitigate market risks include the following:

- Market Risk Policy;
- risk appetite statements, limits and triggers that are in place;
- the monitoring and oversight of market risks through the regular reporting of management information;
- asset and liability management programmes that are in place;
- annual review of the Strategic Asset Allocation;
- use of derivatives including options and futures on equities and interest rates; and
- use of currency hedging.

C.3 Credit risk

C.3.1 Risk exposure and mitigation

The Company is exposed to credit risk by virtue of fixed income assets, primarily corporate bonds, in the shareholder-backed portfolio. There are also substantial volumes of similar assets held in the with-profits fund, the risk of which is largely borne by the with-profits policyholders, but which can impact the shareholder by reducing the size of the shareholder transfers and, in extremis, resulting in burn-through which requires shareholder support. The company is also exposed to credit risk arising from reinsurance and derivative counterparties, and from placing cash with counterparties. Shareholder credit risk has been significantly reduced following the reinsurance of c.£12 billion of UK shareholder annuity liabilities to Rothesay Life. Counterparty credit risk is however now more concentrated due to the significant consequent single exposure to Rothesay Life.

The Company operates a robust credit risk framework, comprising risk policies, risk appetite statements, processes and controls, including:

- Credit Risk Policy;
- the credit rating processes operated by the Group's asset management companies used by the Company;
- investment constraints on the asset portfolios, in relation to credit rating, seniority, sector and issuer;
- investment constraints on counterparties in particular for derivatives, reinsurance and cash;

- an average credit quality target for the assets;
- a credit risk limit framework, and associated monitoring for both the shareholder and policyholder businesses;
- oversight from the ERC and BRCC and from the Group Credit Risk Committee (featuring membership from the Company's Risk Function), with a number of forward-looking indicators being monitored to identify potential counterparty risk materialising in the future;
- invested credit sector reviews; and
- performing deep dive reviews.

C.4 Liquidity risk

C.4.1 Risk exposure and mitigation

The Company's exposure to liquidity risk is considered to be relatively small because of the nature of the operating model. The exposure that does exist primarily arises from:

- higher than expected policyholder withdrawals and collateral requirements;
- surrenders and processing delays;
- unexpected cash outflows; and
- lower than expected market liquidity for assets.

Liquidity risk is not quantified in the Internal Model given this risk is not best managed through holding additional capital. Instead, liquidity risk is managed through a robust Risk Management Framework, which includes:

- a Liquidity Risk Policy;
- a Liquidity Contingency Plan; and
- quarterly monitoring of exposures, under both base and various stressed scenarios, against liquidity coverage ratios triggers / limits.

In 2018, liquidity sources remained sufficient to meet financial obligations as they fell due, and when tested in stressed scenarios.

C.4.2 Expected Profit Included in Future Premiums

The Company is required to calculate and report the expected profit included in future premiums ('EPIFP') included within its own funds, in accordance with Article 260 of the Delegated Regulation. This calculation requires an assessment of the impact of an increase in insurance liabilities (excluding the risk margin) if future premiums relating to in-force business were not received, regardless of the legal or contractual rights of the policyholder to discontinue the policy. The calculation is carried out at the level of homogeneous risk groups, as defined in Article 35 of the Delegated Regulation.

At 31 December 2018, EPIFP was £45.4 million (2017: £nil). This increase was mainly due to a reduction in net costs of guarantees and smoothing (NCOGS), which caused EPIFP to be floored at zero in 2017.

C.5 Operational risk

C.5.1 Risk exposure and mitigation

Operational risk is the risk of loss (or unintended gain or profit) arising from inadequate or failed internal processes, personnel and systems, or from external events. This includes employee error, model error, system failures, fraud, the risk of a cyber-attack or some other event which disrupts business processes. Another important element of operational risk relates to non-compliance with the high rate of regulatory change. As well as prudential regulation, focus is on assessing changes in conduct regulation, including regulations related to anti-money laundering, bribery and corruption, and sales practices. The definition also includes operational elements inherent across other risk categories.

The Company's primary exposure to operational risk arises from business processes (e.g. customer administration, sales), people capabilities, operation of systems and financial reporting activity. The strategic and transformational changes to products, systems and outsourcers will all change the operational risk profile of the business. Additional exposure is anticipated as M&GPrudential rolls out its strategic merger and transformation ambitions and demerges from Prudential plc.

The Company manages and mitigates its operational risk using the following:

- operational risk policies including Third Party Supply;
- an operational risk framework that delivers processes and tools to identify, assess, control and monitor operational risk exposures;
- corporate insurance programmes to limit the impact of operational risks;
- scenario analysis for operational risk capital requirements, which focus on extreme, yet plausible, events;
- internal and external review of cyber security;
- regular testing of elements of the business continuity and disaster recovery plans; and
- robust structural risk challenge, oversight and reporting of merger, transformation and demerger activity.

C.6 Other material risks

C.6.1 Business environment risks

Some of the risks that the Company is exposed to are necessarily broad given the external influences which may impact. These risks include:

- Macroeconomic conditions: Changes in global economic conditions can impact the Company directly; for example by leading to poor returns on investments and increasing the cost of promises the Company has made to customers. They can also have an indirect impact; for example economic pressures could lead to decreased savings, reducing the propensity for people to buy the Company's products. Global economic conditions may also impact on regulatory risk for the Company by changing prevailing political attitudes towards regulation;

- Digital disruption: The emergence of advance technologies is providing an impetus for companies to rethink their existing operating models and how they interact with their customers. The Company is embracing the opportunities presented by digitalisation and is closely monitoring any risks which arise;

- Regulatory: Changes in UK government policy, legislation (including tax), regulation or regulatory interpretation applying to insurance companies may adversely affect the Company's product range, distribution channels, capital requirements and, consequently, reported results and financing requirements. Regulators in other jurisdictions in which the Company operates may also introduce changes in the regulatory framework for long-term savings and retirement arrangements and investments, including to selling practices and solvency requirements. There are a number of ongoing policy initiatives and regulatory developments that are having, and will continue to have, an impact on the way the Company is supervised.

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

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

C.6.2 Strategic risk

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

The key business strategies affecting the Company are:

- the merger and transformation of the M&G and Prudential UK businesses with the aim of delivering capital-light, digitally-enabled, customer-focused solutions; and
- the demerger of M&GPrudential from Prudential plc.

These strategies present a significant opportunity to leverage scale, financial strength and complementary product and distribution capabilities, but also carry strategic risk, as well as delivery and operational risks associated with the size, complexity and interdependencies of the transformation being undertaken.

C.6.3 Technology risk

The Company has a high dependency on technology to operate effectively with the maintenance, integrity and resilience of the IT infrastructure and applications paramount to meeting business and customer needs. The transformation programme should ultimately reduce IT and operational risk but the delivery of, and migration to, a new infrastructure involves significant execution and migration risk. It will create new risks associated with the confidentiality, integrity and availability of data, as it will involve increased use of external outsourcers and Cloud capabilities. Additionally, the increasing and complex cyber threat and importance of customer data security will require the effective operation of existing cyber hygiene controls and the on-going enhancement and automation of external and internal controls, including system and perimeter security tests to mitigate the risks posed by an increasing digital footprint and increasingly sophisticated attacks. Following recent Audit findings and Technology Risk assurance reports, M&GPrudential Enterprise Services have mobilised a Tactical and a Strategic cyber remediation programme to address the immediate control gaps and the medium to longer term improvements required across our IT environment to reduce our security risk exposure.

C.6.4 Reputation risk

The merger, demerger and transformation activities increase exposure to reputation risk for the Company. The anticipated Product Administration System (IT) migrations and increasing use of outsourcing and Cloud-based technologies pose a material threat to the Company's reputation if mishandled, due to the level of customer data potentially impacted and the visibility externally.

Reputational risk considerations are an important part of the Company's management of Environmental, Social and Governance issues.

C.6.5 Conduct risk

Conduct risk is the risk that the Company's decision-making and behaviours are inappropriate, leading to unfair or poor customer outcomes.

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

C.6.5 Group risk

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

C.7 Any other information

C.7.1 Special Purpose Vehicles

There are no special purpose vehicles that fall into the definition under Article 211 of Solvency II Directive.

C.7.2 Risk sensitivity

Stress and scenario testing is embedded in the Company's RMF. It is performed in order to:

- assess the Company's ability to withstand significant deterioration in financial and non-financial conditions;
- provide feedback to the decision making process by identifying areas of potential business failure;
- demonstrate to external stakeholders that the Company has adequate capital and liquidity levels;
- demonstrate that the Company has appropriate and plausible management actions available to cover potential losses incurred during extreme, but plausible events; and
- to assist in the monitoring of adherence to the Company's and the Group's risk appetite.

Stress tests are performed both with and without any allowance for the transitional measures on technical provisions granted by the PRA being recalculated. Stress tests are performed separately for the Company's with-profits funds and shareholder-backed business.

To evaluate the Company's resilience to significant deteriorations in market and credit conditions and other shock events, the risks facing the Company as described in the sections above are grouped together into severe but plausible scenarios. In addition, the Company assesses an annual reverse stress test which gives the directors an understanding of the maximum resilience to extremely severe adverse scenarios. The Company also maintains a risk appetite framework which assesses the Company's ability to withstand a specified level of shock and still cover its solvency capital requirements.

In considering these scenarios the impacts of mitigating management actions designed to maintain or restore key capital, liquidity and solvency metrics to the Company's approved risk appetite are considered. In the scenarios tested, sufficient actions were available to management to maintain the viability of the Company over the three-year period under assessment.

Sensitivity Analysis

The estimated sensitivity of the Company shareholder Solvency II capital position is as follows:

Figure 14: Impact of market sensitivities

	31 December 2018	
	£m	Ratio (%)
Base Shareholder surplus	3,691	172
Impact of:		
20% instantaneous fall in equity markets	(297)	(4)
40% fall in equity markets(1)	(579)	(8)
50 basis points reduction in interest rates(2)	(99)	(6)
100 basis points increase in interest rates(2)	198	14
100 basis points increase in credit spreads	(366)	(2)

(1) The Company has considered the impact of an instantaneous 20% fall and any further fall would be expected over a period of time.
(2) Allowing for further transitional recalculation after the interest rate stress.

The sensitivity analysis above allows for predetermined management actions and those taken to date, but does not reflect all possible management actions which could be taken in future.

Core economic stress scenarios

The Company has a set of core stress scenarios that are based on external economic stresses outside its control. These scenarios are simplistic stresses that have been applied consistently over time, allowing comparisons of results for individual risk exposures.

The summary results from stress testing show that:

- the Company remains exposed to interest rate movements equity and credit risk. These exposures continue to be subject to ongoing monitoring and management;
- the Company retains an exposure to downgrades in the credit portfolio and lighter mortality experience in relation to the annuity business;
- in practice, the Company would expect a number of events to happen simultaneously. The analysis has shown that it would take a strong event to reduce the capital coverage ratio below 100%. At 100% capital coverage, the Company would have sufficient capital to withstand a 1 in 200 year event;
- the balance sheet is materially exposed to longevity risk. In practice, longevity events are expected to emerge over a number of years, and are therefore less of a concern in the short term than changes in market conditions.

C.7.3 Risk concentration

The Company's review of significant risk concentration encompasses a review of its exposure to various balance sheet asset classes, individual counterparties, group of interconnected individual counterparties, specific geographical areas and industry sectors.

The Company complies with the Group's Global Counterparty Limits for Prudential UK, which limit significant concentration risks arising from various balance sheet asset classes. These asset classes are assigned a notional weighting that has been derived to reflect the relative riskiness of each asset class.

The Company also has in place a process whereby invested credit and counterparty credit risk outside the scope of the Group Global Counterparty Limits is limited on a single name basis. Under this process, the Group Chief Risk Officer's approval is required for the undertaking of new or additional exposure greater than predefined thresholds. These thresholds are defined for the company and vary by asset class/counterpart exposure and by credit rating. Timebound exemptions from these thresholds may be approved by the Group Chief Risk Officer based on the merits of the individual cases.

As at 31 December 2018, the four largest counterparties the shareholder-backed business had exposure to are:

- Rothesay Life
- United Kingdom of Great Britain and Northern Ireland;
- United States of America; and
- HSBC Holdings plc.

As at 31 December 2017, the four largest counterparties the shareholder-backed business had exposure to are:

- United Kingdom of Great Britain and Northern Ireland;
- European Investment Bank;
- Federal Republic of Germany; and
- HSBC Holdings plc.

As at 31 December 2018, the four largest counterparties the policyholder-backed business had exposure to are:

- United Kingdom of Great Britain and Northern Ireland;
- European Investment Bank;
- HSBC Holdings plc; and
- Federal Republic of Germany.

As at 31 December 2017, the four largest counterparties the policyholder business had exposure to are:

- United Kingdom of Great Britain and Northern Ireland;
- HSBC Holdings plc;
- Banco Santander SA; and
- Deutsche Bank AG.

The Company's review of significant risk concentration encompasses a review of its exposure to various balance sheet asset classes, individual counterparties, group of interconnected individual counterparties, specific geographical areas and industry sectors.

The Company complies with the Group's Global Counterparty Limits for Prudential UK, which limit significant concentration risks arising from various balance sheet asset classes. These asset classes are assigned a notional weighting that has been derived to reflect the relative riskiness of each asset class.

The counterparty exposure to Rothesay Life arises from the reinsurance of £12 billion (as at 31 December 2017) of the shareholder-backed annuity portfolio to Rothesay Life during the year, that is expected to be followed by a Part VII transfer of most of the portfolio by 30 June 2019. Under the terms of the agreement, the Company has access to a pool of assets placed by Rothesay Life in a custody account in the Company's favour in the event of default by Rothesay Life.

The Company also has in place a process whereby invested credit and counterparty credit risk outside the scope of the Group Global Counterparty Limits is limited on a single name basis. Under this process, the Group Chief Risk Officer's approval is required for the undertaking of new or additional exposure greater than predefined thresholds. These thresholds are defined for the company and vary by asset class/counterpart exposure and by credit rating. Timebound exemptions from these thresholds may be approved by the Group Chief Risk Officer based on the merits of the individual cases.

C.7.4 Prudent Person Principle

The prudent person principle requires that the Company only makes investments on behalf of customers that a "prudent person" would make. In order to comply with this Principle, the Company has to be able to identify, understand, measure and monitor any risks arising from its investment portfolios.

The Company has an investment risk oversight framework which ensures that the Company's investment risks are managed effectively and efficiently. The framework focuses on the integrity and effectiveness of the investment processes, governance and controls, as well as appropriateness of resourcing and compliance of processes with applicable regulatory requirements (e.g. prudent person principles set out in the Solvency II Directive).

The investment risk oversight framework comprises a risk appetite statement, standards, processes and controls, which ensures investment risk is managed appropriately in regards to the Company's risk appetite.

The Company outsources investment management both intra-group and to external asset managers. That business is governed by a common Group-wide Governance framework. The following information provides details on the Group-wide approach to the prudent person principles an insurance entity should apply when making investment decisions:

- Prudential Group's policies provide a common framework for the oversight of financing and investment activities across the Group. They are designed to provide general, prudent and principle-based guidance for both shareholder-backed business and policyholder-backed business.

- The GRF covers all aspects of risk management across all BUs and includes minimum standards, controls and requirements for risk management. The GRF is supported by further documents including specific policies that cover credit, market, insurance, liquidity, operational and investment risk as well as lower level Group-wide Operating Standards and Group Approved Limits.

- The Group Investment Policy specifically sets out the framework for management and oversight of investment performance and investment related risk across the Group. It focuses on ensuring that all of the Group's business units have appropriate policies and procedures in place to manage, monitor and report on the investment risk that they have taken on.

- The Group Dealing Controls Policy provides detail of the controls and monitoring in place in relation to all trading operations, including the operational controls around derivative collateral management. The policy also sets out uniform controls across all asset classes (including non-listed and securitised investments) and clarifies the responsibility of BUs to ensure full compliance with all local regulations and requirements.

- The Company oversees its asset managers by means of ensuring compliance with investment management agreements and investment mandates. These are structured in order to ensure compliance with the prudent person principle, and are overseen by the Investment Office. The Investment Office updates and maintains the investment management agreements and investment mandates in line with changes in investment strategy, and carries out monitoring and due diligence of investment managers' compliance with their respective mandates.

D Valuation for solvency purposes

D.1 Valuation of assets

D.1.1 Overview

The 2018 balance sheet valued under both statutory accounts basis (UK GAAP) and Solvency II basis is summarised in Figure 15 below:

Figure 15: Solvency II and UK GAAP balance sheets for the year-ended 31 December 2018

	Statutory accounts - UK GAAP	Presentation differences (note a)	Ring-fenced funds (note b)	Other valuation differences (note c)	2018 Solvency II	2017 Solvency II
	£m	£m	£m	£m	£m	£m
Assets						
Deferred acquisition cost and intangible assets	46		(3)	(43)	—	—
Investments (other than participations)	137,513	730		100	138,343	153,934
Participations	5,155	(985)		(81)	4,089	10,843
Assets held for index-linked and unit-linked contracts	14,546	(6,781)			7,765	9,022
Loans and mortgages	3,313	7,647	46	32	11,038	11,017
Reinsurance recoverable	18,255		60	329	18,644	6,842
Cash and cash equivalents	2,080	(775)			1,305	1,892
Other[(1)]	2,636	416	(168)	(2)	2,882	2,702
Total assets	**183,544**	**252**	**(65)**	**335**	**184,066**	**196,252**
Liabilities						
Technical provisions	167,265		(125,327)	(41,938)	—	—
Best estimate		170	112,221	42,068	154,459	158,207
Risk margin			1,005	582	1,587	1,564
Other liabilities					—	—
Deferred tax liabilities	711		(27)	(76)	608	1,173
Debts owed to credit institutions	2,609			100	2,709	3,273
Financial liabilities other than debts owed to credit institutions	89	(28)			61	81
Other[(2)]	5,993	110	(227)	307	6,183	6,231
Total liabilities	**176,667**	**252**	**(12,355)**	**1,043**	**165,607**	**170,529**
Excess of assets over liabilities	**6,877**	**—**	**12,290**	**(708)**	**18,459**	**25,723**

[(1)] Other assets include Property, plant and equipment held for own use, Insurance and intermediary receivables, Reinsurance receivables and Receivables (trade, not insurance).
[(2)] Other liabilities includes Provisions other than technical provisions, Pension benefit obligations, Derivatives liabilities, Deposits from reinsurers, Insurance and intermediaries payable, Reinsurance payables, Payables (trade, not insurance) and Contingent liabilities. The breakdown of these are detailed in Section D.3.2 Figure 24.

Notes:

(a) *Presentation differences* represent movements between line items with no overall impact on excess of assets over liabilities. The main differences include £6,781 million relating to assets held by the index-linked funds which are presented together in a single line on the UK GAAP statutory accounts balance sheet rather than within each individual asset/liability category. These amounts reported as index-linked funds for the statutory accounts do not meet the Solvency II definition of index-linked and accordingly are reported in the various individual asset and liability categories. The other large difference of £7,647 million within loans and mortgages mostly relates to the movement of reverse repos which are treated as investments in UK GAAP but moved to loans and mortgages for solvency II.

(b) *Ring-fenced funds* represent the impact on the balance sheet of changes in value and presentation of the policyholder assets and liabilities before any restrictions are applied. For UK GAAP purposes, although the individual assets and liabilities are valued, the overall impact of ring-fenced funds on UK GAAP shareholders' funds is not significant. The UK GAAP technical provisions of £125,327 million are removed and replaced by a Solvency II best estimate liability of £112,221 million. The £12,290 million represents the excess of assets over liabilities on a Solvency II basis before any restrictions are applied and includes the amount attributable to shareholders for the value of future shareholder transfers from the with-profits business.

(c) *Other valuation differences* primarily represent the differences in valuation methods under UK GAAP and on a solvency II basis. The comparison of excess of assets over liabilities on a solvency II basis to UK GAAP is set out within Section E.1.4.

Valuation differences for deferred acquisition cost and intangible assets, participations, loans and mortgages and other assets are explained in Section D.1.2.2. The valuation differences for reinsurance recoverables are explained in Section D.2.8. Valuation differences for technical provisions, best estimate and risk margin are explained in Section D.2.1. Valuation differences for deferred tax liabilities and other liabilities are explained in Section D.3.2.

D.1.2 Valuation of assets

D.1.2.1 Determination of fair value

Within the Solvency II balance sheet, assets are valued using valuation methods that are consistent with the valuation approach set out in the Solvency II Directive. The overall principle when valuing assets and liabilities under Solvency II is to use a fair value, as set out in Article 75 of the Directive. There have been no changes to the recognition and/or valuation basis of assets and other non-insurance liabilities in the Solvency II balance sheet during the year.

When valuing assets and liabilities in accordance with Solvency II, the fair valuation hierarchy set out below is followed:

(a) Quoted market prices in active markets for the same assets or liabilities
As the default valuation method, assets and liabilities are valued using quoted market prices in active markets for the same assets or liabilities, where available.

The investments of the Company which are valued using this method include exchange listed equities, collective investment undertakings 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.

(b) Valuation methods using quoted market prices in active markets for similar assets and liabilities with adjustments to reflect differences or using inputs that are observable in the market
Where quoted market prices in active markets for the same assets or liabilities are not available, the Company applies either of the following two valuation methods on a case by case basis:

- Using quoted market prices in active markets for similar assets and liabilities with adjustments to reflect factors specific to the asset or liability such as condition or volume or level of activity in the markets; or
- Using a method where the significant inputs are observable for the asset directly (i.e. as prices) or indirectly (i.e. derived from prices).

The majority of the assets of the Company that are valued using these valuation methods are corporate bonds, collateralised securities and other non-national government bonds, together with over-the-counter derivatives such as forward exchange contracts and non-quoted collective investment undertakings.

These assets, in line with market practice, are generally valued using independent pricing services or third-party broker quotes. These valuations are determined using independent external quotations from multiple sources and are subject to a number of monitoring controls, such as monthly price variances, stale price reviews and variance analysis on prices achieved on subsequent trades.

Pricing services, where available, are used to obtain the third-party broker quotes. Where pricing services providers are used, a single valuation is obtained and applied.

When prices are not available from pricing services, quotes are sourced directly from brokers. The Company seeks to obtain a number of quotes from different brokers so as to obtain the most comprehensive information available on their capability of being executed. Where quotes are sourced directly from brokers, the price used in the valuation is normally selected from one of the quotes based on a number of factors, including the timeliness and regularity of the quotes and the accuracy of the quotes considering the spreads provided. The selected quote is the one that best represents an executable quote for the security at the measurement date.

Generally, no adjustment is made to the prices obtained from independent third parties. Adjustment is made in only limited circumstances, where it is determined that the third party valuations obtained do not reflect fair value (e.g. either because the value is stale and/or the values are extremely diverse in range). These are usually securities which are distressed or that could be subject to a debt restructure or where reliable market prices are no longer available due to an inactive market or market dislocation. In these instances, prices are derived using internal valuation techniques using standard market practices. For the majority of such securities matrix pricing is used; that 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 ad applying these to the equivalent debt instruments factoring in a specified liquidity premium. The parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

c) Alternative valuation methods - inputs not based on observable market data

As stated at section (b) above, generally, no adjustment is made to the prices obtained from independent third parties. Adjustment is made in only limited circumstances, where it is determined that the third party valuations obtained do not reflect fair value.

In these instances, prices are derived using internal valuation techniques, including Alternative valuation methods, which have 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 techniques used require a number of assumptions relating to variables such as credit risk and interest rates. Examples of such variables include an average credit spread based on the corporate bond universe and the relevant duration of the asset being valued. The Company determines the input assumptions based on the best available information at the measurement dates.

The majority of the investments of the Company that are valued using alternative valuation methods with significant unobservable inputs are held by the Company's ring-fenced funds.

The ring-fenced funds' contribution towards the Company’s own funds is restricted to the amount required to cover the ring-fenced funds’ solvency capital requirement (as described further in Section E). Therefore any change in the fair value of these investments from assumption changes will not impact the Company’s own funds as the contribution to the own funds is restricted to the SCR.

These investments of the Company's ring-fenced funds principally comprise:

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

- Private equity and venture investments which were valued internally based on management information available for these investments. The significant unobservable inputs include the determination of expected future cash flows of the investments being valued and the selection of appropriate discount rates. The valuation is performed in accordance with International Private Equity and Venture Capital Association Valuation guidelines.

The investments in the shareholder fund that are valued using alternative valuation methods with significant unobservable market inputs at 31 December 2018 include equity release mortgage loans that are valued using discounted cash flow models. During 2017, the assumptions used within the discounted cash flow model were refined to reflect developing market practice, including consideration of the Prudential Regulation Authority's industry-wide review in this area and resulting guidance. This refinement incorporates inputs relevant to determining the discount rate that are not market observable. There was no material difference in the fair value of these loans recognised in 2017 arising from this change in the valuation model. Significant assumptions for equity release mortgage assets within the valuation of the no-negative-equity guarantee include the expected annual increase in house prices of 3.05 per cent (2017: 3.19 per cent) and the implied house price volatility of 13 per cent (2017: 13 per cent).

D.1.2.2 Valuation bases under Solvency II compared with UK GAAP

Deferred acquisition costs and intangibles
Deferred acquisition costs and other intangible assets such as distribution rights and software are recognised at cost less amortisation under UK GAAP in the Company's statutory accounts but have no value for Solvency II purposes.

Deferred tax asset
Deferred tax assets, other than the carry forward of unused tax credits and losses, are calculated based upon the differences between the values given to assets and liabilities for tax purposes and their values in the Solvency II balance sheet. The principles of UK GAAP are applied to calculate the extent of deferred tax applicable to those value differences. Changes in the valuation of underlying assets or liabilities will give rise to a change in deferred tax balances. Recoverability is assessed on the basis of the balances held and consideration is given to the probability of taxable profit being available against which the underlying recoverable can be offset.

There is no deferred tax asset on the Solvency II balance sheet as at 31 December 2018.

Investments (other than participations)
Investments (other than participations) comprise the following asset classes as included in the Solvency II balance sheet:

Figure 16: Investments (other than participations) for the year-ended 31 December 2018

	2018 £m	2017 £m
Property (other than for own use)	9,240	9,058
Equities	30,994	36,791
Bonds	65,814	77,761
Collateralised securities	5,759	5,561
Collective investment undertakings	22,589	21,130
Derivatives	2,503	2,912
Deposits other than cash equivalents	1,444	721
Total	**138,343**	**153,934**

All of these categories of investments are valued at fair value within both the Solvency II balance sheet and the Company's UK GAAP financial statements.

Participations
Article 13 of the Solvency II Directive defines a 'participation' as the ownership, direct or by way of control, of 20 per cent or more of the voting rights or capital of an undertaking.

Under Solvency II rules the adjusted equity method is applied to all investments in subsidiary undertakings. The adjusted equity method is based on the excess of assets over liabilities for each subsidiary, with the subsidiaries' individual assets and liabilities valued in accordance with the Solvency

II Directive. Where the related undertaking is an insurance undertaking technical provisions are valued in accordance with Articles 76 to 85 of the directive.

Included within the value of participations is the impact of transitional measures , as applicable to participations which are insurance undertakings. These items are covered further in Section D.2.4.

The solvency capital requirement ('SCR') related to participations that are insurance undertakings are not included within the participation line in the balance sheet, and are included in the Company's SCR.

Assets held for index-linked and unit-linked contracts
These assets are held to cover linked liabilities where the policyholders bear the investment risk of the assets. Under both UK GAAP and Solvency II these assets are recorded in aggregate as a single line entry on the balance sheet. The individual assets and non-insurance liabilities of the linked business are valued in accordance with the Solvency II principles set out in this section.

The difference between UK GAAP and Solvency II relates to the different definitions of index-linked between the two bases. For Solvency II reporting, business is only classified as index-linked where the policyholder bears the risk and not where risks are borne by the shareholder. For UK GAAP all index-linked business is classified as index-linked business, irrespective of the sharing of risks. There is also a small difference in relation to investment contracts without discretionary participation features, where amounts due from reinsurers are reported as reinsurance under Solvency II but as investments under UK GAAP.

Loans and mortgages
Loans and mortgages include interests in residential and commercial mortgage portfolios, the Company's loans to individuals (e.g. policy loans) and other loans.

Under UK GAAP, these loans are accounted for at amortised cost net of impairment. The exceptions include interests in equity release mortgages which have been designated at fair value through profit and loss as this loan portfolio is managed and evaluated on a fair value basis.

Within the Solvency II balance sheet, these loans and mortgages are valued on a 'mark-to-model' valuation basis using the discounted cash flows expected to be received. The rate of discount used is the market rate of interest where applicable.

Other assets
Other assets comprise the following asset classes as included in the Solvency II balance sheet:

Figure 17: Other assets for the year-ended 31 December 2018

	2018 £m	2017 £m
Insurance and intermediaries receivables	21	23
Reinsurance receivables	153	153
Receivables (trade, not insurance)	2,564	2,388
Other	144	139
Total	**2,882**	**2,703**

Other assets in the Solvency II balance sheet are measured at fair value determined using alternate valuation methods that are market consistent and represents the realisable value of individual assets on transfer to third party. If the UK GAAP value is a good proxy for fair value no adjustment is made.

D.1.3 Leasing

The Company's operating and finance lease arrangements relate principally to properties. Further information on the Company's leasing arrangements is provided in Section A.4.2.

D.2 Technical provisions

To the extent these disclosures relate to the risk margin, transitional measures and/or the Solvency Capital Requirement, they are not subject to audit and have not been audited.

D.2.1 Overview

As a general principle, technical provisions are valued at the amount for which they could theoretically be transferred to a third party in an arm's length transaction. The technical provisions consist of the best estimate liability and the risk margin, reduced by the "transitional measures on technical provisions" ('TMTP') where relevant.

The best estimate liability corresponds to the probability-weighted average of future cash-flows, taking account of the time value of money (i.e. the expected present value of future cash-flows), using the risk-free interest rate term structure published by the European Insurance and Occupational Pensions Authority with allowance for a matching adjustment or a volatility adjustment where relevant. The calculation of the best estimate liability is based upon up-to-date and credible information and realistic assumptions (derived from data analysis and expert judgement) and is performed using appropriate actuarial and statistical methods. The cash-flow projections used in the calculation of the best estimate liability take account of all the cash in- and out-flows required to settle the insurance obligations over their lifetime. The cash-flows included in the best estimate liability calculation are derived after applying Solvency II "contract boundary" rules, which determine whether future cash-flows can be recognised as part of the in-force business. The best estimate liability is calculated before deduction of the amounts recoverable from reinsurance contracts. Those amounts are calculated separately (see Section D. 2.8).

The “contract boundary rules” define:
- When a policy is first included in the cash-flows;
- Which premiums should be allowed for in the cash-flows; and
- When a policy should no longer be included in the cash-flows.

The risk margin is calculated in line with Solvency II requirements, and aims to ensure that the total technical provisions are equivalent to the cost of ceding the insurance obligations to a third party. The calculation assumes a 6 per cent per annum cost of capital and applies to non-hedgeable risks only, with no diversification between the risks in different legal entities. This calculation includes simplified methods and requires assumptions as to the run-off profile of non-hedgeable capital requirements for each line of business in each entity, in line with Article 58 of the Delegated Regulation, rather than a full projection of solvency capital requirements ('SCR'). The SCR for each non-hedgeable risk is assumed to run-off in-line with suitable profiles which differ depending on the types of non-hedgeable risks. The SCR each year is aggregated using a simplified correlation matrix.

The main risks are detailed in Section C.

Transfers to the shareholder fund are not part of the technical provisions, but are included in the calculation to determine restrictions to the surplus on certain ring-fenced funds.

Technical provisions at 31 December 2018

Figure 18: Value of technical provisions 31 December 2018

	Best estimate liability £m	Risk margin £m	Total £m	31-Dec-17 £m
Insurance with-profit participation	94,095	407	94,502	93,935
Index-linked and unit-linked insurance	12,817	34	12,851	14,449
Other life insurance	41,107	1,131	42,238	45,201
Accepted reinsurance - insurance with-profit participation	5,512	—	5,512	5,168
Accepted reinsurance - other life insurance	802	14	816	897
Health insurance	(15)	—	(15)	(22)
Non-life business	142	—	142	143
Total	154,460	1,586	156,046	159,771

The technical provisions shown in Figure 18 above include the impact of the transitional measures for technical provisions (see Section D.2.4.1), which are included within the risk margin column. The transitional measures for technical provisions reduce the Company's technical provisions by £2,618 million as at 31 December 2018.

Reinsurance recoverables at 31 December 2018

The following table shows the reinsurance recoverables with comparisons to the previous year. The main change relates to the reinsurance of the annuity portfolio to Rothesay Life totalling £12,464 million reported within "other life insurance" disclosed in section A.1.4.3.

Figure 19: Value of reinsurance recoverables 31 December 2018

	2018 £m	2017 £m
Insurance with-profit participation	(1)	—
Index-linked and unit-linked insurance	5,079	5,453
Other life insurance	13,414	1,235
Accepted reinsurance - other life insurance	10	11
Health insurance	—	—
Non-life business	142	143
Total	18,644	6,842

D.2.2 Methodology and assumptions

Further details of the methodology and assumptions used for each material line of business are discussed below. The methods chosen for each line of business are proportionate to the nature, scale and complexity of the underlying risks.

The key assumptions required in the valuation of technical provisions are:

(i) economic assumptions, most of which are published by the European Insurance and Occupational Pensions Authority and set by reference to market data at the valuation date;

(ii) non-economic assumptions, used to derive non-market related best estimate liability cash-flows (for example future claims and expenses); and

(iii) assumptions in respect of dynamic management actions and policyholder behaviour.

D.2.2.1 Economic assumptions

The principle economic assumption is the risk-free interest rate term structure. The risk-free curves at which best estimate liability cash-flows are discounted are specified by the European Insurance and Occupational Pensions Authority. These curves are based on market swap rates, with "credit risk adjustment". The resulting 10-year risk-free spot rates for the material currencies are given below, after the credit risk adjustment.

Figure 20: 10 year risk-free rates at 31 December 2018 (with comparison to 31 December 2017)

Currency	31 December 2018	31 December 2017	Change
British Pound	1.34%	1.19%	0.15 %
Euro	0.73%	0.80%	(0.07)%

For most non-profit annuity business, a matching adjustment is applied to the risk-free curve to discount the best estimate liability cash-flows (see Section D.2.4.3). In line with Solvency II requirements, the matching adjustment is not applied when calculating the risk margin. The matching adjustment calibration for UK shareholder annuities at 31 December 2018 allowed for 55 basis points ('bps') (2017: 52 bps) per annum of credit provision, including allowances for mismatching.

D.2.2.2 Non-economic assumptions

Persistency, mortality and expense assumptions are derived from analysis of recent historic experience data, and also reflect expected future experience. Where relevant and material, allowance is also made for the way in which policyholder behaviour is expected to vary in line with economic conditions.

Assumptions are set at realistic, best-estimate levels. If experience varies from the assumptions the result would be the Company holding less or more capital than necessary to meet its obligations.

D.2.3 Details on methodology and assumptions by lines of business

D.2.3.1 Participating business

The best estimate liability for participating business is, in most cases, calculated based on a retrospective calculation of accumulated asset shares, adjusted to reflect any future policy-related liabilities and other outgoings that cannot be charged to asset shares (for example, the excess of projected expenses over any fixed charges). Asset shares broadly reflect the policyholders' share of the participating fund assets attributable to their policies. For some business, a retrospective asset share calculation is not appropriate (for example, business where expected future benefit payments are not based on asset shares) and a prospective valuation approach is used, based on discounting expected future benefit and expense cash-flows.

Asset shares methodology, principles and practices are detailed in the Principles and Practices of Financial Management ('PPFM').

The future policy related liabilities include a market-consistent stochastic valuation of the cost of all material guarantees, options and smoothing, less any related charges. The stochastic projections allow for realistic management actions consistent with the operation of the participating funds. Examples of these management actions include:

- *Dynamic adjustments to reversionary and terminal bonus rates.* This includes adjusting reversionary bonuses to target a specified range of terminal bonus cushion at maturity, or to maintain the solvency ratio of the participating fund in stressed conditions. For terminal bonuses, smoothing rules apply, limiting the year-on-year change for the same bonus series.
- *Market value reductions.* For some accumulating with-profits policies, market value reductions may apply, subject to certain limits.
- *Dynamic investment strategy.* Switching into lower-risk assets to maintain the solvency of the own fund in stressed conditions.
- *Dynamic new business strategy.* Restricting the volume of new business written to maintain the solvency of the fund in stressed conditions.

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

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

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

At 31 December 2018, the pension mis-selling amount included within the best estimate liability was £777 million (2017: £505 million). This is stochastically determined on a discounted basis.

D.2.3.2 Non-profit annuity business

The best estimate liability for non-profit annuity business is a discounted value (including a matching adjustment where relevant) of expected future annuity payments and associated expenses. The key assumptions relate to mortality rates, including expectations of future mortality improvements, and the level of credit provisions allowed for within the matching adjustment calibration as prescribed by the European Insurance and Occupational Pensions Authority (see Section D.2.4.3).

Some index-linked non-profit annuity business contains a guarantee that the annuity payment will not reduce during periods of deflation. A simulation method (i.e. stochastic model) was used to determine the associated embedded guarantee cost.

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

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

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

D.2.3.3 Unit-linked business

The best estimate liability for these contracts reflects both the value of policyholder unit funds and the non-unit liability. The non-unit liability can be negative, and reflects the discounted value of fee income from the unit funds less allowances for expenses. Assumptions are also made for expected mortality and morbidity experience, as relevant, where the products include insurance riders.

Some unit-linked business contains a financial guarantee. A simulation method (i.e. stochastic model) is used to determine the associated guarantee cost.

D.2.3.4 Other business

For 'other business' the best estimate liability is calculated as the present value of expected future benefit payments and associated expenses less the value of expected future premium income. Assumptions are made for expected persistency and mortality/morbidity experience, as relevant.

Included within other business is an immaterial amount of non-life legacy business which is fully reinsured.

D.2.4 Long-term guarantee measures on technical provisions

D.2.4.1 Transitional measures

The Company's technical provisions at 31 December 2018 include transitional measures on technical provisions ('TMTP'), in accordance with Article 308d of Directive 2009/138/EC. The TMTP is unaudited. The impact of these transitional measure is to increase the Company's Solvency II surplus by £1,572 million (2017: £2,321 million).

The transitional measures are considered high-quality capital, and are a core part of the Solvency II reporting regime. The Company has received the necessary approvals from the Prudential Regulation Authority ('PRA') in respect of the transitional measures.

The TMTP was recalculated at 31 December 2018 following the transfer of the Hong Kong subsidiaries which caused a change in the risk profile of the business. The Solvency II Written Notice approving the recalculation was received from the PRA on 19 December 2018.

The 31 December 2018 technical provisions and own funds do not include a transitional measure on the risk-free interest rate term structure.

D.2.4.2 Volatility adjustment

The Company has not applied a Volatility Adjustment as at 31 December 2018.

This differs from 31 December 2017 when a Volatility Adjustment was applied in respect of with-profits business denominated in USD in the Hong Kong subsidiaries. These subsidiaries have now been transferred to PCAL and so PAC no longer applies a Volatility Adjustment.

D.2.4.3 Matching adjustment

The matching adjustment referred to in Article 77b of Directive 2009/138/EC has been applied to most of the Company's non-profit annuities.

An adjustment may be applied to the risk-free interest rate term structure if the conditions in Article 77b of the Solvency II Directive are met and approval has been obtained. The risk-free yield curve used to discount most of the Company's non-profit annuity liability cash-flows is increased to include a matching adjustment, as approved by the PRA. The matching adjustment is calculated by reference to the credit spreads on the assigned portfolio of assets, with deductions for the "fundamental spread" (i.e. credit risk allowance) as published by the European Insurance and Occupational Pensions Authority and for cash-flow mismatch allowances.

Separate portfolios are held for the Company's policyholder-backed and shareholder-backed non-profit annuities.

D.2.4.4 Impact of transitional measures and long-term guarantees

The impact of the transitional measures for technical provisions ('TMTP'), which is unaudited, and the matching adjustment ('MA') on the Company's Solvency II results at 31 December 2018 are shown in the table below:

Figure 21: Impact on Solvency II results of excluding the TMTP, VA and MA at 31 December 2018

	As reported in QRTs £m	Impact of removing TMTP £m	Impact of removing MA £m	Total excluding TMTP and MA £m
Technical Provisions	156,045	2,618	3,342	162,005
Basic Own Funds	13,001	(1,322)	(2,014)	9,665
Own Funds eligible to cover SCR	13,001	(1,322)	(2,014)	9,665
Solvency Capital Requirement (SCR)	9,309	250	3,128	12,687
Own Funds eligible to cover MCR	13,001	(1,322)	(2,014)	9,665
Minimum Capital Requirement (MCR)	2,327	62	782	3,171
Solvency Ratio	140%	(17)%	(46)%	76%

D.2.5 Assumption changes

Changes to the assumptions used at 31 December 2018 in the Company's calculation of technical provisions include:

- changes to best estimate annuitant longevity assumptions to reflect a more granular modelling approach at an individual level over the lifetime of the policyholder, also taking into account recent experience. The mortality improvement basis has been updated to use the default calibration of the Continuous Mortality Investigation 2016;
- market-driven changes to economic parameters, including changes to risk-free rates as shown in Section D.2.2.1;
- changes to the matching adjustment allowance to reflect market conditions at 31 December 2018;

- changes to persistency assumptions to reflect the results of the most recent experience investigation, complemented with views from internal experts on industry themes and market trends;
- changes to renewal expense and investment management expense assumptions to reflect forecast expense experience, allowing for planned transformation activity; and
- changes to investment expense assumptions to reflect changes in strategic asset allocation for some with-profits funds, which resulted in a reduction in exposure to alternative assets, and the triennial review of investment mandates, which resulted in a reduction in fees.

D.2.6 Level of uncertainty

The valuation of technical provisions relies upon the Company's best estimate of future liability cash-flows, including the projection of the future level of the solvency capital requirement in the calculation of the risk margin. These cash-flows are derived using best estimate assumptions, which are set using a combination of experience data, market data and expert judgement.

Uncertainty exists in the technical provisions as to whether the actual future cash-flows will match those expected under the Company's best estimate assumptions. Over time, experience may differ from the best estimate assumptions or the Company's forward-looking expectations may evolve, such that assumptions will be updated with a consequent change in the value of future technical provisions.

The best estimate assumptions include assumptions about future economic conditions, for example interest rates and expense inflation levels; and assumptions about future non-economic experience, for example, longevity, mortality and policyholder behaviour. Assumptions are also made about future management actions.

Each assumption is set at the Company's best estimate of future experience and approved by the Board Audit Committee. However, each assumption is by its very nature assumed and so the actual future experience is not certain.

D.2.7 Reconciling Solvency II technical provisions to the financial statements

Figure 22: Comparison of technical provisions between UK GAAP and Solvency II for the year-ended 31 December 2018

	Insurance with profit participation £m	Index-linked and unit-linked insurance £m	Other life insurance £m	Accepted life reinsurance £m	Health insurance £m	Non-life £m	Total 2018 £m	Total 2017 £m
UK GAAP liabilities[1]	112,658	21,681	27,312	5,632	(19)	142	167,406	172,378
Solvency II technical provisions[2]	94,502	12,851	42,238	6,328	(15)	142	156,045	159,771

[1] UKGAAP liabilities are as reported in the financial statements.
[2] SII technical provisions are as reported in template S.02.01.02.

The main differences in technical provisions between the UK GAAP financial statements and Solvency II are:

(a) Surplus assets in with-profits funds are not included as a liability within the technical provisions for Solvency II but are within the UK GAAP financial statements as "Fund for future appropriations" on the balance sheet.

(b) The UK GAAP liabilities are valued using a basis that includes margins for risk and uncertainty within the non-economic assumptions (mortality, persistency and expenses) as well as different economic assumptions to the Solvency II technical provisions. The method of calculation can also differ between the bases.

(c) The UK GAAP liabilities do not include an explicit risk margin as the allowance for risk is included within the non-economic assumptions. The risk margin is explicit under Solvency II. The impact of the transitional measures for technical provisions is to smooth the transition from the previous

Solvency I regime. It is run-off in a straight line over 16 years. The transitional measures for technical provisions has been offset against this explicit risk margin.

(d) The non-life UK GAAP liabilities are included in claims outstanding in the UK GAAP financial statements.

The following table details the differences between UK GAAP and Solvency II liabilities on a monetary basis:

Figure 23: Step-through from UK GAAP liabilities to Solvency II technical provisions for the year-ended 31 December 2018

	£m
UK GAAP liabilities	167,406
Amounts not recognised under Solvency II	(37)
Additional provisions under Solvency II	2,608
Adjustments to measurement basis	(13,932)
Solvency II technical provisions	156,045

Amounts not recognised under Solvency II include the present value of future profits and contract boundaries.

Additional provisions under Solvency II include the risk margin which, as discussed above, does not exist for UK GAAP. This aims to ensure that total technical provisions (the best estimate and the risk margin) are equivalent to the cost of ceding the insurance obligations to a third party. In addition, UK GAAP liabilities do not include other items such as the tax calculated on future shareholder transfers and future enhancements to asset shares in respect of non-profit business.

Adjustments to the measurement basis arise largely due to differences between UK GAAP and Solvency II assumptions and methodology as follows:

- the fund for future appropriations is included in UK GAAP but not Solvency II. This contributes £13,487 million of the total adjustments to the measurement basis;
- longevity assumptions for non-profit annuity business contain margins under UK GAAP compared to the best estimate assumptions applied under Solvency II; and
- UK GAAP liability cash flows for non-profit annuity business are valued using a discount rate derived from the yield on the corresponding assets minus a prudent allowance for defaults of 40 bps at 31 December 2018. Under Solvency II, the discount rate is expressed as a risk free yield curve plus a matching adjustment.

D.2.8 Reinsurance recoverables

The Company primarily uses reinsurance to manage insurance risk exposure, particularly in respect of longevity risk.

In the Solvency II balance sheet, the full expected cost of claims is included within the technical provisions and the corresponding reinsurance recoverables are shown as an asset.

The valuation methods and assumptions for reinsurance recoverables are consistent with the methods and assumptions for the corresponding technical provisions (see Sections D.2.1 to D2.3). The value of the reinsurance recoverable asset is the Company's best estimate of future reinsurance cash flows, where this figure allows for the probability of partial or total default by the reinsurer. In accordance with Article 61 of the Delegation Regulations, a simplified approach to calculating the counterparty default adjustment has been adopted.

The difference in the value of reinsurance recoverables between Solvency II and the UK GAAP financial statements stems from two sources:

- Reinsurers' share of value of technical provisions. This is calculated on a basis consistent with the underlying technical provisions and, for Solvency II, includes an allowance for the probability of reinsurer default; and
- Reclassification of reinsurers' share of investment contracts liabilities without discretionary participation features. For the purposes of the financial statements, the Company applies deposit accounting for investment contracts without discretionary participation features (as defined

under UK GAAP) and accordingly presents the reinsurers' share of its liabilities within investments.

The most significant reinsurance treaty covers the reinsurance of c£12 billion of non-profit annuities to Rothesay Life through a quota share arrangement. There are also several longevity swap treaties with a number of different reinsurance companies, including Hannover Re and Munich Life Re.

D.3 Valuation of other liabilities

D.3.1 Valuation of other liabilities

Other liabilities for solvency purposes are valued separately using valuation methods that are consistent with the valuation approach set out in the Solvency II Directives. Unless otherwise stated, valuation of other liabilities is carried out in conformity with UK GAAP, where this is consistent with the objectives of Solvency II.

D.3.2 Valuation bases under Solvency II compared to UK GAAP

The valuation basis of material classes of other liabilities are described below:

Debt liabilities
'Debt liabilities' includes the following line items from the Solvency II balance sheet:

- Debts owed to credit institutions; and
- Financial liabilities other than debts owed to credit institutions.

Debt liabilities in the UK GAAP financial statements are valued at amortised cost but are valued at fair value for the Solvency II balance sheet. For year ended 31 December 2018 the value under both methods was the same. The major component of debt liabilities are over-the-counter derivatives collateral creditors and obligations under securities lending.

Deferred tax liabilities
Deferred tax liabilities are calculated based upon the differences between the values given to liabilities in the Solvency II balance sheet and their values for tax purposes. The UK GAAP principles of FRS 102 section 29 are applied to calculate the extent of deferred tax applicable to those value differences. Changes in the valuation of underlying liabilities between UK GAAP and Solvency II (as described elsewhere in Section D) give rise to deferred tax value differences. Further information on deferred tax valuation differences is provided in Section D.1.2.2 above under the heading 'Deferred tax assets'.

The aggregate (£76 million) of the other valuation differences for deferred tax between UK GAAP and Solvency II represents the change in the value of the net deferred tax principally as a result of valuation changes relating to the establishment of the risk margin and movement in technical provisions.

The net deferred tax liability of £608 million principally relates to unrealised gains on investments. Tax on these gains will mainly fall due when the underlying assets are sold.

Other liabilities
Figure 24: Other liabilities for the year-ended 31 December 2018

	2018 £m	2017 £m
Provisions other than technical provisions	401	409
Pension benefit obligations	79	138
Derivatives	2,172	1,593
Insurance and intermediaries payable	598	730
Reinsurance payables	119	66
Payables (trade, no insurance)	1,432	1,927
Other liabilities	1,382	1,368
Total	**6,183**	**6,231**

Insurance and intermediaries payable, reinsurance payables, payables (trade, not insurance) and other liabilities are measured at fair value determined using alternative valuation methods that are market consistent and represent the value to settle the liabilities with the third party. Where the UK GAAP valuation is a good proxy for fair value no adjustment is made.

Provisions other than technical provisions
The provisions other than technical provisions of £401 million include a provision for review of past annuity sales after utilisation during the year of £324 million (2017: £369 million). The Company has agreed with the Financial Conduct Authority ('FCA') to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. The review is examining whether customers were given sufficient information about their potential eligibility to purchase an enhanced annuity, either from Prudential or another pension provider. A gross provision of £400 million, before costs incurred, was established at 31 December 2017 to cover the costs of undertaking the review and any related redress and following a reassessment, no change has been made in 2018. The majority of the provision will be utilised in 2019.

The ultimate amount that will be expended by the Company on the review will remain uncertain until the project is completed. If the population subject to redress increased or decreased by 10 per cent, then the provision would be expected to increase or decrease by circa 7 per cent accordingly. Additionally, in 2018, the Company agreed with its professional indemnity insurers that they will meet £166 million of claims costs, which will be paid as the Company incurs costs/redress. This income has been recognised in operating profit and on the SII balance sheet within 'trade receivables' at 31 December 2018.

Derivative liabilities
Derivative liabilities are valued using quoted prices if exchange listed, quotations from third parties or valued internally using the discounted cash flow method in line with standard market consistent valuation techniques, but are subject to independent assessment against external counterparties' valuations.

Pension benefit obligations
The Company does not have any individually material obligations in respect of defined contribution plans, other long-term employee benefits or termination benefits.

The Company has significant obligations in respect of the defined benefit pension schemes.

The majority of staff employed by the Prudential Group in the UK are members of the Prudential Group's pension schemes. The largest scheme is the Prudential Staff Pension Scheme ('PSPS'). This scheme is primarily a defined benefit scheme but no employees with employment offers after 31 July 2003 are eligible for membership of the defined benefit section of the Scheme. They are instead enrolled in the defined contribution section of the scheme.

At 31 December 2018, the underlying PSPS liabilities account for 82 per cent (2017: 82 per cent) of the aggregate liabilities of the Company's defined benefit schemes. Under FRS 102 a surplus is only recognised to the extent that the Company is able to access the surplus either through an unconditional right of refund to the surplus or through reduced future contributions relating to ongoing service, which have been substantively enacted or contractually agreed. Further, the UK GAAP financial position recorded, reflects the higher of any underlying FRS 102 deficit and any obligation for committed deficit funding where applicable. At 31 December 2018 the Company's share of the surplus of £162 million (2017: £166 million), is recognised in the statutory accounts.

Under the Solvency II basis, the FRS 102 surplus in the PSPS scheme has not been recognised.

There is also a smaller defined benefit scheme, Scottish Amicable Staff Pension Scheme ('SASPS') relating to staff formerly employed by the Scottish Amicable Life Assurance Society which the Company acquired in 1997 along with the associated scheme. The Company's share of the deficit in this scheme is £79 million (2017: £138 million) under the Solvency II basis. This includes the liability attributable to the shareholders, which is reported in another group company for UKGAAP purposes.

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

Methodology and assumptions
The FRS 102 valuation prescribes market-based assumptions for the valuation of assets and liabilities. Within the market-based framework, the FRS 102 prescribes that the discount rate for liabilities should be based on high quality corporate bonds (interpreted as corporate bonds with a credit rating of AA).

The actuarial assumptions used in determining the benefit obligations and the net periodic benefit costs for the year-ended 31 December 2018 were as follows:

Figure 25: Pension scheme actuarial assumptions

	2018 %	2017 %
Discount rate[(1)]	**2.8**	2.5
Rate of increase in salaries	**3.3**	3.1
Rate of inflation[(2)]		
Retail prices index (RPI)	**3.3**	3.1
Consumer prices index (CPI)	**2.3**	2.1
Rate of increase of pensions in payment for inflation:		
PSPS:		
Guaranteed (maximum 5%)	**2.5**	2.5
Guaranteed (maximum 2.5%)	**2.5**	2.5
Discretionary	**2.5**	2.5
SASPS	**3.3**	3.1

[(1)] The discount rate has been determined by reference to an 'AA' corporate bond index, adjusted where applicable, to allow for the difference in duration between the index and the pension liabilities.
[(2)] The rate of inflation reflects the long-term assumption for the UK RPI or CPI depending on the tranche of the schemes.

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

Underlying investments of the schemes
On the ‘economic basis’, after including the underlying assets represented by the investments in Prudential insurance policies as scheme assets, the plans’ assets at 31 December comprise the following investments:

Figure 26: Plan assets

	2018		2017	
	£m	%	£m	%
Equities				
UK	**8**	**0%**	16	0%
Overseas	**204**	**5%**	363	7%
Bonds				
Government	**4,943**	**66%**	5,476	68%
Corporate	**1,932**	**20%**	1,659	16%
Asset-backed securities	**263**	**2%**	164	2%
Derivatives	**97**	**2%**	182	3%
Properties	**207**	**2%**	200	1%
Other assets	**227**	**3%**	236	3%
Total value of assets	**7,881**	**100%**	8,296	100%
Of which relate to PSPS	**7,075**		7,474	
Of which relate to SASPS	**806**		822	

Contingent liabilities

Under UK GAAP, contingent liabilities (as determined in accordance with FRS 102) are disclosed but not recognised. For the Solvency II balance sheet, contingent liabilities (under the same definition as UK GAAP) are required to be recognised where they are material. The material contingent liabilities are recognised on Solvency II balance sheet as the probability-weighted average of future cash-flows required to settle the contingent liability over the lifetime of that liability, discounted at a relevant risk-free interest rate structure.

A contingent liability of £31 million at 31 December 2018 (2017: £31 million) in relation to a legal case was recognised on the Solvency II balance sheet. The claim relates to a financial restructuring carried out by a borrower in one of the Company's investments. The Court handed down judgement in favour of the Company in November 2017. However the claimant has exercised their right to appeal that decision. The outcome of litigation is always uncertain but the Company believes it has good grounds to defend this claim and the outcome will not have a material adverse effect on the Company's financial condition.

Leases

There are no material liabilities recognised on the Solvency II balance sheet arising as a result of operating and finance leasing arrangements of the Company. Further information on the leasing arrangements of the Company is disclosed in Section A.4.2.

D.4 Alternative methods for valuation

The use of alternative methods for valuation by the Company are discussed in Sections D.1 to D.3 above.

The Group has developed Group-wide Independent Price Verification procedures - which covers all investment asset classes owned by the Business Units of the Group, including the Company, and set minimum requirements for the governance surrounding valuation pricing. These standards require that processes are established to verify the accuracy and independence of model inputs and market prices provided by third parties. Where mark to market valuations are not available from independent price sources, the Independent Price Verification standards set minimum requirements for alternative methodologies including mark to model valuations. The Independent Price Verification standards require the documentation and monitoring of all assumptions, inputs and any mathematical modelling, using market observable standards and inputs where possible.

Valuation uncertainty refers to the variability of the fair value measurement that exists at any given reporting date/time for a financial instrument or portfolio of positions. The Independent Price Verification standards require documentation of the process for assessing valuation uncertainty, including the controls surrounding valuation models and an understanding of the model assumptions and limitations.

The Group’s valuation policies, procedures and analysis for instruments valued using alternative valuation methods with significant unobservable inputs are overseen by business unit committees as part of the Group’s wider financial reporting governance processes. The procedures undertaken include approval of valuation methodologies, verification processes, and resolution of significant or complex valuation issues. In undertaking these activities, the Group makes use of the extensive expertise of its asset management functions. In addition, the Group has minimum standards for independent price verification to ensure valuation accuracy is regularly independently verified. Adherence to this policy is monitored across the business units.

D.5 Any other information

There is no other material information regarding the Company's valuation of assets and liabilities for solvency purposes other than those disclosed in the sections above.

E Capital management

E.1 Own funds

E.1.1 Objectives, policies and processes for managing own funds

The Company manages its Solvency II own funds as its measure of capital. The Company's own funds at 31 December 2018 in the regulatory template are £13,001 million. A reconciliation from the Solvency II capital position published in the Financial Statements to the Solvency II capital position disclosed in the regulatory template is provided in Section E.1.2 below. The Company's basic, available and eligible own funds to cover the Company's solvency capital requirement and minimum capital requirement at 31 December 2018 are shown in Section E.1.3 below.

The Company manages its Solvency II capital to ensure that sufficient own funds are available on an ongoing basis to meet regulatory capital requirements.

The Company prepares a projected capital position as part of its business planning process. The business plan is prepared annually on a rolling basis and covers a three-year period. There were no material changes in the objectives, policies or processes for managing the Company's own funds during the year.

E.1.2 Shareholder Solvency II capital position

Reconciliation of Solvency II capital position published in the Annual Report to the QRTs

The Company disclosed the estimated Solvency II capital surplus, as at 31 December 2018 in the Company's 2018 Financial Statements of £3,691 million, consistent with the disclosures in this document. This includes the impact of a recalculated TMTP and was calculated as being own funds of £13,001 million less SCR £9,309 million.

E.1.3 Analysis of the components of own funds

The following components make up the Company's basic, available and eligible own funds amounts. The Company has no ancillary own funds.

Figure 27: Analysis of components of own funds for the year-ended 31 December 2018

	Total 2018 £m	Tier 1 unrestricted £m	Total 2017 £m
Ordinary share capital[(b)]	330	330	330
Surplus funds[(c)]	10,642	10,642	10,304
Reconciliation reserve [(d)]	2,029	2,029	9,878
Total eligible own funds to meet the SCR[(a)]	13,001	13,001	20,512
Total eligible own funds to meet the minimum MCR [(a)]	**13,001**	**13,001**	**20,512**

(a) As at 31 December 2018, the Company has no ancillary own funds and hence the Company's basic own funds are equal to the total available own funds. The eligible own funds are derived by applying Solvency II tiering limits to the tiered available own funds.

(b) Ordinary share capital
The Company's ordinary share capital represents the nominal value of 25p for each fully paid equity share issued.

(c) Surplus funds
Surplus funds arise from the Company's with-profit funds (i.e. surplus funds arise from certain of the Company's ring-fenced funds). The value of surplus funds reported

represents the excess of assets over liabilities (excluding the risk margin) of those ring-fenced funds after deducting the present value of the expected future shareholder transfers (net of any related tax borne by the funds). Having considered the features of Tier 1 own fund instruments set out in Article 71 of the Commission Delegated Regulation (EU) 2015/35 and the guidance in the PRA Supervisory Statement SS13/15 (Solvency II: surplus funds) Prudential has classified surplus funds under Tier 1.

In accordance with the template S.23.01.01 (Own Funds) presentation requirements, the value of surplus funds reported on the template is prior to ring-fencing related restrictions being applied. The related restrictions are included as a deduction in the Reconciliation Reserve under "Restrictions applied to own funds due to ring-fencing". As such, the contribution of surplus funds towards the Company's own funds is lower than that reported on the face of the Own Funds template.

(d) Reconciliation reserve

The reconciliation reserve represents the residual of excess of asses over liabilities after deducting (i) equity share capital comprising ordinary share capital and (ii) surplus funds and the restriction applied to own funds due to ring fencing. The reduction in reconciliation reserve from £9,878 million to £2,029 million is mainly due to the transfer of Hong Kong subsidiaries, partially offset by surplus generated in the period, along with dividends paid.

The following table shows the reasons for the changes in the Own Funds between 31 December 2017 and 31 December 2018 and prior year comparatives.

Figure 28: Analysis of components of own funds for the year-ended 31 December 2018

	2018
	£m
Own Funds at 31 December 2017	**20,512**
Surplus arising in respect of Hong Kong subsidiaries prior to transfer	867
Changes to corporate structure - transfer of Hong Kong subsidiaries	(7,761)
Impact of partial sale of annuity portfolio	(234)
Own Funds adjusted for transfer of the Hong Kong subsidiaries and partial sale of the annuity portfolio	**13,384**
Underlying operating experience	1,358
Management actions	403
Operating experience	1,761
Non-operating experience (including market movements)	(1,923)
Other capital movements	
Foreign currency translation impacts	—
Dividends paid	(330)
Deferred tax assets/liabilities	109
Own Funds at 31 December 2018	**13,001**
Change in own funds	**(7,511)**

This table shows the movement in own funds as follows:

- The Hong Kong Subsidiaries contributed a decrease in own funds of £7,761 million. The own funds decrease of £6.9 billion in section A.1.4.2 is based on the 31 December 2017 valuation and consists of £7,761 million as above less the own funds increase of £867 million arising from the Hong Kong subsidiaries in 2018 prior to transfer.
- Underlying operating experience has increased own funds by £1,358 million during 2018. This mainly reflects the unwind of in-force business, a change in longevity assumptions on annuity business, the contribution from new business and the return on surplus assets.
- The impact of management actions of £403 million is mainly due to the transfer of lower yielding assets from the annuity portfolios to the shareholder fund that are no longer required to support the best estimate liabilities; and the insurance recoverables related to an insurance policy in connection with the Thematic Review of Annuity Selling Practices.

- Non-operating experience have decreased own funds by £1,923 million. This reflects market movements, the recalculation of the transitional measures and refinements to the with-profits model.
- Payment of dividends totalling £330 million to Prudential Group.
- Deferred tax assets have increased by £109 million.

E.1.4 Reconciliation of UK GAAP shareholder's equity to Solvency II for the year-ended 31 December 2018

The 'excess of assets over liabilities' on the Solvency II balance sheet is not equivalent to own funds as a number of adjustments are made on the own funds template to restrict the valuation.

The reconciliation of the Company's UK GAAP shareholders' equity to the excess of assets over liabilities on the Solvency II balance sheet and to the Solvency II eligible own funds value of the Company is shown in Figure 29 below:

Figure 29: Analysis of components of own funds for the year-ended 31 December 2018

	2018 £m	2017 £m
UK with-profits funds		
Fund for future appropriations	13,487	13,581
Value of shareholder transfers	(2,394)	(2,731)
Impact of risk margin (net of TMTP)	(1,005)	(726)
Other valuation differences	(451)	(546)
With Profits Ring Fenced Fund - Estimated Solvency II Own Funds	**9,637**	**9,578**
Other long term business		
Shareholders' equity	6,877	15,611
Impact of risk margin (net of TMTP)	(581)	(838)
Value of shareholder transfers	2,394	3,817
Asset valuation differences	250	(2,549)
Other valuation differences	(193)	(29)
Increase in value of net deferred tax liabilities (resulting from valuation differences above)	75	133
Excess of assets over liabilities as recorded in the Solvency II balance sheet	**18,459**	**25,723**
Restrictions on ring-fenced funds	(5,458)	(5,211)
Eligible own funds at 31 December 2018	**13,001**	**20,512**

E.1.5 Restrictions

(Unaudited)

Restriction to own funds arising from ring-fenced funds

The Company has considered the specific provisions of national law, insolvency law, contract law and product regulation of the insurance subsidiary's jurisdiction of operations in determining the appropriate treatment of ring-fenced funds.

For ring-fenced funds, own funds are adjusted to reflect that the funds have a reduced capacity to fully absorb losses on a going-concern basis due to their lack of fungibility within the insurance company. The contribution to own funds from a ring-fenced fund is restricted such that the contribution to own funds from the ring-fenced fund is equal to the notional SCR for that ring-fenced fund. The impact of ring-fenced funds on the Company's solvency position in shown in Figure 29 above.

E.2 Solvency Capital Requirement ('SCR') and Minimum Capital Requirement ('MCR') *(Unaudited)*

E.2.1 Overview

The SCR is the amount of capital the PRA requires the Company to hold. It is calculated based on ensuring that the Company has enough capital to meet its obligations in the event of a 1-in-200 year risk scenario occurring.

For the purpose of Solvency II regulatory reporting and disclosures, risk management, and calculation of any free surplus generation, the Company has approval to use an internal model for calculating the solvency capital requirement ('SCR'). The assets and liabilities are valued on a Solvency II basis.

The SCR decreased due to the transfer of the Hong Kong subsidiaries to PCAL which decreased the Company's Solvency II capital requirement by £2.7 billion.

E.2.2 Components of SCR

At 31 December 2018, the SCR was £9,309 million (2017: £14,397 million).

Figure 30 below shows the undiversified SCR by risk components and the benefit of diversification in relation to the Company at 31 December 2018. A comparison column at 31 December 2017 is included.

Figure 30: SCR for the Company at 31 December 2018

Risk component	2018 £m	2017 £m
Interest rate risk	1,846	5,633
Equity risk	2,771	4,464
Property risk	1,414	1,404
Spread risk	5,148	8,161
Concentration risk	—	—
Currency risk	2,024	3,110
Diversification within market risks	(5,632)	(8,722)
Other counterparty risk	343	305
Mortality risk	9	177
Longevity risk	3,527	5,205
Disability-morbidity risk	15	122
Mass lapse	301	1,072
Other lapse risk	1,039	736
Expense risk	1,463	2,414
Life catastrophe	23	79
Diversification within life underwriting risks	(3,126)	(4,771)
Other non-life underwriting risk	—	4
Operational risk	1,466	1,474
Loss-absorbing capacity of deferred tax	(1,078)	(1,546)
Other adjustments	—	351
Total undiversified components	**11,496**	**19,672**
Diversification between market and underwriting risks	**(2,186)**	**(5,275)**
Total diversification SCR	**9,309**	**14,397**

The material movements in the undiversified risk capital shown in the table above are due to the following:

- Transfer of the Hong Kong subsidiaries to PCAL;
- Partial reinsurance of annuity portfolio;
- Modelling refinements, in particular on with-profits business;
- Movements in equity markets; and
- Increase in risk-free yields and spreads.

Overall the total undiversified capital requirement has fallen due to the sale of the Hong Kong subsidiaries and the partial reinsurance of the annuity business. The largest movements in relation to the transfer of Hong Kong subsidiaries were in interest rate risk, equity risk and lapse risk.

The minimum capital requirement ('MCR') is a formulaic calculation, which is subject to a cap and a floor that are both expressed relative to the SCR. At 31 December 2018, the Company's MCR was £2,327 million. The inputs used to calculate the MCR are detailed in Quantitative Reporting Template S.28.02.01.

The MCR is currently 25 per cent of the SCR (2017: 25 per cent).

E.3 Use of the duration-based equity risk sub-module in the calculation of the SCR
(Unaudited)

The Company has not used the duration-based equity risk sub-module in the calculation of its SCR as it is a standard formula approach and not applicable to an internal model firm.

E.4 Differences between the standard formula and the internal model
(Unaudited)

E.4.1 Overview

The Company's internal model, which is calibrated to the rules and requirements of the Solvency II Directive, is a key risk management tool and refers to the collection of systems and processes used to identify, monitor and quantify risks for the purpose of calculating the Solvency II solvency capital requirement and economic capital requirements. This is a risk-based measure and, compared to the standard formula (as described below), has the advantage of better reflecting the specifics of the Company's business and risks.

The standard formula capital refers to the capital that is calculated in line with the standard formula rules provided by the Solvency II Directive. Even though the standard formula, as part of Solvency II, represents a risk-based measure, it is based on a set of prescribed parameters, calibrated for European insurers and therefore it does not fully reflect the characteristics of the Company and the specific structure and risks the Company is exposed to.

The Company's internal model is used in areas where risk-based decision making or risk-related considerations are required, such as capital management, investment strategy, product development and management.

E.4.2 Internal model application

The Company applied to use an internal model in late June 2015. In early December 2015 the application was approved by the Prudential Regulation Authority ('PRA'). This was followed by an application to the PRA for a "major model change" to the internal model in 2016, which was approved by the PRA to be effective for full year 2016 reporting onwards. During 2018 the Company applied to the PRA for a further "major model change" to the internal model, which was approved by the PRA and was implemented from 2018 Q2 reporting onwards.

The changes during 2018 comprise of the following:

- Revisions to the calibration of Interest Rate Risk to remove floors in the distribution;
- Revisions to the calibration and modelling of Longevity Trend Risk ('LTR') and a reduction in Current Mortality Risk ('CMR') / LTR intra-longevity correlation.

The Company's internal model is described as "partial" because the Group's US insurance companies are aggregated into the Group SCR using method 2: deduction and aggregation. Integration techniques are not required.

As required in Article 101 of Directive 2009/138/EC, the solvency capital requirement from the approved internal model is calculated as the value-at-risk of the basic own funds of an (re)insurance undertaking at a confidence level of 99.5 per cent over a one-year period. The main risk categories allowed for in the internal model are shown in Section E.2.2. Within these categories, underlying "risk drivers" are specified as the result of an annual risk identification process. A model is defined and calibrated for each underlying risk driver and these are combined with an appropriate dependency structure and simulated to generate multiple thousands of combined risk scenarios. These risk scenarios are applied to all the assets and liabilities of the Company (for each entity within the scope of the internal model) to generate a wide range of possible outcomes. For simplicity, and to avoid circularity, the risk margin is held constant in all these risk scenarios. The resulting probability distribution is used to calculate the internal model solvency capital requirement, by subtracting the 99.5th worst percentile outcome from the unstressed balance sheet.

The data used in the internal model covers the following:
- liability data;
- asset data
- finance data;
- operational risk data;
- policyholder data;
- data used in setting assumptions, including demographic, economic and other; and
- other relevant data required by the internal model and technical provisions.

The quality of the data is subject to the internal model data quality framework to ensure the accuracy, completeness, appropriateness and timeliness of the data.

E.4.3 Internal model vs standard formula

Key differences between the calculation of the internal model SCR and the standard formula SCR include:
- Whereas the standard formula stresses and correlations are prescribed, the internal model risk scenarios reflect the Company's specific risk profile and are derived from a combination of data analysis and expert judgement, subject to the internal model tests and standards required by the Solvency II Directive (see further detail in Figure 31 below).
- Although the same broad risk categories are used to group risk drivers in the internal model, the internal model risk drivers within each category are typically much more granular than the broad risk categories considered under the standard formula. For example, the internal model risk drivers typically vary by country, as well as by other attributes of the risk, whereas many of the standard formula stresses do not vary by country.
- The internal model also covers some risks that are not included in the standard formula (for example, equity implied volatility risk, interest rate implied volatility risk and government bond spread risk).
- The internal model SCR is derived by combining underlying risk drivers together into combined stress scenarios, and then ranking the outcomes of applying these stress scenarios to the Company's balance sheet to derive the 99.5th worst percentile outcome. Conversely, the standard formula SCR is derived by calculating the impact on the balance sheet of each prescribed stress separately and then aggregating these outcomes using prescribed correlation matrices. Therefore, the internal model allows for the impact on the balance sheet of combinations of risks occurring together, whereas the standard formula only considers each risk in isolation.
- The internal model allows for the matching adjustment ring-fence to vary in each risk scenario, reflecting changes in the value of the corresponding liabilities. Therefore, diversification is allowed for between risks inside and risks outside the matching adjustment portfolio. Conversely, because the standard formula does not consider the impacts of combinations of risks occurring together, it requires that no diversification is recognised between risks inside the matching adjustment portfolio and risks outside the matching adjustment portfolio.

Figure 31: Overview of standard formula and internal model differences

Risk category	Standard formula	Internal model
Equity	Stresses vary between "Type 1" (listed EEA and OECD stocks) and "Type 2" (other countries, unlisted equities and alternative equity investments). A symmetric adjustment is applied to the level of stress to smooth out significant movements in markets close to the calculation date.	The model includes more granular stresses with calibrations set for each main equity benchmark index. At least one equity index is calibrated for each relevant global economy. Private equity, infrastructure equity and hedge funds are modelled using specific calibrations. Equity implied volatility is also modelled. No symmetric adjustment is applied.

Credit	For corporate bonds, loans and non-exempt sovereign bonds, credit risk is modelled by stressing credit spreads, with stresses varying by rating and duration bucket. European sovereign bonds are exempt from stress. Stresses on assets with an element of securitisation with no credit rating. The matching adjustment is allowed for by a factor-based reduction of the spread stresses by rating.	Credit spreads, ratings migrations, defaults and fundamental spreads (for the UK matching portfolio) are all explicitly modelled. The spread stresses vary by credit rating, with calibrations differentiated by economy, product and duration bucket where appropriate. Internal credit assessments are used for bonds and loans without an agency rating and to uplift stresses for assets where structuring introduces additional risk. Spread stresses are applied to sovereign bonds, taking into account the credit risk of the issuing government. The matching adjustment is calculated dynamically based on the bond yields and fundamental spread being modelled in each risk scenario.
Yields	Interest rate stresses are defined as bi-directional stresses to the base risk-free curve which vary by term but not by country.	Stresses are calibrated for each relevant global economy, and stresses to the shapes of risk-free yield curves are modelled using an industry-standard 'principle component' methodology. Stressed curves are re-extrapolated beyond the last liquid point for each economy using the methodology specified by EIOPA. Interest rate implied volatility and inflation risk are also modelled.
Property	There is a single property stress applied globally to the value of all assets classified as property.	Property stresses are differentiated by type of property, with separate calibrations for commercial and residential property. The model also separates the risks relating to contractually fixed rental income from that relating to capital growth where this is relevant for the matching adjustment.
Currency	A pair of up and down stresses is applied to the non-GBP net asset value in each business, and then aggregated. This approach also implicitly captures any asset-liability currency mismatch in each country.	A calibration is derived for each currency relative to GBP. Currency outcomes are simulated and used to translate all assets and liabilities into sterling in each risk scenario, thereby including the effect of currency "translation" as well as asset-liability currency mismatches within countries.
Concentration	The capital charge is based on the relative size of individual exposures as a proportion of the overall asset portfolio. Some non-EEA sovereigns are included, depending on their credit rating.	A similar approach is used as for the standard formula, with a more risk-based approach adopted for Asia sovereigns.
Counterparty default risk	Counterparty default risk is calculated taking into account the loss-given-default and probability of default, using fixed factors. Separate parameters and different aggregation approaches are applied for Type 1 exposures (e.g. derivatives, reinsurance, deposits) compared to Type 2 exposures (e.g. receivables from intermediaries).	A stochastic portfolio model (calibrated by credit rating) is used to capture counterparty risk, allowing for stochastic default and recovery rates. The model allows for counterparty exposures to increase under stressed conditions arising from other market and insurance risks.

Lapse	Policyholder lapse rates are stressed in both directions and a mass lapse stress is also applied. The capital charge is based on the largest of these impacts. The stresses are fixed for all countries and products (except for "group policies" which have a higher capital charge).	The lapse calibration is more granular and includes stresses to lapse assumptions and mass lapses. The stresses vary by product type as appropriate.
Longevity	A downward stress to mortality rates is applied to all relevant business.	The longevity calibration is more granular and includes stresses to base mortality rates and longevity trend assumptions separately. Calibrations are differentiated by gender and by different blocks of business, as appropriate.
Mortality & Life catastrophe	An increase in best estimate mortality rates and an instantaneous catastrophe risk stress are applied to all relevant business.	The mortality calibration allows for stresses to both best estimate mortality rates and catastrophe risks.
Morbidity	An increase in long-term morbidity rates is applied, including a reduction in morbidity recovery rates. The same stresses apply for all relevant business.	An increase to the best estimate morbidity rates for all future years.
Expense	Both the level of expenses and level of expense inflation are stressed under the standard formula. The same stresses apply to all business.	Expense level and expense inflation risks are modelled, with stresses calibrated by product type where appropriate.
Operational	Operational risk is calculated using a factor based approach applied to premiums, technical provisions and unit linked expenses.	Individual operational risks are assessed bottom-up, and modelled using a frequency-severity model. These are combined with correlation assumptions to produce aggregate probability distributions of potential operational losses.

E.5 Non-compliance with the MCR and the SCR

The Company's SCR and MCR have been met during 2018.

E.6 Any other information

There is no other material information regarding the Company's capital management other than those disclosed in the sections above.

Appendix A - List of subsidiaries and related undertakings

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

(i) Direct subsidiary undertakings

Investment

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

PPMC First Nominees Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Investment (Luxembourg) 2 S.à r.l.	Ordinary shares	100%	Luxembourg	34-38, Avenue de la Liberté, L-1930, Luxembourg
Prudential Loan Investments SCSp	Limited partnership interest	100%	Luxembourg	1, Rue Hildegard von Bingen, L-1282 Luxembourg
Prudential Properties Trusty Pty Limited	Unclassified Shares	100%	Australia	Pricewaterouse Coopers, Level 1, Darling Park Tower 2, 201 Sussex Street, Sydney, NSW 2000, Australia
Prudential Property Investments Limited	Ordinary Shares and Redeemable Preference Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 1 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 2 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Real Estate Investments 3 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prutec Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
PVM Partnerships Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Sealand (No 1) Limited	Ordinary Shares	100%	Jersey	Lime Grove House, Green Street, St Helier, Jersey, JE1 2ST
Sealand (No 2) Limited	Ordinary Shares	100%	Jersey	Lime Grove House, Green Street, St Helier, Jersey, JE1 2ST
Smithfield Limited	Has both £1.00 Ordinary Shares and $1.00 Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Three Snowhill Birmingham SARL	Ordinary Shares	100%	Luxembourg	5, rue Guillaume Kroll, L-1882, Luxembourg
Two Snowhill Birmingham SARL	Ordinary shares	100%	Luxembourg	5, rue Guillaume Kroll, L-1882, Luxembourg
Wessex Gate Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Westwacker Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK

Insurance

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

Pension

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

Holding company

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

Mortgage lending

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

Financing

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

Service

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

In liquidation

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

Dormant

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

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

Investment

Name	Classes of Shares held	Proportion held	Country of Incorporation	Address
ANRP II (AIV VI FC), L.P.	Limited Partnership Interest	37%	Cayman Islands	Walkers Corporate Limited, Cayman Corporate Centre, 27 Hospital Road, George Town KY 9008, Cayman Islands
BWAT Retail Nominee (1) Limited	A Ordinary Shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
BWAT Retail Nominee (2) Limited	A Ordinary Shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Carraway Guildford (Nominee A) Limited	Ordinary Shares	100%	Jersey	IFC 5, St Helier, JE1 1ST, Jersey
Carraway Guildford (Nominee B) Limited	Ordinary Shares	100%	Jersey	IFC 5, St Helier, JE1 1ST, Jersey
Carraway Guildford Investments Unit Trust	Ordinary Shares	100%	Jersey	13 Castle Street, St Helier, Jersey, JE4 5UT
Centaurus Retail LLP	Limited Partnership Interest	50%	United Kingdom	40 Broadway, London, SW1H 0BU, UK
Centre Capital Non-Qualified Investors IV AIV Orion, L.P.	Limited partnership interest	46%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors IV AIV-ELS, L.P.	Limited partnership interest	46%	USA	2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors IV, L.P.	Limited partnership interest	45%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
Centre Capital Non-Qualified Investors V AIV-ELS LP	Limited partnership interest	37%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA

Centre Capital Non-Qualified Investors V LP	Limited partnership interest	33%	USA	Corporation Service Company, 2711 Centreville Road, Suite 400, Wilmington, DE, 19808, USA
CF Prudential European QIS Fund	Ordinary Shares	98%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
CF Prudential Japanese QIS Fund	Ordinary Shares	98%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
CF Prudential North American QIS Fund	Ordinary Shares	99%	United Kingdom	135 Bishopsgate, London EC2M 3UR, UK
CF Prudential Pacific Markets Trust Fund	Ordinary Shares	98%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
CF Prudential UK Growth QIS Fund	Ordinary Shares	99%	United Kingdom	17 Rochester Row, London, SW1P 1QT, UK
CF UK Growth Qualified Investor Scheme	Ordinary Shares	99%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Cribbs Causeway Merchants Association Ltd	Limited by Guarantee	Membership is fluid, therefore there is no fixed percentage interest	United Kingdom	Management Offices, The Mall at Cribbs Causeway, Bristol BS34 5DG
Eastspring Investments - Asia Pacific Equity Fund	Ordinary Shares	97%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Local Bond Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Smaller Companies Fund	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Asian Total Return Bond Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Developed and Emerging Asia Equity Fund	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Global Emerging Markets Dynamic Fund	Ordinary shares	93%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - US Equity Income Fund	Ordinary shares	99%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments - Japan Equity Fund	Ordinary shares	90%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
Eastspring Investments SICAV-FIS Africa Equity FUND	Ordinary shares	100%	Luxembourg	26, Boulevard Royal, L-2449, Luxembourg
European Specialist Investment Funds - M&G Total Return Credit Investment Fund	Ordinary shares	26%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
Folios III Designated Activity Company	Ordinary Shares	60%	Ireland	Fourth Floor, 76 Lower Baggot Street, Dublin 2
Infracapital Partners LP	Limited partnership interest	33%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Infracapital Partners II LP	Limited partnership interest	26%	United Kingdom	Governor's House, Laurence Pountney Hill, London, EC4R 0HH, England

MCF S.r.l.	Ordinary shares	45%	Italy	Via Montenapoleone 29, Milan
M&G Absolute Return Bond Fund Total	Ordinary Shares	42%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Asia Property Fund	A Class Shares	54%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G Corporate Bond Fund	Ordinary shares	31%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Dividend Fund	Ordinary shares	58%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G European Credit Investments Fund	Ordinary Shares	82%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
M&G European High Yield Credit Investments Fund	Ordinary Shares	100%	Luxembourg	80, route d'Esch, L-1470, Luxembourg
M&G European Property Fund SICAV-FIS	Ordinary Shares	50%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G European Secured Property Income Fund	Units	24%	Luxembourg	34-38 Avenue de la Liberté, L-1930, Luxembourg
M&G European Select Fund	Ordinary Shares	42%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Gilt & Fixed Interest Income Fund	Ordinary shares	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Global Convertibles Fund	Ordinary Shares	59%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G (Lux) European Strategic Value Fund	Ordinary Shares	79%	Luxembourg	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Positive Impact Fund Total	Ordinary Shares	52%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
M&G Real Estate Debt Finance VI Designated Activity Company	Ordinary Shares	46%	Ireland	4th Floor, 76 Lower Baggot Street, Dublin 2, D02 Ek81
M&G UK Property Fund	Ordinary Shares	100%	Luxembourg	16, Boulevard Royal, L-2449, Luxembourg
M&G UK Residential Property Fund	Limited Partnership Interest	58%	Luxembourg	34-38, avenue de la Liberté, L-1931, Luxembourg
M&G UK Companies Financing Fund II LP	Limited partnership interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Old Kingsway, LP	Limited Partnership Interest	99%	USA	251 Little Falls Drive, Wilmington, DE 19808, USA
PPM America Private Equity Fund III LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund IV LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund V LP	Limited Partnership Interest	50%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM America Private Equity Fund VI LP	Limited Partnership Interest	40%	USA	874 Walker Road, Suite C, Dover, DE 19904, USA
PPM Core Plus Fixed Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America

PPM Credit Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Funds - PPM Floating Rate Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM High Yield Core Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Small Cap Value Fund	Ordinary Shares	95%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
PPM Strategic Income Fund	Ordinary Shares	99%	USA	C/O PPM America, Inc., 225 West Wacker Drive, Suite 1200, 60606, Chicago, United States of America
Property Partners (Two Rivers) Limited	Ordinary Shares	50%	United Kingdom	Bow Bells House, 1 Bread Street, London, EC4H 9HH, UK
Prudential Credit Opportunities SCSp	Ordinary shares	100%	Luxembourg	1, rue Hildegard von Bingen, L - 1282, Luxembourg
Prudential Dynamic 10-40 Portfolio	Ordinary Shares	29%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 20 - 55 Portfolio	Ordinary Shares	34%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 40-80 Portfolio	Ordinary Shares	35%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 0-30 Portfolio	Ordinary Shares	25%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic 60-100 Portfolio	Ordinary Shares	30%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Dynamic Focused 20 - 55 Portfolio	Ordinary Shares	38%	United Kingdom	17 Rochester Row, London SW1P 1QT, UK
Prudential Equity Release Mortgages Limited	Ordinary Shares	100%	United Kingdom	Governors House, Laurence Pountney Hill, London, EC4R 0HH
Prudential Greenfield LP	Limited partnership interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential M&G UK Companies Financing Fund LP	Limited partnership interest	34%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Limited Partnership	Limited Partnership Interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Nominee 1 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate Nominee 2 Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential UK Real Estate General Partner Limited	Ordinary Shares	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
Prudential Loan Investments 1 S.à.r.l.	Ordinary Shares	100%	Luxembourg	1, Rue Hildegard von Bingen, L-1282 Luxembourg

Randolph Street LP	Limited Partnership Interest	100%	USA	2711 Centreville Road, Suite 400, Wilmington, DE 19808, USA
Sectordate Limited	Ordinary Shares	33%	United Kingdom	1st Floor Cavendish House 39 Waterloo Street Birmingham, B2 5PP
Selly Oak Shopping Park Limited Partnership	Limited Partnership Interest	100%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
SMLLC L.L.C.	Limited Partnership Interest	100%	USA	251 Little Falls Drive, Wilmington, DE 19808, USA
St Edward Homes Limited	Ordinary Shares	50%	United Kingdom	Berkeley House, 19 Portsmouth Road, Cobham, Surrey KT11 1JG, UK
Silverfleet Capital 2004 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2005 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2006 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2009 LP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital 2011-2012 GPLP	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
Silverfleet Capital II WPLF	Limited Partnership Interest	100%	Guernsey	1 Royal Plaza, St Peters Port, Guernsey, GY1 2HL
The Car Auction Unit Trust	Ordinary shares	50%	Guernsey	Dorey Court, Admiral Park St Peter Port GY1 3BG, Guernsey
The Heights Management Company Limited	Limited by Guarantee	50%	United Kingdom	Laurence Pountney Hill, London, EC4R 0HH, UK
The St Edward Homes Partnership	Limited Partnership Interest	50%	United Kingdom	Berkeley House, 19 Portsmouth Road, Cobham, Surrey KT11 1JG
The Strand Property Unit Trust	Limited Partnership Interest	50%	Jersey	Liberte house, 19-23 La Motte Street, St Helier, Jersey, JE2 4SY
The Two Rivers Trust	Ordinary shares	50%	Jersey	Liberte house, 19-23 La Motte Street, St Helier, Jersey, JE2 4SY
Wynnefield Private Equity Partners II, LP	Limited Partnership Interest	99%	USA	1209 Orange Street, Wilmington, DE 19801, USA

In liquidation

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

Financing

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

QIS Waiver

The Financial Conduct Authority, on the application of The Prudential Assurance Company Limited (the firm), made a direction in October 2018 under section 138A of the Financial Services and Markets Act 2000. The effect of the direction is to enable the firm to contract to pay benefits under linked long term contracts relating to;

(i) Ex-Prudential Holborn Life Limited ('PHL') funds in The Prudential Assurance Company Limited ('PAC') (Prudential European, Prudential International, Prudential Managed, Prudential Strategic Growth, Prudential Japanese, Prudential North American and Prudential Equity (Life only);

(ii) Ex-Scottish Amicable Life ('SAL') funds in PAC (Prudential European, Prudential International, Prudential Managed, Prudential Japanese, Prudential North American and Prudential Equity (Life only);

(iii) Ex-Scottish Amicable Life ('SAL') funds in PAC (Prudential European, Prudential International, Prudential Managed, Prudential Japanese, Prudential North American and Prudential Equity (Pension only);

(iv) Ex-M&G funds in PAC (Pru Equity Pension fund (ex M&G), Pru Equity Life fund (ex M&G), Pru Managed life fund (ex M&G) Pru Managed pension fund (ex M&G) and Pru Personal Pension fund (ex M&G) (Life & Pension); and

(v) PAC fund (Prufund Managed Fund) which are themselves determined, either wholly or partly, by reference to units in the CF Prudential European QIS Fund, CF Prudential Japanese QIS Fund, CF Prudential North American QIS Fund, and CF Prudential UK Growth QIS Fund provided that each of these funds comply with the requirements of provisions implementing the Directive 2009/65/EC or would do if they were subject to those provisions and with certain other conditions.

Statement of directors' responsibilities

The Directors of The Prudential Assurance Company Limited acknowledge their responsibility for preparing the Solo SFCR in all material respects in accordance with the PRA rules and Solvency II Regulations.

The directors are satisfied that:

(a) throughout the financial year to 31 December 2018, the Company has complied in all material respects with the requirements of the PRA rules and the Solvency II Regulations as applicable at the level of the Company; and

(b) it is reasonable to believe that in respect of the period from 31 December 2018 to the date of the publication of the SFCR, the Company has continued to comply and therefore will continue to comply for the remainder of the financial year to 31 December 2019.

Signed on behalf of the Board of Directors

C Bousfield
Director
16 April 2019

Independent Auditor's Report

Report of the external independent auditor to the Directors of The Prudential Assurance Company Limited (‘the Company’) pursuant to Rule 4.1 (2) of the External Audit Chapter of the PRA Rulebook applicable to Solvency II firms

Report on the Audit of the Relevant Elements of the Solvency and Financial Condition Report

Opinion

Except as stated below, we have audited the following documents prepared by The Prudential Assurance Company Limited as at 31 December 2018:

- The ‘Valuation for solvency purposes’ and ‘Capital Management’ sections of the Solvency and Financial Condition Report of The Prudential Assurance Company Limited as at 31 December 2018, (‘**the Narrative Disclosures subject to audit**’); and

- Company templates S02.01.02, S12.01.02, S17.01.02, S22.01.21, S23.01.01 and S28.02.01 (‘**the Templates subject to audit**’).

The Narrative Disclosures subject to audit and the Templates subject to audit are collectively referred to as the ‘**Relevant Elements of the Solvency and Financial Condition Report**’.

We are not required to audit, nor have we audited, and as a consequence do not express an opinion on the Other Information which comprises:

- information contained within the Relevant Elements of the Solvency and Financial Condition Report set out about above which are, or derive from the Solvency Capital Requirement, as identified in the Appendix to this report;

- The ‘Business and performance’, ‘System of governance’ and ‘Risk profile’ sections of the Solvency and Financial Condition Report;

- Company templates S05.01.02, S19.01.21, S.25.02.21;

- Information calculated in accordance with the previous regime used in the calculation of the transitional measure on technical provisions, and as a consequence all information relating to the transitional measures on technical provisions as set out in the Appendix to this report where disclosed;

- the written acknowledgement by the directors of their responsibilities, including for the preparation of the solvency and financial condition report (‘**the Responsibility Statement**’).

To the extent the information subject to audit in the relevant elements of the Solvency and Financial Condition Report includes amounts that are totals, sub-totals or calculations derived from the Other Information, we have relied without verification on the Other Information.

In our opinion, the information subject to audit in the Relevant Elements of the Solvency and Financial Condition Report of The Prudential Assurance Company Limited as at 31 December 2018 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, as modified by relevant supervisory modifications, and as supplemented by supervisory approvals and determinations.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) including ISA (UK) 800 and ISA (UK) 805, and applicable law. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Relevant Elements of the Solvency and Financial Condition Report* section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the Solvency and Financial Condition Report in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of Matter - special purpose basis of accounting

We draw attention to the 'Valuation for solvency purposes' and other relevant disclosures sections of the Solvency and Financial Condition Report, which describe the basis of accounting. The Solvency and Financial Condition Report is prepared in compliance with the financial reporting provisions of the PRA Rules and Solvency II regulations, and therefore in accordance with a special purpose financial reporting framework. The Solvency and Financial Condition Report is required to be published, and intended users include but are not limited to the Prudential Regulation Authority. As a result, the Solvency and Financial Condition Report may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you if:

- the directors' use of the going concern basis of accounting in the preparation of the SFCR is not appropriate; or

- the directors have not disclosed in the SFCR any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the SFCR is authorised for issue.

Other Information

The directors are responsible for the Other Information.

Our opinion on the Relevant Elements of the Solvency and Financial Condition Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon.

In connection with our audit of the Solvency and Financial Condition Report, our responsibility is to read the Other Information and, in doing so, consider whether the Other Information is materially inconsistent with the Relevant Elements of the Solvency and Financial Condition Report, or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the Relevant Elements of the Solvency and Financial Condition Report or a material misstatement of the Other Information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of directors for the Solvency and Financial Condition Report

The directors are responsible for the preparation of the Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA rules and Solvency II regulations.

The directors are also responsible for such internal control as they determine is necessary to enable the preparation of a Solvency and Financial Condition Report that is free from material misstatement, whether due to fraud or error; assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Relevant Elements of the Solvency and Financial Condition Report

It is our responsibility to form an independent opinion as to whether the Relevant Elements of the Solvency and Financial Condition Report are prepared, in all material respects, with financial reporting provisions of the PRA Rules and Solvency II regulations on which it they based, as modified by relevant supervisory modifications, and as supplemented by supervisory approvals and determinations.

Our objectives are to obtain reasonable assurance about whether the Relevant Elements of the Solvency and Financial Condition Report are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decision making or the judgement of the users taken on the basis of the Relevant Elements of the Solvency and Financial Condition Report.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities.

Other Matter

The Company has authority to calculate its Solvency Capital Requirement using an internal model ("the Model") approved by the Prudential Regulation Authority in accordance with the Solvency II Regulations. In forming our opinion (and in accordance with PRA Rules), we are not required to audit the inputs to, design of, operating effectiveness of and outputs from the Model, or whether the Model is being applied in accordance with the Company's application or approval order.

Report on Other Legal and Regulatory Requirements

In accordance with Rule 4.1 (3) of the External Audit Chapter of the PRA Rulebook we are also required to consider whether the Other Information is materially inconsistent with our knowledge obtained in the audit of The Prudential Assurance Company Limited statutory financial statements. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

This report of the external auditor is made solely to the company's directors, as its governing body, in accordance with the requirement in Rule 4.1(2) of the External Audit Part of the PRA Rulebook and the terms of our engagement. We acknowledge that the directors are required to submit the report to the PRA, to enable the PRA to verify that an auditor's report has been commissioned by the Company's directors and issued in accordance with the requirement set out in Rule 4.1(2) of the External Audit Part of the PRA Rulebook and to facilitate the discharge by the PRA of its regulatory functions in respect of the company, conferred on the PRA by or under the Financial Services and Markets Act 2000.

Our audit has been undertaken so that we might state to the Company's directors those matters we are required to state to them in an auditor's report issued pursuant to Rule 4.1(2) 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 through its governing body, for our audit, for this report, or for the opinions we have formed.

Daniel Cazeaux
for and on behalf of KPMG LLP
Chartered Accountants
15 Canada Square
Canary Wharf
London
E14 5GL

16 April 2019

The maintenance and integrity of Prudential plc's website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Solvency and Financial Condition Report since it was initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of Solvency and Financial Condition Reports may differ from legislation in other jurisdictions.

Appendix - relevant elements of the Solvency and Financial Condition Report that are not subject to audit

Solo internal model

The relevant elements of the Solvency and Financial Condition Report that are not subject to audit comprise:

The following elements of template S.02.01.02:

- Row R0090: Amount of transitional measure on technical provisions in relation to the technical provisions of Prudential Hong Kong Limited (PHKL)
- Row R0550: Technical provisions - non-life (excluding health) - risk margin
- Row R0590: Technical provisions - health (similar to non-life) - risk margin
- Row R0640: Technical provisions - health (similar to life) - risk margin
- Row R0680: Technical provisions - life (excluding health and index-linked and unit-linked) - risk margin
- Row R0720: Technical provisions - Index-linked and unit-linked - risk margin

The following elements of template S.12.01.02

- Row R0100: Technical provisions calculated as a sum of BE and RM - Risk margin
- Rows R0110 to R0130 - Amount of transitional measure on technical provisions

The following elements of template S.17.01.02

- Row R0280: Technical provisions calculated as a sum of BE and RM - Risk margin
- Rows R0290 to R0310 - Amount of transitional measure on technical provisions

The following elements of template S.22.01.21

- Column C0030 - Impact of transitional measure on technical provisions
- Row R0010 - Technical provisions
- Row R0020 - Adjustment for restricted own fund items in respect of ring fenced funds of the Company and the ring fenced funds of Prudential Hong Kong Limited (PHKL)
- Row R0090 - Solvency Capital Requirement

The following elements of template S.23.01.01

- Row R0580: SCR
- Row R0740: Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds

The following elements of template S.28.02.01

- Row R0310: SCR

Elements of the Narrative Disclosures subject to audit identified as ‘Unaudited’.

Quantitative Reporting Templates (QRTs)
S.02.01.02 Balance Sheet
All amounts are in £'000

		Solvency II value
	Assets	C0010
R0030	Intangible assets	—
R0040	Deferred tax assets	—
R0050	Pension benefit surplus	—
R0060	Property, plant & equipment held for own use	143,841
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	142,432,659
R0080	Property (other than for own use)	9,239,819
R0090	Holdings in related undertakings, including participations	4,089,257
R0100	Equities	30,994,239
R0110	Equities - listed	30,916,900
R0120	Equities - unlisted	77,340
R0130	Bonds	71,573,239
R0140	Government Bonds	15,180,227
R0150	Corporate Bonds	50,633,535
R0160	Structured notes	—
R0170	Collateralised securities	5,759,477
R0180	Collective Investments Undertakings	22,588,773
R0190	Derivatives	2,503,157
R0200	Deposits other than cash equivalents	1,444,175
R0210	Other investments	—
R0220	Assets held for index-linked and unit-linked contracts	7,764,913
R0230	Loans and mortgages	11,038,073
R0240	Loans on policies	2,734
R0250	Loans and mortgages to individuals	1,477,545
R0260	Other loans and mortgages	9,557,794
R0270	Reinsurance recoverables from:	18,643,951
R0280	Non-life and health similar to non-life	141,526
R0290	Non-life excluding health	141,526
R0300	Health similar to non-life	—
R0310	Life and health similar to life, excluding index-linked and unit-linked	13,423,531
R0320	Health similar to life	356
R0330	Life excluding health and index-linked and unit-linked	13,423,174
R0340	Life index-linked and unit-linked	5,078,894
R0350	Deposits to cedants	—
R0360	Insurance and intermediaries receivables	20,615
R0370	Reinsurance receivables	11,308
R0380	Receivables (trade, not insurance)	2,705,375
R0390	Own shares (held directly)	—
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	—
R0410	Cash and cash equivalents	1,305,287
R0420	Any other assets, not elsewhere shown	—
R0500	**Total assets**	184,066,021

S.02.01.02 Balance Sheet

		Solvency II value
	Liabilities	C0010
R0510	Technical provisions - non-life	141,573
R0520	Technical provisions - non-life (excluding health)	141,573
R0530	TP calculated as a whole	—
R0540	Best Estimate	141,573
R0550	Risk margin	—
R0560	Technical provisions - health (similar to non-life)	—
R0570	TP calculated as a whole	—
R0580	Best Estimate	—
R0590	Risk margin	—
R0600	Technical provisions - life (excluding index-linked and unit-linked)	143,052,471
R0610	Technical provisions - health (similar to life)	(15,062)
R0620	TP calculated as a whole	—
R0630	Best Estimate	(15,114)
R0640	Risk margin	52
R0650	Technical provisions - life (excluding health and index-linked and unit-linked)	143,067,533
R0660	TP calculated as a whole	—
R0670	Best Estimate	141,515,320
R0680	Risk margin	1,552,214
R0690	Technical provisions - index-linked and unit-linked	12,851,362
R0700	TP calculated as a whole	—
R0710	Best Estimate	12,817,105
R0720	Risk margin	34,257
R0740	Contingent liabilities	31,344
R0750	Provisions other than technical provisions	401,469
R0760	Pension benefit obligations	79,219
R0770	Deposits from reinsurers	1,352,022
R0780	Deferred tax liabilities	607,650
R0790	Derivatives	2,171,904
R0800	Debts owed to credit institutions	2,708,699
R0810	Financial liabilities other than debts owed to credit institutions	61,409
R0820	Insurance & intermediaries payables	597,616
R0830	Reinsurance payables	118,544
R0840	Payables (trade, not insurance)	1,431,924
R0850	Subordinated liabilities	—
R0860	Subordinated liabilities not in BOF	—
R0870	Subordinated liabilities in BOF	—
R0880	Any other liabilities, not elsewhere shown	—
R0900	**Total liabilities**	165,607,208
R1000	**Excess of assets over liabilities**	18,458,814

S.05.01.02 Premiums claims and expenses by line of business

Unaudited

All amounts are in £'000

	Non-life	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)						Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)						Line of business for: accepted non-proportional reinsurance				Total
		Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Misc. financial loss	Health	Casualty	Marine, aviation and transport	Property	
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0200
	Premiums written																	
R0110	*Gross - Direct Business*																	—
R0120	*Gross - Proportional reinsurance accepted*																	—
R0130	*Gross - Non-proportional reinsurance accepted*																	—
R0140	*Reinsurers' share*																	—
R0200	*Net*	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
	Premiums earned																	
R0210	*Gross - Direct Business*																	—
R0220	*Gross - Proportional reinsurance accepted*																	—
R0230	*Gross - Non-proportional reinsurance accepted*																	—
R0240	*Reinsurers' share*																	—
R0300	*Net*	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
	Claims incurred																	
R0310	*Gross - Direct Business*				1,369				(2,511)									(1,141)
R0320	*Gross - Proportional reinsurance accepted*																	—
R0330	*Gross - Non-proportional reinsurance accepted*																	—
R0340	*Reinsurers' share*				1,369				(2,511)									(1,141)
R0400	*Net*	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
	Changes in other technical provisions																	
R0410	*Gross - Direct Business*																	—
R0420	*Gross - Proportional reinsurance accepted*																	—
R0430	*Gross - Non-proportional reinsurance accepted*																	—
R0440	*Reinsurers' share*																	—
R0500	*Net*	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
R0550	**Expenses incurred**																	—
R1200	**Other expenses**																	
R1300	**Total expenses**																	—

S.05.01.02 Premiums claims and expenses by line of business

Life		Line of Business for: life insurance obligations						Life reinsurance obligations		Total
		Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Health reinsurance	Life reinsurance	
		C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
	Premiums written									
R1410	*Gross*	17,553	11,452,844	580,072	443,296			—	884,518	13,378,283
R1420	*Reinsurers' share*	1,776	863	354,972	13,102,049			—	—	13,459,660
R1500	*Net*	15,777	11,451,981	225,101	(12,658,753)			—	884,518	(81,377)
	Premiums earned									
R1510	*Gross*	17,553	11,452,844	580,072	443,296			—	884,518	13,378,283
R1520	*Reinsurers' share*	1,776	863	354,972	13,102,049			—	—	13,459,660
R1600	*Net*	15,777	11,451,981	225,101	(12,658,753)			—	884,518	(81,377)
	Claims incurred									
R1610	*Gross*	6,035	7,624,473	1,700,865	2,975,581			—	419,604	12,726,559
R1620	*Reinsurers' share*	3,323	1,531	450,988	1,415,559			—	900	1,872,300
R1700	*Net*	2,712	7,622,942	1,249,877	1,560,023			—	418,704	10,854,258
	Changes in other technical provisions									
R1710	*Gross*	(6,954)	2,829,799	928,381	1,516,813			—	(467,954)	4,800,084
R1720	*Reinsurers' share*	(2,005)	12,815	373,959	(10,821,974)			—	—	(10,437,206)
R1800	*Net*	(4,949)	2,816,984	554,422	12,338,787			—	(467,954)	15,237,289
R1900	**Expenses incurred**	1,065	804,592	177,539	235,459			—	—	1,218,655
R2500	**Other expenses**									48,676
R2600	**Total expenses**									1,267,331

S.12.01.02 Life and Health SLT Technical Provisions

All amounts are in £'000

			Index-linked and unit-linked insurance			Other life insurance							Health insurance (direct business)				
		Insurance with profit participation		Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees	Annuities stemming from non-life insurance contracts and relating to insurance obligation other than health insurance obligations	Accepted reinsurance	Total (Life other than health insurance, including Unit-Linked)		Contracts without options and guarantees	Contracts with options or guarantees	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Health reinsurance (reinsurance accepted)	Total (Health similar to life insurance)
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150	C0160	C0170	C0180	C0190	C0200	C0210
R0010	Technical provisions calculated as a whole	—	—			—			—	—	—	—			—	—	—
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated	—	—			—			—	—	—	—			—	—	—
	Technical provisions calculated as a sum of BE and RM																
	Best estimate																
R0030	Gross Best Estimate	94,094,702		12,149,624	667,482		27,637,138	13,469,645	—	6,313,834	154,332,425		(5,008)	(10,106)	—	—	(15,114)
R0080	Total Recoverables from reinsurance/SPV and Finite	(584)		5,078,894	—		10,150,557	3,263,019	—	10,183	18,502,069		1,421	(1,065)	—	—	356
R0090	Best estimate minus recoverables from	94,095,286		7,070,729	667,482		17,486,582	10,206,626	—	6,303,651	135,830,356		(6,429)	(9,041)	—	—	(15,471)
R0100	Risk margin	928,386	126,775			3,105,135			—	44,199	4,204,494	52			—	—	52
	Amount of the transitional on Technical Provisions																
R0110	Technical Provisions calculated as a whole	—	—			—			—	—	—	—			—	—	—
R0120	Best estimate	—		—	—		—	—	—	—	—		—	—	—	—	—
R0130	Risk margin	(521,464)	(92,518)			(1,973,659)			—	(30,383)	—	—			—	—	—
R0200	Technical provisions - total	94,501,623	12,851,362			42,238,260			—	6,327,651	155,918,896	(15,062)			—	—	(15,062)

S.17.01.02 Non-Life Technical Provisions
All amounts are in £'000

		Direct business and accepted proportional reinsurance				Direct business and accepted proportional reinsurance				Direct business and accepted proportional reinsurance				Accepted non-proportional reinsurance				
		Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Miscellaneous financial loss	Non-proportional health reinsurance	Non-proportional casualty reinsurance	Non-proportional marine, aviation and transport reinsurance	Non-proportional property reinsurance	Total Non-Life obligation
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0170	C0180
R0010	**Technical provisions calculated as a whole**																	—
R0050	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default																	—
	Technical provisions calculated as a sum of BE and RM																	
	Best estimate																	
	Premium provisions																	
R0060	Gross																	—
R0140	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default																	—
R0150	**Net Best Estimate of Premium Provisions**																	—
	Claims provisions																	
R0160	Gross				19,441				122,133									141,573
R0240	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default				19,432				122,094									141,526
R0250	**Net Best Estimate of Claims Provisions**				9				39									48
R0260	**Total best estimate - gross**				19,441				122,133									141,573
R0270	**Total best estimate - net**				9				39									48
R0280	**Risk margin**				—				—									—
	Amount of the transitional on Technical Provisions																	
R0290	Technical Provisions calculated as a whole																	—
R0300	Best estimate																	—
R0310	Risk margin																	—
R0320	**Technical provisions - total**				19,441				122,133									141,573
R0330	**Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total**				19,432				122,094									141,526
R0340	**Technical provisions minus recoverables from reinsurance/ SPV and Finite Re - total**				9				39									48

S.19.01.21 Non-Life insurance claims

Unaudited

All amounts are in £'000

Z0010 **Accident year / underwriting year** —

Gross Claims Paid (non-cumulative)

(absolute amount)

	Year	C0010 —	C0020 1	C0030 2	C0040 3	C0050 4	C0060 5	C0070 6	C0080 7	C0090 8	C0100 9	C0110 10 & +	C0170 In Current year	C0180 Sum of years (cumulative)
R0100	Prior											2,911	2,911	2,911
R0160	N-9													
R0170	N-8													
R0180	N-7													
R0190	N-6													
R0200	N-5													
R0210	N-4													
R0220	N-3													
R0230	N-2													
R0240	N-1													
R0250	N													
R0260													Total	

Gross undiscounted Best Estimate Claims Provisions

(absolute amount)

	Year	C0200 —	C0210 1	C0220 2	C0230 3	C0240 4	C0250 5	C0260 6	C0270 7	C0280 8	C0290 9	C0300 10 & +	C0360 Year end (discounted data)
R0100	Prior											141,573	100,768
R0160	N-9												
R0170	N-8												
R0180	N-7												
R0190	N-6												
R0200	N-5												
R0210	N-4												
R0220	N-3												
R0230	N-2												
R0240	N-1												
R0250	N												
R0260												Total	

S.22.01.21 Impact of long term guarantees measures and transitionals
All amounts are in £'000

		Amount with Long Term Guarantee measures and transitionals	Impact of transitional on technical provisions	Impact of transitional on interest rate	Impact of volatility adjustment set to zero	Impact of matching adjustment set to zero
		C0010	C0030	C0050	C0070	C0090
R0010	**Technical provisions**	156,045,407	2,618,023	—	—	3,341,504
R0020	**Basic own funds**	13,000,723	(1,322,475)	—	—	(2,013,871)
R0050	**Eligible own funds to meet Solvency Capital Requirement**	13,000,723	(1,322,475)	—	—	(2,013,871)
R0090	**Solvency Capital Requirement**	9,309,456	249,806	—	—	3,128,373
R0100	**Eligible own funds to meet Minimum Capital Requirement**	13,000,723	(1,322,475)	—	—	(2,013,871)
R0110	**Minimum Capital Requirement**	2,327,364	62,451	—	—	782,093

S.23.01.01 Own Funds

All amounts are in £'000

	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	329,517,064	329,517,064		—	
R0030	Share premium account related to ordinary share capital	—	—		—	
R0040	Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type	—	—		—	
R0050	Subordinated mutual member accounts	—		—	—	—
R0070	Surplus funds	10,642,422,143	10,642,422,143			
R0090	Preference shares	—		—	—	—
R0110	Share premium account related to preference shares	—		—	—	—
R0130	Reconciliation reserve	2,028,783,605	2,028,783,605			
R0140	Subordinated liabilities	—		—	—	—
R0160	An amount equal to the value of net deferred tax assets	—				—
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	—	—	—	—	—
	Own funds from the financial statements that should not be represented by the reconciliation reserve					
R0220	Own funds from the financial statements that should not be represented by the reconciliation reserve and do	—				
	Deductions					
R0230	Deductions for participations in financial and credit institutions	—	—	—	—	
R0290	Total basic own funds after deductions	13,000,722,811	13,000,722,811	—	—	—
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	—			—	
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual	—			—	
R0320	Unpaid and uncalled preference shares callable on demand	—			—	—
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	—			—	—
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	—			—	
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	—			—	—
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	—			—	
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/	—			—	—
R0390	Other ancillary own funds	—			—	—
R0400	**Total ancillary own funds**	—			—	—
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	13,000,723	13,000,723	—	—	—
R0510	Total available own funds to meet the MCR	13,000,723	13,000,723	—	—	
R0540	Total eligible own funds to meet the SCR	13,000,723	13,000,723	—	—	—
R0550	Total eligible own funds to meet the MCR	13,000,723	13,000,723	—	—	
R0580	**SCR**	9,309,456				
R0600	**MCR**	2,327,364				
R0620	**Ratio of Eligible own funds to SCR**	140%				
R0640	**Ratio of Eligible own funds to MCR**	559%				

	Reconcilliation reserve	C0060
R0700	Excess of assets over liabilities	18,458,814
R0710	Own shares (held directly and indirectly)	—
R0720	Foreseeable dividends, distributions and charges	—
R0730	Other basic own fund items	10,971,939
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	5,458,091
R0760	**Reconciliation reserve**	2,028,784
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	45,357
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	—
R0790	**Total Expected profits included in future premiums (EPIFP)**	45,357

S.25.02.21 Solvency Capital Requirement
– for undertakings using the standard formula and partial internal model

Unaudited

All amounts are in £'000

	Unique number of component	Component description	Calculation of the Solvency Capital Requirement	Amount modelled	USP	Simplifications
Row	C0010	C0020	C0030	C0070	C0080	C0090
1	103	Interest rate risk	1,849,014	1,849,014		
2	104	Equity risk	2,710,843	2,710,843		
3	106	Property risk	1,414,493	1,414,493		
4	107	Spread risk	5,148,426	5,148,426		
5	108	Concentration risk	—	—		
6	109	Currency risk	2,023,641	2,023,641		
7	110	Other market risk	—	—		
8	199	Diversification within market risk	(5,632,171)	(5,632,171)		
9	203	Other counterparty risk	342,664	342,664		
10	301	Mortality risk	8,731	8,731		
11	302	Longevity risk	3,527,075	3,527,075		
12	303	Disability-morbidity risk	14,820	14,820		
13	304	Mass lapse	301,322	301,322		
14	305	Other lapse risk	1,038,642	1,038,642		
15	306	Expense risk	1,463,414	1,463,414		
16	308	Life catastrophe risk	22,822	22,822		
17	309	Other life underwriting risk	—	—		
18	399	Diversification within life underwriting risk	(3,125,967)	(3,125,967)		
19	505	Other non-life underwriting risk	—	—		
20	701	Operational risk	1,466,449	1,466,449		
21	801	Other risks	—	—		
22	802	Loss-absorbing capacity of technical provisions	—	—		
23	803	Loss-absorbing capacity of deferred taxes	(1,078,385)	(1,078,385)		
24	804	Other adjustments	—	—		

S.25.02.21 Solvency Capital Requirement
– for undertakings using the standard formula and partial internal model

Unaudited

All amounts are in £'000

	Calculation of Solvency Capital Requirement	C0100
R0110	Total undiversified components	11,495,834
R0060	Diversification	(2,186,378)
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	—
R0200	**Solvency capital requirement excluding capital add-on**	9,309,456
R0210	Capital add-ons already set	—
R0220	**Solvency capital requirement**	9,309,456

	Other information on SCR	
R0300	Amount/estimate of the overall loss-absorbing capacity of technical provisions	(14,263,082)
R0310	Amount/estimate of the overall loss-absorbing capacity of deferred taxes	(1,078,385)
R0400	Capital requirement for duration-based equity risk sub-module	—
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	1,836,986
R0420	Total amount of Notional Solvency Capital Requirement for ring fenced funds	2,276,615
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	5,195,854
R0440	Diversification effects due to RFF nSCR aggregation for article 304	—

S.28.02.01 Minimum Capital Requirement – Both life and non-life insurance activity

All amounts are in £'000

		Non-life activities	Life activities
		MCR(NL,NL) Result	MCR(NL,L) Result
		C0010	C0020
R0010	**Linear formula component for non-life insurance and reinsurance obligations**	5	—

		Non-life activities: Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Non-life activities: Net (of reinsurance) written premiums in the last 12 months	Life activities: Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Life activities: Net (of reinsurance) written premiums in the last 12 months
		C0030	C0040	C0050	C0060
R0020	Medical expense insurance and proportional reinsurance	—	—	—	—
R0030	Income protection insurance and proportional reinsurance	—	—	—	—
R0040	Workers' compensation insurance and proportional reinsurance	—	—	—	—
R0050	Motor vehicle liability insurance and proportional reinsurance	8	—	—	—
R0060	Other motor insurance and proportional reinsurance	—	—	—	—
R0070	Marine, aviation and transport insurance and proportional reinsurance	—	—	—	—
R0080	Fire and other damage to property insurance and proportional reinsurance	—	—	—	—
R0090	General liability insurance and proportional reinsurance	39	—	—	—
R0100	Credit and suretyship insurance and proportional reinsurance	—	—	—	—
R0110	Legal expenses insurance and proportional reinsurance	—	—	—	—
R0120	Assistance and proportional reinsurance	—	—	—	—
R0130	Miscellaneous financial loss insurance and proportional reinsurance	—	—	—	—
R0140	Non-proportional health reinsurance	—	—	—	—
R0150	Non-proportional casualty reinsurance	—	—	—	—
R0160	Non-proportional marine, aviation and transport reinsurance	—	—	—	—
R0170	Non-proportional property reinsurance	—	—	—	—

		MCR(L,NL) Result	MCR(L,L) Result
		C0070	C0080
R0200	**Linear formula component for life insurance and reinsurance obligations**	—	(1,904,634)

		Non-life activities: Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Non-life activities: Net (of reinsurance /SPV) total capital at risk	Life activities: Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Life activities: Net (of reinsurance/ SPV) total capital at risk
		C0090	C0100	C0110	C0120
R0210	Obligations with profit participation - guaranteed benefits	—		29,330,605	
R0220	Obligations with profit participation - future discretionary benefits	—		70,276,441	
R0230	Index-linked and unit-linked insurance obligations	—		7,738,211	
R0240	Other life (re)insurance and health (re)insurance obligations	—		28,469,628	
R0250	Total capital at risk for all life (re)insurance obligations		—		17,827,393

	Overall MCR calculation	C0130
R0300	Linear MCR	(1,904,629)
R0310	SCR	9,309,456
R0320	MCR cap	4,189,255
R0330	MCR floor	2,327,364
R0340	Combined MCR	2,327,364
R0350	Absolute floor of the MCR	3,288
R0400	**Minimum Capital Requirement**	2,327,364

	Notional non-life and life MCR calculation	C0140	C0150
R0500	Notional linear MCR	5	(1,904,634)
R0510	Notional SCR excluding add-on (annual or latest calculation)	(23)	9,309,479
R0520	Notional MCR cap	(10)	4,189,266
R0530	Notional MCR floor	(6)	2,327,370
R0540	Notional combined MCR	(10)	2,327,370
R0550	Absolute floor of the notional MCR	3,288	3,288
R0560	**Notional MCR**	3,288	2,327,370