PRUDENTIAL PLC
Form 20-F
June 28, 2006

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As filed with the Securities and Exchange Commission on June 28, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OR (G) OF THE SECURITIES EXCHANGE ACT OF 1934
OR
ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2005
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
OR
o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number: 1-15040

PRUDENTIAL PUBLIC LIMITED COMPANY

(Exact Name of Registrant as Specified in its Charter)

England and Wales
(Jurisdiction of Incorporation)

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

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

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

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

None

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

None

The number of outstanding shares of each of the issuer's classes of capital or common stock as of December 31, 2005 was:

2,386,784,266 Ordinary Shares, 5 pence par value each

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes X No ____

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes ____ No X

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

Yes X No ____

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer X Accelerated filer ____ Non-accelerated filer ____

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

Item 17 ____ Item 18 X

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ____No X

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

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Item 3. Key Information

SELECTED HISTORICAL FINANCIAL INFORMATION OF PRUDENTIAL

The following table sets forth Prudential's selected consolidated financial data for the periods indicated. Certain data is derived from Prudential's audited consolidated financial statements prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). Were the Group to apply IFRS as published by the IASB, as opposed to EU adopted IFRS, no additional adjustments would be required. Note J to the Prudential audited consolidated financial statements included elsewhere in this document includes a description of the differences between IFRS and US GAAP that are significant to the financial statements and provides a reconciliation from IFRS consolidated profit and shareholders' equity to US GAAP consolidated net income and shareholders' equity, respectively. Item 5, "Operating and Financial Review and Prospects US GAAP Analysis" provides a discussion of the significant differences between IFRS and US GAAP. This table is only a summary and should be read in conjunction with Prudential's consolidated financial statements and the related notes included elsewhere in this document, together with Item 5, "Operating and Financial Review and Prospects".

The Securities and Exchange Commission (SEC) has provided a one-time accommodation relating to financial statements prepared under IFRS for foreign private issuers registered with the SEC. This accommodation applies to companies, such as Prudential, that adopt IFRS prior to or for the first financial year starting on or after January 1, 2007. The accommodation permits eligible foreign private issuers for their first year of reporting under IFRS to file two years rather than three years of statements of income, changes in shareholders' equity and cash flows prepared in accordance with IFRS, with appropriate related disclosure. The Company has prepared the financial information in the current year's Form 20-F in accordance with this accommodation.

The following table presents the income statement and balance sheet data for and as at the years ended December 31, 2004 to 2005, as presented in accordance with IFRS, and for and as at the years ended December 31, 2001 to 2005, as presented in accordance with US GAAP, and has been derived from Prudential's consolidated financial statements, audited by KPMG Audit Plc:

	Year Ended December 31,		
	2005[1]	**2005**	**2004**
	(In $ Millions)	**(In £ Millions)**	
Income statement data IFRS basis			
Gross premium earned	**26,169**	15,225	16,408
Outward reinsurance premiums	**(339)**	(197)	(256)
Earned premiums, net of reinsurance	**25,830**	15,028	16,152
Investment income	**41,274**	24,013	15,750
Other income	**3,582**	2,084	2,002
Total revenue, net of reinsurance	**70,686**	41,125	33,904
Benefits and claims and movement in unallocated surplus of with-profits funds	**(56,892)**	(33,100)	(26,593)
Acquisition costs and other operating expenditure	**(9,543)**	(5,552)	(5,563)
Finance costs: interest on core structural borrowings of shareholder financed operations	**(358)**	(208)	(187)
Goodwill impairment charge	**(206)**	(120)	
Total charges	**(66,999)**	(38,980)	(32,343)
Profit before tax[2]	**3,687**	2,145	1,561
Tax attributable to policyholders' returns	**(1,972)**	(1,147)	(711)
Profit before tax attributable to shareholders	**1,715**	998	850
Tax attributable to shareholders' profits	**(414)**	(241)	(240)
Profit from continuing operations after tax	**1,301**	757	610
Discontinued operations (net of tax)[3]	**5**	3	(94)

	Year Ended December 31,		
Profit for the year	**1,306**	760	516

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	Year Ended December 31,					
	2005[1]	**2005**	**2004**	**2003**	**2002**	**2001**
	(In $ Millions)	**(In £ Millions)**				
Statement of income and comprehensive income data US GAAP basis						
Insurance policy revenues	**12,996**	**7,561**	6,786	4,527	5,201	3,954
Investment results	**32,870**	**19,124**	13,348	11,672	(1,832)	182
Non-operating income:						
Merger break fee, net of related expenses						338
Other income	**3,477**	**2,023**	2,106	677	688	616
Total revenue	**49,343**	**28,708**	22,240	16,876	4,057	5,090
Net income (loss) from continuing operations (after minority interests)[4]	**2,073**	**1,206**	697	694	(641)	(308)
Income from discontinued operations including profit on disposals (net of applicable tax)[3]	**(24)**	**(14)**	(88)	(29)	284	39
Cumulative effect of changes in accounting principles[5]			(518)			(139)
Total net income (loss)	**2,049**	**1,192**	91	665	(357)	(408)
Total comprehensive income (loss)	**2,666**	**1,593**	18	655	(627)	(68)

	As of and for the year ended December 31,					
	2005[1]	**2005**	**2004**	**2003**	**2002**	**2001**
	(In $ Millions, Except Share Information)	**(In £ Millions, Except Share Information)**				
Balance sheet data IFRS basis						
Total assets	**356,440**	**207,377**	180,006			
Total policyholder liabilities and unallocated surplus of with-profits funds	**292,784**	**170,342**	145,211			
Core structural borrowings of shareholder financed operations	**5,485**	**3,191**	3,248			
Total equity	**9,223**	**5,366**	4,626			
Based on profit for the year attributable to the equity holders of the Company:						
Basic earnings per share	**54.3¢**	**31.6p**	24.4p			
Diluted earnings per share^	**54.3¢**	**31.6p**	24.4p			
Dividend per share declared and paid in reporting period[8]	**27.41¢**	**15.95p**	15.48p			
Equivalent cents per share[9]^		**29.61¢**	28.36¢			
Market price at end of period^	$ **9.45**	**550p**	453p	454p	422p	765p
Weighted average number of shares (in millions)^		**2,365**	2,121			
Balance sheet data US GAAP basis						
Total assets	**345,297**	**200,894**	174,058	160,645	150,379	155,668
Policyholder benefit liabilities[5]	**234,176**	**136,244**	122,412	90,307	89,304	84,190
Separate account liabilities[5]	**15,351**	**8,931**	5,531	30,487	25,793	29,729
Total shareholders' equity	**12,363**	**7,193**	5,927	5,128	4,878	5,964
Based on net income after minority interests:						
Basic earnings per share^	**86.6¢**	**50.4p**	4.3p	32.0p	(17.3)p	(19.8)p
Diluted earnings (loss) per share^	**86.5¢**	**50.3p**	4.3p	32.0p	(17.2)p	(19.8)p
Other data						
New business from continuing operations:						
Single premium sales[7]	**22,226**	**12,931**	11,427	8,473	11,802	10,610
New regular premium sales[6][7]	**1,466**	**853**	703	710	707	693

	As of and for the year ended December 31,					
Gross investment product contributions(7)	**46,041**	**26,787**	25,108	22,113	17,392	11,303
Funds under management	**402,199**	**234,000**	197,000			

^

Comparative figures for these lines have been restated to take account of Prudential's rights offering in 2004. The restatement factor is 0.9614 based on a theoretical ex-rights price of 405.71 pence divided by the closing share price on the final day Prudential's shares traded cum-rights of 422.00 pence.

Certain other minor reclassifications and presentational changes have been made to the amounts presented for prior periods to conform these periods to the current presentation. Such reclassifications and presentational changes had no overall effect on the shareholders' funds, profits or cash flows.

(1) Amounts stated in US dollars have been translated from pounds sterling at the rate of $1.7188 per £1.00 (the noon buying rate in New York City on December 30, 2005).

(2) Profit before tax represents income net of post-tax transfers to unallocated surplus of with-profits funds, before tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders' profits.

(3) Discontinued operations predominantly relate to Jackson Federal Bank ('JFB') and Egg France. See Note F6 of the notes to Prudential's consolidated financial statements.

(4) The 2004, 2003 and 2002 US GAAP comparatives have been restated by £20 million, £2 million and £1 million, respectively, for the classification in 2005 of discontinued operations for Funds Direct, Egg's investment wrap platform business. The sale was completed in October 2005. Funds Direct incurred losses before tax of £1 million (2004: gains before tax of £20 million) including exit costs in the year.

(5) Effective January 1, 2004, the Group adopted SOP 03-01 "Accounting and Reporting by Insurance Enterprises for Certain Non-traditional Long Duration Contracts and Separate Accounts". This has resulted in business previously being disclosed as separate accounts business being reclassified to the general account. The cumulative effect of this change in accounting principle is described in Note K of the consolidated financial statements.

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

(7) New business premiums reflect the amount of business Prudential generated during each period shown and do not include renewal premiums on policies written during prior periods. Prudential considers new business premiums to be a measure of its operating performance because they represent new sales of insurance policies during a specified period, rather than its revenues or profitability during that period. This operating measure enables a comparison of operating performance across periods without regard to revenues or profitability related to policies sold in prior periods. Gross investment product contributions reflect the amount invested by Institutional and Retail customers in the period. Prudential considers these to be a measure of its operating performance because it measures the flow of monies into the funds managed by the Group. This operating measure enables a measurement of operating performance across periods.

(8) Under IFRS, dividends declared after the balance sheet date in respect of the prior reporting period are treated as a non-adjusting event. The appropriation reflected in the statement of changes in equity, therefore, includes the final dividend in respect of the prior year. Parent company dividends relating to the reporting period were an interim dividend of 5.30p per share in 2005 (5.19p in 2004) and a final dividend of 11.02p per share in 2005 (10.65p in 2004).

(9) The dividends have been translated into US dollars at the noon buying rate on the date each payment was made.

Dividend Data

Under UK company law, Prudential may pay dividends only if "distributable profits" of the holding company are available for that purpose. "Distributable profits" are accumulated, realized profits not previously distributed or capitalized less accumulated, realized losses not previously written off, on the applicable GAAP basis. Even if distributable profits are available, under UK law Prudential may pay dividends only if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves (such as, for example, the share premium account) and the payment of the dividend does not reduce the amount of its net assets to less than that aggregate. For further information about the holding company refer to Schedule II. The financial information in Schedule II has been prepared under UK GAAP reflecting the legal basis of preparation of the Company's separate financial statements as distinct from the IFRS basis that applies to the Company's consolidated financial statements.

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

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

The following table shows certain information regarding the dividends per share that Prudential declared for the periods indicated in pence sterling and converted into US dollars at the noon buying rate in effect on each payment date. Interim dividends for a specific year generally have a record date in August and a payment date in October of that year, and final dividends generally have a record date in the following March and a payment date in the following May. The comparative figures for 2001 to 2003 have been restated to take account of Prudential's rights offering in 2004. The restatement factor used for these periods is 0.9614 based on a theoretical ex-rights price of 405.71 pence divided by the closing share price on the final day Prudential's shares traded cum-rights of 422.00 pence.

Year	Interim Dividend (pence)	Interim Dividend (US Dollars)	Final Dividend (pence)	Final Dividend (US Dollars)
2001	8.36	0.1204	16.06	0.2313
2002	8.56	0.1329	16.44	0.2688
2003	5.09	0.0863	10.29	0.1867
2004	5.19	0.0952	10.65	0.1950
2005	5.30	0.0942	11.02	0.2046

A final dividend of 11.02 pence per share was approved by the shareholders at the Annual General Meeting held on May 18, 2006, bringing the full year dividend to 16.32 pence per share, an increase of three per cent from 2004. The Board intends to maintain Prudential's current dividend policy, with the level of dividend growth being determined after considering the opportunities to invest in those areas of the business offering attractive growth prospects, financial flexibility and the development of the statutory profits over the medium to long term.

Exchange Rate Information

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

Year ended December 31,	Average rate
2001	1.44
2002	1.51
2003	1.65
2004	1.84
2005	1.82

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

	High	Low
December 2005	1.77	1.72
January 2006	1.79	1.74
February 2006	1.78	1.73
March 2006	1.76	1.73
April 2006	1.82	1.74
May 2006	1.89	1.83

On June 26, 2006, the noon buying rate was £1.00 = $1.82.

RISK FACTORS

A number of factors (risk factors) affect Prudential's operating results, financial condition and trading price. The risk factors mentioned below should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. The information given is as of the date of this report, is not updated, and any forward-looking statements are made subject to the reservations specified below under "Forward-Looking Statements".

Prudential's businesses are inherently subject to market fluctuations and general economic conditions.

Prudential's businesses are inherently subject to market fluctuations and general economic conditions. In the UK, this is because a significant part of Prudential's shareholders' profit is related to bonuses for policyholders declared on its with-profits products, which are broadly based on historic and current rates of return on equity, real estate and fixed income securities, as well as Prudential's expectations of future investment returns.

In the US, fluctuations in prevailing interest rates can affect results from Jackson National Life ('JNL') which is predominantly a spread-based business with the majority of its assets invested in fixed income securities. In particular, fixed annuities and stable value products in JNL expose the Group to the risk that changes in interest rates which are not fully reflected in the interest rates credited to customers will reduce spread. The spread is the difference between the amounts that JNL is required to pay under the contracts and the rate of return it is able to earn on its general account investments to support the obligations under the contracts. Declines in spread from these products or other spread businesses that JNL conducts could have a material impact on its businesses or results of operations.

For some non unit-linked investment products, in particular those written in some of the Group's Asian operations, it may not be possible to hold assets which will provide cash flows to exactly match those relating to policyholder liabilities. This is particularly true in those countries where bond markets are not developed and in certain markets such as Taiwan where regulated surrender values are set with reference to the interest rate environment prevailing at time of policy issue. This is due to the duration and uncertainty of the liability cash flows and the lack of sufficient assets of a suitable duration. This results in a residual asset/liability mismatch risk which can be managed but not eliminated. If interest rates in these markets were to remain lower than surrender values over a sustained period this could have an adverse impact on the Group's reported profit.

In all markets in which Prudential operates, its businesses are susceptible to general economic conditions and changes in investment returns which can change the level of demand for Prudential's products. Past uncertain trends in international economic and investment climates which have adversely affected Prudential's business and profitability could be repeated. This adverse effect would be felt principally through reduced investment returns and credit defaults. In addition, falling investment returns could impair Prudential's operational capability, including its ability to write significant volumes of new business. Prudential in the normal course of business enters into a variety of transactions, including derivative transactions with counterparties. Failure of any of these counterparties, particularly in conditions of major market disruption, to discharge their obligations, or where adequate collateral is not in place, could have an adverse impact on Prudential's results.

Prudential is subject to the risk of exchange rate fluctuations owing to the geographical diversity of its businesses.

Due to the geographical diversity of Prudential's businesses, it is subject to the risk of exchange rate fluctuations. Prudential's international operations in the US and Asia, which represent a significant proportion of operating profit and shareholders' funds, generally write policies and invest in assets denominated in local currency. Although this practice limits the effect of exchange rate fluctuations on local operating results, it can lead to significant fluctuations in Prudential's consolidated financial statements upon translation of results into pounds sterling. The currency exposure relating to the translation of reported earnings is not separately managed. Consequently, this could impact on the Group's gearing ratios (defined as debt over debt plus shareholders' funds). The impact of gains or losses on currency translations is recorded as a component of shareholders' funds within the statement of changes in equity.

Prudential conducts its businesses subject to regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies and interpretations and any accounting standards in the markets in which it operates.

Changes in government policy, legislation or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which Prudential operates, which in some circumstances may be applied retrospectively, may adversely affect Prudential's product range, distribution channels, capital requirements and, consequently, reported results and financing requirements. For instance, regulators in jurisdictions in which Prudential operates may change the level of capital required to be held by individual businesses. Also these changes could include possible changes in the regulatory framework for pension arrangements and policies, the regulation of selling practices and solvency requirements. In the UK, the Financial Services Authority's (FSA) depolarization reforms, implemented in December 2004, under which the sales agent is no longer required to either be tied to a specific product provider or to recommend products from the whole spectrum of product providers in the market, and the rules relating to stakeholder products could have a significant effect on types of products sold by Prudential, how its products are priced, distributed and sold and on shareholders' return on with-profits business. Similar changes in regulation in other jurisdictions could also have an impact elsewhere in the Group.

The EU Financial Conglomerates Directive (FCD) requires European financial services groups to demonstrate net aggregate surplus capital in excess of solvency requirements at the Group level in respect of shareholder-owned entities. The test is a continuous requirement so that Prudential needs to maintain a somewhat higher amount of regulatory capital at the Group level than otherwise necessary in respect of some of its individual businesses to accommodate, for example, short-term movements in global foreign exchange rates, interest rates, deterioration in credit quality and equity markets. In addition, changes in the local regulatory regimes of designated territories could affect the calculation of the Group's solvency position under the FCD. The EU is also currently reviewing future solvency requirements (Solvency II) with a directive expected during 2007 for implementation by member states. Inconsistent application of these directives by regulators in different EU member states may place Prudential at a competitive disadvantage to other European financial services groups.

Various jurisdictions in which Prudential operates have created investor compensation schemes that require mandatory contributions from market participants in some instances in the event of a failure of a market participant. As a major participant in the majority of its chosen markets, circumstances could arise where Prudential, along with other companies, may be required to make such contributions.

See Item 5 "Operating and Financial Review and Prospects Factors Affecting Results of Operations Government Policy and Legislation" and Item 4 "Information on the Company Supervision and Regulation of Prudential".

Any further changes or modification of the recently introduced International Financial Reporting Standards (IFRS) accounting policies and European Embedded Value (EEV) guidance may require a change in the reporting basis of future results or a restatement of reported results.

The resolution of several issues affecting the financial services industry could have a negative impact on Prudential's reported results or on its relations with current and potential customers.

Prudential is, and in the future may be, subject to legal and regulatory actions in the ordinary course of its business, both in the UK and internationally. This could be a review of business sold in the past under previously acceptable market practices at the time. Pending legal and regulatory actions include proceedings relating to aspects of Prudential's business and operations which are typical of the business it operates in such as the requirement in the UK to provide redress to certain past purchasers of pension and mortgage endowment policies and regulatory reviews on products sold and industry practices, including in the latter case businesses it has closed.

In the US, federal and state regulators have focused on, and continue to devote substantial attention to, the mutual fund, variable annuity and insurance product industries including new federal regulations in respect of broker-dealers. As a result of publicity relating to widespread perceptions of industry abuses, there have been numerous regulatory inquiries and proposals for legislative and regulatory reforms.

Although Prudential believes it has adequately reserved in all material aspects for the costs of litigation and regulatory matters, no assurance can be provided that such reserves are sufficient. It is possible that Prudential's future performance could be affected by an unfavourable outcome in these matters.

Prudential's businesses are conducted in highly competitive environments with developing demographic trends and Prudential's continued profitability depends on its management's ability to respond to these pressures and trends.

The markets for the UK, US and Asian financial services are highly competitive, with several factors affecting Prudential's ability to sell its products and continued profitability, including price and yields offered, financial strength and ratings, range of product lines and product quality, brand strength and name recognition, investment management performance, historical bonus levels, developing demographic trends and customer appetite for certain savings products. In some of its markets Prudential faces competitors that are larger, have greater financial resources or a greater market share, offer a broader range of products or have higher bonus rates or claims-paying ratios. Further, heightened competition for talented and skilled employees with local experience, particularly in Asia, may limit the Group's potential to grow its business as quickly as planned.

Within the UK, Prudential's principal competitors in the life market include many of the major stock and mutual retail financial services companies including, in particular, Aviva, Legal & General, HBOS and Standard Life.

JNL's competitors in the US include major stock and mutual insurance companies, mutual fund organisations, banks and other financial services companies. JNL's principal life insurance company competitors in the US include AIG, Allstate Financial, Allianz Life of North America, AXA Financial Inc, Hartford Life Inc., ING, John Hancock, Lincoln Financial Group, Met Life, Pacific Life and Prudential Financial.

Within Asia, the Group's main regional competitors are international financial companies, including AIG, Allianz, ING and Manulife.

Prudential believes competition will intensify across all regions in response to consumer demand, technological advances, the impact of consolidation, regulatory actions and other factors. Prudential's ability to generate an appropriate return depends significantly upon its capacity to anticipate and respond appropriately to these competitive pressures. See Item 4, "Information on the Company Business of Prudential Competition".

Downgrades in Prudential's financial strength and credit ratings could significantly impact its competitive position and hurt its relationships with creditors or trading counterparties.

Prudential's financial strength and credit ratings, which are intended to measure its ability to meet policyholder obligations, are an important factor affecting public confidence in most of Prudential's products, and as a result its competitiveness. Downgrades in Prudential's ratings could have an adverse effect on its ability to market products and retain current policyholders. In addition, the interest rates Prudential pays on its borrowings are affected by its debt credit ratings, which are in place to measure Prudential's ability to meet its contractual obligations. Prudential believes the credit rating downgrades it experienced in 2002 and 2003, together with the rest of the UK insurance industry, have not to date had a discernible impact on the performance of its business.

On June 23, 2006, Standard & Poor's announced that it had lowered its counterparty credit ratings on Prudential's long-term senior debt from AA- (negative outlook) to A+ (stable outlook). At the same time Standard & Poor's revised its outlook on Jackson National Life from AA (negative outlook) to AA (stable outlook).

Prudential's long-term senior debt is currently rated as A2 (stable outlook) by Moody's, A+ (stable outlook) by Standard & Poor's and AA- (stable outlook) by Fitch.

Prudential's short-term debt is rated as P-1 by Moody's, A1+ by Standard & Poor's and F1+ by Fitch.

The PAC long-term fund is rated Aa1 (stable outlook) by Moody's, AA+ (stable outlook) by Standard & Poor's and AA+ by Fitch.

Adverse experience in the operational risks inherent in Prudential's business could have a negative impact on its results of operations.

Operational risks are present in all of Prudential's businesses, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, systems and human error or from external events. Prudential's business is dependent on processing a large number of complex transactions across numerous and diverse products, and is subject to a number of different legal and regulatory regimes. In addition, Prudential outsources several operations, including certain UK processing and IT functions. In turn, Prudential is reliant upon the operational processing performance of its outsourcing partners.

Further, because of the long-term nature of much of Prudential's business, accurate records have to be maintained for significant periods. Prudential's systems and processes are designed to ensure that the operational risks associated with its activities are appropriately controlled but, for example, any weakness in the administration systems or actuarial reserving processes could have an impact on its results of operations during the effective period. Prudential has not experienced or identified any operational risks in its systems or processes during 2005, or which have subsequently caused, or are expected to cause, a significant negative impact on its results of operations.

Adverse experience against the assumptions used in pricing products and reporting business results could significantly affect Prudential's results of operations.

Prudential needs to make assumptions about a number of factors in determining the pricing of its products and for reporting the results of its long-term business operations.

For example, the assumption that Prudential makes about future expected levels of mortality is particularly relevant for its UK annuity business. In exchange for a premium equal to the capital value of their accumulated pension fund, pension annuity policyholders receive a guaranteed payment, usually monthly, for as long as they are alive. As part of its pension annuity pricing and reserving policy, Prudential assumes that current rates of mortality continuously improve over time. During the year, Prudential carried out a review of its mortality experience across all of its non-profit annuity business. As a result of this review, it strengthened the realistic and statutory male assumptions and weakened the realistic female assumptions to align the realistic assumptions with recent experience. Prudential continues to assume future improvements in mortality for males and females at levels projected on the Continuous Mortality Investigations (CMI) medium cohort table as published by the Institute and Faculty of Actuaries. If mortality improvement rates significantly exceed the improvement assumed, Prudential's results of operations could be adversely affected.

A further example is the assumption that Prudential makes about future expected levels of the rates of early termination of products by its customers (persistency). This is particularly relevant to its lines of business other than its UK annuity business. Prudential's persistency assumptions reflect recent past experience for each relevant line of business. Any expected deterioration in future persistency is also reflected in the assumption. If actual levels of future persistency are significantly lower than assumed (that is, policy termination rates are significantly higher than assumed), Prudential's results of operations could be adversely affected.

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

As a holding company, Prudential is dependent upon its subsidiaries to cover operating expenses and dividend payments.

Prudential's insurance and investment management operations are generally conducted through direct and indirect subsidiaries. As a holding company, Prudential's principal sources of funds are dividends from subsidiaries, shareholder-backed funds, the shareholder transfer from Prudential's long-term funds and any amounts that may be raised through the issuance of equity, debt and commercial paper.

Certain of the subsidiaries have regulatory restrictions that can limit the payment of dividends, which in some circumstances could limit the Group's ability to pay dividends to shareholders.

Prudential operates in a number of markets through joint ventures and other arrangements with third parties. These arrangements involve certain risks that Prudential does not face with respect to its consolidated subsidiaries.

Prudential operates, and in certain markets is required by local regulation to operate, through joint ventures. Prudential's ability to exercise management control over its joint venture operations and its investment in them depends on the terms of the joint venture agreements, in particular, the allocation of control among, and continued co-operation between, the joint venture participants. Prudential may also face financial or other exposure in the event that any of its joint venture partners fails to meet its obligations under the joint venture or encounters financial difficulty. In addition, a significant proportion of the Group's product distribution is carried out through arrangements with third parties not controlled by Prudential and is dependent upon continuation of these relationships. A temporary or permanent disruption to these distribution arrangements could affect Prudential's results of operations.

FORWARD-LOOKING STATEMENTS

This annual report may contain certain forward-looking statements with respect to certain of Prudential's plans and its current goals and expectations relating to its future financial condition, performance, results, strategy and objectives. Statements containing the words "believes", "intends", "expects", "plans", "seeks" and "anticipates", and words of similar meaning, are forward-looking. By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events and circumstances which are beyond Prudential's control including among other things, economic and business conditions in the countries in which Prudential operates, market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally; the policies and actions of regulatory authorities, the impact of competition, inflation, and deflation; experience in particular with regard to mortality and morbidity trends, lapse rates and policy renewal rates; the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; and the impact of changes in capital, solvency or accounting standards, and tax and other legislation and regulations in the jurisdictions in which Prudential and its affiliates operate, together with other factors discussed in "Risk Factors". This may for example result in changes to assumptions used for determining results of operations or re-estimations of reserves for future policy benefits. As a result, Prudential's actual future financial condition, performance and results may differ materially from the plans, goals, and expectations set forth in Prudential's forward-looking statements.

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

- certain statements in Item 4, "Information on the Company" with regard to strategy and management objectives, trends in market shares, prices, market standing and product volumes and the effects of changes or prospective changes in regulation, and

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

Prudential may also make or disclose written and/or oral forward-looking statements in reports filed or furnished to the US Securities and Exchange Commission, Prudential's annual report and accounts to shareholders, proxy statements, offering circulars, registration statements and prospectuses, press releases and other written materials and in oral statements made by directors, officers or employees of Prudential to third parties, including financial analysts. Prudential undertakes no obligation to update any of the forward-looking statements contained in this annual report or any other forward-looking statements it may make.

Item 4. Information on the Company

BUSINESS OF PRUDENTIAL

Overview

Prudential is a leading international financial services group, providing retail financial services in the markets in which it operates, primarily the United Kingdom, the United States and Asia. At December 31, 2005, Prudential was one of the 30 largest public companies in the United Kingdom in terms of market capitalization on the London Stock Exchange. Prudential is not affiliated with Prudential Financial, Inc. or its subsidiary, The Prudential Insurance Company of America.

Prudential has been writing life insurance policies in the United Kingdom for over 150 years and has had one of the largest long-term funds in the United Kingdom for over a century. Prudential expanded its business into British Commonwealth countries, including Singapore and Malaysia, in the 1920s and 1930s. In 1986, Prudential acquired Jackson National Life Insurance Company, a US insurance company writing life and fixed annuity business. A group strategy review in the early 1990s identified significant opportunities for Prudential in the Asian life sector and Prudential Corporation Asia was established in 1994 to develop a material and profitable Asian business. In 1998, Prudential launched Egg, now a leading e-commerce retail financial services provider, and in 1999, Prudential acquired M&G, a leading UK fund manager. In June 2000, Prudential completed its listing on the New York Stock Exchange. In December 2005, the Company announced its intention to acquire the minority interests in Egg representing approximately 21.7 per cent of the existing issued share capital of Egg. In February 2006, the Board of Egg announced the delisting of Egg shares, and in May 2006, Prudential completed the repurchase of Egg's shares bringing Prudential's holding to 100 per cent.

In the United Kingdom, Prudential offers a range of retail financial products and services, including long-term insurance and asset accumulation and retirement income products (life insurance, pensions and pension annuities), retail investment and unit trust products, fund management services and banking products. Prudential primarily distributes these products through financial advisors, partnership agreements with banks and other financial institutions, and direct marketing, by telephone, mail and the internet.

At December 31, 2005, in the United Kingdom, Prudential was:

- the second-largest life insurance group in terms of market capitalization,[(1)]
- the proprietor of one of the largest long-term funds of investment assets supporting long-term insurance products (the Prudential Assurance Company long-term fund),[(2)]
- the fourth largest asset manager in the United Kingdom,[(3)]
- through Egg, one of the largest pure on-line banks with over 5 per cent share of total UK credit card balances[(4)], and
- rated as Aa1 (stable outlook) by Moody's, AA+ (stable outlook) by Standard and Poor's and AA+ (stable outlook) by Fitch for the long-term fund of Prudential Assurance. The ratings from Standard & Poor's, Moody's and Fitch for Prudential Assurance's long-term fund represent the second highest ratings in their respective rating categories.

In the United States, Prudential offers a range of products through JNL, including fixed, fixed-indexed and variable annuities, life insurance, guaranteed investment contracts and funding agreements. Prudential distributes these products through independent insurance agents, securities broker-dealers, registered investment advisors and banks, a small captive agency channel, consisting of approximately 100 life insurance agents, credit unions and other financial institutions. Prudential also offers fee-based separately managed accounts and investment products through Curian Capital LLC, which is JNL's registered investment advisor channel established in 2003. At December 31, 2005, in the United States, Jackson National Life was:

- the fifteenth largest life insurance company in terms of General Account assets[(5)]
- the seventh largest provider of individual traditional fixed deferred annuities in terms of sales[(6)],
- the seventh largest provider of fixed-index annuities in terms of sales[(6)],
- the twelfth largest provider of variable annuities in terms of sales, and[(7)]
- rated AA (negative outlook) by Standard & Poor's, AA (stable outlook) by Fitch and A1 (stable outlook) by Moody's in terms of financial strength rating. The ratings from Standard & Poor's and Fitch represent the third highest ratings and the rating from Moody's represents the fifth highest rating out of their respective rating categories. On June 23, 2006, Standard & Poor's revised its outlook on Jackson National Life to stable from negative.

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Prudential Corporation Asia is the leading European-based life insurer in Asia in terms of market coverage and number of top 5 positions in markets, with operations in 12 Asian countries. Prudential Corporation Asia offers a mix of life insurance with accident and health options, mutual funds and selected personal lines property and casualty insurance with the product range tailored to suit the individual country markets. Its insurance products are distributed mainly through an agency sales-force and complementary bancassurance agreements whilst the majority of mutual funds are sold through banks and brokers. Its life insurance operations in China and India are conducted through joint ventures in which it holds 50 per cent and 26 per cent, respectively. In addition, in India, Prudential holds 49 per cent of a fund management joint venture with ICICI, in China it has a 33 per cent stake in a funds management joint venture with CITIC, which is called CITIC-Prudential, and in Hong Kong, it holds a 36 per cent stake in a joint venture with Bank of China International for MPF and mutual funds.

At December 31, 2005 Prudential Corporation Asia had:

- operations in 12 countries and was Europe's leading life insurer in Asia in terms of market coverage and number of top 5 market positions,
- licenses to sell insurance and mutual fund products in ten cities in China,
- over 170,000 tied agents and multiple third party distribution agreements, and
- over seven million policies in force.

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(1) Source: London Stock Exchange at December 31, 2005

(2) Source: Company return to FSA

(3) Source: Investment Management Association

(4) Source: British Banking Association

(5) Source: National Underwriter Insurance Data Services from Highline Data

(6) Source: LIMRA

(7) Source: VARDS

Strategy

In 2005, Prudential undertook a comprehensive strategic review of the retail financial services markets in all major geographies, with an aim of identifying the opportunities, ambitions and business strategies best suited to maximize sustainable growth in value for Prudential's shareholders over the longer term. The key conclusions of the review were that:

- Demographic trends and the increasing concentration of wealth in the hands of those approaching retirement or already retired presents a major opportunity to establish the Group as a leading provider of 'financial services for retirement' by playing to our strengths and areas of competitive advantage;

- the Group is well positioned in its existing markets that offer highly attractive opportunities for strong organic growth over the next 10 years;

- to exploit these opportunities fully Prudential needs to broaden its product range to align them more closely with anticipated retail financial sector profit pools;

- in addition, we must complement our strong and important intermediary links by expanding the proportion of revenue derived from direct customers and ensure that we build deep life-cycle relationships with our customers;

- Prudential should also develop the global reach and profile of our excellent asset management businesses.

Each of Prudential's businesses has operational autonomy within its market and this is critical to our success, since it is the key to our ability to tailor products and services to meet local market needs. However, the review also concluded that there are material synergies that can be achieved through closer working across the Group, consistent with our decentralised approach.

Finally, the review concluded that Prudential must continue to enhance the effectiveness of our capital management processes, to ensure that investment and capital allocation decisions are focused on those areas of activity that will generate the best returns to shareholders.

Shareholder Focus

Prudential's strong mix of businesses around the world positions it well to benefit from the growth in customer demand for asset accumulation and income in retirement. Prudential believes that its international reach and diversity of earnings will continue to give it a significant advantage.

Prudential's commitment to its shareholders is to maximize the value over the time of their investment. Prudential does this by investing for the long-term to develop and bring out the best in its people and its business to produce superior products and services, and hence superior financial returns.

Prudential's aim is to develop lasting relationships with its customers and policyholders, through products and services that offer value for money and security. Prudential seeks to continually enhance its reputation, built over 150 years, for integrity and for acting responsibly within society.

Building the Platform

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

Prudential has significantly restructured its operations in both the United Kingdom and the United States over the last few years to improve its customer focus and management accountability, and to broaden its product range and distribution reach.

In the United Kingdom, Prudential restructured its long-term savings business into an integrated business combining Prudential's UK businesses with that of Scottish Amicable, which was acquired in 1997, to form Prudential UK Insurance Operations. This has resulted in improved operational effectiveness through removal of duplication, greater customer focus and reduced operating costs.

The Boards of Prudential and Egg announced on December 1, 2005 a recommended Offer by Prudential for the 21.7 per cent of shares in Egg that Prudential did not already own. On February 20, 2006, Egg shares were delisted from the official list. The transfer of the balance of the outstanding shares was completed on May 16, 2006. Prudential anticipates that the acquisition of the minority interest in Egg will enable it and Egg to capitalize on the product capabilities, customer relationships and brand strengths of Prudential, M&G and Egg and to facilitate the realization of substantial annualized pre-tax cost savings, with £40 million expected to be realized by the end of 2007, as well as opportunities for revenue synergies.

In the United States, Prudential has an extensive and diversified product range that includes variable annuities, fixed annuities, fixed-index annuities, life assurance and stable value products. Prudential has also significantly diversified its distribution of these products by now distributing through independent and regional broker-dealer channels and the bank channel. With the launch of Curian in 2003, Prudential extended its distribution into the registered investment advisor channel, and the acquisition of Life Insurance Company of Georgia ('Life of Georgia') in 2005 created Prudential's first captive agency distribution in the US, with approximately 100 life assurance agents.

In Asia, building on a solid base of established operations in Singapore, Hong Kong and Malaysia, Prudential has followed since 1994 a clear, value creating strategy of entering new markets, building and diversifying distribution and launching innovative products targeting profitable market segments.

This value is clearly demonstrated by the scale and mix of Prudential's new business sales. In 2005, new business sales were approximately £40 billion with over half coming from mutual fund sales, and 62% coming from outside the United Kingdom.

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

Growing the Business

Prudential is conscious that the retail financial services industry continues to evolve, and it expects to continue to adapt its business to maintain a strong advantage over its competitors while delivering returns to shareholders. Prudential's goal is to pursue its key strategic themes of maintaining focus on its customers, investing in technology to improve further customer access and service, driving down costs and driving growth in its existing markets.

The strength of Prudential's businesses and positive developments in a number of its markets represent an opportunity to enhance its market position and generate improved returns for its shareholders. A strong financial position at a Group level provides increased financial flexibility and allows Prudential to capitalize on these opportunities as they arise. In response to these developments the Board decided in October 2004 to launch a 1 for 6 rights offering. As at December 31, 2005 approximately 25 per cent of the net proceeds of Prudential's rights offering (£1,021 million) have been used to provide capital to support Prudential's shareholder-backed UK life businesses. The remainder of the proceeds have been invested centrally within the Group in short-term financial instruments.

Driving Growth

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

The UK insurance market suffered three years of decline until 2004 when the market showed signs of recovery which continued in 2005. During the period of decline, Prudential transformed its UK insurance business from a direct-sales operation, selling with-profits products, into a company that sells mainly shareholder-backed products through a range of channels, including financial advisors, business to business and partnership agreements with other companies. Prudential also improved its efficiency and broadened its product range. Over the next few years, Prudential intends to continue to focus on efficient profitable growth seeking new opportunities within its distribution channels and product range.

Following the introduction of the new depolarization rules in December 2004 whereby insurers can distribute their products via multi-tied advisor panels as well as the previous single-tied or whole-of-market advisors, many financial advisor groups have used the opportunity to establish multi-tie panels. Prudential has made good progress with the new panels announced to date, and believes that it is strongly positioned to take advantage of the depolarized marketplace as this develops over the next few years. Prudential achieved sales of £37 million through this channel in 2005 and expects that multi-ties will start to have a greater impact on sales in the future.

Prudential's 'partnerships channel', which is part of the Group's UK marketing effort, focuses on distributing products via banks and other financial institutions, signed a number of significant new agreements during 2005. These included St. James's Place for annuities; National Australia Bank for annuities and healthcare; Wesleyan's multi-tie panel for protection; Zurich Financial Services and Openwork for annuities; and the Barclays multi-tie panel. In addition, Prudential and Royal London reached agreement for all pension annuities arising from vesting of policies written under the Scottish Life brand in the period between January 2005 and December 2010 to be reassured to Prudential.

In October 2004 Prudential launched PruHealth, a UK healthcare product that links health and fitness to the cost of medical insurance. The business has made good progress with sales growing on average more than 30 per cent per month in 2005. Total premium income for the year was £9 million, and PruHealth now covers over 30,000 individuals. The product has been developed through a joint venture with Discovery of South Africa.

In October 2005, Prudential launched Prudential Property Value Release Plan. A life time mortgage product which gives customers greater flexibility and control over the timing of when they draw down funds, thereby reducing total interest charges over the lifetime of the loan. It has been well received by advisors and customers.

M&G has four main business lines with distinct growth strategies: (a) the internal business aims to create value through investment performance and liability matching for internal clients' and to develop skills to facilitate the Life Fund's move into non-correlated assets; (b) the institutional business utilizes skills developed primarily for internal clients to build new business streams and diversify revenues; (c) the retail business aims to maximize the leverage offered by investment performance and a single product manufacturing hub; and (d) Prudential Finance combines the management of Prudential's balance sheet with M&G's market positions to develop a new profit stream.

In the US, Prudential completed the purchase of Life of Georgia in May 2005 for a preliminary consideration of £142 million. This acquisition doubled the number of Jackson National Life's in-force life and annuity policies, adding scale to its operating platform and expanding its distribution capability, as well as further diversifying its income streams. Prudential believes that this transaction will enable Jackson National Life to grow its life business at a higher return and faster rate than could be achieved organically.

The Company expects that JNL will continue to consider further US bolt-on acquisitions as opportunities arise.

In October 2004, JNL completed the sale of JFB to Union Bank of California for £166 million. JFB's principal area of business was banking and commercial real estate lending, which no longer aligned with JNL's strategy. Accordingly, the results of operations for JFB are reported as discontinued operations in the accompanying financial statements.

Prudential believes that Asia offers significant long-term growth opportunities and its strategy is designed to create material and sustainable value in Asia by focusing on three dimensions: participating in countries where there are opportunities to leverage its strengths, building and diversifying distribution and providing innovative customer-focused products. In India, our joint venture with ICICI continues to be a leading private sector player. In 2004, the Indian government announced its intention to allow increased foreign ownership in Indian companies, and Prudential remains interested in increasing our stake in the joint venture. However, the relevant legislation has not yet been put before the Indian Parliament.

In 2005, licenses to sell financial products in six new cities in China were granted by the Chinese authorities, bringing the total number of such licenses on December 31, 2005 to ten. As of April 30, 2006, CITIC-Prudential had been granted 13 life insurance licenses to operate in China. Prudential believes the main challenge facing foreign players trying to become established in China is the need to develop local management teams to support geographic expansion. Prudential believes that it has a real advantage in being able to leverage its existing Chinese speaking operations to help develop new teams quickly. In 2005, sales in China increased by 47 per cent over 2004.

Prudential and Bank Simpanan Nasional ('BSN'), which was originally the Malaysian Post Office Savings Bank and is now wholly owned by the Malaysian Ministry of Finance, established a joint venture to leverage Prudential's existing network of 7,000 agents and BSN's network of 391 branches. In January 2006, the Malaysian authorities granted the joint venture a license to develop and market life insurance products to Muslim Malays who make up more than 60 per cent of the population.

In June 2005, The Prudential Vietnam Fund Management Company was launched with a mandate to manage the life fund. It also has plans to develop the emerging retail funds market in Vietnam and to launch retail funds

Focusing on Customers

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

In the United Kingdom, Prudential has complementary businesses and market-leading positions in key product areas, enabling it to selectively participate on a value basis. The businesses comprising Prudential's UK Insurance Operations have undergone enormous strategic transformations in recent years, bringing together several operating units under the powerful Prudential brand and improving service to over seven million customers. In 2002, Prudential's UK Insurance Operations announced the development of an outsourced customer service operation in Mumbai, India. In May 2003, the Mumbai customer service center opened and at the end of 2005 employed over 1,000 people.

M&G is Prudential's UK and European fund management business and had over £149 billion of funds under management as of December 31, 2005, of which £113 billion related to Prudential's long-term business funds. M&G operates in markets where it has a leading position and competitive advantage, including retail fund management, institutional fixed income, pooled life and pension funds, property and private finance. Based on December 2005 data from the Investment Management Association, M&G ranks as the fourth largest asset manager in the UK.

Egg offers a proven direct to consumer distribution channel that will provide UK financial services consumers a full range of product offerings under both the Egg and Prudential brands going forward. Prudential expects that these product offerings, specifically, credit cards, unsecured personal loans, mortgages, savings and general consumer insurance products will allow the combined entity to meet customer needs at each stage of their lifecycles. The Egg brand will continue to be focused on credit cards, unsecured personal loans, mortgages, savings and general consumer insurance products with the Prudential brand providing longer term savings and protection products.

In the United States, Prudential, through JNL maintains a significant market position across the range of fixed, variable and fixed-indexed annuity products. These products offer guarantees and longevity protection that will become increasingly important in the US as the 77 million 'baby boomers' reach retirement age over the next decade. JNL also offers life and institutional products, and through the acquisition of Life of Georgia in 2005, JNL doubled its number of in-force life and annuity policies, adding scale to its operating platform and expanding its distribution capability. JNL continues to expand its distribution channels and now distributes through independent agents, broker-dealers, banks, registered investment advisors, a small captive agency channel, and other financial institutions.

In Asia, Prudential has a reputation for developing customer-focused and innovative savings and insurance products. It leverages UK and US product expertise and works with Asian regulators to bring new products to market, achieving particular success with unit-linked products. While Prudential believes customer needs in Asia are well met by traditional tied agents in most markets, it also gives customers the choice to access its products through complementary bancassurance arrangements, direct distribution and brokers.

Corporate Activity

In March 2006, Prudential received a proposal from Aviva plc about a possible combination of the businesses of Prudential and Aviva. Aviva's offer, which was valued at an aggregate purchase price of approximately £17 billion, included an all-share merger of the two companies based on a merger ratio of 82 Aviva shares for every 100 shares of Prudential, resulting in an implied value of 708 pence per Prudential share based on closing relative share prices on March 17, 2006. The Board of Prudential plc, which had taken independent financial advice, did not consider that the proposal was in the best interests of Prudential shareholders and rejected it. On March 24, 2006, Aviva announced the withdrawal of its proposal.

Summary

- Prudential has compelling positions in the world's leading retail financial services markets and the resources to capitalize on these;

- In the UK, Prudential has three excellent and profitable franchises in Prudential UK Insurance Operations, Egg and M&G on which to build for the future;

- In the US, JNL is a significant cash-generative business with the market positioning for profitable growth in the retirement market. It has competitive advantage in the sectors in which it chooses to operate; and the ability to participate in market consolidation through bolt-on acquisitions;

- In Asia, Prudential has an unrivalled exposure to opportunities for life insurance sales and profit growth across the region, whilst continuing our programme of rapid expansion and profit growth; and

- Prudential's asset management business has significant growth prospects and is providing solid cash flow generation.

There is tremendous scope to deliver increasing value for shareholders from each individual business operation, and from the Group as a whole which derives both financial advantage and resilience from the diversity of its portfolio of businesses, and the opportunities for collaboration between them.

Company Address and Agent

Prudential plc is a public limited company organized under the laws of England and Wales. Our registered office is Laurence Pountney Hill, London EC4R 0HH, England (telephone: +44 20 7220 7588). Our agent in the United States is Jackson National Life Insurance Company, located at 1 Corporate Way, Lansing, Michigan 48951, United States of America.

Significant Subsidiaries

The table below sets forth Prudential's significant subsidiaries.

Name of Company	Percentage Owned(1)	Country of Incorporation
The Prudential Assurance Company Limited	100%	England and Wales
Prudential Annuities Limited(2)	100%	England and Wales
Prudential Retirement Income Limited(2)	100%	Scotland
M&G Investment Management Limited(2)	100%	England and Wales
Egg Banking plc(2)(3)	79%	England and Wales
Jackson National Life Insurance Company(2)	100%	United States
Prudential Assurance Company Singapore (Pte) Limited(2)	100%	Singapore
PCA Life Assurance Company Limited(2)	99%	Taiwan

(1) Percentage of equity owned by Prudential directly or indirectly. The percentage of voting power held is the same as the percentage owned. Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for Prudential Retirement Income Limited which operates mainly in England and Wales.

(2) Owned by a subsidiary of Prudential.

(3) Egg Banking plc is a subsidiary of Egg plc. At December 31, 2005, the ordinary shares of Egg plc were listed and there was only one class of shares that were 78% owned by Prudential, 1% owned by other companies within the Prudential Group and 21% owned by shareholders external to the Prudential Group. In December 2005, Prudential announced its intention to acquire the whole of the issued and to be issued shares of Egg not already owned by the Prudential Group. In February 2006, the Board of Egg announced the delisting of Egg shares. The transfer of all the outstanding shares was completed on May 16, 2006.

UK Business

Introduction

As at December 31, 2005, Prudential's UK business was structured into three business units, each focusing on its respective target customer markets. Prudential's UK business units are UK Insurance Operations, M&G and Egg.

The following discussion describes:

- the UK retail financial services market,
- Prudential's UK business units and products,
- Prudential's reinsurance arrangements and reserving practices,
- shareholders' participation in Prudential's long-term insurance business, and
- compliance matters, including pension mis-selling.

In 2005, Prudential's UK business generated new business insurance premiums of £7,276 million and investment flows of £7,916 million. As of December 31, 2005, M&G had over £149 billion funds under management and Egg had customer deposits of £5,830 million and a credit card book of £3,491 million. See " M&G" below for an analysis of funds under management.

UK Retail Financial Services Market Overview

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

The historical divisions between insurance, banking and other financial products are being eroded. It is increasingly common for providers to offer a range of pension products, life products and services, property and casualty insurance, banking products and retail investment products and services. Consumers are increasingly being offered access to these products through direct marketing and over the internet, as well as through the traditional company sales force, financial advisors, and bank branch distribution channels. However, for more complicated products, detailed "fact finds" are often required and consequently face-to-face advice is still preferred.

Financial advisors continue to be the principal channel for the distribution of life and pension products for insurers in the UK. This channel is undergoing significant change with the introduction by the Financial Services Authority (FSA) of new "depolarization" rules in December 2004, leading to the establishment of multi-tie panels. Over the next few years, Prudential UK expects that a significant proportion of whole of market providers, which were previously known as independent financial advisors (IFAs), will move to a panel approach whereby they distribute the product range of a select number of life insurance companies.

Depolarization is also expected to have an effect on the UK bank distribution market as some banks move to offer their customers products from a panel of different providers rather than from a single product provider.

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

Prudential believes that the prospects for the UK life insurance industry are improving and that it is now well positioned to take advantage of the opportunities presented. In accordance with this, the majority of the net proceeds of the Right Issues raised in 2004 are being used to provide capital to support Prudential's growth plans in the UK.

Prudential is determined to focus its participation in the UK market in propositions with high returns on capital invested and high margins.

UK Products and Profitability

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

With-profits policies are supported by a with-profits sub-fund and can be single premium (for example, Prudence Bond) or regular premium (for example, certain corporate pension products). Prudential's primary with-profits sub-fund is part of Prudential Assurance Company's (PAC) long-term fund. The return to shareholders on virtually all with-profits products is in the form of a statutory transfer to PAC shareholders' funds which is analogous to a dividend from PAC's long-term fund and is dependent upon the bonuses credited or declared on policies in that year. Prudential's with-profits policyholders currently receive 90 per cent of the distribution from the main with-profits sub-fund as bonus additions to their policies and shareholders receive 10 per cent as a statutory transfer.

The profits from almost all of Prudential's new non-participating business accrue solely to shareholders. Such business is written in the non-profit sub-fund within PAC's long-term fund, or in various shareholder owned direct or indirect subsidiaries, the most significant of which is Prudential Retirement Income Limited (PRIL), which also writes all new immediate annuities arising from vesting deferred annuity policies in the with-profits sub-fund of PAC. There is a substantial volume of in-force non-participating business in PAC's with-profits sub-fund and that fund's wholly owned subsidiary Prudential Annuities Limited (PAL), which is closed to new business; profits from this business accrue to the with-profits sub-fund.

Products

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

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

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

Accounts, referred to as ISAs, a tax-advantaged product that offers equity, insurance and deposit investment options. ISAs will continue until 2010 based on government pronouncements.

The UK government introduced "stakeholder pensions" in April 2001 with the intention of creating a pension for individuals who were earning enough to be able to afford to make a contribution towards a pension but were not currently doing so.

Prudential anticipates that 2006 will be a year of change for the retirement savings market due to Government pension reforms that came into force on April 6 (A-day). Prudential believes the changes will have a positive impact and create an improved savings environment over time, although it is unclear how quickly consumers will respond to these new regulations.

Prudential made a significant investment in its A-day preparations, including systems development and customer communications. Prudential launched a new Flexible Retirement Plan in 2005 and it will undertake a review of its overall individual pension offerings in 2006.

Historically, the majority of the life and pensions business written in the United Kingdom was with-profits business. However, in response to regulatory scrutiny and subsequent changes in the regulatory environment and customer requirements, with-profits products are being increasingly supplemented by simpler unit-linked products. For a detailed description of Prudential's with-profits products and policies, see " Shareholders' Interests in Prudential's Long-term Insurance Business With-profits Products".

Distribution

Retail financial services and products are distributed face-to-face, through branches, tied agents, company sales forces and financial advisors, or directly by mail, telephone and over the internet. Tied agents are exclusive agents who represent only one insurer and must offer customers the products most suitable to their needs, but only from the range of products offered by that insurer. In recent years the high costs of company sales forces and tied agency networks, combined with customers perceiving a lack of choice, have meant that sales forces and tied agents have lost significant market share to financial advisors, with the result that many insurers, including Prudential, have chosen to close these tied agents and direct sales force networks.

Direct and e-commerce distribution methods are generally lower-cost than other methods but have not been conducive to providing financial advice to the consumer to date. Accordingly, products distributed directly are generally more straightforward and have lower, often fee-based, charges.

Previously, IFAs were required by the UK polarization laws to provide the best advice to customers, considering all of the products available in the market and the customer's particular circumstances, and were legally responsible for their own advice. In contrast, company sales forces could only sell the products of the company they were employed by, but nevertheless had to provide the best advice in light of the customer's particular circumstances. A company had legal responsibility for the advice its sales force provided and the conduct of its tied agents.

The FSA announced a relaxation of the polarization rules in March 2001 with respect to stakeholder pension schemes and direct offer financial promotions for packaged products (which include life policies other than pure protection policies, pensions, regulated collective investment schemes and investment trust savings schemes). As a result of these changes, tied sales forces and appointed representatives of product provider firms are now free to market stakeholder pensions manufactured by any other company.

The FSA, following a consultation process, implemented new 'depolarization' rules at the end of 2004. Advisors now have the choice of being 'single tied' as before, or multi-tied advising on the products of a limited range of providers, or equivalent to an IFA where they offer products from the 'whole of market' as now, but they also have to offer a 'fee alternative', a fee-based charging structure as an alternative to commission. Our view is that over time a significant number of existing whole of market advisors will choose to adopt a 'multi tie' selecting a limited number of large brands.

Prudential has worked with major financial advisor groups to design and build multi tie propositions, and Prudential UK has been appointed to multi-tie panels for Millfield, THINC Destini, Sesame, Bankhall and Barclays.

As of December 31, 2005, Prudential UK Insurance operations distributes its products through the following channels:

Direct to Consumer

The direct to consumer distribution channel is primarily charged with increasing revenue from existing Prudential customers and by seeking new customers. Direct to Consumer includes the telephone and Internet and focuses on annuities, protection and health products.

Business to Business

The business to business distribution channel focuses on the maximization of the value of the existing book of corporate pension schemes and winning new schemes. This channel targets Prudential's strong base of corporate pensions through workplace marketing. Prudential UK corporate pension products are marketed through consulting actuaries, benefits advisors and its company employer and employee relationship management teams. Consulting actuaries and benefits advisors are IFAs, but are not generally the same as the retail financial advisors being targeted via the intermediary channel discussed below. In addition, Prudential markets bulk annuities to trustees of Defined Benefit schemes via employee benefit consultants.

Within the Corporate Pensions sector the advisor market is heavily dominated by a small number of Employee Benefit Consultants (EBCs) who control the majority of the 250 plus lives sectors. Prudential targets its proposition at medium to large sized employers, distributed via the major EBCs on a nil commission basis. Prudential has a well developed and comprehensive worksite communication proposition that is effectively deployed within both its new and existing clients to educate and inform members as well as increasing the take up within the arrangements.

Intermediaries

The intermediary channel focuses on the distribution of products to individual customers via retail financial advisors. This channel was restructured during 2004 in response to the new regulatory regime effective from December 2004. A new infrastructure was created to customize the levels of support required. A new divisional structure was implemented that matches field-based account managers with high value customer segments. Lower value segments are serviced by telephone-based account managers. The new organization structure positions the Intermediaries business to extract maximum value from the opportunities the new regulatory regime presents.

Following the introduction of the new depolarization rules, many financial advisor groups have used the opportunity to establish multi-tie panels. Prudential has made good progress with the new panels announced to date, and is strongly positioned to take advantage of the depolarized marketplace as this develops over the next few years. Prudential achieved sales of £37 million through this channel in 2005 and expects that multi-ties will start to have a greater impact on sales in the future.

Corporate Partnerships

The corporate partnerships channel focuses on developing strong relationships with banks, retail brands and other distributors. Corporate partnerships also seeks to help our distribution partners in their distribution and product development strategies. We now have a range of providers including Barclays, Lloyds TSB, Pearl Assurance, Zurich Financial Services, Openwork, National Australia Bank, St James

Place and with Royal London to provide pension annuities for vesting Scottish Life policies. In June 2005, Prudential reached agreement with Resolution Life to acquire a portfolio of the in-force pension annuities from its subsidiary, Phoenix Life & Pensions.

UK Business Units

UK Insurance Operations

Products

Prudential offers a wide range of products, which traditionally have been marketed under the "Prudential" and "Scottish Amicable" brands. From January 2003, however, products have only been sold under the Prudential brand. See " Item 5 Operating and Financial Review and Prospects Analysis by Geographic Region UK Insurance operations UK Restructurings". The products distributed include long-term products consisting of:

- life insurance savings-type products and pure protection products,
- individual and corporate pensions, and
- pension annuities.

In October 2004 Prudential launched PruHealth, a UK healthcare product that links health and fitness to the cost of medical insurance. As PruHealth is not a life insurance product its premium income is not reported as long-term new business sales. In 2005, gross written premiums were £9 million, with over 30,000 covered individuals. Support for PruHealth is strong in both the intermediaries channel and the direct to consumer channel, and its rate of growth is accelerating. The product has been developed through a joint venture with Discovery of South Africa. For further information see "Strategy Driving Growth" above.

In October 2005, Prudential launched Prudential Property Value Release Plan. A life time mortgage product that gives customers greater flexibility and control over the timing of when they draw down funds, thereby reducing total interest charges over the lifetime of the loan. It has been well received by advisors and customers.

Long-term Products

Prudential's long-term products in the United Kingdom consist of life insurance, pension products and pensions annuities. The following table shows Prudential's UK Insurance Operations new business insurance and investment premiums by product line for the periods indicated. New business premiums include deposits for policies with limited or no life contingencies.

	Year Ended December 31,	
	2005	**2004**
	(in £ millions)	
Life insurance		
With-profits	**175**	246
Unit-linked	**1,780**	1,565
Total life insurance	**1,955**	1,811
Pensions		
With-profits individual	**30**	28
Unit-linked individual	**73**	60
Department of Work and Pensions rebates	**327**	354
Corporate	**438**	432
Total pensions	**868**	874
Pension annuities and other retirement products		
Fixed	**3,752**	3,482
Retail Price Index	**347**	204
With-profits	**153**	76
Total pension annuities	**4,252**	3,762
Total new business premiums	**7,075**	6,447

New business premiums in 2005 were £7,075 million, up approximately 10 per cent on 2004. This increase principally reflects a growth in sales of unit-linked life and pension products and pension annuities. The growth in Pension Annuities was mainly driven by the acquisition of the £1,450 million portfolio of in-force pension annuities from Phoenix Life & Pensions. This is the second transaction of this type and magnitude achieved following the £1,108 million transaction with Royal London in 2004.

Life Insurance Products

Prudential's UK life insurance products are predominantly medium to long-term savings products with life cover attached, and also include pure protection (term) products. The main savings products Prudential offers are investment bonds.

Savings Products Investment Bonds

Prudential offers customers a choice through a range of investment funds to meet different risk and reward objectives. Prudential launched the Flexible Investment Plan ("FIP") in November 2003. Through this plan, its customers have the option to invest in the Prudence Bond (With-Profits) along with a range of unit linked investment funds. Advisors can build an individual portfolio and asset allocation model to accurately match a client's risk / reward profile. FIP also gives financial advisors the opportunity to choose from different external fund management groups and the flexibility to make changes to portfolio and asset allocation over time. In 2005, sales of the Unit-linked option of FIP were £516 million.

The Prudence Bond, a single premium, unitized with-profits policy with no fixed term, is one of the United Kingdom's leading investment bond products in terms of with-profits market share. Prudential launched the Prospect Bond, another single premium with-profits bond, in October 2003. The Prospect Bond gives investors the opportunity to move out of under performing funds elsewhere in the market, and into the Prudential With-Profits Fund. In September 2004, Prudential launched the next generation with-profits investment bond, entitled PruFund. A replacement for Prudence Bond it is designed to

provide increased transparency and smoothed investment returns to the customer. In 2005, total new business premiums attributable to the PruFund, Prudence Bond, Prospect Bond and the Prudential Investment Bond, were in excess of £158 million. Sales of Prudential's offshore bonds, the International Prudence Bond and International Prudential Portfolio Bond, were £308 million in 2005.

With-profits products aim to provide capital growth over the medium to long-term, and access to a range of investment sectors without the costs and risks associated with direct investment into these sectors. Capital growth for the policyholder on with-profits bonds apart from PruFund is achieved by the addition of reversionary or regular bonuses, which are credited to the bond on a daily basis from investment returns achieved within Prudential Assurance's long-term with-profits fund, off-set by charges and expenses incurred in the fund. A final bonus may also be added when the bond is surrendered. PruFund delivers growth through a published expected growth rate, updated quarterly, and a transparent formulaic smoothing mechanism. In contrast the capital return on unit-linked bonds directly reflects the movement in the value of the assets underlying those funds. When funds invested in Prudential Assurance's long-term with-profits fund are either fully or partially withdrawn, Prudential may apply a market value adjustment to the amount paid out.

Life Protection

Prudential underwrites Life protection for companies providing loans to their customers. Sales in 2005 were £833 million mostly generated through Prudential's partnership agreements with Lloyds TSB and Alliance and Leicester.

Pension Products

Prudential provides both individual and corporate pension products. In 2005, new business premiums totalled £103 million for individual pensions and £438 million for corporate pensions. Pension products are tax-advantaged long-term savings products that comply with rules established by the UK Inland Revenue and are designed to supplement state- provided pensions. These rules require that, upon retirement, maturity benefits are used to purchase pension annuities by policyholder election at retirement or at least by the age of 75, although they do permit a portion to be taken as a tax-free lump sum. Prior to retirement, these products typically have minimal mortality risk to Prudential and are primarily considered investment products. An exception is where a guaranteed annuity option has been offered on the product, with an element of risk to Prudential both in underlying mortality and investment assumptions.

Prudential ceased marketing Guaranteed Annuity Options ("GAOs") in 1987, but for a minority of corporate pension schemes GAOs still apply for new members. Current liabilities for this type of business make up less than 1 per cent of the with-profits sub-fund.

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

Individual Pensions

Prudential's individual pension range offers unit-linked and unitized with-profits products.

In 2001, Prudential introduced products that meet the criteria of the UK government's stakeholder pension program. The stakeholder pension is intended for individuals earning enough to be able to afford to make contributions to a pension but who are not currently doing so. The introduction of stakeholder pensions has had implications for, among other things, how Prudential designs, administers, charges for and distributes pension products. The most significant requirements involve capped charges and a low minimum contribution which must be accepted by the provider. The government has capped charges at 1.5 per cent per annum of the policyholder account balance for stakeholder pensions for the first ten years, decreasing to 1 per cent thereafter, which is below the charges on personal pension products previously offered by the UK pensions industry.

Prudential launched a new retirement savings product, the Flexible Retirement Plan in 2005 and will undertake a review of its overall individual pensions offering in 2006.

Department of Work and Pensions Rebates ("DWP Rebate")

Prudential also provides individual personal pension products through the DWP Rebate arrangement. Under this arrangement, individuals may elect to contract out of the UK's State Second Pension (referred to as SP2) which was previously known as State Earnings Related Pension Scheme, administered by the UK Department of Work and Pensions. If an individual elects to contract out, then he or she will designate a pension provider, such as Prudential. Premiums on products sold in this manner are paid through "rebates" from the Department of Work and Pensions, which represent the amount that would be otherwise paid into SP2. Rebate amounts are invested to provide benefits to the individual. Premiums from Department of Work and Pensions rebates are typically reported in the first quarter of each year.

In 2005, Prudential wrote to 440,000 of its customers contracted out of the second state pensions and provided updated information and views to enable them to make an informed decision about whether to contract back in for the 2005/6 tax year onwards. As a result of this mailing, approximately 132,000 customers elected to contract back into the State scheme resulting in a decline in DWP rebate business of 29 per cent in the first quarter of 2006.

Corporate Pensions

There are two categories of corporate pension products: defined benefit and defined contribution. Prudential has an established defined benefit plan client base covering the small to medium sized employer market. Prudential's defined contribution client base ranges from small-unlisted companies to some of the largest companies in the United Kingdom as well as a number of clients in the public sector (in particular the Additional Voluntary Contribution Sector). Additional Voluntary Contribution plans enable employees to make additional pension contributions, either regularly or as a lump sum, to supplement their occupational pension plans.

Defined benefit plans and products continue to dominate the corporate pensions market in terms of funds under management. In recent years, however, most new plans established have been defined contribution products. In addition, there is an increasing trend among companies to close the plans to new members or to convert existing schemes from defined benefit to defined contribution in order to stabilize or reduce potential pension liabilities.

Prudential offers group unit linked policies and with-profits policies to the corporate pensions market. Prudential's defined contribution products are Additional Voluntary Contribution plans, Group Money Purchase Plans, Group Personal Pension plans, Group Stakeholder Pension plans and Executive Pension plans.

Prudential also has a Company Pension Transfer Plan (or Bulk S32), designed to accept benefits from both defined benefit and defined contribution pension schemes which are winding-up (cease to exist or being replaced by a new type of scheme).

Pension Annuities and other retirement products

Prudential offers individual conventional immediate annuities that are either fixed or retail price indexed (referred to as RPI), where annuity payments are guaranteed from the outset, or with-profits annuities, where annuity payments are variable. A total of £2,222 million of individual conventional annuities were sold in 2005. Of this total, £1,130 million were sold to existing Prudential customers with maturing pension policies. The other £1,092 million were sold to new customers, typically individuals with a pension maturing with another provider who chose Prudential to provide their annuity. Prudential also offers bulk annuities, whereby it manages the assets and accepts the liabilities, of a company pension scheme, usually when it is being wound up by the employer. Due to the nature of the product, the volume of Prudential's bulk annuity sales is unpredictable as it depends on the decision of scheme trustees. In 2005, Prudential sold £2,030 million of bulk annuities, of which £1,450 million related to the acquisition of the portfolio of in-force pension annuities from Resolution Life's subsidiary, Phoenix Life & Pensions.

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

Conventional Annuities

Prudential's conventional annuities include level (non-increasing), fixed increase and retail price index ("RPI") annuities. Prudential's fixed increase annuities incorporate automatic increases in annuity payments by fixed amounts over the policyholder's life. The RPI annuities provide for a regular annuity payment to which an additional amount is added periodically based on the increase in the UK Retail Prices Index. In 2005, sales of RPI annuities were £347 million (including £245 million of bulk annuities). In 2005, sales of level and fixed increase annuities amounted to £3,752 million (including £2,080 million of bulk annuities and £26 million of unit-linked Flexible Retirement Income Account products ("FRIA")).

With-profits Annuities

Prudential is one of only a few companies in the United Kingdom writing with-profits annuities. In 2005, Prudential wrote £153 million of this business. Prudential's with-profits annuities combine the income features of annuity products with the investment smoothing features of with-profits products and enable policyholders to obtain equity-type returns over time. Policyholders select an "anticipated bonus" from the specific range Prudential offers for the particular product. The value of the annuity payment each year depends upon the anticipated bonus rate selected by the policyholder when the product is purchased and the bonuses Prudential declares each year during the term of the product. If bonus rates fall below the anticipated rate, then the annuity income falls.

Flexible Retirement Income Account

FRIA offers customers a flexible retirement solution and consists of two separate products. The Flexible Income Draw-down Plan ("FIDP") offers wide investment choice, income flexibility and options on death, including the repayment of the remaining fund as a lump sum. Under the current rules for approval of pension schemes, customers can use this draw-down product to provide retirement income up to age 75. These rules require customers to purchase annuities with any remaining pension funds at age 75. The Flexible Lifetime Annuity ("FLA") offers similar investment choice and income flexibility to FIDP but no lump sum death benefits. Prudential sold £29 million of the FRIA products in 2005.

Lifetime mortgage

In October 2005, Prudential launched Prudential Property Value Release Plan. A life time mortgage product which gives customers greater flexibility and control over the timing of when they draw down funds, thereby reducing total interest charges over the lifetime of the loan. It has been well received by advisors and customers.

M&G

M&G is Prudential's fund management business in the United Kingdom and continental Europe and comprises retail, institutional and internal fund management activities. Its key metrics of performance are profits, net sales and investment performance.

Gross fund inflows into M&G's retail products were a record £3.8 billion in 2005, a 90 per cent increase on 2004 as M&G maintained its fixed income sales and continued to increase fund flows into equity funds on the back of its strong fund performance. Net fund inflows for 2005 were £1.3 billion. This enabled M&G to consolidate its position as one of the top four retail fund managers in the United Kingdom, measured in terms of total funds under management (source: Investment Management Association).

In its institutional businesses, M&G continued to reap the benefits of its position as a leading innovator in fixed income and private finance, with gross fund inflows increasing by 5 per cent to £4.1 billion during 2005. Net fund inflows were £2.5 billion. The successful strategy of developing new external business lines with attractive margins, using expertise developed for internal funds, generated increased revenue streams, especially in the area of non-correlated assets such as leveraged loans. M&G's private finance business successfully completed two more Collateralized Debt Obligations ("CDOs") during the year, bringing the total number of CDOs launched since 2001 to eleven.

Over three years Prudential UK's main with-profits fund, which is principally managed by M&G, has generated annual returns 1.03 per cent higher than its strategic benchmark and 2.77 per cent higher than its competitor benchmark. Total performance fees in 2005 were £24 million, including £7 million of performance related fees for the management of the Prudential Assurance Company long-term and annuity funds which continued to beat their strategic and competitor benchmarks during the year. M&G also received £17 million which related to the disposal of some of the investments by PPM Capital that are not expected to recur.

According to Standard & Poor's within the Retail business 46 per cent of M&G funds were in the top quartile over the last three years up to December 31, 2005 and 50 per cent of equity funds were in the top quartile.

M&G's property division, Prudential Property Investment Managers ("PruPIM"), which invests primarily on behalf of the Prudential Assurance Company, significantly increased its funds under management during 2005 and expanded its product offering into the retail marketplace with the launch of the M&G Property Fund alongside its growing unit-linked funds. PruPIM is one of the largest institutional property fund managers in the UK with over £17.2 billion invested in the property market.

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

	At December 31,	
	2005	**2004**
	(In £ Billions)	
Retail fund management	**15**	11
Institutional fund management	**21**	17
Internal fund management	**113**	98
Total	**149**	126

Retail Fund Management

M&G's retail fund management business comprises management and distribution of retail investment products. In its most important market, the United Kingdom, distribution is increasingly through various types of intermediaries and it also sells directly to customers. M&G is also expanding its distribution into certain European markets (via M&G International) and some Asian markets.

Institutional Fund Management

M&G's institutional business is focused on fixed income and pooled pension mandates. Clients are typically large institutional investors, primarily pension funds and insurance companies. In addition to traditional institutional fund management activities, M&G has also expanded its activities in more specialist areas, primarily through its Private Finance and Prudential Finance business units. Private Finance provides fund management services in project finance and securitized debt and Prudential Finance manages the Group's banking relationships, core debt issuance and commercial paper programs and provides capital market solutions for Prudential group companies. M&G also carries out securities lending on behalf of its clients.

Internal Fund Management

M&G's internal fund management activities are based in the United Kingdom. Total internal funds under management at December 31, 2005 were £113 billion. Internal funds are invested by M&G in equities, fixed income securities, property and private equity.

Where Prudential chooses to invest internal funds in the United States or Asia, this is done through PPM America in the United States and Prudential Asset Management in Asia. See " US Business PPM America" and " Asian Business Funds Management" for descriptions of PPM America and Prudential Asset Management, respectively.

Prudential Finance

Prudential Finance manages the Group's banking relationships, core debt issuance and commercial paper programs and provides capital market solutions for Prudential group companies. Prudential Finance also carries out securities lending on behalf of M&G's clients.

Egg

Egg offers banking and insurance products and services, including credit cards, unsecured personal loans, mortgages, savings and general consumer insurance products. It was launched in October 1998 with the goal of attracting a new segment of customers and developing a new direct distribution channel. The Egg brand has consistently targeted consumers who like to manage their own financial affairs, seek consistently good value and simple products and prefer the flexibility offered by remote access. Following its unprecedented success in attracting new customers, Egg began accepting new applications for deposit accounts exclusively through the internet in April 1999 and since then its business model has remained internet-led, supported by the telephone.

Egg has completed the re-focus on its core UK banking business over the last 12 months with the completion of the sale of its investment wrap, an electronic platform allowing investors or their advisors to organize and transact holdings in investment funds offered by a number of investment companies, business "Funds Direct" in October 2005 and its 49.9 per cent stake in Marlborough Sterling Mortgage Services in January 2006. The exit from France was completed during 2005 with total costs incurred within the provision established in 2004. See " Acquisitions and Disposals".

The following table shows the total product balances for both Egg and Prudential branded products at the dates indicated.

Products

	At December 31,	
	2005	**2004**
	(In £ Millions)	
Customer savings	**5,830**	6,336
Mortgage loans	**1,484**	1,693
Credit card receivables	**3,491**	3,578
Personal loans	**2,790**	2,619

Egg Card, the UK's first credit card designed for the internet, was launched in September 1999. Egg achieved a market share of over 5 per cent of outstanding UK credit card balances at December 31, 2005 and the balance outstanding on credit cards stood at £3,491 million. At December 31, 2005, Egg's branded savings in the UK totaled £5,706 million and Egg's own-branded mortgage balances stood at £1,019 million and its personal loan balances stood at £2,790 million.

Egg also offers motor, travel, home and contents and life assurance, with each product type underwritten by different insurers and Egg receiving a sales commission.

Egg also markets Prudential branded products. These product balances, included in the above table, were £465 million of mortgage loans, £124 million of savings and £0.1 million of personal loans at December 31, 2005.

The closer partnership of Egg with Prudential's UK insurance business, as announced in December 2005, is expected to achieve revenue and cost synergies. The work to maximize the synergies between the two businesses has already started with PruHealth policies now being sold through Egg.

Acquisitions and Disposals

Egg France

During 2003 the decision was taken that the development of the business in France required a level of investment greater than that which Egg was prepared to take on a standalone basis. Egg therefore began negotiations with potential partners that may have led to a joint venture or similar transaction. However, no suitable business partner was identified. On July 13, 2004, Egg announced its withdrawal from the French market to focus on its successful UK business. The trading in France ceased in 2005 and the total closure costs are expected to be within the provision of £113 million established in July 2004.

Funds Direct

Following the decision to focus on its core UK business, Egg put Funds Direct, its investment wrap platform business, up for sale and booked a £17 million impairment charge against the full carrying value of the underlying assets in 2004. The sale was completed in October 2005.

Marlborough Sterling Mortgage Services

In order to focus the UK business more closely on consumer retail financial services, Egg took the decision to sell its stake in its mortgage processing joint venture back to its partner, Vertex Financial Services Ltd. This sale was completed in January 2006.

Reinsurance

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

Reserves

In the United Kingdom, a long-term insurance company's reserve and other requirements are determined by its Board, with advice from its Actuarial Function Holder, subject to minimum reserve requirements. These minimum reserve requirements are established by the rules of the Integrated Prudential Sourcebook for Insurers and have been interpreted by mandatory professional guidance notes.

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

Prudential's regulatory reserving for with-profits products as required by UK regulation, takes into account annual bonuses/annual interest credited to policyholders because these are "attached" to the policies and are guaranteed. Realistic reserves are also calculated for with-profits products under UK regulation. These include an allowance for final bonuses based on the asset share or a prospective valuation of the policies and the cost of guarantees, smoothing and enhancements.

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

As well as the reserves, the company's assets must also cover other capital requirements set out in the Integrated Prudential Sourcebook. These comprise a resilience capital requirement, which makes prudent allowance for potential future adverse movements in investment values; a with-profits insurance capital component, which is a measure of the difference in the surplus assets on regulatory and realistic bases; and the long-term insurance capital requirement, which must be held by all European Union insurance companies. See "Financial Strength of Prudential Assurance's Long-term Fund" for further information on solvency and "Realistic Financial Strength Reporting" for further information on realistic reporting.

Financial Strength of Prudential Assurance's Long-term Fund

The fund is very strong with an inherited estate measured on an essentially deterministic valuation basis of around £9.0 billion at the end of 2005, compared with £6.8 billion at the end of 2004.

The PAC long-term fund is rated AA+ by Standard & Poor's, Aa1 by Moody's and AA+ by Fitch Ratings.

The table below shows the change in the investment mix of Prudential's main with-profits fund:

	2005 %	2004 %
UK equities	**40**	33
International equities	**19**	15
Property	**15**	18
Bonds	**21**	29
Cash and other asset classes	**5**	5
Total	**100**	100

For the main UK with-profits fund 83 per cent of fixed income securities are investment grade with 25 per cent rated AA or above. For Prudential Annuities Limited 95 per cent of the fixed income securities are investment grade with 48 per cent rated AA or above. For Prudential Retirement Income Limited 98 per cent of total assets are investment grade with 57 per cent rated AA or above.

With-profits contracts are long-term contracts with relatively low guaranteed amounts. This, combined with the strong financial position of the fund, enables Prudential to invest primarily in equities and property. At the end of 2005 the equity backing ratio (equity plus property) was nearly 74 per cent which reflects an approximate 10 per cent increase in the equity exposure over the year. This strategy has been driven by the perceived attractive pricing of equities relative to other assets in the earlier part of 2005. To some extent this is a retracing of the substantial (and successful) equity reduction strategy implemented towards the end of the 1990s 'bubble' period. The fund remains extremely well diversified geographically, by asset type and within the underlying stock portfolios, which we believe is an attractive feature of the Prudential with profits proposition. It helps reduce risk or expected volatility by insulating the total fund from potential weakness in any particular market or stock. The active management of the asset mix in recent years has had a substantial beneficial impact on investment returns. The broad asset mix will continue to be reviewed as the economic environment and market valuations change.

The investment return on the Prudential main with-profits fund was 20 per cent in the year to December 31, 2005 compared with the rise in the FTSE All Share (Total Return) Index of 22 per cent over the same period. Over the last ten years the with-profits fund has consistently generated positive fund returns with 3, 5 and 10 year compound returns of 16.6 per cent per annum, 7.1 per cent per annum and 10.1 per cent per annum respectively, compared with corresponding increases in the FTSE All Share index (Total Return) of 18.5 per cent, 2.2 per cent and 7.9 per cent. These returns demonstrate the benefits of the fund's strategic asset allocation and long-term outperformance.

Realistic Financial Strength Reporting

The FSA published its Integrated Prudential Sourcebook, which in addition to the regulatory basis that previously applied includes regulations for a more "realistic" valuation basis which applied from December 31, 2004. In the aggregate, the basis has the effect of placing a value on the liabilities of UK with-profits contracts that reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances.

Prudential supported the FSA's objective of moving to a more realistic basis of solvency reporting. This makes companies' financial health more transparent to policyholders, intermediaries and regulators alike, and enables more informed choices to be made by policyholders. The PAC long-term with-profits sub-fund is very strong with the inherited estate (free assets) measured on a realistic basis, valued at £8.0 billion at the year end before deducting for the risk capital margin.

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

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

With-profits Products

With-profits products provide an equity-type return to policyholders through bonuses that are "smoothed". There are two types of bonuses: "annual" and "final". Annual bonuses, often referred to as reversionary bonuses, are declared once a year and, once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, final bonuses are only guaranteed until the next bonus declaration. Final bonuses are only credited on a product's maturity or surrender or on the death of the policyholder. Final bonuses can represent a substantial portion of the ultimate return to policyholders.

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

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

Prudential Assurance's board of directors, with the advice of its Actuarial Function Holder and its With-Profits Actuary determines the amount of annual and final bonuses to be declared each year on each group of contracts.

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

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

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

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

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

In 2005, Prudential declared a total surplus of £2,234 million from Prudential Assurance's primary with-profits fund, of which £2,011 million was added to with-profits policies and £223 million was distributed to shareholders. This includes annual bonus rates of 3.25 per cent for the Prudence Bond and 3.25 per cent for personal pensions. In 2004, Prudential declared a total surplus of £1,986 million from Prudential Assurance's primary with-profits fund, of which £1,788 million was added to with-profits policies and £198 million was distributed to shareholders. This includes annual bonus rates of 3.25 per cent for the Prudence Bond and 3.25 per cent for personal pensions.

The closed Scottish Amicable Insurance Fund (referred to as SAIF) declared total bonuses in 2005 of £455 million compared to £379 million in 2004. Shareholders have no interest in profits from the SAIF fund, although they are entitled to the investment management fees paid by this business. For greater detail on the SAIF fund, see " The SAIF Sub-fund and Accounts" below.

Surplus Assets in Prudential Assurance's Long-term With-profits Fund

The long-term fund contains the amount that PAC expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the with-profits sub-fund is equal to the policyholders' accumulated asset shares plus any additional payments that may be required for smoothing or to meet guarantees. The balance of the assets of the with-profits subfund is called the 'inherited estate' and represents the major part of the working capital of Prudential's long-term fund which enables PAC to support with-profits business by:

- providing the benefits associated with smoothing and guarantees;
- providing investment flexibility for the fund's assets;
- meeting the regulatory capital requirements, which demonstrate solvency; and
- absorbing the costs of significant events, or fundamental changes in its long-term business without affecting bonus and investment policies.

The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

The Company believes that it would be beneficial if there were greater clarity as to the status of the inherited estate. In due course, after discussions with the FSA, the Company may therefore take steps to achieve that clarity, whether through guidance from the court or otherwise. In any event, the Company expects that the entire inherited estate will need to be retained within the long-term fund for the foreseeable future to provide working capital, and so it is not considering any distribution of the inherited estate to policyholders and shareholders.

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

Depletion of Surplus Assets and Shareholders' Contingencies

As a proprietary insurance company, Prudential Assurance is liable to meet its obligations to policyholders even if the assets of the long-term funds are insufficient to do so. The assets, in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers (the excess assets) in the long-term funds, represented by the unallocated surplus of with-profits funds could be materially depleted over time by, for example, a significant or sustained equity market downturn, costs of significant fundamental strategic change or a material increase in mis-selling provisions. In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the Group's ability to treat its customers fairly was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

In 1998, Prudential stated that deducting personal pensions mis-selling costs from the inherited estate of the With-Profits Sub-Fund would not impact the Company's bonus or investment policy. The Company gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged.

The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing. The mis-selling review was completed on June 30, 2002 and consequently the assurance has not applied to new business issued since January 1, 2004. New business in this context consists of new policies, new members to existing pension schemes plus regular and single premium top-ups, transfers and switches to existing arrangements. The assurance will continue to apply to any policy in force as at December 31, 2003, both for premiums paid before January 1, 2004 and for subsequent regular premiums (including future fixed, retail price index or salary related increases and Department for Work and Pensions rebates).

The maximum amount of capital support available under the terms of the assurance for policies in-force at December 31, 2003 will reduce over time as Prudential pays claims on the policies covered by it.

The bonus and investment policy for each type of with-profits policy is the same irrespective of whether or not the assurance applies. Hence removal of the assurance for new business has had no impact on policyholder returns and this is expected to continue for the foreseeable future.

The SAIF Sub-fund and Accounts

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

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

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

SAIF sub-fund pays an annual charge to the other part of Prudential Assurance's long-term fund in respect of this memorandum account.

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

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

The adoption on January 1, 2005 of realistic reporting of liabilities in SAIF has had the effect of including the surplus assets over declared bonuses in liabilities rather than as unallocated surplus.

With the exception of certain guaranteed annuity products, referred to below, the majority of SAIF with-profits policies do not guarantee minimum rates of return to policyholders. Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations to the policyholders of SAIF, the Prudential Assurance long-term fund would be liable to cover any such deficiency. Due to the quality and diversity of the assets in SAIF and the ability of SAIF to revise guaranteed benefits in the event of an asset shortfall, the directors believe that the probability of either the Company's long-term fund or the Company's shareholders' funds having to contribute to SAIF is remote.

Non-participating Business

The majority of Prudential-branded non-participating business is written in the non-profit sub-fund of Prudential Assurance's long-term fund or in subsidiaries owned by the Company. Since mid-2004, Prudential has written all of its new non-profit annuity business through Prudential Retirement Income limited ('PRIL'), from which the profits are attributed solely to shareholders. Prior to that time, certain non-profit annuity business was written through Prudential Annuities Limited ('PAL'), which is wholly owned by PAC's with-profits fund. The profits on this business are attributable to the fund and not to shareholders, although indirectly shareholders get one ninth of additional amounts paid to policyholders through the declaration of bonuses.

The unit-linked business written by Prudential Assurance and Prudential International Assurance is written with capital provided by shareholders.

Pension Mis-selling Review

In 1988, the UK government introduced new pensions legislation intended to encourage more individuals to make their own arrangements for their pensions. During the period from April 1988 to June 1994, many individuals were advised by insurance companies, Independent Financial Advisors and other intermediaries to not join, to transfer from or to opt out of their occupational pension schemes in favor of private pension products introduced under the UK Income and Corporation Taxes Act 1988. The UK insurance regulator (previously the Personal Investment Authority, now the Financial Services Authority (FSA)), subsequently determined that many individuals were incorrectly advised and would have been better off not purchasing the private pension products sold to them. Industry participants are responsible for compensating the persons to whom private pensions were mis-sold. As a result, the FSA required that all UK life insurance companies review their potential cases of pension mis-selling and pay compensation to policyholders where necessary and, as a consequence, record a provision for the estimated costs. The Company met the requirement of the FSA to issue offers to all cases by 30 June 2002.

Provisions in respect of the costs associated with the review have been included in benefits and claims in the consolidated income statement and the movement in unallocated surplus of with-profits funds has been determined accordingly. A provision of £331 million was held as at December 31, 2005. The table below summarizes the change in the pension mis-selling provision for the year ended December 31, 2005. The provisions shown have been calculated on a realistic basis in accordance with FRS 27; provisions reported in previous years were calculated in accordance with the November 2003 version of the ABI's Statement of Recommended Practice on Accounting for Insurance Business.

	Year ended December 31, 2005 £m	**Year ended December 31,2004 £m**
Balance at beginning of year	**487**	530
Change arising from adoption of FRS 27	**(109)**	
Changes to actuarial assumptions and method of calculation	**(28)**	(32)
Discount unwind	**14**	22
Redress to policyholders	**(21)**	(26)
Payment of administrative costs	**(12)**	(7)
Balance at end of the year	**331**	487

The FSA regularly updates the actuarial assumptions to be used in calculating the provision, including interest rates and mortality assumptions. The pension mis-selling provision represents the discounted value of future expected payments, including benefit payments and all internal and external legal and administrative costs of adjudicating, processing and settling those claims. To the extent that amounts have not been paid, the provision increases each year reflecting the shorter period of discount.

The directors believe that, based on current information, the provision, together with future investment return on the assets backing the provision, will be adequate to cover the costs of pension mis-selling as well as the costs and expenses of the Group's pension review unit established to identify and settle such cases. Such provision represents the best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

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

In 1998, Prudential stated that deducting mis-selling costs from the inherited estate would not impact its bonus or investment policy and it gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged. The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing.

This review was completed on June 30, 2002. The assurance will continue to apply to any policy in force at December 31, 2003, both for premiums paid before January 1, 2004, and for subsequent regular premiums (including future fixed, retail price index or salary related increases and Department of Work and Pensions rebate business). The assurance has not applied to new business since January 1, 2004. New business in this context consists of new policies, new members to existing pension schemes plus regular and single premium top-ups, transfers and switches to existing arrangements. The maximum amount of capital support available under the terms of the assurance will reduce over time as claims are paid on the policies covered by it.

The bonus and investment policy for each type of with-profits policy is the same irrespective of whether or not the assurance applies. Hence removal of the assurance for new business has had no impact on policyholder returns and this is expected to continue for the foreseeable future.

Mortgage Endowment Products Review

In common with several other UK insurance companies, the Group used to sell low-cost endowment products related to repayment of residential mortgages. At sale, the initial sum assured is set at a level such that the projected benefits, including an estimate of the annual bonus receivable over the life of the policy, will equal or exceed the mortgage debt. Because of a decrease in expected future investment returns since these products were sold, the FSA is concerned that the maturity value of some of these products will be less than the mortgage debt. The FSA has worked with insurance companies to devise a programme whereby the companies write to customers indicating whether they may have a possible shortfall and outline the actions that the customers can take to prevent this possibility.

The Group is exposed to mortgage endowment products in respect of policies issued by Scottish Amicable Life plc (SAL) and policies issued by Scottish Amicable Life Assurance Society (SALAS) and transferred into the Scottish Amicable Insurance Fund (SAIF). Provisions of £6 million in the non-profit sub-fund and £50 million in SAIF were held at December 31, 2005 to cover potential compensation in respect of mortgage endowment product mis-selling claims. As SAIF is a separate sub-fund of the Company's long-term business fund, this provision has no impact on shareholders.

In addition, the Prudential Assurance Company's main with-profits fund paid compensation of £24 million in respect of mortgage endowment products mis-selling claims in the year ended December 31, 2005 and held a provision of £63 million at December 31, 2005, in respect of further compensation. This provision has no impact on the Group's profit before tax.

Guaranteed Annuities

The Prudential Assurance Company used to sell guaranteed annuity products in the UK and held a provision of £52 million at December 31, 2005 compared to £49 million in 2004, within the main with-profits fund to honor guarantees on these products. The Company's main exposure to guaranteed annuities in the UK is through the Scottish Amicable Insurance Fund (SAIF) and a provision of £619 million (2004: £648 million) was held in SAIF at December 31, 2005, to honor the guarantees. As SAIF is a separate sub-fund of the Company's long-term business fund, this provision has no impact on shareholders.

US Business

Prudential conducts its US insurance operations through Jackson National Life Insurance Company and its subsidiaries, including Curian Capital LLC, a registered investment advisor. The US operations also include PPM America, Prudential's US internal and institutional fund manager, and Prudential's US broker-dealer operations (National Planning Corporation, SII Investments, Inc., IFC Holdings, Inc. and Investment Centers of America, Inc.). At December 31, 2005, Prudential's US operations had more than 3 million policies and contracts in effect and PPM America managed approximately US$71 billion (£42 billion) of assets. In 2005, total new business premiums were £5,023 million.

US Market Overview

The United States is the world's largest life insurance market in terms of retirement assets, with 67 per cent, or $12.9 trillion of the world's retirement savings assets concentrated in the US at the end of 2005. The ageing demographics of the US, with the first of the 77 million 'baby boomers' reaching 60 in 2006, is expected, over the next decade, to create a very significant increase in the level of distributions from retirement savings plans. Life expectancy in the US continues to increase while at the same time the average retirement age is decreasing. This has led to a large increase in the average time individuals will spend in retirement, and consequently, there is a growing risk that individuals' finances will be insufficient to cover the cost of living through retirement. These consumers are likely to have a growing need for independent financial advice and are expected to seek increasing guarantees and longevity protections from the products they purchase.

Despite favorable demographics, the US insurance industry faces a number of challenges, both from within and outside the industry. The life insurance business is projected to grow slowly and competition is expected to be fierce. While the growth prospects for the annuity industry are more favorable, there are many players fighting for market share within the life insurance industry. Life insurance companies also compete with other financial services providers, in particular, mutual fund companies and banks, for a share of savings assets in the US, where competition is expected to intensify.

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

The US investment markets experienced two years of unusually poor returns in 2001 and 2002, with equity markets suffering significant declines and bond defaults reaching record levels. Like its competitors, Jackson National Life was affected by these market forces. The market in 2003 was also affected by weak growth in the economy at the start of the year and declining interest rates. However, there was dramatic growth in the second half of 2003 and the first annual, positive stock index gains in three years. In 2004 interest rates remained low and equity markets were up, with the S&P index increasing by 9 per cent. During 2005, interest rates began to rise and the S&P index rose by 3 per cent.

Prudential believes that JNL is well positioned to take advantage of the evolving opportunities in the US retirement market given its relationship-based distribution model, innovative product manufacturing capability, low cost operating model and award-winning service.

Products

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

When annuity products initially became popular in the United States, they were interest-rate based and provided a minimum guaranteed rate of return. However, declining interest rates eroded the after-tax benefits of these products. Meanwhile, during the 1990s there was significant growth in equity markets. As a result, equity-based and equity-linked products, with and without guarantees, became increasingly important product offerings. Reflecting this shift, industry sales of individual variable annuity products grew from $29 billion in 1992 to $128 billion in 2000, a compound annual growth rate of 20.7 per cent. During the same period, industry individual variable annuity assets grew from $212 billion to $971 billion, a compound annual growth rate of 20.9 per cent.

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

The above trends reversed in 2001 when, for the first time in twelve years, industry-wide variable annuity sales did not increase. In 2002, annuity providers continued to face the challenges of the previous year. By year-end 2002, the S&P 500 and NASDAQ Composite Indices had declined from their year 2000 peaks by 40 per cent and 67 per cent, respectively. In these volatile equity markets, fixed annuity sales benefited from a flight to safety. In 2002, total industry individual annuity sales increased by 20 per cent to $223 billion, with the bulk of the increase coming from a continuing surge in fixed annuity sales. Nevertheless, variable annuity sales managed some increase in 2002, with significant amounts going to fixed account options.

From 2003 to 2005, total industry individual variable annuity sales were driven by sales of principal guaranteed benefits and living benefits, and by contract holders shifting from fixed options and fixed income funds into equities as these markets improved. This resulted in an increase in total industry individual variable annuity sales of 11 per cent, 3 per cent and 3 per cent in 2003, 2004 and 2005 respectively. In 2003, total industry individual fixed annuity sales fell by 15 per cent reflecting declining interest rates, tightening spreads and declining margins, whilst in 2004 they increased by 1 per cent as a result of interest rate increases during the year and customers' expectations of further increases. In 2005, individual fixed annuity sales fell by 10 per cent reflecting the continued low interest rate environment and relatively flat yield curve on the bond market in the US.

Distribution

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

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

The regional broker-dealer channel focuses on firms with captive agents in specific regions of the United States. Distribution is through branch offices with an average of 10 to 15 brokers per office. Captive agents are employees of JNL licensed to distribute only JNL products.

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

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

The registered investment advisor market began as a service offered to very high net worth investment clients, focusing on platforms rather than specific products, and providing institutional quality management, custom portfolios and tax services. The industry has evolved to offer personalized investment advice, very high quality money management, good returns and reasonable costs to a broader range of clients.

Jackson National Life

Jackson National Life is a leading provider of long-term savings and retirement products to retail and institutional customers throughout the United States. Jackson National Life offers variable annuities, fixed-index annuities, individual fixed annuities, life insurance and institutional products. By developing and offering a wide variety of products, Jackson National Life believes that it has positioned itself to compete effectively in various stock market and interest rate environments. Jackson National Life markets its retail products through various distribution channels, including independent agents, broker-dealer firms (including financial planners), regional broker-dealers, banks and the registered investment advisor channel, and beginning in 2005, through its captive insurance agency, acquired through the purchase of Life of Georgia.

The interest-sensitive fixed annuities, fixed-index annuities, immediate annuities and life insurance products are sold through independent agents, broker-dealers and banks. For variable annuity products, which can only be sold through broker-dealers licensed by the US National Association of Securities Dealers, Jackson National Life has selling agreements with such firms and is continuing to focus on its own broker-dealer distribution channel. Its institutional products division sells institutional products. In early 2003, Jackson National Life commenced operating in the registered investment advisor channel, with the launch of Curian Capital, LLC. In 2005, Jackson National Life began selling life insurance products through its newly established captive agency, JNL Southeast Agency LLC. For further information, see " Captive Agency".

Products

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

	Year Ended December 31,		Policyholder Liabilities At December 31,
	2005	**2004**	**2005**
	(In £ Millions)		
By Product			
Annuities			
Fixed annuities			
Interest-sensitive	**742**	1,087	**12,772**
Fixed-index	**616**	429	**2,436**
Immediate	**46**	43	**710**
Variable annuities	**2,605**	1,981	**10,615**
Total	**4,009**	3,540	**26,533**
Life insurance	**25**	28	**4,234**
Institutional products			
GICs, funding agreements and Federal Home Loan Bank of Indianapolis (FHLBI) advances	**355**	180	**1,214**
Medium term note funding agreements	**634**	672	**3,267**
Total	**989**	852	**4,481**
Total	**5,023**	4,420	**35,248**
By Distribution Channel			
Independent agents	**670**	647	
Bank	**877**	1,089	
Broker-dealer	**2,483**	1,832	
Captive agents	**4**		
Institutional products department	**989**	852	
	5,023	4,420	

Annuities

Fixed Annuities

Interest-sensitive Annuities

In 2005, interest-sensitive fixed annuities accounted for 15 per cent of total new business premiums and 36 per cent of policyholder liabilities of the US operations. Interest-sensitive fixed annuities are primarily deferred annuity products that are used for retirement planning and for providing income in retirement. They permit tax-deferred accumulation of funds and flexible payout options.

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

The policy provides that at Jackson National Life's discretion it may reset the interest rate, subject to a guaranteed minimum. The minimum guarantee varies from 1.50 per cent to 5.50 per cent, depending on the date of issue, with 78 per cent of the fund at 3.0 per cent or less at December 31, 2005. In addition, Jackson National Life also offers multi-year guaranteed products.

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

Approximately 29 per cent of the interest-sensitive fixed annuities Jackson National Life wrote in 2005 provide for an adjustment, referred to as a market value adjustment, on surrenders in the surrender period of the policy. This formula based adjustment approximates the change in value that assets supporting the product would realize as interest rates move up or down. This adjustment can be positive or negative. The minimum guaranteed rate is not affected by this adjustment.

Jackson National Life bears the investment and surrender risk on interest-sensitive fixed annuities, and its profits come from the spread between the yield on investments and the interest credited to policyholders (net of any surrender charges or market value adjustment) less initial and recurring expenses.

Fixed-index Annuities

Jackson National Life ranked seventh in the sale of fixed-index annuities in the United States in 2005. Fixed-index annuities accounted for 12 per cent of total new business premiums in 2005 and 7 per cent of policyholder liabilities of the US operations. Fixed-index annuities vary in structure, but generally are deferred annuities that enable policyholders to obtain a portion of an equity index-linked return but provide a guaranteed minimum return.

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

Jackson National Life bears the investment and surrender risk on fixed-index annuities. Profit arises from the investment income earned and the fees charged on the policy, less the expenses incurred, which include the costs of the guarantees, and the return credited to the policy. Fixed-index annuities contain penalties for early surrender.

Immediate Annuities

In 2005, immediate annuities accounted for 1 per cent of total new business premiums and 2 per cent of policyholder liabilities of the US operations. Immediate annuities guarantee a series of payments beginning within a year of purchase and continuing over either a fixed period of years and/or the life of the policyholder. If the term is for the life of the policyholder, then Jackson National Life's primary risk is mortality risk. This product is generally used to provide a guaranteed amount of income for policyholders and is used both in planning for retirement and in retirement itself. The implicit interest rate on these products is based on the market conditions that exist at the time the policy is issued and is guaranteed for the term of the annuity.

Variable Annuities

Jackson National Life began offering variable annuity products in 1995. In 2005, variable annuities accounted for 52 per cent of total new business premiums and 30 per cent of policyholder liabilities of the US operations. Variable annuities are deferred annuities that have the same tax advantages and payout options as interest-sensitive and fixed-index annuities. They also are used for retirement planning and to provide income in retirement.

The primary differences between variable annuities and interest-sensitive or fixed-index annuities are investment risk and return. If a policyholder chooses a variable annuity, the rate of return will depend upon the performance of the underlying fund portfolio. The policyholder bears the investment risk except for fixed account options, where Jackson National Life guarantees a minimum fixed rate of return. Jackson National Life issues variable annuity contracts where it contractually guarantees to the contract holder either a) return of no less than total deposits made to the contract adjusted for any partial withdrawals, b) total deposits made to the contract adjusted for any partial withdrawals plus a minimum return, or c) the highest contract value on a specified anniversary date adjusted for any withdrawals following the contract anniversary. These guarantees include benefits that are payable in the event of death (guaranteed minimum death benefit), annuitisation (guaranteed minimum income benefit) or at specified dates during the accumulation period (guaranteed minimum withdrawal benefit). Annuitisation refers to an income stream from the policy over the remainder of the beneficiary's life or a defined term. Jackson National Life generally charges a fee for these benefits and hedges the equity related risk of the product using equity options and futures contracts.

Jackson National Life credits premiums on variable annuities to a separate account or to the fixed account, depending on the policyholders' elections. The policyholders determine how the premiums will be allocated by choosing to allocate all or a portion of their accounts either to a variety of variable sub-accounts, with a choice of investment managers, or to guaranteed fixed-rate options. The rate of election of the fixed account option within variable annuities in 2005 of 20 per cent compares with 29 per cent in 2004. The value of the portion of the separate account allocated to variable sub-accounts fluctuates with the underlying investment. Jackson National Asset Management, LLC (a subsidiary of Jackson National Life) earns fee income as the investment advisor for the underlying funds and has retained the services of a number of other investment advisors to act as sub-advisors to Jackson National Asset Management, LLC. Additionally, Jackson National Life Distributors, Inc. (a subsidiary of Jackson National Life) earns a fee for distributing the funds.

The non-fixed account portion of variable annuity products is backed by specific assets that are held in separate accounts. The assets in these separate accounts are "segregated" pursuant to state insurance law and do not form part of the assets in the US general account, which backs the remainder of the insurance business in the United States. Amounts held in the separate accounts are not chargeable with liabilities arising out of any other business Jackson National Life may conduct. All of the income and gains or losses from these assets less specified management charges are credited to or against this portion of the policies and not any other policies that Jackson National Life may issue. For IFRS reporting, separate account assets and liabilities are presented in this Form 20-F as a component of general account assets and liabilities.

Jackson National Life earns fee income on the underlying separate account investment, earns profits from the spread between what it earns on investments backing the fixed rate accounts and the interest credited, and earns fee income for the additional elective benefits in the contract. Variable annuity policies provide for early surrender charges.

Life Insurance

Reflecting the competitive life insurance market place and the overall trend towards asset accumulation products, Jackson National Life's life insurance products accounted for only 1 per cent of the total new business premiums and 12 per cent of policyholder liabilities of the US operations in 2005. The products offered include term life insurance, interest-sensitive life insurance and variable universal life insurance. Each of these types of insurance policies can be modified using several options and riders to provide particular benefits, including waiver of premium, accidental death benefit and supplemental term insurance.

Institutional Products

Institutional products consist of guaranteed investment contracts (GICs), funding agreements, including agreements issued in connection with participation in the FHLBI programme, and medium term note funding agreements. In 2005, institutional products accounted for 20 per cent of total new business premiums and 12 per cent of policyholder liabilities of US operations. Jackson National Life began marketing GICs to institutional investors in December 1995. The GICs are marketed by its institutional products department to defined contribution pension and profit-sharing retirement plans. Funding agreements are marketed to institutional investors, including corporate cash accounts and securities lending funds, as well as money market funds, and are issued to the Federal Home Loan Bank of Indianapolis in connection with the FHLBI programme see "Funding Agreements" below. Sales of institutional products increased in 2005 as Jackson National Life was able to take advantage of attractive issuance opportunities. Three types of institutional products are offered:

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

Traditional Guaranteed Investment Contracts

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

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

Jackson National Life sells GICs to retirement plans, in particular 401(k) plans. The traditional GIC market is extremely competitive. This is due in part to competition from synthetic GICs, which Jackson National Life does not sell.

Funding Agreements

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

Typically, brokerage accounts and money market mutual funds are required to invest a portion of their funds in cash or cash equivalents to ensure sufficient liquidity to meet their customers' requirements. The funding agreements permit termination by the policyholder on 7 to 90 days notice, and thus qualify as cash equivalents for the clients' purposes. Funding agreements terminable by the policyholder with less than 90 days notice account for less than 1 per cent of Jackson National Life's total policyholder reserves.

During 2005, Jackson National Life became a member of the FHLBI. Membership allows Jackson National Life access to advances from FHLBI that are collateralized by mortgage related assets in Jackson National Life's investment portfolio. These advances are in the form of funding agreements issued to FHLBI. Jackson National Life is authorized to draw a maximum of $603.1 million in advances under this program. In 2005, the total premiums generated from advances from the FHLBI were $100 million.

Medium Term Note Funding Agreements

Jackson National Life has also established European and global medium-term note programs. The notes offered may be denominated in any currency with a fixed or floating interest rate. Notes are issued to institutional investors by a special purpose vehicle and are secured by funding agreements issued by Jackson National Life.

Distribution and Marketing

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

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

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

Independent Agents

The insurance and fixed annuity products are distributed through independent agents located throughout the United States. These approximately 22,000 licensed insurance agents or brokers, who also may represent other companies, are supported by four regional marketing offices. Jackson National Life generally deals directly with writing agents and brokers thereby eliminating intermediaries, such as general agents. This distribution channel has enabled it to generate significant volumes of business on a low, variable cost basis. Jackson National Life is responsible for providing agents with product information and sales materials.

Broker-Dealers

Jackson National Life Distributors, Inc. (JNLD), a broker-dealer, is the primary wholesale distribution channel for the variable annuity products. JNLD also sells fixed-index annuities and fixed annuities. An internal network of wholesalers supports this distribution channel. These wholesalers meet directly with broker-dealers and financial planners and are supported by an extensive home office sales staff. There are more than 700 active selling agreements with regional and independent broker-dealer organizations throughout the United States, which provides JNL access to nearly 73,000 appointed agents.

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

Banks, Credit Unions and Other Financial Institutions

Jackson National Life's Institutional Marketing Group distributes its annuity products through banks, credit unions and other financial institutions and through third-party marketing organizations that serve these institutions. Jackson National Life is a leading provider of annuities offered through banks and credit unions and can access over 19,000 financial institution representatives through existing relationships with banks and credit unions. Jackson National Life has established distribution relationships with medium-sized regional banks, which it believes are unlikely to develop their own insurance product capability.

Independent Broker-Dealers

Jackson National Life's retail distribution is managed by its independent broker-dealer network, National Planning Holdings ("NPH"), which is made up of four firms, National Planning Corporation, SII Investments, Inc., INVEST Financial Corporation and Investment Centers of America, Inc. Jackson National Life's broker-dealer group had contracts with more than 2,500 registered representatives at the end of 2005.

Registered Investment Advisor

Commencing operation in early 2003, Curian Capital, LLC (Jackson National Life's registered investment advisor channel) provides innovative fee-based separately managed accounts and investment products to advisors through a sophisticated technology platform.

The registered investment advisor industry began as a service offered to very high net worth investment clients, focusing on platforms rather than specific products, and providing institutional-quality management, custom portfolios and tax services. The industry has evolved to offer personalized investment advice, very high quality money management, good returns and reasonable costs to a broader range of clients.

Institutional Products Department

Jackson National Life markets its institutional products through its institutional products department. It has direct contacts with banks, municipalities, asset management firms and direct plan sponsors. Institutional products are distributed and marketed through intermediaries to these groups.

Captive Agency

In connection with the acquisition of Life of Georgia in 2005, Jackson National Life established the JNL Southeast Agency ("JNLSA"), the Company's first captive agency since 1970. JNLSA, with approximately 100 life insurance agents, was formed to help retain the Life of Georgia book of business and to create a new distribution channel for Jackson National Life's life insurance products.

Factors Affecting Pricing of Products and Asset Liability Management

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

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

Jackson National Life segregates its investment portfolio for certain investment management purposes and as part of its overall investment strategy into four portfolios: fixed annuities without market value adjustment, fixed annuities with market value adjustment, fixed-index annuities and institutional liabilities. The portfolios backing fixed annuities with and without market value adjustments and the fixed-index annuities have similar characteristics and differ primarily in duration. The portfolio backing the institutional liabilities has its own mix of investments that meet more limited duration tolerances. Consequently, the institutional portfolio is managed to permit less interest rate sensitivity and has limited exposure to mortgage-backed securities. At December 31, 2005, 4 per cent of the institutional portfolio was invested in residential mortgage-backed securities.

The fixed-rate products may incorporate surrender charges, market value adjustments, two-tiered interest rate structures or other limitations relating to when policies can be surrendered for cash, in order to encourage persistency. At December 31, 2005, Jackson National Life's fixed annuity reserves that had surrender penalties or other withdrawal restrictions remained unchanged at 72 per cent compared to 2004. Substantially all of the institutional portfolio had withdrawal restrictions or market value adjustment provisions.

Fixed-index annuities issued by Jackson National Life also include an equity component that is hedged using equity options and futures contracts issued on the corresponding exchange. The equity component of these annuities, constitutes an embedded derivative under IAS 39, 'Financial Instruments: Recognition and Measurement' that is carried at fair value, as are other derivative instruments.

Guaranteed benefits issued by Jackson National Life in conjunction with the sales of variable annuity contracts expose Jackson National Life to equity risk as the benefits generally become payable when equity markets decline below the guaranteed amount. Certain of these benefits are carried at fair value under IAS 39 with changes in fair value recorded in income. Jackson National Life hedges this risk using equity options and futures contracts, which are also carried at fair value under IAS 39. As certain benefits have mortality risk and, are therefore, precluded from being carried at fair value, the income statement includes a timing difference due to changes in fair value.

Underwriting

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

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

Reserves

Except for certain non-insurance deposit type accounts and as allowed under IFRS, Jackson National Life uses reserves established on a US GAAP basis as the basis for consolidation into Prudential's IFRS accounts.

For the fixed and variable annuity contracts and institutional products, the reserve is the policyholder's account value. For the immediate annuities, reserves are determined as the present value of future policy benefits. Mortality assumptions are based on the 1983a Individual Annuitant Mortality Table and the Annuity 2000 Mortality Table for newer issues. Interest rate assumptions currently range from 2.0 per cent to 8.0 per cent.

For the traditional term life contracts, reserves for future policy benefits are determined using the net level premium method and assumptions as to mortality, interest, policy persistency and expenses.

Mortality assumptions are generally from 25 per cent to 160 per cent of the 1975-1980 Basic Select and Ultimate tables, depending on underwriting classification and policy duration. Interest rate assumptions range from 4.0 per cent to 8.0 per cent. Persistency and expense assumptions are based on Jackson National Life's experience.

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

Reinsurance

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

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

Jackson National Life limits the amount of risk it retains on new policies. Currently, the maximum risk that is retained on new policies is $2.0 million. Jackson National Life is not a party to any risk reinsurance arrangement with any reinsurer pursuant to which the amount of reserves on reinsurance ceded to such reinsurer equals more than 1 per cent of total policy reserves.

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

Effective from December 31, 2002, Jackson National Life cedes the guaranteed minimum death benefit coverage associated with certain variable annuities issued prior to December 31, 2002 to an affiliate, Prudential Atlantic Reinsurance Company, Dublin, Ireland.

Jackson National Life cedes the guaranteed minimum income benefit on variable annuities to an unaffiliated reinsurer.

In connection with the purchase of Life of Georgia, Jackson National Life acquired certain lines of business that have been wholly ceded to non-affiliates. These include both direct and assumed accident and health business, direct and assumed life insurance business and certain institutional annuities.

Policy Administration

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

PPM America

PPM America is Prudential's US fund management operation, with offices in Chicago and New York. Its primary focus is to manage funds for Jackson National Life and therefore the majority of funds under management are fixed interest in nature. PPM America has also launched a number of institutional high yield and special investment vehicles to leverage their fund management capabilities into new areas. PPM America also serves as investment advisor for certain mutual funds, several private investment funds and structured finance vehicles, and the US equity and fixed income portion of portfolios of certain affiliates within Prudential.

Life Insurance Company of Georgia (Life of Georgia')

Jackson National Life completed the purchase of Life of Georgia in May 2005 for a preliminary consideration of £142 million. This acquisition doubled the number of Jackson National Life's in-force life and annuity policies, adding scale to its operating platform and expanding its distribution capability, as well as further diversifying its income streams. This transaction enabled Jackson National Life to grow its life business at a higher return and faster rate than could be achieved organically.

The preliminary purchase price is subject to post-closing adjustments with resolution expected in 2006.

The purchase of Life of Georgia utilized a portion of the capital generated through Jackson National Life's sale of Jackson Federal Bank completed in October 2004 to Union Bank of California for a consideration of £166 million.

On December 31, 2005, Life of Georgia was merged into Jackson National Life. At year end 2005 Jackson National Life had substantially completed the integration of the 1.5 million Life of Georgia policies onto its own operating platform, demonstrating its capability in consolidating large blocks of business. The Company expects that Jackson National Life will continue to consider further US bolt-on acquisitions as opportunities arise.

Asian Business

Asia's life insurance markets are very attractive with large scale and high growth rates supported by economic growth, favorable demographics and market liberalizations. However, there are some formidable barriers to successful entry, including entrenched incumbents, the pace of change and nature of regulations, mandatory domestic partners in some markets and a shortage of experienced staff. Acquisition opportunities, particularly of scale businesses, are limited and in North Asian markets are likely to involve back books that currently experience negative spread and hence require material provisions under European regulatory capital requirements.

Since the mid 1990s Prudential has been progressively building its Asian platform; strengthening and protecting its market leading positions in its established markets (Singapore, Hong Kong and Malaysia), entering emerging markets (Thailand, Indonesia, Philippines, Vietnam), securing strong joint venture partners for the sizable opportunities in India and China (ICICI and CITIC respectively) and taking positions in the large North Asian markets of Taiwan, Japan and Korea. Prudential now has over 7 million customers in Asia, up from 1.5 million in 2000.

Prudential has been focused on building proprietary distribution as the most effective way of delivering sustainable new business volumes and managing the product range typically through growing tied agency and integrated bancassurance arrangements (such as with Standard Chartered Bank in Hong Kong). Prudential also prioritizes economic capital efficiency, profitability and customer focus in its Asian product portfolio as seen, for example, with the introduction of unit linked products across the region, an emphasis on regular premium policies, life stage themed marketing and purposely limiting participation in the lowest margin sectors.

Taiwan's macro economic environment remains challenging with interest rates currently at record lows leading to negative spread issues affecting the whole industry, particularly on tranches of business sold prior to 2002. Prudential remains confident that any potential deficits are more than adequately supported by the profitable new business, particularly unit-linked, that it has now been writing for a number of years. Prudential remains firmly focused on long-term profitability. In 2005, Prudential's sales mix was 82 per cent linked products compared to the industry total of 39 per cent and new business premiums on an Annual Premium equivalent basis increased by approximately 7 per cent in 2005 compared to 2004.

A new business processing hub was launched in Kuala Lumpur, Malaysia in early 2005 under the name Prudential Services Asia. This is already successfully processing business for the Malaysian and Singaporean life operations and plans are in place for a second hub to be launched in China in 2006.

In 2005, significant progress was made with embedding a risk management and compliance framework. Prudential employs 'three lines of defense'; the operational management in each business, strong risk management related functions and an independent internal audit function.

Prudential Corporation Asia's high proportion of profitable, regular premium business combined with sound operational management means cash flows can be predicted with some certainty. As previously announced, it is expected that the business is on target to fund continued strong growth internally and begin remitting surplus cash back to the Group from 2006 onwards.

In summary, Prudential has an excellent track record of building a profitable business in Asia and the scale of the opportunity for continued growth is clear.

Development of Prudential's Asian Business

Prudential's Asian operations are managed by its Hong Kong-based regional head office. Prudential's operations in Asia date from 1923, when it opened a branch office in India, which served the Indian sub-continent and several Middle Eastern countries with historic ties to the United Kingdom. In 1924, Prudential opened a branch office in Malaysia. Prudential expanded into Singapore in 1931 and opened a branch office in Hong Kong in 1964 first selling general insurance products followed by life insurance a few years later. In 1956, Prudential's Indian operations were nationalized and, in 1984, the Malaysian government required Prudential to sell a majority interest in its Malaysian operations to a local company. A majority share of the Malaysian operations was then reacquired in 1998. A group strategy review in the early 1990s identified significant opportunities for Prudential in the Asian life sector and Prudential Corporation Asia was established in 1994 to develop a material and profitable Asian business.

During 1995 and 1996, Prudential Corporation Asia entered Thailand and Indonesia through acquisitions and launched a new operation in the Philippines. These were followed by re-entry into India with a joint venture mutual fund operation in 1998 (currently 49 per cent ownership), the acquisition of a Taiwanese life insurance operation and the launch of a new life insurance operation in Vietnam in 1999. In 2000, Prudential acquired a mutual fund business in Taiwan, launched new life insurance operations in China (50 per cent ownership) and India (26 per cent ownership) and established a joint venture in Hong Kong for the Mandatory Provident Fund ("MPF") and mutual funds (36 per cent ownership).

Prudential Corporation Asia continued its geographic expansion in 2001 with acquisitions of small, life companies in Japan and South Korea. Also in 2001, Prudential Corporation Asia acquired Allstate's small operations in Indonesia and the Philippines. In June 2002, Prudential Corporation Asia acquired ING's small life operation in the Philippines and in October 2002 acquired Good Morning ITMC, a mid-sized South Korean mutual fund operation.

The Japanese life market remains very challenging and in 2003, Prudential scaled back its operations to focus on higher value distribution channels and more profitable products. While the operation is now somewhat more efficient with lower expense levels and has made some progress with establishing new distribution channels, it will take some time to deliver material volumes and become a positive contributor to Prudential Corporation Asia's overall results. During 2005, the acquired goodwill of the

Japanese life company was tested for impairment and a charge of £120 million has been separately disclosed in the consolidated income statement. The charge reflects the slower than expected development of the Japanese life business.

Prudential Corporation Asia has also launched mutual fund operations in Japan, Singapore, Malaysia, China (joint venture with CITIC 33 per cent ownership) and maintains its composite insurance licenses in Singapore and Malaysia though little general insurance business is currently written.

In India, our joint venture with ICICI continues to be a leading private sector player. In 2004, the Indian government announced its intention to allow increased foreign ownership in Indian companies, and Prudential remains interested in increasing our stake in the joint venture. However, the relevant legislation remains to be put before the Indian Parliament.

In 2005, licences to sell financial services products in six new cities in China were granted to CITIC-Prudential by the Chinese authorities, bringing the total number of such licences on December 31, 2005 to ten. As of April 30, 2006, CITIC-Prudential had been granted 13 life insurance licences to operate in China. Prudential believes the main challenge facing foreign players trying to become established in China is the need to develop local management teams to support geographical expansion. Prudential believes that it has a real advantage in being able to leverage its existing Chinese speaking operations to help develop new teams quickly. In 2005, sales in China increased by 47 per cent over 2004.

Prudential and Bank Simpanan Nasional ("BSN') which was originally the Malaysian Post Office Bank and is now wholly owned by the Ministry of Finance, established a joint venture to leverage Prudential's existing network of over 7,000 agents and BSN's network of 391 branches.

In January 2006, the Malaysian authorities granted the joint venture a license to develop and market insurance products to Muslim Malays who make up more than 60 per cent of the population.

Prudential believes the key ingredients for the long-term Asian growth model are firmly in place: high population densities, high personal savings rates, improving education levels, increasingly entrepreneurial environment, rapid urbanization and deregulation.

Prudential Corporation Asia's strategic themes are to:

- build scale in the markets with the potential to deliver profitability over long-term,
- continue its core distribution strategy of building agency, with a strong emphasis on productivity and quality of sales,
- continue to build complementary bank and direct distribution,
- deliver good customer service,
- continue to build a profitable and significant mutual fund business,
- leverage opportunities to create value from synergies, and
- operate high standards of governance, risk management and compliance throughout.

Distribution

Strengthening distribution continues to be a major priority. In 2005, agent numbers grew by 26 per cent to over 170,000 with geographic expansion in India and China being a key driver (up 36 per cent and 37 per cent respectively). In Indonesia the business has excellent momentum and has increased agent numbers by 89 per cent during the year. In the established markets (Singapore, Hong Kong and Malaysia) improving agency productivity is a key initiative and whilst this improved in 2005 there is still significant room for growth. Prudential believes that its multi-channel distribution model in Korea is a valuable asset as, whilst volumes from direct campaigns such as a home shopping channel have waned

and bank distribution has been limited by regulatory caps and industrial action, insurance sales growth for 2005 of 88 per cent reflects great success in increasing the number of tied financial advisors (up 132 per cent) and extending the number of general agents (brokers).

Currently 75 per cent of Prudential Corporation Asia's sales come from its tied agency distribution, and whilst this will remain the primary channel for some time, there is the potential to further expand alternate channels, particularly banks and direct marketing. Bancassurance with Standard Chartered Bank in Hong Kong continues to be especially successful, and Prudential believes there is considerable potential for further development in bancassurance particularly in Singapore, Malaysia and Taiwan over the short- to medium-term. Prudential believes that the life insurance business in Japan remains challenging, and after piloting a financial advisor channel with little success and high running costs, this channel was closed in January 2006; the emphasis is now on developing profitable partnership distribution opportunities.

Products

Prudential Corporation Asia offers a range of products including life insurance with some accident and health options, personal lines property and casualty insurance and also mutual funds. In January 2006, it also received approval to launch new products in Malaysia with joint venture partner Bank Simpanan Nasional (BSN).

Life Insurance

The life insurance products offered by Prudential Corporation Asia include a range of with-profits and non-participating term, whole life, endowment and unit-linked policies. Prudential Corporation Asia also offers health, disability, critical illness and accident coverage to supplement its core life products.

Prudential Corporation Asia has a strong focus on capital-efficient product innovation and packages products to meet specific customer needs. In 1992, Prudential Corporation Asia was the first company to launch unit-linked products in Singapore and subsequently has leveraged this expertise with great success across the region. Only Thailand and Vietnam do not have unit linked products as these products are not yet permitted by their regulators.

Funds Management

In addition to the life insurance products described above, Prudential offers mutual fund investment products in India, Taiwan, Japan, Singapore, Malaysia, Hong Kong and Korea, allowing customers to participate in debt, equity and money market investments. The Company earns a fee based on assets under management. In 2005, Prudential also received licenses to sell mutual funds in China and Vietnam.

In Hong Kong, Prudential Corporation Asia has a successful joint venture with Bank of China International ("BOCI") for the Mandatory Provident Fund ("MPF") and also unit trusts. As from December 1, 2000, employees, employers and the self-employed in Hong Kong became obliged to make contributions to the MPF. The plans that comprise the MPF are defined contribution pension plans with immediate vesting, preservation until retirement (or some other event specified by legislation) and full portability. Individuals are required to make monthly mandatory contributions of 5 per cent of salary and employers make contributions equal to 5 per cent of the employee's salary to the individual's accounts in the Fund. Both employee and employer contributions are subject to a maximum amount, currently HK$1,000 per month, the equivalent of £65 per month. Additional voluntary contributions are possible.

Prudential Asset Management ("PAM") (formerly PPM Asia) is Prudential Corporation Asia's fund management division responsible for managing Prudential Corporation Asia's life and third party institutional funds including the Prudential group's investments in the Asia-Pacific region. PAM has offices in Singapore, Hong Kong and Tokyo.

The Asian fund management business had £26.2 billion of funds under management as at December 31, 2005, of which £10.1 billion related to third party funds in operations in India, Taiwan, Japan, Korea, Malaysia, Singapore and Hong Kong. Prudential Corporation Asia is a top five foreign provider of mutual funds in all countries in which it operates with the exception of Japan, where significant progress has been made in a very competitive mutual fund market. In 2005, the fund management business continued to expand geographically with the securing of fund management licenses in China, through the joint venture with CITIC, and in Vietnam. This takes the total number of countries in which the business has a presence to nine. The geographic expansion of the past few years has been matched by growth in market share, with Korea, Japan, India and Malaysia being notable successes.

Net inflows from third parties of £1.3 billion were driven by strong net inflows in Japan of £905 million and Korea of £926 million, although these were offset by net outflows in Taiwan of £745 million due to an unsettled bond fund market.

Total reported third party funds under management of £10.1 billion were up 13 per cent on 2004. In August last year, ICICI increased its stake in Prudential's India asset management joint venture from 45 per cent to 51 per cent. As a result, Prudential no longer consolidates this business at 100 per cent and the year end numbers are reported at 49 per cent, resulting in a £1.5 billion reduction in funds under management for the year.

Products and Profitability

Life Insurance Products

Unit-linked products combine savings with protection and the cash value of the policy depends on the value of the underlying unitized funds. Participating products provide savings with protection where the basic sum assured can be enhanced by a profit share (or bonus) from the underlying fund as determined at the discretion of the insurer. Non-participating products offer savings with protection where the benefits are guaranteed or determined by a set of defined market related parameters. Accident and Health ("A&H") products provide mortality or morbidity benefits and include health, disability, critical illness and accident coverage. A&H products are commonly offered as supplements to main life insurance policies but can also be sold separately.

Life Product Profitability

The profits from participating policies are shared between the policyholder and insurer (typically in a 90:10 ratio) in the same way as with-profits business in the UK. Under unit-linked products the profits that arise from managing the policy, its investments and the insurance risk accrue entirely to shareholders, with investment gains accruing to the policyholder within the underlying unitized fund. The profits from non-participating products consist of any surplus remaining after paying the defined policy benefits. All the profits from A&H products accrue to shareholders.

Unit-linked products tend to have higher profit than traditional non-linked products as expenses and charges are better matched and solvency capital requirements are lower. At the end of 2005 Prudential Corporation Asia offered unit-linked products in 10 of the 12 countries in Asia in which it operates.

Mutual Fund Products

Prudential Corporation Asia's mutual fund range includes debt, equity, balanced and money market funds. Prudential Corporation Asia makes transaction charges (initial and surrender depending on the type of fund and the length of the investment) and also makes a service charge based on assets under management. The charges vary by country and fund with money market style funds generally having the lowest charges and equity funds the highest.

New Business Premiums

In 2005, total sales of insurance products were £1,485 million, up 27 per cent from 2004 (£1,172 million). Of this amount, regular premium insurance sales were up 27 per cent to £648 million and single premium insurance sales increased 26 per cent from £662 million in 2004 to £837 million.

The following table shows Prudential's Asian life insurance new business premiums by territory for the periods indicated. In this table "Other Countries" includes, Thailand, The Philippines and Vietnam.

	2005	2004
	(In £ Millions)	
Singapore	**342**	246
Hong Kong	**372**	333
Malaysia	**75**	68
Taiwan	**274**	231
Japan	**34**	24
Korea	**161**	96
China	**40**	25
Indonesia	**84**	66
India (Group's 26% interest in joint venture with ICICI)	**61**	38
Other countries	**42**	45
Total	**1,485**	1,172

In addition, for the year ended December 31, 2005, Prudential Corporation Asia's mutual funds had third party funds under management of £10.1 billion, up from £8.5 billion in 2004, following net sales of £1.3 billion during the year, up 3 per cent from 2004. The £10.1 billion of funds under management at the end of 2005 primarily comprised of, Korea £2.8 billion, Japan £2.7 billion, India £1.5 billion and Taiwan £1.3 billion.

Investments

General

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

Prudential's Total Investments

The following table shows Prudential's insurance and non-insurance investments at December 31, 2005. In addition, at December 31, 2005 Prudential had £41.6 billion of external mutual funds under management. Assets held to cover linked liabilities relate to unit-linked and variable annuity products. In this table, investments are valued as set out in Note A4 of the notes to Prudential's consolidated financial statements.

	At December 31, 2005							
	UK £m	M&G £m	Egg £m	Total UK £m	United States £m	Asia £m	Other £m	Total £m
Investment properties	11,751	1	0	11,752	41	39	0	11,832
Investments accounted for using the equity method	0	0	5	5	0	0	0	5
Financial investments:								
Loans and receivables	1,128	0	7,430	8,558	3,577	1,105	0	13,240
Equity securities	47,861	9	0	47,870	273	3,138	0	51,281
Debt securities	42,350	456	2,117	44,923	24,290	3,957	788	73,958
Other investments	1,759	917	195	2,871	825	42	82	3,820
Deposits	5,747	0	0	5,747	380	307	76	6,510
Total financial investments	98,845	1,382	9,742	109,969	29,345	8,549	946	148,809
Total investments excluding assets held to cover linked liabilities, portfolio holdings in unit trusts and other eliminations	110,596	1,383	9,747	121,726	29,386	8,588	946	160,646
Assets held to cover linked liabilities, portfolio holdings in unit trusts and other eliminations	20,667			20,667	8,574	2,676	(171)	31,746
Total investments	131,263	1,383	9,747	142,393	37,960	11,264	775	192,392

Prudential's Investment Yields

The following table shows the income from the investments of Prudential's operations by asset category for the periods indicated. This table does not include investment income from assets held to cover linked liabilities, portfolio holdings in unit trusts and separate account assets. Yields have been calculated using the average of opening and closing balances for the appropriate asset.

	Year Ended December 31,			
	Yield	2005 Amount	Yield	2004 Amount
	(In £ Millions, Except Percentages)			
Investment properties				
Net investment income	**6.4%**	**768**	7.2%	829
Net realized investment gains (losses)	**6.2%**	**753**	2.3%	261
Net unrealized investment gains (losses)	**5.0%**	**600**	8.5%	979
Ending assets		**11,832**		12,332
Investments accounted for using the equity method				
Net investment income	**0%**	**0**	0%	0
Net realized investment gains (losses)	**0%**	**0**	0%	0
Net unrealized investment gains (losses)	**0%**	**5**	0%	5
Ending assets		**5**		5
Loans and receivables				
Net investment income	**7.8%**	**999**	7.7%	916
Net realized investment gains (losses)	**3.4%**	**434**	1.3%	153
Net unrealized investment gains (losses)	**11.2%**	**1,435**	10.3%	1,219
Ending assets		**13,240**		12,421
Equity securities				
Net investment income	**6.1%**	**2,731**	5.2%	1,883
Net realized investment gains	**4.8%**	**2,177**	3.4%	1,234
Net unrealized investment gains (losses)	**14.7%**	**6,609**	6.7%	2,443
Ending assets		**51,281**		38,763
Debt securities				
Net investment income	**6.2%**	**4,455**	6.5%	4,548
Net realized investment gains (losses)	**0.4%**	**287**	0%	0
Net unrealized investment gains (losses)	**2.5%**	**1,779**	1.1%	763
Ending assets		**73,958**		69,613
Other investments				
Net investment income	**3.6%**	**115**	4.3%	100
Net realized investment gains	**4.0%**	**125**	1.3%	31
Net unrealized investment gains (losses)	**13.1%**	**414**	10.4%	245
Ending assets		**3,820**		2,491
Deposits				
Net investment income	**5.6%**	**327**	3.2%	141
Net realized investment gains	**0%**	**0**	0%	0
Net unrealized investment gains (losses)	**0%**	**0**	0%	0
Ending assets		**6,510**		5,200
Total				
Net investment income	**6.2%**	**9,395**	6.3%	8,417
Net realized investment gains	**2.5%**	**3,776**	1.3%	1,679
Net unrealized investment gains (losses)	**7.2%**	**10,842**	4.2%	5,654

	Year Ended December 31,	
Ending assets	**160,646**	140,825

Prudential's Insurance Investment Strategy and Objectives

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

Internal funds under management

Prudential manages 88 per cent of its group funds principally through its fund management businesses, M&G in the United Kingdom, together with PPM America in the United States and Prudential Asset Management (formerly PPM Asia) in Singapore, Hong Kong and Japan. Approximately 5 per cent of the group's funds relate to assets held by the banking operations and the remaining 7 per cent mainly relate to assets held to back unit linked, unit trust and variable annuity liabilities.

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

Investments Relating to UK Insurance Business

Strategy

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

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

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

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

Investments

The following table shows the investments relating to Prudential's UK insurance business, other than its unit-linked business, at December 31, 2005. The with-profits fund also includes two other businesses, SAIF and Prudential Annuities Limited. The investments in respect of SAIF are shown separately. The investments in respect of Prudential Annuities Limited are included within the Annuities column. The "Other" column includes investments relating to solvency capital of unit-linked funds and investments relating to non-life long-term business.

	At December 31, 2005					
	With-Profits	Shareholder-backed Annuities	SAIF	Other	Total	Total %
	(In £ Millions, Except Percentages)					
Investment properties	9,962	198	1,586	5	11,751	10.6
Financial investments:						
Loans and receivables:						
Mortgage loans	213	37	0	9	259	
Policy loans	30	0	16	1	47	
Other loans	616	7	197	2	822	
Total loans and receivables	859	44	213	12	1,128	1.0
Equity securities:						
United Kingdom:						
Listed	26,617	6	5,129	0	31,752	
Unlisted	313	0	36	0	349	
Total United Kingdom	26,930	6	5,165	0	32,101	29.0
International:						
United States	1,992	0	288	0	2,280	
Europe (excluding the United Kingdom)	4,846	0	796	0	5,642	
Japan	1,653	0	313	0	1,966	
Pacific (excluding Japan)	3,079	0	646	0	3,725	
Other	1,839	0	307	1	2,147	
Total international	13,409	0	2,350	1	15,760	14.3
Total equity securities	40,339	6	7,515	1	47,861	43.3
Debt securities:						
UK government	1,910	1,361	250	835	4,356	
US government	421	0	0	15	436	
Other	25,134	5,898	4,460	2,066	37,558	
Total debt securities	27,465	7,259	4,710	2,916	42,350	38.3
Other investments:						
Participation in investment pools	621	0	63	0	684	
Other financial investments	620	0	117	0	737	

	At December 31, 2005					
Derivative asset	**225**	**6**	**57**	**50**	**338**	
Total other investments	**1,466**	**6**	**237**	**50**	**1,759**	**1.6**
Deposits	**3,987**	**438**	**723**	**599**	**5,747**	**5.2**
Total investments	**84,078**	**7,951**	**14,984**	**3,583**	**110,596**	**100.0**

Equity Securities

Prudential's UK insurance operations, excluding unit-linked business, had £47,861 million invested in equities at December 31, 2005. Most of these equities support Prudential Assurance's with-profits fund and the SAIF fund, both of which are managed using the same general investment strategy. The following table shows the geographic spread of this equity portfolio by market value in accordance with the policies described in Note A4 of the notes to the consolidated financial statements.

	At December 31, 2005	
	Market Value	%
	(In £ Millions, Except Percentages)	
United Kingdom	32,101	67.1
United States	2,280	4.8
Europe (excluding United Kingdom)	5,642	11.8
Japan	1,966	4.1
Pacific (excluding Japan)	3,725	7.7
Other	2,147	4.5
Total	47,861	100.0

The UK equity holdings are well diversified and broadly mirror the FTSE All-Share share index. Prudential holds equities in 553 UK companies. At December 31, 2005, the ten largest holdings in UK equities amounted to £13,362 million, accounting for 41.6 per cent of the total UK equity holdings of £32,101 million supporting the UK insurance operations. The following table shows the market value of the ten largest holdings in UK equities at December 31, 2005.

	At December 31, 2005	
	Market Value	%
	(In £ Millions, Except Percentages)	
B.P.	2,987	9.3
GlaxoSmithKline	1,784	5.6
Vodafone Group	1,614	5.0
HSBC Holdings	1,546	4.8
Royal Dutch Shell	1,243	3.9
The Royal Bank of Scotland Group	1,128	3.5
Barclays	1,072	3.3
Astra Zeneca	801	2.5
Rio Tinto	596	1.9
Diageo	591	1.8
Total	13,362	41.6

All industry sectors are represented in Prudential's equity portfolio. At December 31, 2005, within the £32,101 million in UK equities supporting the UK insurance operations, Prudential had £22,153 million, or 68.9 per cent of the holdings invested in ten industries. The following table shows the primary industry concentrations based on market value of the portfolio of UK equities relating to the UK insurance business at December 31, 2005.

	At December 31, 2005	
	Market Value	**%**
	(In £ Millions, Except Percentages)	
Banks	**5,533**	**17.2**
Oil and Gas	**4,753**	**14.8**
Pharmaceuticals and Biotech	**2,740**	**8.5**
Telecommunication Services	**2,685**	**8.4**
Mining	**1,655**	**5.2**
Media and Entertainment	**1,099**	**3.4**
Leisure and Hotels	**1,041**	**3.2**
Construction & Building Materials	**1,031**	**3.2**
Investment Companies	**811**	**2.5**
Utilities	**805**	**2.5**
Total	**22,153**	**68.9**

Debt Securities

At December 31, 2005, 88.7 per cent of Prudential's debt securities supporting the UK insurance operations were issued by corporations and overseas governments other than the US, 10.3 per cent were issued or guaranteed by the UK government and 1.0 per cent were issued or guaranteed by the US government. These guarantees relate only to payment and, accordingly, do not provide protection against fluctuations in market price that may occur during the term of the fixed income securities.

The following table shows the market value of the debt securities portfolio by maturity at December 31, 2005, in accordance with the policies described in Note A4 of the notes to the consolidated financial statements.

	At December 31, 2005	
	Market Value	**%**
	(In £ Millions, Except Percentages)	
Securities maturing:		
Within one year	**1,122**	**2.7**
Over one year and up to five years	**5,060**	**12.0**
Over five years and up to ten years	**7,723**	**18.2**
Over ten years and up to fifteen years	**4,751**	**11.2**
Over fifteen years	**23,694**	**55.9**
Total debt securities	**42,350**	**100.0**

The following table shows debt securities by rating:

	At December 31, 2005	
	Market Value	%
	(In £ Millions, Except Percentages)	
S&P AAA	11,245	26.6
S&P AA+ to AA-	3,450	8.1
S&P A+ to A-	10,274	24.3
S&P BBB+ to BBB-	4,495	10.6
S&P Other	930	2.2
	30,394	71.8
Moody's Aaa	1,261	3.0
Moody's Aa1 to Aa3	1,012	2.4
Moody's A1 to A3	1,113	2.6
Moody's Baa1 to Baa3	771	1.8
Moody's Other	389	0.9
	4,546	10.7
Fitch	949	2.2
Other	6,461	15.3
Total debt securities	42,350	100.0

Real Estate

At December 31, 2005, Prudential's UK insurance operations had £11,751 million of investments in real estate. The following table shows the real estate portfolio by type of investment. The real estate investments are shown at market value in accordance with the policies described in Note A4 of the notes to the consolidated financial statements.

	At December 31, 2005	
	Market Value	%
	(In £ Millions, Except Percentages)	
Office buildings	3,763	32.1
Shopping centers/commercial	4,574	38.9
Retail warehouses/industrial	2,978	25.3
Development	227	1.9
Other	209	1.8
Total	11,751	100.0

Approximately 51.1 per cent of the UK held real estate investment is located in London and Southeast England (Buckinghamshire, Berkshire, East and West Sussex, Hampshire, Isle of Wight, Kent, Oxfordshire and Surrey) with 42.6 per cent located throughout the rest of the United Kingdom and the remaining 6.3 per cent located overseas.

Investments Relating to Prudential's US Insurance Business

Strategy

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

The investment portfolio of the US Operations consists primarily of debt securities, although the portfolio also contains investments in mortgage loans, policy loans, common and preferred stocks, derivative instruments, cash and short-term investments and miscellaneous other investments.

Investments

The following table summarizes the total insurance investments of the US Operations, excluding the separate account investments supporting the variable annuity business, at December 31, 2005.

	December 31, 2005	
	(In £ Millions)	
Non-institutional		
Investment properties	41	0.1
Loans	2,968	10.2
Equity securities	240	0.8
Corporate securities and commercial loans	15,052	51.2
Residential mortgage-backed securities	2,089	7.1
Commercial mortgage-backed securities	1,125	3.8
Other	1,404	4.8
Total debt securities	19,670	66.9
Other investments	561	1.9
Deposits	369	1.3
Total non-institutional	23,849	81.2
Institutional		
Investment properties	0	
Loans	609	2.1
Equity securities	33	0.1
Corporate securities and commercial loans	3,155	10.7
Residential mortgage-backed securities	171	0.6
Commercial mortgage-backed securities	285	1.0
Other	1,009	3.4
Total debt securities	4,620	15.7
Other investments	264	0.9
Deposits	11	0.0

	December 31, 2005	
Total institutional	**5,537**	**18.8**

Total		
Investment properties	**41**	**0.1**
Loans	**3,577**	**12.3**
Equity securities	**273**	**0.9**
Corporate securities and commercial loans	**18,207**	**61.9**
Residential mortgage-backed securities	**2,260**	**7.7**
Commercial mortgage-backed securities	**1,410**	**4.8**
Other	**2,413**	**8.2**
Total debt securities	**24,290**	**82.66**
Other investments	**825**	**2.8**
Deposits	**380**	**1.3**
Total	**29,386**	**100**

Debt securities are shown at fair value under IFRS. Previously, under UK GAAP, debt and other fixed income securities were carried at amortized cost, with the exception of certain securities held by the US fund management operation, which were shown at fair value. Loans are shown at amortized cost. Equity securities and investment properties are shown at fair value. The fair value of unlisted securities is estimated by Jackson National Life using independent pricing services or analytically determined values.

Debt Securities

Corporate Securities and Commercial Loans

At December 31, 2005, the US Operations had £18,207 million of corporate securities and commercial loans, representing 62.0 per cent of US insurance total investments. Of the £18,207 million, £15,007 million consisted of debt securities that are publicly traded or trade under Rule 144A of the Securities Act of 1933, as amended ("Rule 144A") and £3,200 million consisted of investments in non-Rule 144A privately placed fixed income securities.

For statutory reporting in the United States, debt securities are classified into six quality categories specified by the Securities Valuation Office of the National Association of Insurance Commissioners ("NAIC"). The categories range from Class 1 (the highest) to Class 6 (the lowest). Performing securities are designated Classes 1-5. Securities in or near default are designated Class 6. Securities designated as Class 3, 4, 5 and 6 are non-investment grade securities. Generally, securities rated AAA to A by nationally recognized statistical ratings organizations are Class 1, BBB in Class 2, BB in Class 3 and B and below in Classes 4 through 6. If a designation is not currently available from the NAIC, Jackson National Life's investment advisor, PPM America, provided the designation for the purposes of the disclosure contained herein.

The following table shows the credit quality of the portfolio of publicly traded and Rule 144A fixed income securities at December 31, 2005.

	At December 31, 2005	
	Book Value	% of Total
	(In £ Millions, Except Percentages)	
NAIC Designation		
1	**5,852**	**39.0**
2	**7,622**	**50.8**
3	**1,183**	**7.9**
4	**320**	**2.1**
5	**30**	**0.2**
6		**0.0**
Total	**15,007**	**100.0**

The following table shows the credit quality of the non-Rule 144A private placement portfolio at December 31, 2005.

	At December 31, 2005	
	Book Value	% of Total
	(In £ Millions, Except Percentages)	
NAIC Designation		
1	**1,368**	**42.8**
2	**1,471**	**46.0**
3	**299**	**9.3**
4	**51**	**1.6**
5		
6	**11**	**0.3**
Total	**3,200**	**100.0**

Residential Mortgage-Backed Securities

At December 31, 2005, the US insurance operations had £2,260 million of residential mortgage-backed securities, representing 7.7 per cent of US insurance total investments. Although this percentage is higher than the average US insurance company, Jackson National Life believes these securities provide additional yield and liquidity. At December 31, 2005, 86.9 per cent of the US insurance Operations' residential mortgage-backed securities were rated AAA or the equivalent by a nationally recognized statistical ratings organization (these include Standard & Poor's, Moody's and Fitch) and 99.9 per cent were rated NAIC 1.

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

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Commercial Mortgage-Backed Securities

At December 31, 2005, the US Operations had £1,410 million of commercial mortgage-backed securities, representing 4.8 per cent of US insurance total investments. 100 per cent of this total was rated by a nationally recognized statistical ratings organization (these include Standard & Poor's, Moody's and Fitch) and 98.5 per cent was rated investment grade. Due to the structures of the underlying commercial mortgages, these securities do not present the same pre-payment or extension risk as residential mortgage-backed securities.

Other Debt Securities

At December 31, 2005, the US Operations had £2,413 million of other debt securities, representing 8.2 per cent of US insurance total investments.

Loans

Loans totaled £3,577 million, representing 12.2 per cent of US insurance total investments at December 31, 2005. Of the total, £3,107 million related to commercial mortgage loans and £470 million to policy loans.

Commercial Mortgage Loans

Commercial mortgage loans represented 10.6 per cent of US insurance total investments at December 31, 2005. This total included 507 first mortgage loans with an average loan balance of approximately £6.1 million, collateralized by properties located in the United States and Canada. More than 95 per cent of the US Operations' commercial mortgage loan investments have been directly originated in the last eight years.

Jackson National Life has addressed the risk of these investments by building a portfolio that is diverse both in geographic distribution and property type, emphasizing four main institutional property types: multi-family residential, retail, suburban office and warehouse/distribution facilities.

As of December 31, 2005, approximately 26.2 per cent of the portfolio was industrial 21.3 per cent multi-family residential, 19.7 per cent suburban office, 19.6 per cent retail, 11.4 per cent hotel and 1.8 per cent other. Approximately 12.7 per cent of the portfolio is collateralized by properties in California and 10.6 per cent of the portfolio is collateralized by properties in Texas, with no other state representing more than 7.1 per cent of the outstanding balance.

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

Policy Loans

Policy loans represented 1.6 per cent of US insurance total investments at December 31, 2005. Policy loans are fully secured by individual life insurance policies or annuity policies and are contractual arrangements made under the policy.

Other

Other financial investments of £825 million, representing 2.8 per cent of US insurance total investments at December 31, 2005, were made up of £ 414 million of limited partnership interests, derivative assets of £167 million and £244 million of other miscellaneous investments.

The largest investment in the limited partnerships category is a £168 million interest in the PPM America Private Equity Fund. The remainder of this category consists of diversified investments in 160 other partnerships managed by independent money managers that generally invest in various equity and fixed income loans and securities.

Equity Securities

Equity securities supporting US insurance operations totaled £273 million at December 31, 2005.

Investments Relating to Asian Insurance Business

Prudential's Asian operations' investments, other than investments in respect of unit-linked business, largely support the business of its Singapore, Hong Kong, Malaysia, Japan and Taiwan operations.

The following table shows Prudential Corporation Asia's investments, other than investments from unit-linked business, at December 31, 2005. In this table, investments are valued in accordance with the policies described in Note A4 of the notes to the consolidated financial statements.

	At December 31, 2005	
	Market Value	% of Total
	(In £ Millions, Except Percentages)	
Investment Properties	39	0.4
Financial investments:		
Loans and receivables	1,105	12.9
Equity securities	3,138	36.5
Debt securities	3,957	46.1
Other investments	42	0.5
Deposits	307	3.6
Total financial investments	8,549	99.6
Total investments	8,588	100.0

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

Debt Securities

The following table shows consolidated investment categorization of the debt security investments of Prudential Corporation Asia's long-term insurance fund, other than investments from unit-linked business, at December 31, 2005.

	At December 31, 2005	
	Market Value	% of Total
	(In £ Millions, Except Percentages)	
Debt securities:		
Government Bonds	**2,313**	**58.4**
Quasi Government Bonds	**210**	**5.3**
Investment grade Corporate Bonds	**1,223**	**30.9**
Non-Investment grade Corporate Bonds	**7**	**0.2**
Un-rated bonds	**204**	**5.2**
Total	**3,957**	**100.0**

Equity Securities

The following table shows a geographic analysis of equity security investments of Prudential Corporation Asia's long-term insurance fund, other than investments from unit-linked business, at December 31, 2005.

	At December 31, 2005	
	Market Value	% of Total
	(In £ Millions, Except Percentages)	
Hong Kong	**1,458**	**46.5**
Singapore	**957**	**30.5**
Taiwan	**321**	**10.2**
India	**220**	**7.0**
Malaysia	**106**	**3.4**
Japan	**23**	**0.7**
Korea	**22**	**0.7**
Other	**31**	**1.0**
Total	**3,138**	**100.0**

Investments Relating to Banking Business

At December 31, 2005, Prudential had total banking investments of £9,747 million. The following table summarizes the investment portfolios relating to the UK banking business. In this table, investments are valued as described in Note A4 to Prudential's consolidated financial statements.

At December 31, 2005

	At December 31, 2005	
	Market Value	Total %
	(In £ Millions, Except Percentages)	
Debt securities	**2,117**	**21.7**
Loans and other	**7,630**	**78.3**
Total	**9,747**	**100.0**

Of the £9,747 million of investments, £357 million matures within one month and £3,782 million matures between one and three months.

The following table shows UK banking business loans by type and repayment period at December 31, 2005.

	At December 31, 2005				
	Due in One Year or Less	Due in Over One Year and Up to Five Years	Due in Over Five Years	Provision for bad and doubtful debts	Total
	(In £ Millions)				
Unsecured personal loans	38	1,605	1	(184)	1,460
Credit card receivables	3,496	0	0	(151)	3,345
Residential mortgages	0	0	2,625	0	2,625
Total	3,534	1,605	2,626	(335)	7,430

The following table shows UK banking business loans by type and interest rate at December 31, 2005.

	At December 31, 2005			
	Fixed Rate	Variable Rate	Provision for bad and doubtful debts	Total
	(In £ Millions)			
Unsecured personal loans	1,644	0	(184)	1,460
Credit card receivables	0	3,496	(151)	3,345
Residential mortgages	45	2,580	0	2,625
Total	1,689	6,076	(335)	7,430

Description of Property

As at December 31, 2005, Prudential's UK based businesses occupied approximately 30 properties in the United Kingdom, Europe and Mumbai. These properties are primarily offices with some ancillary storage or warehouse facilities. Prudential's headquarters are located in London. Of the remainder, the most significant are offices in London, Reading, Chelmsford, Dudley and Derby in England, Stirling in Scotland, Belfast in Northern Ireland and Mumbai in India. The property in Stirling, one property in Reading and one in Derby are held on a freehold basis. The properties in Stirling and in Reading are leased by the business from Prudential Assurance's long-term fund. The rest of the properties occupied by Prudential UK based businesses, both in the UK and in Mumbai, are held on long-term leaseholds. The leasehold properties range in size from 1,800 to 270,000 square feet. Overall, the occupied property portfolio totals approximately 1,300,000 square feet.

In addition to these properties, the Prudential group owns the freehold of a sports facility in Reading for the benefit of staff.

The Prudential group also holds approximately 60 other leasehold properties in the United Kingdom. This surplus accommodation is spread geographically across the United Kingdom and totals approximately 500,000 square feet.

In the United States, Prudential owns Jackson National Life's executive and principal administrative office located in Michigan. Prudential also leases premises in Michigan, Colorado, California, Illinois, New York, New Jersey, Georgia, Florida, Wisconsin, Texas, Massachusetts, Connecticut, New Hampshire and North Dakota for certain of its operations. Prudential holds 36 operating leases with respect to office space, throughout the United States. In the United States, Prudential owns and leases a total of approximately 731,000 square feet of property.

In Asia, Prudential owns or leases properties principally in Hong Kong, Singapore, Malaysia, Indonesia, Thailand, the Philippines, China, Taiwan, Japan, Vietnam, India and Korea. Within these countries, Prudential holds 65 offices on a freehold basis, 7 offices on a leasehold basis and 670 operating leases in respect of office space, totaling approximately 5,800,000 square feet of property. In addition, Prudential is planning to lease approximately 657,000 square feet of additional property in 2006 to support expansion plans throughout the region.

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

Competition

General

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

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

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

An important competitive factor is the ratings Prudential receives in some of its target markets, most notably in the United States, from recognized rating organizations. The intermediaries with whom Prudential works, including financial advisors, tied agents, brokers, wholesalers and financial institutions consider ratings as one factor in determining from which provider to purchase financial products.

Prudential Assurance's long-term fund is currently rated AA+ (stable outlook) by Standard & Poor's, Aa1 (stable outlook) by Moody's and AA+ (stable outlook) by Fitch Ratings. The ratings from Standard & Poor's, Moody's and Fitch Ratings represent the second highest ratings of their respective rating categories.

Jackson National Life is currently rated AA (stable outlook) by Standard & Poor's, AA (stable outlook) by Fitch Ratings and A1 (stable outlook) by Moody's. The ratings from Standard & Poor's and Fitch Ratings represent the third highest rating category respectively and the ratings from Moody's represent the fifth highest rating category. Prior to June 23, 2006, Standard & Poor's rated Jackson National Life as AA (negative outlook).

Prudential offers different products in its different markets of the United Kingdom, the United States and Asia and, accordingly, faces different competitors and different types of competition in these markets. In all of the markets in which Prudential operates its products are not unique and, accordingly, it faces competition from market participants who manufacture a varying range of similar and identical products.

United Kingdom

Prudential's principal competitors include many of the major stock and mutual retail financial services and fund management companies operating in the United Kingdom. These companies include Aviva, Legal & General, Standard Life, Friends Provident, Lloyds TSB, HBOS, Aegon, AXA, Zurich

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Financial Services, Fidelity, Invesco, Jupiter, Threadneedle and Schroders. Prudential competes with other providers of financial products to be included on financial advisors panels of preferred providers.

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

UK retail banking continues to be dominated by HBOS, RBS, Barclays, Lloyds TSB, HSBC and Abbey. In recent years, these big players have increasingly focused on unsecured lending products which traditionally have offered high returns on capital. Margins, whilst still healthy, continue to be squeezed by regulatory pressure on default fees and creditor insurance. 2005 saw rising bad debt charges across the industry.

M&G's principal competitors are the main fund management companies operating in the United Kingdom and Europe. These companies include Fidelity, Invesco Perpetual, Jupiter, Threadneedle, New Star, Artemis, Schroders, Morley, Legal and General, Friends Provident, Aegon, AXA and Zurich Financial Services.

United States

Jackson National Life's competitors in the United States include major stock and mutual insurance companies, mutual fund organizations, banks and other financial services companies. National banks, in particular, may become more significant competitors in the future for insurers who sell annuities, as a result of recent legislation, court decisions and regulatory actions. Jackson National Life's principal life insurance company competitors in the United States include AIG, Allstate Financial, Allianz Life of North America, AXA Financial Inc., Hartford Life Inc., ING, John Hancock, Lincoln Financial Group, Met Life, Pacific Life and Prudential Financial.

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

Asia

Competition in the Asian markets in which Prudential operates is mainly focused on distribution, with particular emphasis on the size and competency of the agency sales force. Within Asia, Prudential is second to AIG in terms of penetration and overall life market share across the region. Other main regional competitors are Allianz, ING and Manulife. While there are large local participants in individual markets, for example, Great Eastern Life in Singapore and Malaysia, Nippon Life in Japan, Cathay Life in Taiwan, and LIC in India, none of these has pan-regional businesses. Regional players are typically of North American or European origin.

In addition, Prudential competes with the above as well as smaller competitors for talented and skilled employees with local experience, which are in particular demand in Asia. See Item 3 "Key Information-Risk Factors"

In the regional mutual fund market in terms of market presence and position, Prudential ranks alongside leading international participants such as Templeton and Fidelity.

Intellectual Property

Prudential does not operate in the United States under the Prudential name and there have been long-standing arrangements between it and Prudential Financial, Inc. and its subsidiary, the Prudential Insurance Company of America, relating to their respective uses of the Prudential name. Prudential and Prudential Financial, Inc. entered into a new trade mark co-existence agreement in 2004, under which it was agreed that Prudential Financial Inc would have the right to use the Prudential name in the Americas and certain parts of the Caribbean, Japan, Korea and Taiwan and Prudential would have the right to use the name everywhere else in the world although third parties have rights to the name in certain countries.

Legal Proceedings

Prudential Group

Prudential and its subsidiaries are involved in other litigation arising in the normal course of business. While an adverse ruling in any individual case may not in itself be material to Prudential, if applied across all similar cases, the potential liabilities may be more significant. Although the outcome of such matters cannot be predicted with certainty, management believes that the ultimate outcome of such litigation will not have a material adverse effect on the group's financial condition, results of operations or cash flows.

Jackson National Life

JNL is involved in litigation arising in the ordinary course of business. It is the opinion of management that the ultimate disposition of such litigation will not have a material adverse affect on JNL's financial condition or results of operations. JNL has been named in civil litigation proceedings, which appear to be substantially similar to other class action litigation brought against many life insurers alleging misconduct in the sale and administration of insurance products. JNL generally accrues for legal contingencies once the contingency is deemed to be probable and estimable. Accordingly, at December 31, 2005 and 2004, the JNL had recorded accruals totaling $16.5 million and $20.8 million, respectively.

Sources

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

SUPERVISION AND REGULATION OF PRUDENTIAL

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

UK Supervision and Regulation

The Financial Services and Markets Act 2000

Prudential's insurance, investment and banking businesses in the United Kingdom are regulated by the Financial Services Authority (the "FSA"), the statutory regulator granted powers under the 2000 Act. In addition, those businesses are subject to various United Kingdom laws governing the terms and the sale of products (for example, the Consumer Credit Act 1974 in relation to the banking business) some of which require the relevant Prudential entity to be licensed or registered.

Risk-Based Regulation

The FSA employs a risk-based regulatory approach under the 2000 Act pursuant to which each regulated firm's risk is assessed using a risk assessment methodology known as ARROW. This is a high-level review aimed at assessing the significance of a particular risk posing a threat to the FSA's statutory objectives under the 2000 Act. These objectives relate to market confidence, public awareness, consumer protection and the reduction of financial crime.

The ARROW framework is the core of the FSA's risk-based approach to regulation. Using the process, the FSA will consider the particular risk a firm might pose to the statutory objectives by assessing the impact and probability of a particular risk materializing.

The FSA aims to create a single set of prudential requirements organized according to risk category with sections containing rules and guidance on credit, market, operational and insurance risks, as well as capital adequacy and consolidated supervision.

A key feature of the risk-based regime is the introduction of a single Integrated Prudential Sourcebook to replace the separate "Interim Prudential Sourcebooks" that currently regulate businesses in different regulated sectors. While the FSA initially envisaged that the Integrated Prudential Sourcebook would be fully implemented on January 1, 2004, developments and delays in the agreement of international legislation (such as the new Basel capital accord) have led to a phased introduction of its provisions. However, since the regulation of insurance has not been affected by many of these delays, the FSA proceeded with the early introduction of substantially all of the new prudential regime for insurance firms in its original target year of 2004.

The FSA has begun a consultation, which outlines various proposals to revise the Handbook, largely as a consequence of implementing the Capital Requirements Directive and the Markets in Financial Instruments Directive. The FSA proposes to complete the new structure by, first, creating, from existing material, prudential sourcebooks for insurers, mortgage firms and insurance intermediaries, and UCITS firms; and, second, deleting large parts of the existing interim prudential sourcebooks for banks and building societies as they are superseded by the Capital Requirement Directive regime.

Overview of 2000 Act Regulatory Regime

Single Regulator

The FSA is the single regulator for all authorized persons with respect to regulated activities in the financial services sector. In this regard, the FSA is authorized to make rules and issue guidance and codes in relation to a wide sphere of activity encompassing the governance of the conduct of business by, and the prudential supervision of, authorized persons.

Permission to carry on "Regulated Activities"

Under the 2000 Act, no person may carry on or purport to carry on a regulated activity by way of business in the United Kingdom unless he is an authorized person or is an exempt person. A firm which is granted permission by the FSA to carry on regulated activities becomes an authorized person for the purposes of the 2000 Act. "Regulated activities" are prescribed in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 and include banking activities, insurance activities and certain other activities, such as dealing in investments as principal or agent, as described below.

Authorization Procedure

When considering an application for authorization by a firm, the FSA may delineate the scope of, and include such restrictions on, the grant of permission as it deems appropriate. In granting or varying the terms of a firm's permissions, the FSA must ensure that the firm meets certain threshold conditions, which, among other things, require the firm to have adequate resources for the carrying on of its business, and to be a fit and proper person, having regard to all the circumstances.

Once authorized, and in addition to continuing to meet the threshold conditions to authorization, firms are obliged to comply with the FSA Principles for Business, which are high level principles for conducting financial services business in the United Kingdom. These include the maintenance of adequate systems and controls, treating customers fairly and communicating with customers in a manner that is clear, fair and not misleading.

Moreover, the 2000 Act obliges firms to secure the FSA's prior approval of the appointment of individuals performing certain important functions within a firm or on its behalf with respect to the carrying on of regulated activities (approved persons).

Principles for business

A key feature of the FSA regime is the existence of 11 'Principles for business' which all firms are expected to abide by. These cover key areas such as firms' relationship with the regulator, the need to act with integrity and honesty as well as that to treat customers fairly.

The FSA has expressed the wish to move away from detailed rules in favor of principle-based regulation, much of which would rely on the Principles for business mentioned above. While many firms welcome this, they are also likely to face greater uncertainty as what would be deemed to be 'compliant' under such a regime and this is a concern in the industry.

Application of 2000 Act Regulatory Regime to Prudential

Each of Prudential's principal UK insurance, investment and banking businesses is subject to regulation and supervision by the FSA in the carrying on of its regulated activities. The following discussion considers, in turn, the main features of the 2000 Act regime applicable to Prudential's insurance, investment and banking businesses in the United Kingdom.

Regulation Applicable to Prudential's Insurance, Investment and Banking Businesses

Supervision of Management and Change of Control of Authorized Firms

The FSA closely supervises the management of authorized firms through the approved person's regime, under which any appointment of persons who hold positions of significant influence within an authorized firm must be pre-approved by the FSA.

The FSA also regulates the acquisition of control over authorized firms. Under the 2000 Act, any person proposing to acquire control of an authorized firm must first obtain the consent of the FSA. In considering whether to grant or withhold its approval to the acquisition of control, the FSA must be satisfied both that the acquirer is a fit and proper person to have control over the authorized firm, and that the interests of consumers would not be threatened by his acquiring control.

Control over a UK authorized firm ("A") is acquired if the acquirer holds 10 per cent or more of the shares in A or a parent undertaking of A ("P"); is able to exercise significant influence over the management of A or P by virtue of his shareholding in that company; is entitled to exercise, or control the exercise, of 10 per cent or more of the voting power of A or P; or is able to exercise significant influence over the management of A or P by virtue of his voting power in that company. Increases in 'control', once they reach thresholds of 20 per cent, 33 per cent and 50 per cent of the shares or voting power of an authorized firm or one of its controllers, also require the consent of the FSA. The European Commission has launched a consultation on how to improve the supervisory approval process for mergers and acquisitions in the banking, insurance and securities sectors. Current European Union rules allow Member States' supervisory authorities to block proposed mergers and acquisitions if they consider that the "sound and prudent management" of the target company could be put at risk.

In order to determine whether a person or a group of persons is a "controller" for the purposes of the 2000 Act, the holdings (shares or voting rights) of the person and his "associates", if any, are aggregated.

Intervention and Enforcement

The FSA has extensive powers to investigate and intervene in the affairs of an authorized firm. The 2000 Act imposes on the FSA statutory obligations to monitor compliance with the requirements imposed by, and to enforce the provisions of, the 2000 Act, related secondary legislation and the rules made there under.

The FSA's enforcement powers, which may be exercised against both authorized firms and approved persons, include public censure, imposing unlimited fines and, in serious cases, the revocation or variation of permission to carry on regulated activities or of an approved person's approved status. In addition, the FSA may vary or revoke an authorized firm's permission if it is desirable to protect the interests of consumers or potential consumers, or if the firm has not engaged in regulated activity for 12 months, or if it is failing to meet the threshold conditions for authorization. The FSA has further powers to obtain injunctions against authorized persons and to impose or seek restitution orders where persons have suffered loss. Once the FSA has made a decision to take enforcement action against an authorized or approved person (other than in the case of an application to the court for an injunction or restitution order), the person affected may refer the matter to the Financial Services and Markets Tribunal. Breaches of certain FSA rules by an authorized firm may also give a private person who suffers loss as a result of the breach a right of action against the authorized firm for damages.

In addition to its ability to apply sanctions for market abuse, the FSA has the power to prosecute criminal offences arising under the 2000 Act and insider dealing under Part V of the Criminal Justice Act 1993 and breaches of money laundering regulations. The FSA's stated policy is to pursue criminal prosecution in all appropriate cases.

The FSA, although not a creditor, may seek administration orders under the Insolvency Act 1986 (as amended), present a petition for the winding-up of an authorized person or have standing to be heard in the voluntary winding-up of an authorized person. It should be noted that insurers carrying on long-term insurance business cannot voluntarily be wound up without the consent of the FSA.

FSA Conduct of Business Rules

The FSA's Conduct of Business Rules apply to every authorized firm carrying on regulated activities and regulate the day-to-day conduct of business standards to be observed by authorized persons in carrying on regulated activities.

There are detailed rules in the FSA's Conduct of Business Rules introduced in January 2004 concerning the sale of packaged products (such as life insurance policies with an investment element) and the mechanics of the sale process. In contrast to the previous rules, firms may sell not only their own products, but those of other providers as well, without limit on the number of providers whose products can be sold.

The FSA's Conduct of Business Rules also included provisions restricting the terms on which product providers can take up direct or indirect holdings in, or provide credit to, intermediaries offering advice on packaged products (which do not apply in between firms in the same immediate group). Furthermore, the FSA's Conduct of Business Rules were amended to include rules governing the extent to which product providers can provide intermediaries with indirect benefits, in order to avoid the development of conflicts of interest (which rules, again, are disapplied for firms in the same immediate group).

The "depolarization" reform has also led the FSA to review a number of areas of its rulebook such as the product disclosure regime. The FSA had hoped to introduce reduced point-of-sale product disclosure requirements. However, the industry has expressed concerns about the practical difficulties of such a reform as well as the potential legal consequences of making reduced disclosures to customers generally. As a result, the FSA is now reviewing its original plans in this area.

The FSA is proceeding with its 'Handbook Reform' programme. The FSA's key driver is to move towards more of a principles based regime and to eliminate redundant and over-prescriptive provisions where it believes that high-level requirements suffice. A key element of this work relates to the Conduct of Business Sourcebook and key proposals are expected to be published by the FSA in the autumn. The FSA's work on this is, in part, constrained by the implementation of the EU Markets in Financial Services Directive ('MiFID'), the main aspects of which are covered under Regula tion of investment business' below.

Financial Promotion

The FSA's Conduct of Business Rules govern the circumstances and manner in which authorized firms may communicate and approve "financial promotions", which are communications in the course of business that constitute invitations or inducements to engage in investment activity.

Treating Customers Fairly

Under FSA Principle 6, firms are expected to pay due regard to the interest of their customers and to treat them fairly. This principle is seen as key to the operation of an efficient retail market for financial services and is closely linked to maintaining consumer confidence. Until recently the meaning of the duty had not been further defined and the FSA has sought to remedy this through its Treating Customers Fairly' (TCF') initia tive.

Although the FSA has refrained from making rules, it has published a number of case studies providing an indication of its expectations in the areas of product development, complaint handling, financial promotions and systems and controls. Firms are expected to perform a gap analysis of their 'TCF compliance' and address any weaknesses thus identified.

The Financial Ombudsman Service

The Financial Ombudsman Service is intended to provide speedy, informal and cost effective dispute resolution of complaints made against authorized firms by individuals and small-business customers. The Ombudsman is empowered to order firms to pay fair compensation for loss and damage and may order a firm to take such steps as it determines to be just and appropriate to remedy a complaint. Authorized firms must have appropriate complaints handling procedures.

In *R (on the application of IFG Financial Services Ltd) v Financial Ombudsman Services Ltd [2005] EWHC 1153 (Admin),* the High Court of England and Wales has ruled that the Financial Ombudsman may depart from principles of English law when deciding levels of compensation in order to achieve a result which is fair and reasonable in his opinion.

The Financial Services Compensation Scheme

The 2000 Act provides for the establishment of a compensation scheme intended to compensate individuals and small businesses for claims against an authorized firm where the authorized firm is unable or unlikely to be able to meet those claims (generally, when it is insolvent or has gone out of business). The scheme is divided into three sub-schemes of banking, insurance and investment business, reflecting the different kinds of business undertaken by authorized firms. The scheme is funded by contributions from industry participants referable to the particular sub-schemes so as to minimize cross-subsidy between authorized persons whose businesses are not similar. Prudential estimates its reserve for future fund assessments for its UK business to be insignificant, and believes the reserves in place are adequate for all payments for known insolvencies. In the event of a failure of a market participant, Prudential could be required to make contributions to compensate investors.

Regulation of Insurance Business

Effecting and carrying out contracts of insurance as principal are regulated activities for the purposes of the 2000 Act, and the carrying on of such regulated activities is referred to as insurance business. Some of Prudential's subsidiaries, including The Prudential Assurance Company Limited, Prudential Annuities Limited, Prudential Retirement Income Limited, Prudential Pensions Limited, Prudential Holborn Life Limited and Prudential (AN) Limited carry on insurance business in the United Kingdom with the permission of the FSA and are supervised by the FSA under the 2000 Act.

Conduct of business requirements for insurance business

Insurance business is the subject of the FSA's conduct of business requirements laid down in the FSA's Conduct of Business Sourcebook, the main features of which are described above.

Developments in Prudential Regulation

The FSA's rules on the prudential regulation of insurance business are principally contained in those sections of the FSA's Integrated Prudential Sourcebook which prescribe rules and guidance for authorized persons carrying on insurance business. Under rules in the Integrated Prudential Sourcebook, an insurance company is restricted from carrying on any commercial business other than insurance business and activities directly arising from that business. The FSA Interim Prudential Sourcebook for Insurers (the "Interim Prudential Sourcebook") continues to govern some matters such as the reporting requirements.

Capital requirements of the Integrated Prudential Sourcebook

The FSA made the majority of the rules which govern the prudential regulation of insurers in 2004 and these rules are now in force as part of the Integrated Prudential Sourcebook. Overall, the requirements of the Integrated Prudential Sourcebook are intended to align the capital adequacy requirements for insurance businesses more closely with those of banking and investment firms and building societies, for example, by addressing tiers of capital, rather than looking at net admissible assets.

The Integrated Prudential Sourcebook also introduced an Individual Capital Assessment framework for life and non-life insurers. The Individual Capital Assessment requires all insurers to assess for themselves the amount of capital needed to back their business. If the FSA views the result of this assessment as insufficient, it may draw up its own Individual Capital Guidance for a firm, which can be imposed as a requirement on the scope of the authorized firm's permission.

Long-term Assets and Liabilities

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

The extent to which long-term fund assets may be used for purposes other than long-term business is restricted by the rules in the Integrated Prudential Sourcebook and Interim Prudential Sourcebook. Only the "established surplus" the excess of assets over liabilities in the long-term fund, as determined by an actuarial investigation may be transferred so as to be available for other purposes. Restrictions also apply to the payment of dividends by the insurance company, as described below. The rules in the Integrated Prudential Sourcebook require, in addition to the capital requirements referred to below, the maintenance of sufficient assets in the separate long-term insurance fund to cover the actuarially determined value of the insurance liabilities.

Capital Requirements

The Integrated Prudential Sourcebook requires that insurance companies maintain assets sufficient to meet the relevant capital requirement at all times in respect of both any long-term insurance and general insurance undertaken by the insurance company, the calculation of which requirement in any particular case being dependent on the type and amount of insurance business a company writes. The method of calculation of the capital requirement is set out in the Integrated Prudential Sourcebook and the level of an insurer's capital resources is also determined in accordance with the rules set out in the Integrated Prudential Sourcebook. Failure to maintain the required capital resources requirement is one of the grounds on which wide powers of intervention conferred upon the FSA may be exercised.

Under the Integrated Prudential Sourcebook, an authorized person carrying on insurance business must hold capital resources equal at least to the Minimum Capital Requirement (the "MCR"). Insurers with with-profits liabilities of more than £500 million must hold capital equal to the higher of MCR and the Enhanced Capital Requirement (the "ECR"). The ECR is intended to provide a more risk responsive and "realistic" measure of a with-profits insurer's capital requirements, whereas the MCR is broadly speaking equivalent to the previous required minimum margin under the Interim Prudential Sourcebook and satisfies the minimum EU standards.

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

(i) the requirement comprised by the mathematical reserves plus the sum of the "Long Term Insurance Capital Requirement" (the "LTICR") and the resilience capital requirement, together known as the "regulatory peak"; and

(ii) a calculation of the "realistic" present value of the insurer's expected future contractual liabilities together with projected "fair" discretionary bonuses to policyholders, plus a risk capital margin, together known as the "realistic peak".

The LTICR is made up of several components, but in general is equal to approximately 4 per cent of the mathematical reserves, although the formula varies according to the type of business written. The resilience capital requirement is in respect of the potential effects of market risk. If the calculation of the realistic peak produces a requirement in excess of the regulatory peak, then the difference is known as the with-profits insurance capital component.

Actuarial functions

The rules in the FSA's Supervision Manual require that every insurance company that carries on long-term business must appoint one or more actuaries to perform the "actuarial function" in respect of all classes of its long-term insurance business and, if it has any with-profits business, the "with-profits actuary function" in respect of all classes of that with-profits business.

The actuary performing the "actuarial function" must prepare an annual report for the company's directors quantifying the company's long-term liabilities attributable to the insurance company's long-term insurance business, determining the value of any excess over those liabilities of the assets representing the long-term insurance fund and where any rights of long-term policyholders to participate in profits relate to particular parts of such a fund, a valuation of any excess of assets over liabilities in respect of each of those parts.

The actuary performing the "with-profits actuary function" must advise the firm's management, at the level of seniority that is reasonably appropriate, on key aspects of the discretion to be exercised affecting those classes of the with-profits business of the firm in respect of which he has been appointed. He must also, at least once a year, in respect of each financial year commencing on or after January 1, 2005, report to the firm's governing body on key aspects (including those aspects of the firm's application of its Principles and Practices of Financial Management on which the advice described has been given) of the discretion exercised in respect of the period covered by his report affecting those classes of with-profits business of the firm.

Distribution of Profits and With-profits Business

The Interim Prudential Sourcebook provides that, once an allocation of surplus in a with-profits fund has been made to policyholders, no transfer of assets representing any part of a subsequent surplus can be made, to shareholders or otherwise, unless either the "relevant minimum" (as defined in the Interim Prudential Sourcebook) of the surplus has been allocated to policyholders or a statutory notification procedure has been followed. Calculation of the relevant minimum is based upon the percentage of the relevant surplus previously allocated to eligible policyholders.

Under the Interim Prudential Sourcebook, an insurance company is prohibited from declaring dividends in circumstances where the value of the long-term insurance business assets is less than the amount of the long-term insurance business liabilities. While its parent is not subject to the same restriction, HM Treasury however is given power under the 2000 Act to make regulations preventing an insurance company's parent from doing anything to lessen the effectiveness of any "asset identification rules" made by the FSA, which will include in this context rules requiring insurers to maintain the solvency of the long-term fund.

There has been considerable public debate regarding the rights and legitimate expectations of with-profits policyholders to assets forming part of an insurance company's surplus, particularly where such assets do not derive from the payment of current policyholders' premiums but are rather "inherited" from previous generations of policyholders or from other entities.

The FSA also mandated that firms carrying on with-profits business must:

- define and make publicly available the Principles and Practices of Financial Management (the "PPFM") applied in their management of with-profits funds,
- ensure their governance arrangements offer assurance that they have managed their funds in line with the PPFM they have established and published,
- produce annual reports for with-profits policyholders on how they have complied with this obligation, including how they have addressed any competing or conflicting rights, interests or expectations of policyholders and, if applicable, shareholders,

comply with (i) modified regulatory reporting requirements designed to achieve the FSA's objective of making directors and senior management more explicitly responsible for setting up technical provisions and other decisions taken on actuarial advice and (ii) new audit requirements for liabilities, and

comply with consequential changes to certification in the insurance returns.

Since April 1, 2004, firms carrying on with-profits business have been required to produce PPFM and to make them publicly available. From the same date, firms have also been required to have in place the relevant governance arrangements and reporting procedures to with-profits policyholders.

Treating Customers Fairly and with-profits business

One of the areas of focus of FSA's Treating Customers Fairly work has been the with-profit business. The FSA published Policy Statement 05/01, which contained a set of specific rules on this area in relation to with-profits policyholders.

The new rules became fully effective in December 2005. They address, among other things, the costs charged to a with-profits fund by the firm managing the fund; penalties and charges levied on policyholders who surrender their policies early, the need for funds to be managed with the objective of ensuring that maturity payouts fall within a target range set for the fund; and the provision of information to with-profits policyholders or potential policyholders in a format that they can more readily understand through the introduction of "Consumer Friendly Principles and Practices of Financial Management" (CFPPFMs).

In addition, life insurers writing with-profits business must provide information to with-profits policyholders within 28 working days of a decision to close a fund to new business or of the appointment of a policyholder advocate to protect the interest of policyholders should a firm decide to make a reattribution of its inherited estate.

Reporting Requirements

Under the Interim Prudential Sourcebook, insurance companies must file with the FSA their audited annual accounts and balance sheets and life insurers' annual reports from the actuary performing the actuarial function.

The FSA began consultation in 2002 on the use of implicit items to form part of an insurer's capital resources, and has now produced rules and guidance in the Integrated Prudential Sourcebook to indicate that the FSA will not permit implicit items to be included in the calculation of a firm's capital resources, except where the firm in question has obtained a formal waiver of the rules under the 2000 Act. The guidance notes that certain implicit items are not eligible for inclusion beyond December 31, 2009.

Transfer of Insurance Business

Before any transfer of insurance business may take place, the 2000 Act requires a scheme of transfer to be prepared and approved by the High Court.

Winding-Up Rules

The general insolvency laws applicable to UK companies are modified in certain respects in relation to insurance companies. Since the introduction of the Financial Services and Markets Act 2000 (Administration Orders Relating to Insurers) Order 2002 (the "2002 Order"), which came into force in May 2002, insurance companies in the UK have become subject to the administration procedures contained in Part II of the Insolvency Act 1986 (which previously did not apply). These administration procedures have, however, also been slightly modified by the 2002 Order in relation to, for example, the power of an administrator to make any payments due to a creditor.

Additionally, in the United Kingdom, all FSA authorized insurance companies, except for pure reinsurers, are subject to the Insurers (Reorganisation and Winding-up) Regulations 2004, which came into force in February 2004.

These Regulations provide, among other things, that direct insurance claims will have priority over the claims of other unsecured creditors, including reinsurance creditors, on a winding-up by the court or a creditors' voluntary winding up of the insurance company. Furthermore, instead of making a winding-up order when an insurance company has been proved unable to pay its debts, a UK court may, under Section 377 of the 2000 Act, reduce the amount of one or more of the insurance company's contracts on terms and subject to conditions (if any) which the court considers fit. Where an insurance company is in financial difficulties but not in liquidation, the Financial Services Compensation Scheme may take measures for securing the transfer of all or part of the business to another insurance company.

Section 376 of the 2000 Act provides further insolvency protection to policyholders of insurance companies effecting or carrying out contracts of long-term insurance. Unless the court orders otherwise, a liquidator must carry on the insurer's business so far as it consists of carrying out the insurer's contracts of long-term insurance with a view to it being transferred as a going concern to a person who may lawfully carry out those contracts. In carrying on the business, the liquidator may agree to the variation of any contracts of insurance in existence when the winding-up order is made, but must not effect any new contracts of insurance.

EU Directive on Group Supervision

The European Union formally adopted Directive 98/78/EC on the supplementary supervision of insurance undertakings within a group (the "Insurance Groups Directive") in October 1998. The Insurance Groups Directive required member states to introduce the following measures to strengthen supervision of insurance companies, which are part of a group:

- an adjustment to the solo-supervision solvency calculation in relation to participating interests in other insurance undertakings in order to eliminate "double-gearing" (the use of the same regulatory capital in more than one entity of a group),

- an additional parent undertaking solvency margin calculation analogous to the adjusted solo solvency margin test referred to above, to be applied at the level of the parent undertaking,

- the introduction of new solo-supervision requirements, including rules as to internal control within the insurance undertaking regarding the production of information relevant to supplementary supervision, the exchange of information within the group and the supervision of intra-group transactions, and

- further provisions aimed at ensuring co-operation between competent regulatory authorities of member states.

These requirements have been implemented in the UK by the Insurer's Interim Prudential Sourcebook and the Integrated Prudential Sourcebook.

The parent undertaking solvency calculation under the rules that implement the requirements of the Insurance Group Directive is filed with the FSA and differs from the adjusted solo solvency margin test in that it is currently only a calculation rather than a formal test. However, insurers will be required under the rules in the Integrated Prudential Sourcebook from December 31, 2006 to ensure that the group capital resources of the each undertaking included in the parent undertaking solvency calculation are equal to or exceed the group capital resources requirement for that undertaking.

EU Directive on Financial Conglomerates

In November 2002, the European Union formally adopted Directive 2002/87/EC the Financial Conglomerates Directive which applies to groups that include regulated entities which are active in the banking/investment services sectors and the insurance sector, and which meet certain criteria. The Financial Conglomerates Directive, as implemented in the UK through the Integrated Prudential Sourcebook, came into force for those firms and groups affected (which for the time being includes Prudential) from financial years beginning on or after January 1, 2005. The aim of the Financial Conglomerates Directive is to impose additional prudential requirements in respect of regulated entities within financial conglomerates including, to a certain extent, any mixed financial holding company. The additional supervision is organized at the level of the financial conglomerate and covers capital adequacy, risk concentration and intra-group transactions.

The Financial Conglomerates Directive requires European financial services groups, including Prudential, to maintain on a continuous basis net aggregate surplus capital in excess of solvency requirements at the Group level. The Financial Conglomerates Directive requires a continuous parent company solvency test which requires the aggregating of surplus capital held in the regulated subsidiaries, from which group borrowings are deducted, other than those subordinated debt issues which qualify as capital. The test is passed when this aggregate number is positive. A negative result at any point in time is a notifiable breach of UK regulatory requirements. Since December 31, 2005, the FSA requires public disclosure of the Financial Conglomerates Directive solvency position.

New EU Rules on Solvency Margins

In addition to the solvency requirements of the Insurance Groups Directive and Financial Groups Directive, under rules amending the solvency margin requirements for life and non-life insurance undertakings, which have been implemented in EU member states in 2004 (the FSA's new rules in this respect apply to firms from the beginning of their 2004 financial years), each UK insurer must maintain capital resources (shareholders' equity and quasi-equity) at a level that depends on the nature of the insurer's activity and that is calculated with reference to certain balance sheet and income statement items, subject to an absolute minimum (so-called minimum guaranteed fund) of €3 million (€2 million for some classes of non-life insurance). The rules are part of the European Commission's efforts to achieve a single European market for financial services. These rules were introduced by the Solvency I Directives (2002/12/EC and 2002/13/EC). They were fully implemented in the United Kingdom in January 1, 2005 and make up part of the FSA's Integrated Prudential Sourcebook. The rules also give regulators greater powers to intervene in the event of concerns regarding an insurance company's financial position.

The European Commission continues to work on a more comprehensive review of solvency requirements for insurance undertakings, the so-called "Solvency II" project, which will be based on a three-pillar structure, comprised of capital requirements, supervisory review and public disclosure. Although the final form of the Directive is yet to established, and there can be no certainty of its impact on solvency requirements, it is expected that the new solvency rules will be based on two levels of regulatory capital requirements for insurers: a solvency capital requirement, which is expected to adopt a more risk-based approach along the lines introduced in the United Kingdom through the Integrated Prudential Sourcebook and will be aimed at reflecting and quantifying the exposure of the relevant insurance undertaking, and a minimum capital requirement, which will be computed in a less refined manner and which would act as trigger for supervisory intervention. The European Commission Roadmap (published in July 2005) forsees the adoption of a Framework Directive around July 2007.

Other EU Measures

In May 2003, the European Union adopted Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision, which member states were required to implement into their national law by September 2005. This Directive is intended to permit employee pension schemes to be operated and managed on an EU-wide basis. The Directive contains certain prudential rules and "prudent person" investment requirements, which could be extended by member states to the occupational retirement schemes operated by life insurance companies. This was achieved in the United Kingdom with the enactment of the Pensions Act in 2004 and the subsequent adoption of various regulations, relating to occupational pension schemes.

On October 16, 2005, the European Union adopted Directive 2005/68/EC ("Reinsurance Directive"), which establishes a regulatory framework for reinsurance activities in the European Union. The Reinsurance Directive lays down the minimum necessary conditions to obtain official authorization for reinsurance activities. These conditions stipulate that undertakings must have a specific legal form, submit a scheme of operations and hold a minimum guarantee fund. Member States must implement the Reinsurance Directive into their national law by December 2006.

Regulation of Investment Business

Certain of Prudential's subsidiaries are authorized by the FSA to carry on investment business. These entities are subject to regulation and supervision by the FSA and must comply with the FSA Conduct of Business Rules and all other applicable rules prescribed by the 2000 Act regime.

EU Markets in Financial Instruments Directive (MiFID)

As indicated under 'Conduct of Business rules' above, the UK along with other EU member states will soon start implementing the MiFID. This directive will replace the Investment Services Directive and is relevant to all firms conducting 'investment business', which includes activities such as dealing, arranging and advising on 'investments'. 'Investments' in this context exclude contracts of insurance.

The MiFID has two main purposes:

1. Enhance firms' ability to 'passport' their activities through the addition of 'providing investment advice' as a core 'passportable' activity. This means that firms may do pan-EU business on a cross-border basis or through branches established in other member-states without having to become authorized in the target country.

2. Harmonize requirements in relation to, for example, governance, systems and controls and conduct of business for all firms affected by the MiFID.

The MiFID must be implemented by member-states by November 1, 2007 and FSA is now engaged in a consultation process regarding necessary changes to its Handbook. Although insurance companies and some investment firms are not within the scope of the MiFID, it may be expected that the FSA may seek to apply the 'MiFID style' provision across all firms where consistency is desirable.

Regulation of mortgage lending, sales and administration and general insurance mediation

Mortgage lending, sales and administration as well as long-term care insurance became activities regulated under the 2000 Act on October 31, 2004, for which authorization by the FSA is now required. General insurance sales and administration became activities regulated under the 2000 Act on January 14, 2005, for which authorization by the FSA is now required.

Regulation of Banking Business

The FSA has sole responsibility for banking supervision and regulation in the United Kingdom and has wide discretionary powers in relation to those banks it regulates. The FSA has wide investigatory and enforcement powers, including the power to require information and documents from banks, appoint investigators, apply to the court for injunctions in cases of breaches or likely breaches of rules, impose financial penalties, issue a public statement or censure and vary, cancel or withdraw authorization to carry on banking business.

Supervision

In its role as supervisor of banks, the primary objective of the FSA is to fulfill its responsibilities under the 2000 Act regime relating to the safety and soundness of banks with the aim of strengthening, but not guaranteeing, the protection of depositors. The FSA has adopted a risk-based approach to bank supervision.

The FSA requires Egg Banking plc to maintain a certain minimum capital adequacy ratio of total capital to risk-weighted assets and to provide supervisory reports on capital adequacy and on large exposures. There is also a requirement to provide consolidated supervisory reports for capital adequacy and large exposures for the parent of the banking group (Egg). The Interim Prudential Sourcebook for Banks, on a general level, requires banks operating in the United Kingdom to maintain adequate liquidity, taking into account the nature and scale of their business so that they are able to conduct business in a prudent manner and meet their obligations as they fall due. As part of its supervision, the FSA requires the banks subject to its supervision to provide it with information that the FSA may reasonably require to perform its functions under the 2000 Act regime.

Solvency Requirements

The requirement to have adequate financial resources is one of the criteria for permission to accept deposits under the 2000 Act. A bank should have sufficient capital to provide a stable resource to absorb any losses arising from the risks in its business. In assessing a bank's capital adequacy, the FSA takes into account not only the level of a bank's own funds but also other matters such as concentration of the loan book (large exposures) and liquidity.

The FSA applies capital adequacy rules and guidelines that accord with relevant EC Directives and which are based on the Basel Accord of 1988, which established a framework for measuring the capital adequacy of international banking organizations. These rules and guidelines implement the requirements of the Banking Consolidation Directive and the Capital Adequacy Directive ('CAD'), as amended, which require credit institutions and investment firms to provide capital for counterparty risk and market risk. The FSA's rules and guidelines impose on banks a requirement that they maintain a minimum level of capital to support on and off-balance sheet exposures, weighted according to broad categories of risk. Each bank is subject to the FSA's rules and guidelines and must maintain a required capital adequacy ratio (the Internal Capital Ratio ('ICR')) of total capital to risk-weighted assets. This ratio is set by the FSA individually for each such bank, but the ratio is in no case less than 8 per cent. Egg's and Egg Banking's ICRs are 11 per cent.

The FSA introduced a new market risk regime as from October 1, 1998 for implementation of its policy based on the Basel Accord and the parallel EC Market Risk Directive, known as the "CAD Amending Directive". Both the 1996 Basel Amendment to the Basel Accord and the CAD Amending Directive enable banks and investment firms to use internal value-at-risk models to calculate capital charges for market risks.

Banks that have a trading book over a certain size are obliged to meet the trading book capital requirements of the CAD and the CAD Amending Directive in respect of the market-related and credit-related risks arising from their proprietary trading activities. This involves splitting their business between trading and banking books.

Most UK banks are required to maintain, in non-interest-bearing accounts at the Bank of England, a cash balance, known as the cash ratio deposit, which is based on eligible liabilities, primarily pound sterling deposits less amounts on loan to other monetary institutions. Although these balances count towards the liquidity requirements for the real time gross settlement system introduced in the United Kingdom during 1996, they are generally regarded as non-operational and, accordingly, do not count towards overall liquidity requirements. The liquidity standard for sterling, which the UK government introduced in January 1996, requires the maintenance of sufficient holdings of liquid assets to cover potential cash outflows over the next five business days. This policy applies to UK-incorporated retail banks and group UK-based sterling operations.

The Basel Committee on Banking Supervision published a new accord in June 2004 which will replace the Basel Accord of 1988. Basel II consists of three "pillars": minimum capital, a supervisory review of an institution's capital adequacy and internal assessment process and market discipline to strengthen disclosure. With respect to the first pillar, the new capital framework will not merely expand and develop the standardized rules set out in the 1988 Accord, but will allow banks to compute their capital charges for credit risk on the basis of their own internal ratings, subject to rigorous quantitative and qualitative criteria. Egg will apply the principles of Basel I and Basel II from January 1, 2007, and transfer to Basel II from January 1, 2008.

In June 2006, The European Union adopted the Capital Requirements Directive for credit institutions and investment funds ("Capital Requirements Directive"), which it had proposed on July 14, 2004. The Capital Requirements Directive technically recast two existing Directives The Banking Consolidation Directive and the Capital Adequacy Directive and introduces a supervisory framework in the European Union, which reflects the Basel II Rules on capital measurement and capital standards, and similarly contains minimum capital requirements, supervisory review, and disclosure as an aid to market discipline.

The FSA published in January 2005 Consultation Paper 05/03 on the implementation of the New Basel Capital Accord and the EC Capital Requirements Directive ('CRD'). The main proposals in the Consultation Paper are:

- Greater flexibility in the application of consolidation techniques including a new regime for integrated groups;
- Greater harmonization of the definition of capital for banks, building societies and investment firms;
- Introduction of individual capital adequacy standards and a new capital adequacy assessment process;
- Detailed guidance on the Internal Ratings Based approach to Credit Risk ('IRB') model validation process;
- Extension of credit risk mitigation techniques recognized by the FSA; and
- Treatment of the outsourcing of operational risk.

Regulatory developments

In February 2006, the FSA issued a new consultation paper CP06/03. This paper builds on FSA's CP05/03 to develop proposals in the areas of:

- Economic cycle stress testing, where banks will be expected to stress test for a potential recession of the severity that might be expected once every 25 years; and
- Diversification benefits, where banks will receive a capital benefit under pillar 2 of the diversification of their business.

The paper also gives clear guidance on the FSA's view on IRB and Advanced Measurement Approaches ('AMA') waiver applications, where they will expect applicants to have made sufficient progress in areas of governance under the pillar 2 Internal Capital Adequacy Assessment Process ('ICAAP') process.

With regard to implementation of the CRD, the FSA stated in CP06/03 that it will come into force on January 1, 2007, while those firms wishing to apply the advanced approaches will be able to do so from January 1, 2008.

US Supervision and Regulation

General

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

Insurance regulatory authorities in each of the jurisdictions in which Jackson National Life does business require it to file detailed quarterly and annual financial statements and these authorities have the right to examine its operations and accounts. In addition, Jackson National Life is generally subject to federal and state laws and regulations that affect the conduct of its business. New York and Michigan require their state insurance authorities to conduct an examination of an insurer under their jurisdiction at least once every five years. The New York insurance authorities conducted an examination of Jackson National Life of New York in 2003 for the examination period of January 1, 2000 through December 31, 2002 and the examination report included no material findings. The New York insurance authorities informed Jackson National Life of New York that an examination will commence in the fall of 2006 covering the period of January 1, 2003 through December 31, 2005. Michigan insurance authorities are currently performing a routine examination of Jackson National Life for the period ending December 31, 2004. The examination is substantially complete and no material findings have been identified to date. Michigan insurance authorities previously conducted an examination of Jackson National Life during the year 2001 for the period ending December 31, 2000 and the examination report included no material findings.

Jackson National Life's ability to pay shareholder dividends is limited under Michigan insurance law. The Commissioner of the Michigan Office of Financial and Insurance Services (the "Michigan Insurance Commissioner") may limit, or not permit, the payment of shareholder dividends if the Michigan Insurance Commissioner determines that an insurer's surplus, as regards policyholders, is not reasonable in relation to its outstanding liabilities and is not adequate to meet its financial needs as required by Michigan insurance law. Jackson National Life must report any shareholder dividends to the Michigan Insurance Commissioner before they can be paid. In the case of an extraordinary shareholder dividend or distribution, an insurer must give 30 days advance notice to the Michigan Insurance Commissioner and may not pay the dividend or distribution if the Michigan Insurance Commissioner disapproves within such 30-day period. For this purpose, an extraordinary dividend or distribution means any dividend or distribution of cash or other property whose fair market value together with that of other dividends or distributions that an insurer made within the preceding twelve months exceeds the greater of 10 per cent of the insurer's surplus as regards policyholders as of December 31 of the immediately preceding year, or the net gain from operations of the insurer, not including realized capital gains, for the prior year. In 2003, 2004 and 2005, Jackson National Life paid shareholder dividends of $85.2 million, $120.0 million, and $410.8 million, respectively.

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

Guaranty Associations and Similar Arrangements

Each of the 50 states of the United States, the District of Columbia and the Commonwealth of Puerto Rico have laws requiring insurance companies doing business within their jurisdictions to participate in various types of guaranty associations or other similar arrangements. These associations and arrangements provide certain levels of protection to policyholders from losses under insurance policies issued by insurance companies that became impaired or insolvent. Typically, these associations levy assessments, up to prescribed limits, on member insurers on a basis that is related to the member insurer's proportionate share of the business in the relevant jurisdiction of all member insurers in the lines of business in which the impaired or insolvent insurer is engaged. Some jurisdictions permit member insurers to recover assessments that they paid through full or partial premium tax offsets, usually over a period of years. Prudential estimated its reserve for future guarantee fund assessments for Jackson National Life to be £11.2 million ($19.3 million) at December 31, 2005. Prudential believes this reserve to be adequate for all anticipated payments for known insolvencies.

Asset Valuation Reserve

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

Interest Maintenance Reserve

State regulators generally require that insurers establish an interest maintenance reserve to defer non-credit-related realized capital gains and losses, net of taxes, on fixed income investments (primarily bonds and mortgage loans) which are amortized into net income over the estimated remaining periods to maturity of the investments sold and to defer material gains or losses, net of taxes, resulting from market value adjustments on policies and contracts backed by assets carried at book value. The extent of the impact of the interest maintenance reserve on earnings and surplus depends on the amount of future interest-rate related realized capital gains and losses on fixed maturity investments and deferred gains or losses resulting from market value adjustments on policies and contracts backed by assets that are valued at book/adjusted carrying value.

The National Association of Insurance Commissioners Ratios

On the basis of statutory financial statements that insurers file with state insurance regulators, the National Association of Insurance Commissioners annually calculates twelve financial ratios to assist state regulators in monitoring the financial condition of insurance companies. A usual range of results for each ratio is used as a benchmark and departure from the usual range on four or more of the ratios can lead to inquiries from individual state insurance departments. In 2005, all of Jackson National Life's ratios fell within the usual range.

Policy and Contract Reserve Sufficiency Analysis

Michigan insurance law requires Jackson National Life to conduct annually an analysis of the sufficiency of its life and annuity reserves. A qualified actuary must submit to the insurance department an opinion that states that the reserves, when considered in the light of the assets that an insurance company holds with respect to such reserves, make good and sufficient provision for the associated contractual obligations and related expenses of the insurance company. If a qualified actuary cannot provide such an opinion, then the insurance company must set up additional reserves by moving funds from unassigned surplus. The 2005 opinion has been submitted to the Michigan Office of Financial and Insurance Services without any qualifications.

Jackson National Life's Capital and Surplus

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

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

Risk-based Capital

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

Any state adopting the model act gives the state insurance commissioner explicit regulatory authority to require various actions by, or take various actions against, insurance companies whose adjusted capital does not meet minimum risk-based capital standards. The Michigan Insurance Commissioner takes into account the National Association of Insurance Commissioners' risk-based capital standards to determine adequate compliance with Michigan insurance law. Effective December 31, 2005, the National Association of Insurance Commissioners implemented new requirements, referred to as C-3

Phase II, for calculating risk based capital in connection with variable annuity products with death and living benefit guarantees. These changes did not have a material effect on Jackson National Life Insurance Company, and at December 31, 2005, the Company's total adjusted capital under the National Association of Insurance Commissioners' definition substantially exceeded Michigan standards.

Regulation of Investments

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

USA Patriot Act

In 2001, the US Congress enacted the USA Patriot Act, which includes numerous provisions designed to fight international money laundering and to block terrorist access to the US financial system. The US Treasury Department has issued a number of regulations implementing the USA Patriot Act that apply certain of its requirements to financial institutions including broker-dealers and insurance companies. Among other things, the regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Jackson National Life as well as other Prudential subsidiaries, to the extent necessary and appropriate, have established policies and procedures to ensure compliance with the USA Patriot Act's provisions and the Treasury Department regulations.

Securities Laws

Jackson National Life, certain of its affiliates and certain policies and contracts that Jackson National Life offers are subject to various levels of regulation under the federal securities laws administered by the US Securities and Exchange Commission (the "SEC").

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

Jackson National Asset Management, LLC is registered with the SEC as an investment advisor pursuant to the Investment Advisors Act of 1940, as amended ("Investment Advisors Act of 1940"), and is also registered by notice filed in all applicable states. Jackson National Asset Management, LLC is registered as a transfer agent pursuant to the Securities Exchange Act of 1934, as amended ("Securities Exchange Act"). The investment companies (mutual funds) for which Jackson National Asset Management, LLC serves as an investment advisor are subject to SEC registration and regulation pursuant to the Securities Act of 1933, as amended ("Securities Act"), and the Investment Company Act of 1940, as amended ("Investment Company Act"). In addition, each variable annuity and variable life product sponsored by Jackson National Life is subject to SEC registration and regulation pursuant to the Securities Act and the Investment Company Act, and applicable state insurance and securities laws. Each variable annuity and variable life product is offered through a separate account that is a unit investment trust under the Investment Company Act.

Curian Capital, LLC is registered with the SEC pursuant to the Investment Advisors Act of 1940 and is also registered or notice filed in all applicable states.

BH Clearing, LLC is registered as a broker-dealer with the SEC pursuant to the Securities Exchange Act, and is registered as a broker-dealer in all applicable states. In addition, BH Clearing, LLC is a member firm of the National Association of Securities Dealers (the "NASD").

Jackson National Life Distributors, Inc. is registered as a broker-dealer with the SEC pursuant to the Securities Exchange Act, and is registered as a broker-dealer in all applicable states. In addition, Jackson National Life Distributors, Inc. is a member firm of the NASD.

Each of SII Investments, Inc., National Planning Corporation, Investment Centers of America, Inc., and IFC Holdings, Inc. (which does business under the name INVEST Financial Corporation), is a broker-dealer, investment advisor, and insurance agency (or affiliated with an insurance agency), licensed and qualified to transact business pursuant to its respective registration and/or membership with the SEC, the NASD, the Municipal Securities Rulemaking Board, applicable state securities and insurance authorities, and all other applicable jurisdictional authorities.

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

PPM America, Inc. and certain of its subsidiaries are subject to various levels of regulation under the federal securities laws that the SEC administers as well as state securities laws.

To the extent that PPM America, Inc. manages assets of employee benefit plans subject to the Employee Retirement Income Security Act of 1974 ("ERISA"), or the Internal Revenue Code, it may be subject to certain restrictions imposed by ERISA and taxes imposed by the Internal Revenue Code. The Department of Labor and the Internal Revenue Service have interpretive and enforcement authority over the applicable provisions of ERISA and the Internal Revenue Code.

Financial Services Regulatory and Legislative Issues

Proposals to change the laws and regulations governing the financial institutions industry are frequently introduced in the US Congress, in the state legislatures and before the various regulatory agencies. The likelihood and timing of any proposals or legislation and the impact they might have on Jackson National Life and its subsidiaries cannot be determined at this time.

State legislatures and/or state insurance regulatory authorities frequently enact laws and/or regulations that significantly affect insurers supervised by such authorities. Although the US federal government does not directly regulate the insurance business, federal initiatives may also have an impact on the insurance industry.

A major issue at the state level involves the Insurance Product Regulation Compact (the "Compact"), which (as of May 23, 2006) has already been adopted by 26 of the 50 states and is being actively considered in a number of other state legislatures. The Compact was developed by the National Association of Insurance Commissioners to serve as an agreement among member states to create a more streamlined system of insurance product regulation. A principal component of the Compact is the creation of a multi-state commission governed by participating states. It is contemplated that the commission would serve as a single point of filing for life insurance and annuity products, and would establish uniform, national standards for those products. The Compact commission has started to consider organizational issues such as bylaws and governing rules in anticipation of the Compact's implementation. It is anticipated that the Compact will become operational once such issues have been addressed.

In recent years, the US President, Treasury Department and / or members of Congress have, from time to time, proposed to increase the taxes levied against the insurance industry to increase the federal budget revenues. The industry has been very successful in resisting these proposals on the grounds that an increase in taxes on insurance companies or insurance policies would have a negative effect on US citizens saving for their retirement. The insurance industry is very vigilant in monitoring these proposals and taking action to oppose them, as well as to support proposals that would provide more favorable tax treatment for certain annuity products.

The governor of Michigan has recently proposed to increase the state tax assessed on insurance companies' premiums. This proposal was actively considered by the state legislature and was not acted upon favorably. It does not appear that a material tax increase on insurance company premiums will be enacted as Michigan law in the near future.

Proposed US federal legislation, the State Modernization and Regulatory Framework (the "SMART Act"), intended to streamline and modernize the state insurance regulatory framework has garnered some Congressional support. The SMART Act would require states to comply with uniform standards and resolve disputes, speed up the process of getting new products to the market and move toward a system of market-based rates, without creating a federal regulator to monitor compliance. A coalition of national insurance and banking organizations has supported the recent introduction of US federal legislation that would allow insurance companies to obtain a federal charter as a regulatory alternative to a state charter. Under legislation (S.5095) introduced in April 2006, insurers with a federal charter would be permitted to do business in any state without the need for any additional license(s). Under the proposals so called "national insurers" would be subject to the regulation of the US Treasury Department. Prudential cannot predict whether any federal (or state) legislative initiative to change the nature or scope of the regulation of the insurance industry will be enacted into law.

Federal and state regulators have focused on, and continue to devote substantial attention to, the mutual fund and variable annuity and insurance product industries including the broker-dealer system. As a result of publicity over the past few years relating to widespread perceptions of industry abuses, including fraudulent and anticompetitive practices among insurance brokers and mutual funds, there have been numerous regulatory inquiries and proposals for legislative and regulatory reforms. In addition, the Attorney General of New York State and the New York State Insurance Department have recently launched an investigation into alleged fraud and bid rigging in the insurance industry and have compelled certain insurance companies to adopt reforms in their business practices. Jackson National Life has not, to our knowledge, been a target in the ongoing probe. It is difficult to predict at this time whether changes resulting from industry investigations and/or new laws and regulations will affect our insurance or investment management businesses, and, if so, to what degree.

Asian Supervision and Regulation

Prudential's businesses in Asia are subject to relevant local regulatory and supervisory schemes. These laws and regulations vary from country to country, but the regulators typically grant (or revoke) licenses and therefore control the ability to operate a business.

The industry regulations are usually widely drawn and will include provisions governing both financial matters and the way business is conducted in general. Examples include the registration of agents, the approval of products, asset allocation, minimum capital and the basis for calculating the company's solvency and reserves and the valuation of policyholder liabilities. Regulatory authorities may also regulate affiliations with other financial institutions, shareholder structures and the injection of capital and payment of dividends. Financial statements and other returns are filed with the regulators. The regulators may also conduct physical inspections of the operations from time to time.

A number of Asian countries require insurance companies to participate in policyholder protection schemes (i.e., contribute to a fund to support policyholders in the event of an insurance company failing).

To date Prudential Corporation Asia has had no regulatory issues giving rise to a material impact on its results.

For Prudential Corporation Asia's more material operations the details of the regulatory regimes are as follows:

Hong Kong

The Insurance Companies Ordinance ("ICO") empowers a Commissioner of Insurance to establish an office for the administration of the industry including approvals for a company to conduct insurance business.

The Hong Kong branch of Prudential Assurance is authorized to carry on both long-term business and general business under a composite license.

Japan

The Financial Services Agency of Japan ("JFSA") regulates insurance companies and other financial institutions. The Insurance Business Division of the JFSA specifically undertakes the supervision of insurance companies. The fundamental principles of insurance regulation are set out in the Insurance Business Law.

PCA Life Japan is licensed by and registered with the JFSA as a life insurance company.

Korea

The Ministry of Finance and Economy of Korea set the insurance law after consultation with the Financial Supervisory Commission ("FSC"). The FSC's responsibilities include regulation of the insurance industry but it delegates to the Financial Supervisory Services ("FSS") work such as supervision, examination and direct contact with insurance companies. The detailed rules under the supervisory regulation are prepared by the FSS.

PCA Life Korea is licensed by and registered with the FSC as a life insurance company.

Singapore

The Monetary Authority of Singapore ("MAS") is responsible for insurance company regulation and supervision. In order to sell insurance in Singapore, companies need to be licensed by the MAS.

Prudential Assurance Company Singapore is registered and licensed to manufacture and sell both life and general insurance business.

Taiwan

The Taiwanese Ministry of Finance ("MOF") is responsible for approving a company's participation in insurance activities and for regulating and supervising authorized insurers.

PCA Life Taiwan operation is licensed for life insurance business.

Malaysia

In Malaysia, Bank Negara is the regulatory body responsible for supervising and regulating the conduct of financial services including insurance business.

All insurance companies must be licensed with the Ministry of Finance. In addition, they are required to be a member of the Life Insurance Association of Malaysia and/or General Insurance Association of Malaysia.

Prudential Assurance Malaysia Berhad has a license for both life and general insurance business.

China

Historically, the People's Bank of China was responsible for the supervision of the insurance industry but in October 1998, a new authority, China Insurance Regulatory Commission ("CIRC") was formed.

Consistent with WTO requirements, geographic restrictions on foreign players have been eased as of December 2004, however, entry into any new province still requires approval by CIRC. Within a province the China Insurance Regulatory Bureau ("CIRB") manage all insurance regulatory matters on behalf of CIRC including foreign companies' application for sales office licenses within the provinces where they are already operating.

India

Insurance is subject to federal regulation in India. The primary legislation is the Insurance Act, 1938, and the Insurance Regulatory & Development Authority Act, 1999 ("IRDA").

The IRDA's duties include issue of certificates of registration to insurance companies and it has a mandate to protect the interests of the policy holders

Indonesia

The Indonesian insurance industry is regulated by the Insurance Directorate of the Ministry of Finance.

The anomaly in the country's bankruptcy rules that allowed insurance companies to be declared bankrupt via the commercial courts rather than by the Ministry of Finance has recently been overturned.

Future Regulatory Development

Prudential Corporation Asia expects the regulatory regimes in Asia to continue to develop, potentially driven by, for example, consumers requiring greater degrees of product transparency and more sophisticated advice. Regulators may introduce new legislation and hence there is a risk past sales may be assessed against new compliance requirements and investment conditions. Given the size of Prudential Corporation Asia's agency force, the introduction of more complex regulation may increase the risk of compliance issues in the future.

Item 4A. Unresolved staff comments

None.

Item 5. Operating and Financial Review and Prospects

OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion and analysis should be read in conjunction with Prudential's consolidated financial statements and the related notes to Prudential's consolidated financial statements included elsewhere in this document. Prudential's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), which differs in certain material respects from US GAAP. Information related to the nature and affect of such differences is presented in Sections J and K of the notes to the consolidated financial statements in this document. A summary of the critical accounting policies which have been applied to these statements is set forth in the section below entitled " Factors Affecting Results of Operations IFRS Critical Accounting Policies".

The results discussed below are not necessarily indicative of the results to be expected in any future periods. This discussion contains forward-looking statements based on current expectations, which involve risks and uncertainties. Actual results and the timing of certain events may differ significantly from those projected in these forward-looking statements due to a number of factors, including those set forth in the section below entitled " Factors Affecting Results of Operations", in Item 3, "Key Information Risk Factors" and elsewhere in this document.

Introduction

Prudential provides a broad range of financial products and services, primarily to the retail market.

In the UK, following the introduction of the new depolarization rules in December 2004, many financial advisor groups have used the opportunity to establish multi-tie panels. Prudential has worked with major advisor groups to design and build multi tie propositions and Prudential UK has been appointed to the regulated multi-tie panels for Millfield, THINC Destini, Sesame, Bankhall, and Barclays and is strongly positioned to take advantage of the depolarized marketplace as this develops over the next few years.

In October 2004, Prudential launched PruHealth, a UK healthcare product that links health and fitness to the cost of medical insurance. The business has made good progress with sales growing on average more than 30 per cent per month in 2005. Total premium income for the year was £9 million and PruHealth now has over 30,000 covered individuals. The product has been developed through a joint venture with Discovery of South Africa.

In October 2005, Prudential launched Prudential Property Value Release Plan. A life time mortgage product which gives customers greater flexibility and control over the timing of when they draw down funds, thereby reducing total interest charges over the lifetime of the loan. It has been well received by advisors and customers.

At the end of 2005, M&G, Prudential's UK and European fund management business, had £149 billion of funds under management, of which £113 billion relates to Prudential's long-term business funds. M&G operates in markets where it has a leading position and competitive advantage, including retail fund management, institutional fixed income, pooled life and pension funds, property and private finance. M&G also manages Prudential's balance sheet for profit. Prudential believes that M&G has scale in all key asset classes: it is one of the largest active managers in the UK stock market, one of the largest bond investors in the UK and one of the UK's largest property investors.

Egg is an innovative financial services company primarily offering banking products and services, specifically, unsecured personal loans, credit cards, mortgages and savings accounts.

In 2005, licences to sell financial services products in six new cities in China were granted to CITIC-Prudential by the Chinese authorities, bringing the total number of such licences on December 31, 2005 to ten. As of April 30, 2006, CITIC-Prudential had been granted 13 life insurance licences to operate in

China. Prudential believes the main challenge facing foreign players trying to become established in China is the need to develop local management teams to support geographical expansion. Prudential believes that it has a real advantage in being able to leverage its existing Chinese speaking operations to help develop new teams quickly. In 2005, sales in China increased by 47 per cent over 2004.

In June 2005 The Prudential Vietnam Fund Management Company was launched with a mandate to manage the Prudential Vietnam's life fund. It also has plans to develop the emerging retail funds market in Vietnam and to launch retail funds.

Prudential and Bank Simpanan Nasional ('BSN') which was originally the Malaysian Post Office Bank and is now wholly owned by the Ministry of Finance, established a joint venture to leverage Prudential's existing network of over 7,000 agents and BSN's network of 391 branches. In January 2006, the Malaysian authorities granted the joint venture a license to develop and market insurance products to Muslim Malays who make up more than 60 per cent of the population.

In October 2004, JNL completed the sale of JFB to Union Bank of California for £166 million. JFB's principal area of business was banking and commercial real estate lending, which no longer aligned with JNL's strategy. Accordingly, the results of operations for JFB are reported as discontinued operations in the accompanying financial statements.

In November 2004, Prudential announced the purchase of Life Insurance Company of Georgia for £142 million, and completed the purchase in May 2005. This acquisition doubled the number of JNL's in-force life and annuity policies, added scale to its operating platform and expanded its distribution capability. This is enabling JNL to grow its life business at a higher return and faster rate than can be achieved organically. JNL anticipates the capital provided will be returned over a period of about 5 years. The planning for the integration of the business is on track and full integration is anticipated within 12 months of closing the transaction.

In October 2004, the Board decided to launch a 1 for 6 rights offering. As at December 31, 2005, approximately 25 per cent of the net proceeds of the rights offering (£1,021 million) have been used to provide capital to support Prudential's shareholder backed UK life businesses. The remainder of the proceeds have been invested centrally within the Group in short-term financial instruments.

Factors Affecting Results of Operations

Prudential's results of operations are affected, to a greater or lesser degree, by a variety of factors, including demographics, general economic and market conditions, government policy and legislation and regulation, as discussed in greater detail below. See Item 3, "Key Information Risk Factors" for more information on risks associated with these and other factors. In addition, changes to the composition of its businesses and the execution of its growth strategy may result in increased variation in profits from year to year.

General Economic and Market Conditions

Prudential believes that the historical strength of the UK and US equity markets, combined with demographic factors and governmental efforts to increase individual savings and self-provision for retirement, are leading to an increased consumer focus on savings and investment products.

In Asia, Prudential believes the potential for strong economic growth remains and that it is in a strong position to benefit from the long-term growth potential throughout the region. In 2005 Asian economies performed exceptionally well, with strong GDP growth. The composition of demand and economic activity has been shifting recently towards being more domestically driven and Prudential expects this trend to continue, resulting in less dependence on Western economies. Short interest rates are expected to continue to rise slowly as central banks balance normalizing economic policy with containing pressure for currencies to appreciate. Long bond yields are expected to climb from current levels as economic activity broadens and domestic inflation rises. Equity investments will be supported by continued economic growth and the current valuation levels. Overall, it is expected that these factors will continue to encourage investors into long term savings products.

Changes in interest rates and returns from equity, real estate and other investments as well as volatility in these items may affect Prudential's profitability. In the United Kingdom, where Prudential invests in debt and other fixed income securities, equity securities and real estate, shareholders' profits under IFRS are strongly related to the bonuses it declares on with-profits products. The most important influences on the bonus rates are the overall rate of return earned on investments and Prudential's expectation of future investment returns. See " Analysis by Geographic Region United Kingdom Basis of Profits", " With-profits Products" and " Bonus Rates" below. Prudential's bonus policy and its impact on profitability are addressed in more detail in "IFRS Critical Accounting Policies" below.

In the United States, fluctuations in prevailing interest rates, including changes in the difference between the levels of prevailing short-term and long-term rates, can affect results from Jackson National Life, which is predominantly a spread-based business with the majority of its assets invested in fixed income securities. Changes in interest rates, either upward or downward, can expose Jackson National Life to the risk of not earning anticipated spreads between the rate earned on investments and the rate credited on its policies. For example, if interest rates go up and/or competitors offer higher crediting rates, withdrawals on annuity contracts may increase as policyholders seek higher investment returns elsewhere. In response, Jackson National Life could (1) raise its crediting rates to stem withdrawals, decreasing its spread; (2) sell assets which may have depressed values in a high interest rate environment, creating realized investment losses; or (3) pay out existing cash which would otherwise have earned interest at the higher interest rates. Moreover, to the extent that Jackson National Life holds illiquid private placements and commercial mortgages, there is a risk that it will incur losses if it needs to sell those assets. Conversely, if interest rates decrease, withdrawals from annuity contracts may decrease relative to original expectations, creating more cash than expected to be invested at lower rates. Jackson National Life may have the ability to lower the rates it credits to policyholders as a result, but may be forced to maintain crediting rates for competitive reasons or because there are minimum interest rate guarantees in certain contracts. In either case, the spread earned by Jackson National Life would be lowered.

The profitability of Jackson National Life's spread-based businesses depends in large part on its ability to manage interest rate spreads, as well as the credit and other risks inherent in its investment portfolio. There can be no guarantee that these risks will be managed successfully. Prudential designs its US products and manages the investments supporting this business to reduce interest rate sensitivity. This has the effect of moderating the impact on Prudential's results of changes in prevailing interest rates. See Item 11, "Quantitative and Qualitative Disclosures about Market Risk" for a discussion of the management of Prudential's exposure to such market risk.

Government Policy and Legislation

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

Regulation

In recent years, the insurance sectors in the markets in which Prudential operates have seen considerable regulatory change. Failure to comply with local regulation may result in sanctions, which could take the form of a financial penalty. Pension mis-selling is discussed in more detail under Item 4, "Information on the Company Business of Prudential UK Business Shareholders' Interests in Prudential's Long-term Insurance Business Pension Mis-selling". Mortgage endowment mis-selling and regulatory actions taken by the FSA to address the issue are discussed in more detail under Item 4, "Information on the Company Business of Prudential UK Business Shareholders' Interests in Prudential's Long-term Insurance Business Mortgage Endowment Products Review".

Additional regulation, scrutiny and related costs have put pressure on the margins on new business. In the United States, Prudential has been the subject of regulatory sanctions and class actions. These legal proceedings are discussed in more detail under Item 4, "Information on the Company Business of Prudential Legal Proceedings". Changes in pension, financial services and tax regulation could have an impact on Prudential's results. See Item 4, "Information on the Company Supervision and Regulation of Prudential" for a summary of the current regulatory environment in which Prudential conducts its business.

Exchange Rates

Due to the geographical diversity of Prudential's businesses, it is subject to the risk of exchange rate fluctuations. Prudential's international operations in the United States, Asia and Europe, which represent a significant proportion of total group income and expenses, generally write policies and invest in the same local currency, which although limiting the effect of exchange rate fluctuations on local operating results, can lead to fluctuations in Prudential's consolidated financial statements upon translation of results into pounds sterling.

IFRS Critical Accounting Policies

Prudential's discussion and analysis of its financial condition and results of operations are based upon Prudential's consolidated financial statements, which have been prepared in accordance with International Financial Reporting Standards ('IFRS') adopted for use in the European Union ('EU'). Were the Group to apply IFRS as published by the International Accounting Standards Board, as opposed to EU adopted IFRS, no additional adjustments would be required.

The preparation of these financial statements requires Prudential to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, Prudential evaluates its estimates, including those related to long-term business provisioning, the fair value of assets and the declaration of bonus rates. Prudential bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. Prudential believes that its critical accounting policies are limited to those described below. For further details see "US GAAP Analysis US GAAP Critical Accounting Policies" below.

The critical accounting policies in respect of the items discussed below are critical for the group's results in so far as they relate to the group's shareholder financed business, in particular for Jackson National Life (JNL).

Investments

Determining the fair value of unquoted investments

Of the Group's financial investments, assets with a fair value of £4.9 billion are not quoted on active markets. Their fair values are determined in full or in part by using valuation techniques. These techniques include discounted cash flow analysis, option-adjusted spread models and enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments. This impact would, however, be mostly mitigated by an equal and offsetting transfer to the liability for unallocated surplus as the majority of these investments are held by the UK with-profits fund. Further information on these instruments is provided in note G1 to the financial statements.

Determining impairments relating to financial assets

Available-for-sale securities

Financial investments carried on an available-for-sale basis, such as JNL's debt securities portfolio, are considered to be impaired if there has been a significant and prolonged period of decline in fair value below its amortized cost or if there is objective evidence of impairment. The consideration of this requires management's judgement. Among the factors considered is whether the decline in fair value results from a change in quality of the security itself, or from a downward movement in the market as a whole and the likelihood of recovering the carrying value based on the current and short-term prospects of the issuer. Unrealized losses that are considered to be primarily the result of market conditions, such as increasing interest rates, unusual market volatility, or industry-related events, and where the Group also believes there is a reasonable expectation for recovery and, furthermore, it has the intent and ability to hold the investment until maturity or the market recovery, are usually determined to be temporary. Prudential's review of fair value involves several criteria including economic conditions, credit loss experience, other issuer-specific developments and future cash flows. These assessments are based on the best available information at the time. Factors such as market liquidity, the widening of bid/ask spreads and a change in cash flow assumptions can contribute to future price volatility. If actual experience differs negatively from the assumptions and other considerations used in the consolidated financial statements, unrealized losses currently in equity may be recognized in the income statement in future periods.

Assets held at amortized cost

For financial assets carried at amortized cost, the Group measures the amount of the impairment loss by comparing the carrying amount of the asset with the present value of its estimated future cash flows.

In estimating the future cash flows, the Group looks at the expected cash flows of the assets and applies historical loss experience of assets with similar credit risks that have been adjusted for conditions in the historical loss experience which no longer exist, or for conditions that are expected to arise. The estimated future cash flows are discounted using the financial asset's original or variable effective interest rate and exclude credit losses that have not yet been incurred.

The risks inherent in reviewing the impairment of any investment include the risk that market results may differ from expectations; facts and circumstances may change in the future and differ from estimates and assumptions; or the Group may later decide to sell the security as a result of changed circumstances.

Life Assurance contracts

Product classification

IFRS 4 requires contracts written by insurers to be classified as either insurance contracts' or investment contracts' depending on the level of insurance risk transferred. If significant insurance risk is transferred by the contract then it is classified as an insurance contract. Contracts that transfer financial risk but not significant insurance risk are termed investment contracts. Furthermore, some contracts, both insurance and investment, contain discretionary participation features representing the contractual right to receive additional benefits as a supplement to guaranteed benefits:

(a) that are likely to be a significant portion of the total contractual benefits;

(b) whose amount or timing is contractually at the discretion of the issuer and

(c) that are contractually based on asset or fund performance, as discussed in IFRS 4.

Accordingly, insurers must perform a product classification exercise across their portfolio of contracts issued to determine the allocation to these various categories. IFRS 4 permits the continued usage of previously applied GAAP for insurance contracts and investment contracts with discretionary participating features. Except for UK regulated with-profits funds, as described subsequently, this basis has been applied by the Company.

For investment contracts that do not contain discretionary participating features, IAS 39 and, where the contract includes an investment management element, IAS 18, apply measurement principles to assets and liabilities attaching to the contract that may diverge from previously applied. The principal line of business for which measurement changes arise on adoption of IFRS are certain unit-linked savings and similar contracts in the UK. Further details of this exercise are given in note D1 to the financial statements.

Valuation assumptions

The Group's insurance contracts and investment contracts with discretionary participation features are primarily with-profits and other protection type policies. For UK regulated with-profits funds for 2005 the contract liabilities are valued by reference to the UK FSA's realistic basis. In aggregate this basis has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances. A detailed explanation is contained in note D2(d)(ii) to the financial statements. Key elements of the value placed on the liability are that (a) the component for the with-profits benefit reserve is based on retrospective calculation of documented asset shares. Asset shares are calculated as the accumulation of all items of income and outgo that are relevant to each policy type and (b) the component for future policy related liabilities includes a market consistent valuation of costs and guarantees, options and smoothing determined using either a stochastic approach, hedging costs or a series of deterministic projections with attributed probabilities.

For other contracts, and for UK with-profits contracts in 2004, the liabilities are estimated using actuarial methods based on assumptions relating to premiums, interest rates, investment returns, expenses, mortality and surrenders. The assumptions to which the estimation of these reserves is particularly sensitive are the interest rate used to discount the provision and the assumed future mortality experience of policyholders. From the perspective of shareholder's results, the key sensitivity relates to assumed future investment returns for the Taiwan life operation. The in-force business of the Taiwan life operations includes traditional whole-of-life policies where the premium rates have been set by the regulator at different points for the industry as a whole. Premium rates were set to give a guaranteed minimum sum assured on death and a guaranteed surrender value on early surrender based on prevailing interest rates at the time of policy issue. Premium rates also included an allowance for mortality and expenses. The required rates of guarantee have fallen over time as interest rates have reduced from a high of 8 per cent to current levels of around 2 per cent. The current low level of bond rates in Taiwan gives rise to a negative spread against the majority of these policies. The current cash costs of funding in-force negative spread in Taiwan is around £30 million a year.

The profits attaching to these contracts are particularly affected by the rates of return earned, and estimated to be earned, on the assets held to cover liabilities and on future investment income and contract cash flows. Under IFRS, the insurance contract liabilities of the Taiwan business are determined on the US GAAP basis as applied previously under UK GAAP. Under this basis the policy liabilities are calculated on sets of assumptions, which are locked in at the point of policy inception, and a deferred acquisition cost is held in the balance sheet.

The adequacy of the insurance contract liabilities is tested by reference to best estimates of expected investment returns on policy cash flows and reinvested income. The assumed earned rates are used to discount the future cash flows. The assumed earned rates consist of a long-term best estimate determined by consideration of long-term market conditions, and rates assumed to be earned in the trending in period. It has been projected that rates of return for Taiwanese bond yields will trend from the current levels of some 2 per cent to 5.5 per cent by December 31, 2012.

The liability adequacy test results are sensitive to the attainment of the trended rates during the trending period. Based on the current asset mix, margins in other contracts that are used in the assessment of the liability adequacy tests, and currently assumed future rates of return, if interest rates were to remain at current levels in 2006 the premium reserve, net of deferred acquisition costs, would be broadly sufficient. If interest rates were to remain at current levels in 2007 then some level of write-off of deferred acquisition costs may be necessary. However, the amount of the charge, currently estimated at £50-70 million is sensitive for the previously mentioned variables.

The adequacy of the liability is also sensitive to the level of the projected long-term rate. The current long-term assumption of 5.5 per cent has been determined on a prudent best estimate basis by reference to detailed assessments of the financial dynamics of the Taiwanese economy. In the event that the rate applied was reduced or increased, the carrying value of the liabilities would be affected.

In broad terms, if the assumed long-term rate applied was to fall by 0.25 per cent, from 5.5 per cent to 5.25 per cent, the impact on IFRS basis results would be a charge of some £120-130 million. If the rate was to further reduce, the incremental increase in liabilities would be of a similarly commensurate size. The effects of changes in any one year reflect the combination of the short-term and long-term factors described above.

Deferred acquisition costs

Significant costs are incurred in connection with acquiring new insurance business. Except for acquisition costs of with-profits contracts of the UK regulated with-profits funds, which are accounted for under the realistic FSA regime as described in detail in note A4 to the financial statements, these costs, which vary with, and are primarily related to, the production of new business, are capitalised and amortized against margins in future revenues on the related insurance policies. The recoverability of the asset is measured and the asset is deemed impaired if the projected future margins are less than the carrying value of the asset. To the extent that the future margins differ from those anticipated, then an adjustment to the carrying value of the deferred acquisition cost asset will be necessary.

The deferral and amortization of acquisition costs is of most relevance to the Group's reported profits for shareholder-financed long-term business operations. In 2005, the application of the liability adequacy testing for the Taiwan Life business resulted in a write off of deferred acquisition costs of £21 million.

Pensions

The Group applies the requirements of IAS 19, Employee Benefits' to its defined benefit pension schemes. The economic participation in the deficits attaching to the main Prudential Staff Pension Scheme (PSPS) and the smaller Scottish Amicable Pension Scheme (SAPS) are shared between the PAC with-profits sub-fund (WPSF) and shareholder operations. The economic interest reflects the source of contributions over the scheme life, which in turn reflects the activity of the members during their employment. In the case of PSPS, at December 31, 2004, the attribution between WPSF and shareholders' funds was in the ratio 80/20. In 2005, following extensive analysis, this ratio was revised to 70/30. For SAPS the ratio for both 2005 and 2004 is estimated to be 50/50 between the WPSF and shareholders' funds.

Deferred tax

Deferred tax assets are recognized to the extent that they are regarded as recoverable, that is to the extent that, on the basis of all the available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which the losses can be relieved. The UK taxation regime applies separate rules to trading and capital profits and losses. The distinction between temporary differences that arise from items of either a capital or trading nature may affect the recognition of deferred tax assets. The judgements made, and uncertainties considered, in arriving at deferred tax balances included in the financial statements are discussed in note H4 to the financial statements.

Goodwill

Goodwill impairment testing requires the exercise of judgement by management as to prospective future cash flows.

Other features of IFRS accounting that are of particular significance to an understanding of Prudential's IFRS results

The other features that are of significance relate to the timing of adoption of certain IFRS standards and their consequential impact upon the financial statements; the accounting for UK with-profits funds; and the presentation of certain items in the financial statements.

Adoption of IAS 32, IAS 39 and IFRS 4

Three IFRS accounting standards, IAS 32, Financial Instruments: Disclosure and Presentation', IAS 39, Financial Instruments: Recognition and Measurement' and IFRS 4, Insurance Contracts', have been adopted as at January 1, 2005 rather than January 1, 2004. This treatment is consistent with the policy typically applied by groups with banking operations where the practical consequences of adopting these standards for 2004 are significant.

Accordingly, the amounts recorded for revenue and expenses and assets and liabilities of certain items reflected in the Group's financial statements are not on a consistent basis in 2005 compared to amounts recorded for the comparative period. The main area where this inconsistency applies is valuation and accounting presentation of fair value movements of derivatives and debt securities of JNL (as described below). In addition, the measurement of assets and liabilities and income and expenses of those UK unit-linked contracts, and those with similar features, that do not contain significant insurance risk, is altered.

Insurance contract accounting

With the exception of investment contracts without discretionary participation features, the Group's life assurance contracts are classified as insurance contracts and investment contracts with discretionary participating features. As permitted by IFRS 4, assets and liabilities of these contracts (see below) are accounted for under previously applied GAAP. Accordingly, except as described below, the modified statutory basis (MSB) of reporting as set out in the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers (ABI) in November 2003 has been applied for the 2005 results.

In the UK, for the 2004 comparative results, with the exception of minor accounting adjustments, the technical provisions reflect the UK regulatory basis of reporting that has applied previously for many years. This effectively constitutes the Peak 1 basis under the current Financial Services Authority (FSA) regime.

From January 1, 2005 the Group has chosen to improve its accounting for UK regulated with-profits funds by the application of the UK accounting standard FRS 27, Life Assurance'. Under this standard, the main accounting changes that are required for UK with-profits funds are:

- Derecognition of deferred acquisition costs and related deferred tax; and
- replacement of MSB liabilities with adjusted realistic basis liabilities.

The primary effect of these changes is to fundamentally alter the basis of accounting and carrying value of deferred acquisition costs (as set out in note H2 to the financial statements) and the reported level of unallocated surplus of with-profits funds (as set out in note H12 to the financial statements).

Under UK GAAP, the fund for future appropriations (FFA) represents the excess of assets over policyholder liabilities for the Group's with-profit funds. Under IFRS the FFA is termed unallocated surplus and the Group has opted to account for it wholly as a liability with no allocation to equity. This treatment reflects the fact that shareholders' participation in the cost of bonuses arises only on distribution. As a consequence of this accounting treatment, shareholder profits on with-profits business continue to reflect the one-ninth cost of declared bonus previously applied under UK GAAP.

Valuation and accounting presentation of fair value movements of derivatives and debt securities of JNL

Under IAS 39, derivatives are required to be carried at fair value. Unless hedge accounting is applied, value movements on derivatives are recognized in the income statement.

For derivative instruments of JNL, the Group has considered at length whether it is appropriate to undertake the necessary operational changes to qualify for hedge accounting so as to achieve matching of value movements in hedging instruments and hedged items in the performance statements. In reaching the decision a number of factors were particularly relevant. These were:

- IAS 39 hedging criteria has been designed primarily in the context of hedging and hedging instruments that are assessable as financial instruments that are either stand-alone or separable from host contracts, rather than, for example, duration characteristics of insurance contracts;
- the high hurdle levels under IAS 39 of ensuring hedge effectiveness at the level of individual hedge transactions for specific transactions;
- the difficulties in applying the macro hedge provisions under IAS 39 (which are more suited to banking arrangements) to JNL's derivative book;
- the complexity of asset and liability matching of US life insurers such as those with JNL's product range; and
- whether it is possible or desirable, without an unacceptable level of costs and restraint on commercial activity, to achieve the accounting hedge effectiveness required under IAS 39.

In this regard, the issues surrounding the IAS 39 application are very similar to those considered by other US life insurers when the US financial reporting standard FAS 133 was first applied for US GAAP reporting. Taking account of these considerations the Group has decided that, except for certain minor categories of derivatives, it is not appropriate to seek to achieve hedge accounting under IAS 39 by completely reconfiguring the structure of JNL's derivative book. As a result of this decision, the total income statement results are more volatile as the movements in the value of JNL's derivatives are reflected within it.

Under IAS 39, unless carried at amortized cost (subject to impairment provisions where appropriate) under the held-to-maturity category, debt securities are also carried at fair value. The Group has chosen not to classify any financial assets as held-to-maturity. Debt securities of JNL are designated as available-for-sale with value movements being recorded as movements within shareholders' equity.

Accounting for with-profits business

For with-profits business (including non-participating business of Prudential Annuities Limited which is owned by the PAC with-profits fund), adjustments to liabilities and any related tax effects are recognized in the income statement. However, except for any impact on the annual declaration of bonuses, shareholder profits for with-profits business and shareholders' funds would not be affected by adjustments to liabilities. This is because the income statements solely reflect one-ninth of the cost of bonuses declared for with-profits policies for the year.

For both 2005 and 2004, adjustments to the long-term business provision for the PAC with-profits fund would normally reflect changes that have also been reflected in the annual regulatory returns submitted to the FSA. Except to the extent of any second order effects on other elements of the regulatory returns, such changes can be expected to have a consequent effect on the excess of assets over liabilities of the fund for purposes of solvency calculations, and the related free asset ratio which is an indicator of the overall financial strength of the fund. Similar principles apply to the Group's Asian with-profits business.

Profits Recognition

As outlined in " Analysis by Business Segment and Geographic Region United Kingdom Basis of Profits" below, Prudential's results include an annual profit distribution to shareholders from long-term with-profits funds that represents an amount of up to one-ninth of the value of that year's bonus declarations to policyholders. The distribution corresponds directly to the post-tax basis profit for with-profits business. The boards of directors of the subsidiary companies that have with-profits operations, using actuarial advice, determine the amount of annual and final bonuses to be declared each year on each group of contracts.

Unallocated surplus

As discussed above, the unallocated surplus represents the excess of assets over policyholder liabilities of the Group's with-profits funds. The annual excess or shortfall of income over expenditure of the with-profits funds after declaration and attribution of the cost of bonuses to policyholders and shareholders is transferred to, or from, the unallocated surplus through a charge or credit to the income statement. The balance is determined after full provision for deferred tax on unrealized appreciation of investments.

Changes to the level of the unallocated surplus do not directly impact shareholders' results or funds. After allowing for differences in the basis of preparation of the financial statements and UK regulatory returns, movements in the level of the unallocated surplus are broadly indicative of movements in the excess of regulatory basis assets over liabilities of the fund. In turn, movements in this excess as a proportion of liabilities are indicative of changes in the financial strength of the fund.

Differences in the basis of preparation of financial statements and UK regulatory returns arise principally from the treatment of certain regulatory basis liabilities, such as mismatching reserves (that are accounted for as reserves within the unallocated surplus), recognition of deferred acquisition costs in the financial statements, and asset valuation differences and admissibility deductions reflected in the regulatory returns.

Fair Value of Assets

Changes in the fair value of assets of Prudential's long-term with-profits funds will primarily be reflected in the excess of assets over liabilities recorded as the unallocated surplus. Shareholders' profits from with-profits business and shareholders' funds are not directly impacted by movements in the fair values of the assets. However, current investment performance is a factor that is taken into account in the setting of the annual declaration of bonuses which, in turn, affects UK shareholder profits to the extent of one-ninth of the cost of bonus.

Changes in the fair value of assets of unit-linked (separate account) funds are normally accompanied by a matching change in unit-linked business liabilities that is also recognized in the income statement.

Investment Returns

For with-profits business, investment returns together with other income and expenditure are recorded within the income statement. However, the difference between net income of the fund and the cost of bonuses and related statutory transfers is reflected in an amount transferred to or from the unallocated surplus within the income statement. Except to the extent of current investment returns being taken into account in the setting of bonus policy, the investment returns of with-profits fund in a particular year do not affect shareholder profits or with-profits funds.

Presentation of results before tax

The total tax charge for the Group reflects tax that in addition to relating to shareholders' profits is also attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. This is explained in more detail in note F5 to the financial statements. However, pre-tax profits are determined after transfers to or from unallocated surplus of with-profits funds. These transfers are in turn determined after taking account of tax borne by with-profits funds. Consequently reported profit before the total tax charge is not representative of pre-tax profits attributable to shareholders. In order to provide a measure of pre-tax profits attributable to shareholders the Group has chosen to adopt an income statement presentation of the tax charge and pre-tax results that delineates between policyholder and shareholder components.

Overview of Consolidated Results

Introduction

Prudential has built strong positions in the United Kingdom, the United States and Asia, three of the most attractive financial services markets in the world.

Prudential achieved these positions by adopting a disciplined approach to investment and growth, allocating capital to those businesses that deliver sustainable high returns. At the same time, Prudential managed its risks by maintaining a diversified portfolio of businesses across its chosen markets, principally in the UK, the US and Asia, including several mature cash generators, as well as attractive newer businesses which require investment.

The following table shows Prudential's IFRS consolidated total profit for the periods indicated.

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Total revenue, net of reinsurance	**41,125**	33,904
Total charges	**(38,980)**	(32,343)
Profit before tax*	**2,145**	1,561
Tax attributable to policyholders' returns	**(1,147)**	(711)
Profit before tax attributable to shareholders	**998**	850
Tax expense	**(1,388)**	(951)
Less: tax attributable to policyholders' returns	**1,147**	711
Tax attributable to shareholders' profits	**(241)**	(240)
Profit from continuing operations after tax	**757**	610
Discontinuing operations (net of tax)	**3**	(94)
Profit for the year	**760**	516

* Profit before tax represents income net of post-tax transfers to unallocated surplus of with-profits funds, before tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders' profits.

Basis of preparation of overview

In previous annual reports on Form 20-F the structure of the section on the overview of consolidated results has been prepared in accordance with the basis for financial reporting used by Prudential's management in preparation of the Company's interim and annual financial statements that appear in Prudential's distributions to UK shareholders and the UK financial market, through the Company's preliminary results release and UK Annual Report.

The basis previously applied has been to analyze profit before shareholder tax between management's chosen performance measure of operating profit based on longer-term investment returns and other items.

Two features of the previous reporting framework under UK GAAP enabled this treatment. First, the ability to focus on profit before shareholder tax (rather than policyholder and shareholder tax) was facilitated by the requirements of the 1985 Companies Act. Second, the Statement of Recommended Practice of the Association of British Insurers specifically recommended the reporting of operating profit based on longer-term investment returns.

On the adoption of the IFRS basis of reporting in the consolidated financial statements these two features no longer apply. It is therefore necessary for the structure of the overview of the consolidated results to be reconfigured to meet US reporting requirements.

Under IFRS the pre-tax GAAP measure of profits is profit before policyholder and shareholder taxes. This measure is not relevant for reflecting pre-tax results attributable to shareholders for two reasons. First, this profit measure represents the aggregate of pre-tax results attributable to shareholders and a pre-tax amount attributable to policyholders. Second, the amount is determined after charging the transfer to the liability for unallocated surplus, which in turn is determined in part by policyholder taxes borne by the ring-fenced with-profits funds. It is noted that this circular feature is specific to with-profits funds in the UK, and other similarly structured overseas funds, and should be distinguished from other products, which are referred to as 'with-profits' and the general accounting treatment of premium or other policy taxes.

Accordingly, the Company has chosen to explain its consolidated results by reference to profits for the year, reflecting profit after tax for continuing and discontinued operations. In explaining movements in profit for the year reference is made to trends in profit before shareholder tax and the shareholder tax charge.

Profit for the year

Profit for 2005 was £760 million compared with £516 million in 2004. This £244 million increase reflects an increase in the profit from continuing operations after tax of £147 million from £610 million to £757 million and an increase of £97 million in the net of tax result for discontinued operations from a charge of £94 million to a profit of £3 million.

The increase in profit from continuing operations after tax reflects growth in profits before tax attributable to shareholders of £148 million, which grew from £850 million in 2004 to £998 million in 2005, and a £1 million increase in the tax charge attributable to shareholders, which grew from £240 million in 2004 to £241 million in 2005.

The growth in profit before tax attributable to shareholders primarily reflects growth in underlying profits and a higher level of short-term value movements on financial instruments credited to income. These increases offset a goodwill impairment charge and an increased negative level of actuarial and other gains and losses attaching to the Group's defined benefit pension schemes.

In comparison to the growth in profits before tax attributable to shareholders, the small increase in the shareholder tax charge corresponds to a reduction in the effective tax rate from 28 per cent to 24 per cent. The reduction in the 2005 effective tax rate arises from a number of factors, including settlement of a number of outstanding issues with HM Revenue and Customs and benefit taken for prior year losses incurred in France following a recent European Court of Justice decision.

Discontinued operations in 2005 relate to the completion of Egg's withdrawal from France and the losses incurred by Funds Direct. The discontinued operations in 2004 relate to the profit on sale of Jackson Federal Bank, the profit generated by the sale of a stake in Life Assurance Holding Corporation Limited and losses relating to Egg France.

Analysis by Business Segment and Geographic Region

The Group's reportable segments are based on the organizational structure used by management for making operating and investment decisions and for assessing performance. The Group's business segments are long-term business, banking, and broker dealer and fund management whilst its geographical segments comprise the territories in which the Group conducts business, which are the United Kingdom, the United States and Asia.

The following table shows Prudential's IFRS consolidated total profit for the periods indicated divided by business segment and geographic region. The accounting policies applied to the segments below are the same as those used in the Group's consolidated accounts and are described in Note A4 to the consolidated financial statements. The Group has taken advantage of the exemption within IFRS that allows comparative information presented in the first year of adoption of IFRS not to comply with standards IAS 32, IAS 39 and IFRS 4. Accordingly, reported profit for the year in 2004 does not reflect the impact of these standards. For further information on the impact of adopting these standards see Note A6 to the consolidated financial statements.

Total profit for the year reflecting profit after tax for continued and discontinued operations:

2005	UK £m	US £m	Asia £m	Total £m
Long-term	**288**	**350**	**148**	**786**
Banking	**48**			**48**
Broker-dealer and fund management	**99**	**5**	**0**	**104**
Unallocated corporate	**(178)**			**(178)**
Total profit for the year	**257**	**355**	**148**	**760**

2004	UK £m	US £m	Asia £m	Total £m
Long-term	247	235	103	585
Banking	(95)	33		(62)
Broker-dealer and fund management	94	(8)	14	100
Unallocated corporate	(107)			(107)
Total profit for the year	139	260	117	516

Profit from Long-term business operations

Total profit from long-term business in 2005 was £786 million compared to £585 million in 2004.

Profit from long-term business operations increased from £585 million in 2004 to £786 million in 2005 and the non-recurrence of a £4 million contribution (net of tax) for discontinued operations in 2004.

The growth in 2005 of profits from continuing operations after tax was supported by a 38 per cent increase in profit before shareholder tax from £832 million in 2004 to £1,152 million in 2005 and an increase in the shareholder tax charge from £251 million in 2004 to £366 million in 2005.

The growth in profit before tax attributable to shareholders of £320 million compared to 2004 primarily reflects an increase in underlying profits and a higher level of short-term value increases on financial instruments. The growth in profit before tax in 2005 also reflects short-term value increases of £122 million on derivatives held by Jackson National Life, which are used for economic hedging purposes. Prior to the adoption of IAS 39 at January 1, 2005, these derivatives were carried at amortized cost and, as a result, the 2004 income does not include any attributable value movement.

The effective shareholder tax rate on profits from continuing long-term business operations increased from 30 per cent in 2004 to 32 per cent in 2005 resulting from minor variations on the rates applicable to UK and Asian businesses.

In order to understand how Prudential's results are derived it is necessary to understand how profit emerges from its business. This varies from region to region, primarily due to differences in the nature of the products and regulatory environment in which Prudential operates.

United Kingdom

Basis of Profits

Prudential's results comprise an annual profit distribution to shareholders from its UK long-term with-profits fund, hereafter referred to as the with-profits fund, as well as profits from its other businesses. For most of Prudential's operations, other than its UK long-term insurance businesses, the IFRS basis of accounting matches items of income and related expenditure within the same accounting period. This is achieved through the deferral of acquisition costs and application of the accruals concept.

With-profits Products

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

Bonus Rates

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

Unallocated Surplus

The annual excesses of premiums and investment returns over claim payments, operating expenses and the change in policyholder provisions within Prudential's with-profits fund that are not distributed in that year as bonuses and related shareholders' profit are transferred to the liability for unallocated surplus by a charge to the income statement of the with-profits fund. Any shortfall in such amounts would result in a transfer from the unallocated surplus by a credit to the income statement of the long-term fund. Current year amounts in respect of premiums, investment returns, operating expenses and unusual charges or credits do not directly affect the distribution of profit to shareholders from the with-profits business in that year. Current year claims, which include final bonus payments, do have an effect on shareholders' profit through the shareholders' proportion of the value of those final bonuses.

Surplus Assets and Their Use

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

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

The "SAIF" and "PAL" Funds

Prudential's with-profits fund also includes the Scottish Amicable Insurance Fund ("SAIF") and the wholly-owned subsidiary, Prudential Annuities Limited ("PAL"). All assets of the SAIF business are solely attributable to former policyholders of Scottish Amicable Life Assurance Society (predating the acquisition of Scottish Amicable by Prudential in October 1997). The SAIF with-profits fund is discussed in more detail under Item 4, "Information on the Company Business of Prudential UK Business Shareholders' Interests in Prudential's Long-term Insurance Business The SAIF Sub-fund and Accounts". Since PAL is a wholly owned subsidiary of the with-profits fund, profits from this business affect shareholders' profits only to the extent that they affect the annual with-profits bonus declaration and resultant transfer to shareholders.

Comparison of total profit arising from UK long-term business

Profit from UK long-term business increased from £247 million in 2004 to £288 million in 2005. The increase of £41 million reflects a rise of £45 million in profit from continuing operations after tax from £243 million in 2004 to £288 million in 2005 and the non-recurrence of the £4 million net of tax profit that arose in 2004 on the sale of Prudential's stake in Life Assurance Holding Company.

The growth in profits from continuing operations after tax reflects an increase in profit before shareholder tax from £334 million in 2004 to £416 million in 2005 and an increase in the shareholder tax charge from £91 million in 2004 to £128 million in 2005.

The growth in profit before tax attributable to shareholders of £82 million primarily reflects growth in underlying profits. This growth was partially offset by a £20 million charge in 2005 (2004: £nil million) for the effect of strengthening actuarial provisions for increases in ongoing contributions for future service of active scheme members of the Prudential Staff Pension Scheme.

The effective shareholder tax rate on profits from continuing UK long-term business operations increased from 27 per cent in 2004 to 31 per cent in 2005.

United States

Basis of Profits

The profit on Jackson National Life's business predominantly arises from spread income from interest-sensitive products, such as fixed annuities, institutional products and fee income on variable annuities. Except for institutional products and certain term certain annuities which are classified as investment products under IAS39, for the purposes of IFRS reporting, deposits into these products are recorded as premiums, withdrawals and surrenders are included in benefits and claims and the resulting net movement is recorded under other reserve movements within benefits and claims. Benefits and claims also include interest credited to policyholders in respect of deposit products and fees charged on these policies. While the presentation of these items differs between IFRS and US GAAP, there is no net impact on total profits.

Comparison of total profit arising from US long-term business

Profit from US long-term business increased from £235 million in 2004 to £350 million in 2005. This increase of £115 million reflects a rise in profit before shareholder tax from £357 million in 2004 to £526 million in 2005 and an increase in the shareholder tax charge from £122 million to £176 million over the same period.

The £169 million growth in 2005 of profit before tax attributable to shareholders mainly reflects growth in underlying profits (as described in the additional analysis of consolidated results reflecting the basis used by management and reported externally to UK shareholders and the UK financial market) and a significant increase in the accounting value of short-term value movements in financial instruments reflected in the IFRS income statement. £122 million of the increase is attributable to an increase in the value of derivatives used by JNL for economic hedging purposes. Prior to the adoption of IAS 39 at January 1, 2005, these derivatives were carried at amortized cost and therefore these increases were not reflected in the 2004 income statement.

Asia

Basis of Profits

The assets and liabilities of contracts classified as insurance under IFRS 4 are determined in accordance with methods prescribed by local GAAP and adjusted to comply, where necessary, with UK GAAP. Under IFRS 4, subject to the conditions of that standard, the continued application of UK GAAP in this respect is permitted.

For Asian operations in countries where local GAAP is not well established and in which the business is primarily non-participating and linked business, US GAAP is used as the most appropriate reporting basis. Of the more significant Asia operations, this basis is applied in Taiwan, Japan and Vietnam. For with-profits business in Hong Kong, Singapore and Malaysia the basis of profit recognition is bonus driven as described in the section " United Kingdom, with-profits products".

Comparison of total profit arising from Asian long-term business

Profit from Asian long-term business increased from £103 million in 2004 to £148 million in 2005. This £45 million increase largely reflects a rise in profit before shareholder tax from £141 million to £210 million and an increase in the shareholder tax charge from £38 million to £62 million during the same period.

£30 million of the growth in profit before tax attributable to shareholders arose from various non-recurring items.

The effective shareholder tax rate increased from 27 per cent in 2004 to 30 per cent in 2005.

A goodwill impairment charge of £120 million has been incurred in 2005 in respect of the Group's Japanese life business. This charge is reflected in the explanation of profit and losses for unallocated corporate activity.

Profit from banking operations

Basis of Profits

The Group's banking operations now solely comprises Egg in the UK, which is an innovative financial services company primarily offering unsecured personal loans, credit cards, mortgages and savings accounts. The basis of profits is the margin between interest income and expense and fee and commission income.

Comparison of total profit arising from banking operations

In 2005, profit for the year was £48 million compared with a loss of £62 million in 2004. The £110 million increase reflects a £143 million rise in the profit for UK banking from a loss of £95 million in 2004 to a profit of £48 million in 2005 and the non-recurrence of a £33 million profit resulting from the discontinued Jackson Federal Bank business, which was disposed of in 2004.

The banking business £143 million growth largely reflects an increase in the contribution from continuing operations from £36 million in 2004 to £45 million in 2005 and an increase of £134 million in the result from discontinued operations, which increased from a loss of £131 million in 2004 to a profit of £3 million in 2005.

The £9 million increase in profit from continuing operations mainly reflects a decrease of £17 million in profit before shareholder tax from £61 million in 2004 to £44 million in 2005, offset by a reduction in the tax charge of £26 million mainly arising from the benefit of previously unused tax losses.

The result for UK discontinued banking operations reflects the results and closure of the Egg France operation and the discontinuation of Egg's Funds Direct operation.

Profit from broker-dealer and fund management

In 2005 total profit from broker-dealer and fund management increased by £4 million from £100 million in 2004 to £104 million in 2005. This increase results primarily from an improvement in profit earned from M&G's UK and European operations, from £94 million in 2004 to £99 million in 2005 and the improvement in profits from the US operations from a loss of £8 million in 2004 to a profit of £5 million in 2005. These profit gains offset a reduction in the Company's Asian operations profit from a profit of £14 million in 2004 to £nil in 2005.

The increase of £4 million in total profit largely reflects an increase of £5 million in profit before shareholder tax from £149 million in 2004 to £154 million in 2005 and an increase in the tax charge of £1 million from £49 million in 2004 to £50 million in 2005.

The increase in profit before shareholder tax reflects growth in underlying profits, as explained in the additional analysis of consolidated results reflecting the basis used by management and reported externally to UK shareholders and the financial market, which was offset by adverse changes in the short-term value increases of certain financial instruments, a reduction in the result attributable to minorities of US funds consolidated under IFRS, and actuarial losses attributable to the M&G defined benefit pension scheme.

Unallocated corporate

Total net of tax charges for unallocated corporate activity increased by £71 million from £107 million in 2004 to £178 million in 2005. The change primarily reflects a £160 million pre-tax increase from £192 million in 2004 to £352 million in 2005 offset by an increase of £89 million in the tax credit, from £85 million to £174 million.

The increase in pre-tax expenditure primarily reflects a consistent level of underlying expenditure, a goodwill impairment charge of £120 million in 2005 on the Japanese life insurance business, a decrease in the short-term value changes and technical adjustments for consolidated investment funds.

The increase in the tax credit largely reflects the settlement of outstanding issues with HM Revenue and Customs at amounts below those previously provided, the tax credit arising from relief for excess expenses in respect of the shareholder backed protection business, and adjustments for prior years resulting from routine revisions of tax returns.

Business Segment and Geographical Analysis by Nature of Revenue and Charges

The following table shows Prudential's consolidated total revenue and consolidated total charges for the following periods.

	Year Ended December 31,	
	2005	2004
	(In £ Millions)	
Earned premiums, net of reinsurance	**15,028**	16,152
Investment income	**24,013**	15,750
Other income	**2,084**	2,002
Total revenue	**41,125**	33,904
Benefits and claims and movement in unallocated surplus of with-profits funds	**(33,100)**	(26,593)
Acquisition costs and other operating expenditure	**(5,552)**	(5,563)
Finance costs: interest on core structural borrowings of shareholder-financed operations	**(208)**	(187)
Goodwill impairment charge	**(120)**	
Total charges	**(38,980)**	(32,343)
Profit before tax*	**2,145**	1,561
Tax attributable to policyholders' returns	**(1,147)**	(711)
Profit before tax attributable to shareholders	**998**	850
Tax attributable to shareholders' profits	**(241)**	(240)
Profit from continuing operations after tax	**757**	610
Discontinued operations (net of tax)	**3**	(94)
Total profit	**760**	516

* Profits before tax represents income net of post-tax transfers to unallocated surplus of with-profits funds, before tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders' profits.

Earned premiums

	Year Ended December 31,	
	2005	2004
	(In £ Millions)	
Long-term business:		
UK Operations	**7,800**	9,096
US Operations	**4,270**	4,647
Asian Operations	**2,958**	2,409

	Year Ended December 31,	
Total	**15,028**	16,152

Earned premiums, net of reinsurance, for long-term business totaled £15,028 million in 2005 compared to £16,152 million in 2004. The main reason for the reduction in earned premiums is the adoption of IAS 39 and IFRS 4 from January 1, 2005. For 2004, the income statement includes premiums on all contracts that were then classified under previous GAAP as insurance, including deposit style 'investment contracts' where the insurance risk in the contracts is insignificant. For 2005, the recognition basis in the income statement remains the same except for investment contracts, as defined under IFRS 4, which do not contain discretionary participation features, where the accounting reflects the deposit nature of the arrangement. In 2004, the earned premiums for the UK, US and Asia included approximately £1,381 million, £873 million and £5 million, respectively, of premiums for investments contracts.

a) United Kingdom

After adjusting for the effects of IAS 39 and IFRS 4, adapted prospectively from January 1, 2005, earned premiums from insurance contracts increased from £7,715 million in 2004 to £7,800 million in 2005.

This increase largely reflects increased sales of bulk annuities including the £1,450 million Phoenix Life and Pensions in-force annuity book transaction announced in June 2005 (the 2004 comparatives included a £1,108 million annuity book transaction with Royal London). In addition, sales of individual annuities improved relative 2004 results as a result of higher sales through the partnerships and direct to consumer channels.

b) United States

Earned premiums from insurance contracts increased by 13.1 per cent in 2005 from £3,774 million in 2004 to £4,270 million in 2005, after adjusting for the effects of IAS 39 and IFRS 4.

This increase was predominantly due to growth in variable annuity and fixed index annuity sales. Prudential believes that JNL's strong sales of variable annuities reflect its differentiated product structure, distribution proposition and service offering.

Stronger fixed index annuity sales in 2005 reflected customers' increasing preference for products with the potential for higher returns linked to equity index performance. JNL believes it has benefited from its approach to educating broker-dealers about a complex product, while at the same time offering lower commissions and passing the benefit to the end consumer.

The growth in sales of variable annuity and fixed indexed annuity products was partially offset by lower sales of fixed annuities. This primarily reflects the continued low interest rate environment and the relatively flat interest yield curve in the United States.

c) Asia

After adjusting for the effects of IAS 39 and IFRS 4, earned premiums in 2004 and 2005 were £2,404 million and £2,958 million, respectively, an increase of 23 per cent.

While the majority of these earned premiums relate to sales made through Asia's tied agency distribution channel, Prudential believes that there is potential to expand alternate channels, particularly banks and direct marketing. Growth in earned premiums in 2005 was most significant in Singapore, Korea and India with increases of £127 million, £76 million and £59 million, respectively.

Singapore's operations grew largely as a result of the broadening of its unit linked range and also increased bank distribution. In contrast, growth in sales in Korea was mainly due to the increased success in the tied financial advisor and general agency channels and the continued appeal of our universal life product. In addition, Prudential's Indian life insurance joint venture, ICICI-Prudential Life, supported its growth in 2005 primarily through ongoing expansion. The Indian business now has 74 branches and has grown agent numbers by 36 per cent during the year to 70,000.

Investment income

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Long-term business:		
UK Operations	**20,852**	13,541

	Year Ended December 31,	
US Operations	**2,391**	1,474
Asian Operations	**770**	735
Total	**24,013**	15,750

Investment income consists of interest income, dividends and realized and unrealized gains and losses on investments designated as fair value through profit and loss. As allowed by IFRS, the Group adopted IAS 39 on January 1, 2005.

a) United Kingdom

In the UK, investment income increased from £13,541 million in 2004 to £20,852 million in 2005. The main reason for this increase in investment income has been the appreciation of UK share and bond prices. This has resulted in an increase in investment income of approximately £6 billion. The effect of adopting IAS 39 in 2005 has been to increase investment income by £192 million.

b) United States

In the US, investment income increased from £1,474 million in 2004 to £2,391 million in 2005. The effect of adopting IAS 39 has been to increase investment income by £578 million. The remaining increase in investment income is due to an increase in external investments income such as dividends and interest income by £171 million and realized gains by £152 million reflecting an increase in investment yields from 5.6 per cent in 2004 to 6.3 per cent in 2005.

c) Asia

In Asia, investment income has increased from £735 million in 2004 to £770 million in 2005. The main reason for the movement is an increase in external investment income by £39 million. The adoption of IAS 39 did not have any material effect in Asia.

Benefits and claims and movement in unallocated surplus of with-profits funds

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Long-term business:		
United Kingdom	**(24,782)**	(18,832)
United States	**(5,591)**	(5,339)
Asia	**(2,727)**	(2,422)
Total	**(33,100)**	(26,593)

Benefits and claims represent payments, including final bonuses, to policyholders in respect of maturities, surrenders and deaths plus the change in technical provisions (which primarily represents the movement in amounts owed to policyholders).

Total benefits and claims increased by £6,507 million in 2005 to £33,100 million, compared to £26,593 million in 2004. This principally reflects the movement in policyholder liabilities as a result of the increase in investment income discussed above, which has been passed on to the policyholders in the form of bonus declaration for with-profits products or through direct increase in policyholder liabilities for unit-linked and similar products, or transferred to unallocated surplus.

a) United Kingdom

Overall benefits, claims and the transfer to unallocated surplus increased from £18,832 million in 2004 to £24,782 million in 2005. There are two principal reasons for this increase, both of which relate to the accounting treatment of investment returns allocated for assets backing liabilities and unallocated surplus of with-profits funds. First for unit-linked, variable annuity and other policies which are classified as insurance contracts under IFRS 4 where there is a direct relationship between policyholder benefits and asset returns on attaching pools of assets, the charge for benefits and claims reflects investment return credited to policyholder balances. With increased market returns in 2005 compared to 2004 there

is a natural increase in the charge. This feature also applies in a similar manner for closely matched UK annuity business where the calculation of liabilities reflects period-end yields.

The second reason relates to the basis of accounting for with-profits funds. The charge to the income statement for these funds reflects two items namely:

a) Liabilities for contract benefits either include bonuses declared to date (as applied in 2004 for all with-profits business and in 2005 for the Singapore and Malaysia with-profits funds) or "asset share" attribution (as applied in 2005 for UK regulated with-profits funds on the application of FRS 27 as part of the adoption of IFRS 4 as explained in note D2 of the financial statements), and

b) The movement in the excess of assets over policyholder liabilities is charged to the income statement as a movement on the liability for unallocated surplus.

The combined effect of these two items is that there is a close correlation between the level of increase in the values of assets of the funds and the level of combined charge for benefits and movement on unallocated surplus. With market returns of 20 per cent on the Prudential Assurance long-term fund in 2005 compared to 13.4 per cent for 2004, there is an attendant increase in the charge to the income statement.

The annual movements in benefits and claims also include changes in the pension mis-selling provision, which decreased in 2005, and 2004. For a detailed analysis of this provision, see Item 4, "Information on the Company Business of Prudential UK Business Shareholders' Interests in Prudential's Long-term Insurance Business Pension Mis-selling". With the consent of the UK regulator, the total cost of pension mis-selling is included within the transfer to the unallocated surplus of the Prudential Assurance long-term with-profits fund. Payments related to pension mis-selling will be met from the surplus assets in the Prudential Assurance long-term with-profits fund and not from amounts intended to fund existing and future bonuses.

As described in "United Kingdom Basis of Profits" above, because shareholders' profit from the Prudential Assurance with-profits sub-fund represents an amount of up to one-ninth of the value of that year's bonus declaration to policyholders, shareholders' profit from the fund has not been affected by the increase in the provision for pension mis-selling. Given the strength of the fund, Prudential does not believe that pension mis-selling costs will have an adverse impact on the levels of bonuses paid to policyholders and, therefore, shareholders' profit from the fund. In the unlikely event that this proves not to be the case, Prudential's intention would be that an appropriate contribution to the long-term with-profits fund be made from shareholders' funds with a consequential impact on shareholders' profit.

b) United States

In 2005, the accounting charge for benefits and claims increased by 4.7 per cent to £5,591 million.

The change reflects underlying movements in claims, benefits and maturities for contracts classified as insurance products under IFRS 4. The charge for 2004 includes maturities and other changes for institutional business and certain term certain annuities.

c) Asia

In 2005, benefits and claims totaled £2,727 million, up 12.6 per cent on £2,422 million in 2004 reflecting an increase in policyholder benefits of 30 per cent from £719 million to £938 million. The adoption of IFRS 4, IAS 39 and FRS 27 did not have material effects on the change in the accounting charges for benefits and claims for the Group's Asian operations.

Acquisition costs and other operating expenditure

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Long-term business:		
United Kingdom	**(4,018)**	(4,282)
United States	**(767)**	(650)
Asia	**(767)**	(631)
Total	**(5,552)**	(5,563)

Total acquisition costs and other operating expenditure of £5,552 million in 2005 were 0.2 per cent lower than the £5,563 million incurred in 2004.

a) United Kingdom

Total UK acquisition costs and other operating expenses in 2005 were £4,018 million, compared to £4,282 million in 2004. The decrease of £264 million in 2005 mainly relates to a decrease in operating expenses from £2,793 million to £2,404 million.

b) United States

Acquisition costs and other operating expenses of £767 million in 2005 were 18 per cent higher than expenses in 2004 of £650 million. The increase in expenses primarily reflects higher amortization of deferred acquisition costs (DAC) by £55 million from £221 million in 2004 to £276 million in 2005.

c) Asia

Total Asian acquisition costs and other operating expenses in 2005 were £767 million, an increase of £136 million compared to £631 million in 2004. This increase reflects an increase in DAC amortization from £285 million in 2004 to £431 million in 2005 and an increase in operating expenses from £308 million in 2004 to £401 million in 2005. The increase in operating expenses in part reflects development expenses of £20 million, restructuring costs of £14 million in Japan and an increase in administrative expenses of £20 million.

Additional analysis of consolidated results reflecting the basis used by management and reported externally to UK shareholders and the UK financial market

For many years, the assessment of performance by management has been, and continues to be, applied to profit before shareholder tax by analysis of the result between operating profit based on longer-term investment returns and other reconciling items. The focus on profit before shareholder tax, rather than profit before policyholder and shareholder tax, reflects the shareholders' interests in surpluses as they arise and the regulatory basis of ring-fenced long-term funds in the UK. In particular, taxes borne by policyholders of with-profits contracts are borne by the liability for unallocated surplus of with-profits funds.

Until the adoption of IFRS, operating profit based on longer-term investment returns was a GAAP measure arising from the specific recommendation of the Statement of Recommended Practice (SORP) for accounting for insurance business issued by the Association of British Insurers (ABI). With the adoption of IFRS, the ABI SORP is no longer authoritative literature for the purposes of determining GAAP measures. Nevertheless, it continues to be the basis applied by the Company for internal performance assessment and a fundamental element of the analysis provided to shareholders and the UK stock market. The analysis that follows reflects information published with the Group's results on March 16, 2006.

Reconciliation of total profit by business segment and geography to underlying performance measure

A reconciliation of profit before all taxes to profit before tax attributable to shareholders and profit for the year is shown below.

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Profit before tax	**2,145**	1,561
Tax attributable to policyholders' returns	**(1,147)**	(711)
Profit before tax attributable to shareholders	**998**	850
Tax expense	**(1,388)**	(951)
Less: tax attributable to policyholders' returns	**1,147**	711
Tax attributable to shareholders' profits	**(241)**	(240)
Profit from continuing operations after tax	**757**	610
Discontinued operations (net of tax)	**3**	(94)
Profit for the year	**760**	516

A reconciliation of profit before shareholder tax to operating profit based on longer-term investment returns is provided below:

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Performance measure: operating profit from continuing operations based on long-term investments returns (i)	**957**	708
Goodwill impairment charge (ii)	**(120)**	
Short-term fluctuations in investment returns on shareholder-backed business (iii)	**211**	149
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes (iv)	**(50)**	(7)
Profit from continuing operations before tax attributable to shareholders	**998**	850

Notes:

(i)

Operating profit based on longer-term investment returns

Operating profit based on longer-term investment returns is a supplemental measure of results. For the purposes of measuring operating profit, investment returns on shareholder financed business are based on expected long-term rates of return. The expected long-term rates of return are intended to reflect historical real rates of return and, where appropriate, current inflation expectations adjusted for consensus economic and investment forecasts. The significant operations that require adjustment for the difference between actual and longer-term investment returns are JNL and certain businesses of the Group's Asian operations. The amounts included in operating results for long-term capital returns for debt securities comprise two components. These are a risk margin reserve based charge for expected defaults, which is determined by reference to the credit quality of the portfolio, and amortization of interest-related gains and losses for operating results based on long-term results to the date when sold bonds would otherwise have matured.

(ii)

Goodwill impairment charge

The charge for goodwill impairment of £120 million relates to the Japan life insurance business. The charge reflects the slower than expected development of the Japanese life insurance business.

(iii)

Short-term fluctuations in investment returns on shareholder-backed business

The fluctuations arise as follows:

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
US operations:		
Movements in market value of derivatives used for economic hedging purposes (2004 not applicable because of formal adoption of IAS 32, IAS 39 and IFRS 4 on January 1, 2005)	**122**	
Actual less longer-term investment returns for other items	**56**	61
Asian operations	**32**	37
Other operations (including £6m (2004: £nil) on sale of partial stake in Indian subsidiary)	**1**	51
	211	149

(iv)

Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes

	Year Ended December 31,	
	2005	**2004**
	(In £ Millions)	
Actuarial losses		
Actual less expected return on scheme assets	**544**	115
Experience gains (losses) on liabilities	**1**	(17)
Losses on changes of assumptions for plan liabilities (based on long-term inflation of 2.8%)	**(489)**	(141)
	56	(43)
Less: amount attributable to the PAC with-profits fund	**(58)**	36
Total	**(2)**	(7)
Non-recurrent credit (charge)		
Shareholders' share of credit arising from reduction in level of assumed future discretionary increases for the Prudential Staff Pension Scheme (PSPS) for pensions in payment to 2.5%	**35**	
Losses on re-estimation of shareholders' share of deficits arising from the PSPS (a)	**(63)**	
Strengthening in actuarial provisions for increase in ongoing contributions for future service of active scheme members (b)	**(20)**	
	(48)	
Total	**(50)**	(7)

(a) Up to December 31, 2004, the deficits arising on the PSPS had been assessed as being 80 per cent attributable to the PAC with-profits fund and 20 per cent to shareholder operations. In 2005, following additional analysis this apportionment was altered to a ratio of 70/30.

(b) As a result of the April 2005 scheme valuation and subsequent discussions, the contribution levels for future ongoing service of active members will approximately double. The charge of £20 million reflects the actuarial provision for this increase in future expenses for certain insurance contracts.

The Group uses a performance measure of operating profit based on longer-term investment returns, excluding charges for goodwill impairment and actuarial and other gains and losses on defined benefit pension schemes. The directors believe that this performance measure better reflects underlying performance. It is the basis used by management for the reasons outlined below. It is also the basis on which analysis of the Group's results has been provided to UK shareholders and the UK financial market for some years under long standing conventions for reporting by proprietary UK life assurers.

Longer-term investment returns included within the performance measure are determined by reference to expected long-term rates of return. These are intended to reflect historical rates of return on assets, and where appropriate, current inflation expectations adjusted for consensus economic and investment forecasts. The overriding reason for distinguishing longer-term investment returns from short-term fluctuations is that the investments are generally held for the longer-term to back long duration insurance contract liabilities and solvency capital rather than for short-term trading purposes.

Furthermore, the income statement recognition of investment appreciation, short-term value movements on derivatives, and the charge for the policyholder benefits under IFRS 4 give rise to accounting mismatches that are not representative of the underlying economic position.

Goodwill impairment charges reflect adverse changes in assessment in a given period as to whether the excess of the amount paid over the accounting value of acquired assets and liabilities is expected to be recoverable in the future. It is thus appropriate for such charges to be distinguished from current period operational performance.

Actuarial and other gains and losses on defined benefit pension schemes principally reflect short-term value movements on scheme assets and the effects of changes in actuarial assumptions. Under the Group's accounting policies these items are recorded within the income statement, rather than through other comprehensive income, solely due to the interaction of the Group's approach to adoption of IFRS 4 for with-profits funds and the requirements of IAS 19. In analyzing profit before shareholder tax the separate identification of these gains and losses is analogous to the more normal treatment of inclusion as a movement on other comprehensive income i.e. not within profit for the period.

The following tables reconcile 'operating profit based on longer-term investment returns', the Group's performance measure, to 'profit before shareholder tax attributable to shareholders', the Group's reported performance within the consolidated IFRS income statement by business segment and geography.

	2005			
	UK	US	Asia	Total
	(In £ Millions)			
Long term business:				
Performance measure: operating profit based on longer-term investment returns	400	348	175	923
Goodwill impairment charge				
Short-term fluctuations in investment returns	36	178	32	246
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(20)		3	(17)
Reported performance: profit before tax attributable to shareholders	416	526	210	1,152
Banking:				
Performance measure: operating profit based on longer-term investment returns	44			44
Goodwill impairment charge				
Short-term fluctuations in investment returns				
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes				
Reported performance: profit before tax attributable to shareholders	44			44
Broker-dealer and fund management:				
Performance measure: operating profit based on longer-term investment returns	163	14	12	189
Goodwill impairment charge				
Short-term fluctuations in investment returns	(1)		(8)	(9)
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(26)			(26)
Reported performance: profit before tax attributable to shareholders	136	14	4	154
Unallocated corporate:				
Performance measure: operating profit based on longer-term investment returns	(199)			(199)
Goodwill impairment charge	(120)			(120)
Short-term fluctuations in investment returns	(26)			(26)
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(7)			(7)
Reported performance: profit before tax attributable to shareholders	(352)			(352)
Total:				
Performance measure: operating profit based on longer-term investment returns	408	362	187	957
Goodwill impairment charge	(120)			(120)
Short-term fluctuations in investment returns	9	178	24	211
	(53)		3	(50)

	2005			
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes				
Reported performance: profit before tax attributable to shareholders	244	540	214	998

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	2004			
	UK	US	Asia	Total
	(In £ Millions)			
Long term business:				
Performance measure: operating profit based on longer-term investment returns	305	296	102	703
Goodwill impairment charge				0
Short-term fluctuations in investment returns	29	61	37	127
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes			2	2
Reported performance: profit before tax attributable to shareholders	334	357	141	832
Banking:				
Performance measure: operating profit based on longer-term investment returns	61			61
Goodwill impairment charge				0
Short-term fluctuations in investment returns				0
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes				0
Reported performance: profit before tax attributable to shareholders	61	0	0	61
Broker-dealer and fund management:				
Performance measure: operating profit based on longer-term investment returns	136	(14)	19	141
Goodwill impairment charge				0
Short-term fluctuations in investment returns		9		9
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(1)			(1)
Reported performance: profit before tax attributable to shareholders	135	(5)	19	149
Unallocated corporate:				
Performance measure: operating profit based on longer-term investment returns	(197)			(197)
Goodwill impairment charge				0
Short-term fluctuations in investment returns	13			13
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(8)			(8)
Reported performance: profit before tax attributable to shareholders	(192)	0	0	(192)
Total:				
Performance measure: operating profit based on longer-term investment returns	305	282	121	708
Goodwill impairment charge				0
Short-term fluctuations in investment returns	42	70	37	149
Shareholders' share in actuarial and other gains and losses on defined benefit pension schemes	(9			