I: Other notes

I1: Staff and pension plans

a Staff and employment costs

The average number of staff employed by the Group during the year were:

	2008	2007
Business operations:		
UK operations	6,231	7,732
US operations	3,298	3,123
Asian operations	20,154	16,807
Venture fund investment subsidiaries of the PAC with-profits fund (see below)	–	21,184
Continuing operations	29,683	48,846
Discontinued banking operations	–	770
Total	29,683	49,616

The costs of employment for continuing operations were:

	2008 £m	2007 £m
Business operations:		
Wages and salaries	791	819
Social security costs	54	62
Other pension costs (see below)	78	96
Pension actuarial and other (gains) losses charged to income statement	(10)	2
	68	98
Venture fund investment subsidiaries of the PAC with-profits fund (see below)	–	423
Total for continuing operations	913	1,402
Discontinued banking operations	–	21
Total	913	1,423

Other pension costs comprises £47 million (2007: £68 million) relating to defined benefit schemes and £31 million (2007: £28 million) relating to defined contribution schemes of continuing operations. Of the defined contribution scheme costs, £21 million (2007: £19 million) related to overseas defined contribution schemes. The £47 million (2007: £68 million) comprises a charge of £29 million (2007: £41 million) relating to PSPS and a charge of £18 million (2007: £27 million) for other schemes.

Consistent with the derecognition of the Company's interest in the underlying IAS 19 surplus of PSPS as described in note (b)(i)1 below, the £29 million (2007: £41 million) for PSPS represents the cash cost of contributions for ongoing service of active members and the unwind of discount on the opening provision for deficit funding for PSPS. The charge of £18 million (2007: £27 million) for other schemes comprises a £7 million (2007: £17 million) charge on an economic basis, reflecting the total assets of the schemes, and a further £11 million (2007: £10 million) charge to adjust for amounts invested in Prudential insurance policies to arrive at the IAS 19 basis charge.

The gains of £10 million (2007: loss of £2 million) for actuarial and other gains comprises a loss of £21 million (2007: loss of £7 million) for actuarial and other losses on an economic basis and £31 million actuarial gains (2007: gain of £5 million) to adjust for amounts invested in Prudential insurance policies. The derivation of these amounts is shown in note (b)(i)7 below.

Of the £423 million costs of employment for venture fund investment subsidiaries in 2007, £349 million related to wages and salaries, £70 million related to social security costs and £4 million related to pension costs. Following the change of control arrangements put in place at the same time as the sale by the Group of PPM Capital in November 2007, the Group no longer controls those venture fund investment subsidiaries managed by the sold entity and consequently ceased to consolidate these operations subsequent to this, with the average number of staff employed and costs of employment for 2007 detailed above reflecting the period prior to disposal.

Of the £21 million costs of employment for discontinued banking operations in 2007, £18 million related to wages and salaries, £2 million related to social security costs and £1 million related to pension costs.

b Pension plans

i Defined benefit plans

1 Summary and the effects of the adoption of IFRIC 14

The Group business operations operate a number of pension schemes. The specific features of these plans vary in accordance with the regulations of the country in which the employees are located, although they are, in general, funded wholly by the Group and based either on a cash balance formula or on years of service and salary earned in the last year or years of employment. The largest defined benefit scheme is the principal UK scheme, namely the Prudential Staff Pension Scheme (PSPS), 87 per cent (2007: 87 per cent) of the underlying scheme liabilities of the Group defined benefit schemes are accounted for within PSPS.

I1: Staff and pension plans continued

The Group also operates two smaller defined benefit schemes for UK employees in respect of Scottish Amicable and M&G activities. For all three schemes the projected unit method was used for the most recent full actuarial valuations. There is also a small defined benefit scheme in Taiwan.

Defined benefit schemes in the UK are generally required to be subject to full actuarial valuation every three years in order to assess the appropriate level of funding for schemes in relation to their commitments. These valuations include assessments of the likely rate of return on the assets held within the separate trustee administered funds. PSPS was last actuarially valued as at 5 April 2005. This valuation demonstrated the scheme to be 94 per cent funded, with a shortfall of actuarially determined assets to liabilities of six per cent, representing a deficit of £243 million.

As a result, changes were made to the basis of funding for the scheme with effect from that date. Based on that valuation, deficit funding amounts designed to eliminate the actuarial deficit over a 10 year period have been and are being made. Total contributions to the Scheme for deficit funding and employer's contributions for ongoing service for current employees are expected to be of the order of £70-75 million per annum subject to a reassessment when the subsequent valuation is completed. In 2008, total contributions for the year including expenses and augmentations were £79 million (2007: £82 million). Deficit funding for PSPS is apportioned in the ratio of 70/30 between the PAC life fund and shareholder-backed operations following detailed consideration in 2005 of the sourcing of previous contributions. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity. The PSPS valuation as at 5 April 2008 is currently being finalised.

The deficit of the Scottish Amicable Pension Scheme of £44 million (2007: £54 million) has been allocated 50 per cent to the PAC with-profits fund and 50 per cent to the PAC shareholders fund.

The adoption of IFRIC 14

As mentioned in notes A2 and A5, the Group has adopted IFRIC 14 for pension schemes in 2008. The adoption of IFRIC 14, which gives guidance on assessing the limit in IAS 19 on the amount of surplus in a defined benefit pension scheme that can be recognised as an asset thereby providing reliable and more relevant information. The recognition of an asset is restricted to those that are demonstrably recoverable, either by refund or reduction in future contributions. It also addresses when a minimum funding requirement might give rise to a liability. The assessment of recoverability and any additional liability is made by reference to the terms of the Trust Deed of pension schemes and, unless substantively enacted or contractually agreed, with no account taken of potential changes to current funding arrangements.

This adoption of the principles of IFRIC 14 has had an effect on the Group's interest in the financial position of the Group's main UK defined benefit pension scheme, PSPS. The change relates solely to the accounting measurement of the Group's interest in the financial position of PSPS. Adoption of the principles of IFRIC 14 does not affect the Group's interest in the Group's other defined benefit pension schemes.

Under the terms of the Trust Deed, the Group has no unconditional right of refund to any surplus in PSPS. Also, the Group has no ability under the guidance in IFRIC 14 to anticipate a reduction in the level of future contributions for ongoing services from those currently being paid. In addition, the Group currently has a committed five-year deficit funding arrangement in place as agreed with the Trustees of the PSPS following the last triennial valuation of PSPS as at 5 April 2005.

The asset and liabilities of PSPS are unaffected by the impact of the adoption of IFRIC 14. PSPS is managed on an economic basis for the longer-term benefit of its current and deferred pensioners and active members. The surplus in PSPS is available to absorb future adverse asset value movements and, if required, strengthening in mortality assumptions. The fluctuating nature of the surplus is demonstrated by the increase in the underlying gross surplus from £528m at 31 December 2007 to £728m at 31 December 2008.

The summary effect of the adoption of IFRIC 14

In respect of the position at 31 December 2008, the Group has not recognised the underlying PSPS pension surplus of £728 million (£615 million net of deferred tax), reflecting the difference between the market value of the scheme assets and the discounted value of the liabilities, which would have otherwise been recognised as an asset on its balance sheet under the previous policy. In addition, the Group has recognised a liability for deficit funding to 5 April 2010 of £65 million (£55 million net of deferred tax) in respect of PSPS. Of these, the amounts attributable to shareholders are £223 million (£160 million net of deferred tax) for the surplus not recognised as an asset and £20 million (£15 million net of deferred tax) for the additional liability for deficit funding. In total the impact on shareholders' equity at 31 December 2008 is a reduction of £175 million as shown below.

The 2007 comparative figures in these consolidated financial statements have been adjusted accordingly for the adoption of IFRIC 14.

The effect of the change on the consolidated income statement, earnings per share and consolidated balance sheet are as follows:

Consolidated income statement	2008 Adjustments incorporated in the results	2007 Adjustments made to the previously published results
	Increase (decrease) in profit (£m)	
Investment return	47	4
Benefit and claims and movement in unallocated surplus of with-profits funds	66	205
Other operating expenditure	(173)	(336)
Profit (loss) before tax *(being tax attributable to shareholders' and the policyholders' returns)*	(60)	(127)
Tax attributable to policyholders' returns	11	24
Profits (loss) before tax attributable to shareholders	(49)	(103)
Tax attributable to shareholders' (loss) profit	13	28
Profit (loss) from continuing operations after tax/profit (loss) for the year	(36)	(75)

Earnings per share	Increase (decrease) in earnings per share (in pence)	
Basic and diluted based on profit (loss) from continuing operations attributable to equity holders of the company	(1.5)p	(3.1)p

Consolidated balance sheet	Increase (decrease) in shareholders' equity (£m)	
Deferred tax assets	10	26
Other debtors	(625)	(388)
Policyholders' liability – contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	(103)	(140)
Unallocated surplus of with-profits funds	495	392
Deferred tax liabilities	113	73
Provisions	(65)	(102)
Shareholders' equity	(175)	(139)

Effect on the Group's supplementary analysis of profit and movements in shareholders' equity

	2008 £m			2007 £m		
	Previous basis	Effect of adoption of IFRIC 14	Revised basis	As previously published	Effect of adoption of IFRIC 14	After change
Operating profit based on longer-term investment returns	1,371	(24)	1,347	1,213	(12)	1,201
Short-term fluctuations in investment returns on shareholder-backed business	(1,783)	–	(1,783)	(137)	–	(137)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	11	(25)	(14)	90	(91)	(1)
(Loss) profit before tax	(401)	(49)	(450)	1,166	(103)	1,063
Tax	46	13	59	(382)	28	(354)
(Loss) profit after tax	(355)	(36)	(391)	784	(75)	709
Profits from discontinued operations	–	–	–	241	–	241
Less minority interests	(5)	–	(5)	(3)	–	(3)
(Loss) profit for the year	(360)	(36)	(396)	1,022	(75)	947
Other movements in reserves	(608)	–	(608)	(309)	–	(309)
Shareholders' equity at the beginning of the year	6,201	(139)	6,062	5,488	(64)	5,424
Shareholders' equity at the end of the year	5,233	(175)	5,058	6,201	(139)	6,062

I1: Staff and pension plans continued

As at 31 December 2008, after the effect of the adoption of IFRIC 14, the shareholders' share of the pension liability for PSPS deficit funding obligation and the deficits of the defined benefit pension schemes amounted to a £61 million liability net of related tax relief (2007: £63 million). These amounts are determined after including amounts invested by the M&G scheme in Prudential policies as explained later in this note.

On the economic basis (including investments of the M&G scheme in Prudential policies as assets) for 2008, a £26 million (2007: £35 million) pre-tax shareholder charge to operating results based on longer-term returns arises. In addition, outside the operating result but included in total profits is a pre-tax shareholder loss of £14 million (2007: £1 million).

In addition, also on the economic basis, the PAC with-profits sub-fund was charged £10 million (2007: charge of £23 million) for its share of the pension charge of PSPS and Scottish Amicable and charged with £7 million (2007: £6 million) for its share of net actuarial and other losses on the scheme assets and liabilities. As shareholder profits for the PAC with-profits sub-fund reflects the surplus for distribution, these amounts are effectively absorbed by an increased charge in the income statement for the transfer to the liability for unallocated surplus.

At 31 December 2008, after the effect of the adoption of IFRIC 14, the total share of the liability for deficit funding on PSPS and the deficit on the smaller Scottish Amicable Scheme attributable to the PAC with-profits fund amounted to a liability of £60 million (2007: £88 million) net of related tax relief.

2 Corporate governance

The rules of the Group's largest pension arrangement, the defined benefit section of PSPS, a final salary scheme, specify that, in exercising its investment powers, the Trustee's objective is to achieve the best overall investment return consistent with the security of the assets of the scheme. In doing this, regard is had to the nature and duration of the scheme's liabilities. The Trustee sets the benchmark for the asset mix, following analysis of the liabilities by the Scheme's Actuary and, having taken advice from the Investment Managers, then selects benchmark indices for each asset type in order to measure investment performance against a benchmark return.

The Trustee reviews strategy, the asset mix benchmark and the Investment Managers' objectives every three years, to coincide with the Actuarial Valuation, or earlier if the Scheme Actuary recommends. Interim reviews are conducted annually based on changing economic circumstances and financial market levels.

The Trustee sets the general investment policy and specifies any restrictions on types of investment and the degrees of divergence permitted from the benchmark, but delegates the responsibility for selection and realisation of specific investments to the Investment Managers. In carrying out this responsibility, the Investment Managers are required by the Pensions Act 1995 to have regard to the need for diversification and suitability of investments. Subject to a number of restrictions contained within the relevant asset management agreements, the Investment Managers are authorised to invest in any class of investment asset. However, the Investment Managers will not invest in any new class of investment asset without prior consultation with the Trustee.

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

The investment policies and strategies for the other two UK defined benefit schemes, the M&G Group Pension Scheme and the Scottish Amicable Staff Pension Scheme, which are both final salary schemes, follow similar principles, but have different target allocations reflecting the particular requirements of the schemes.

3 Assumptions

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

	2008 %	2007 %
Discount rate*	6.1	5.9
Rate of increase in salaries	5.0	5.3
Rate of inflation	3.0	3.3
Rate of increase of pensions in payment for inflation:		
Guaranteed (maximum 5%)	3.0	3.3
Guaranteed (maximum 2.5%)†	2.5	2.5
Discretionary†	2.5	2.5
Expected returns on plan assets	6.2	5.9

* The discount rate of 6.1% has been determined by reference to an 'AA' corporate bond index adjusted to allow for the difference in duration between the index and the pension liabilities.

† The rates of 2.5 per cent shown are those for PSPS. Assumed rates of increase of pensions in payment for inflation for all other schemes are 3.0 per cent in 2008 (2007: 3.3 per cent).

The calculations are based on current actuarially calculated mortality estimates with a specific allowance made for future improvements in mortality, which is broadly in line with that adopted for the 92 series of mortality tables prepared by the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries. In 2007, the mortality assumptions were strengthened by including a floor to the medium cohort improvements.

The tables used for PSPS at 31 December 2008 were:

Male: 100 per cent PMA92 with CMIR17 improvements to the valuation date and medium cohort improvements subject to a floor of 1.75 per cent up to the age of 90, decreasing linearly to zero by age of 120; and
Female: 100 per cent PFA92 with CMIR17 improvements to the valuation date and 75 per cent medium cohort improvements subject to a floor of one per cent up to the age of 90 and decreasing linearly to zero by age of 120.

The assumed life expectancies on retirement at age 60, based on the mortality table used was:

	2008 years		2007 years	
	Male	Female	Male	Female
Retiring today	26.4	28.4	26.2	28.3
Retiring in 15 years' time	28.9	29.8	28.7	29.3

The mean term of the current PSPS liabilities is around 18 years.

Using external actuarial advice provided by Watson Wyatt Partners for the valuation of PSPS and by Aon Limited for the M&G scheme, and Hazell Carr for the Scottish Amicable scheme, the most recent full valuations have been updated to 31 December 2008, applying the principles prescribed by IAS 19.

4 Summary financial position

The Group liability in respect of defined benefit pension schemes is as follows:

	2008 £m	2007 £m
Economic position:		
Deficit, gross of deferred tax, based on scheme assets held, including investments in Prudential insurance policies:		
Attributable to the PAC with-profits fund (i.e. absorbed by the liability for unallocated surplus)	(67)	(98)
Attributable to shareholder-financed operations (i.e. to shareholders' equity)	(82)	(85)
Economic deficit – as explained in note 5 below	(149)	(183)
Add back: investments in Prudential insurance policies (offset on consolidation in the Group financial statements against insurance liabilities)	(157)	(172)
Deficit included in balance sheet under IAS 19 – as explained in note 7 below	(306)	(355)

The following disclosures explain the economic position and IAS 19 basis of accounting after eliminating investment in Prudential insurance policies on consolidation.

5 Group economic financial position

The economic financial position of the defined benefit pension schemes reflects the total assets of the schemes including investments in Prudential policies. This is to be contrasted with the IAS 19 basis assets of the M&G schemes, as consolidated into the Group balance sheet, which exclude investments in Prudential insurance policies which on the financial statement presentation are offset against policyholder liabilities.

The M&G pension scheme has invested £157 million at 31 December 2008 (2007: £172 million) in Prudential insurance policies. As required by IFRS, this amount of scheme asset is eliminated against the policyholder liability and hence, for the purposes of preparing the consolidated balance sheet, the IAS 19 basis net pension liability is £157 million (2007: £172 million) lower than the 'economic basis' deficit of £149 million (2007: 'economic basis' deficit of £183 million). Additionally, the PSPS scheme has invested £103 million at 31 December 2008 (2007: £140 million) in Prudential insurance policies. However, these assets are not recognised due to the effects of the change in accounting policy for the adoption of IFRIC 14 as described in note 1 above.

I1: Staff and pension plans continued

On the 'economic basis', after including the underlying assets represented by the investments in Prudential insurance policies as scheme assets, the underlying balance sheets of the schemes at 31 December were:

	2008 £m				2007 £m			
	PSPS	Other schemes note iii	Total	%	PSPS	Other schemes note iii	Total	%
Equities	823	213	1,036	19	1,278	265	1,543	28
Bonds	2,430	277	2,707	51	1,134	249	1,383	25
Properties	283	18	301	6	545	54	599	11
Cash-like investments note i	1,267	6	1,273	24	1,932	5	1,937	36
Total value of assets	4,803	514	5,317	100	4,889	573	5,462	100
Present value of benefit obligations	(4,075)	(598)	(4,673)		(4,361)	(654)	(5,015)	
	728	(84)	644		528	(81)	447	
Effect of the adoption of IFRIC 14 for pension schemes:								
Derecognition of PSPS surplus	(728)	–	(728)		(528)	–	(528)	
Set up obligation for deficit funding for PSPS until 5 April 2010	(65)	–	(65)		(102)	–	(102)	
Pre-tax deficit note ii	(65)	(84)	(149)		(102)	(81)	(183)	

Notes

i The PSPS has entered into a derivatives based strategy to match the duration and inflation profile of its liabilities. This involved a reallocation from other investments to cash-like investments with an interest and inflation swap overlay. In broad terms, the scheme is committed to making a series of payments related to LIBOR on a nominal amount and in return the scheme receives a series of fixed and inflation-linked payments which match a proportion of its liabilities. As at 31 December 2008, the nominal value of the interest and inflation-linked swaps amounted to £1.2 billion (2007: £1.2 billion) and £0.3 billion (2007: £0.7 billion) respectively.

ii The resulting scheme deficit arising from the excess of liabilities over assets at 31 December 2008 of £149 million comprised a deficit of £67 million (2007: deficit of £98 million) attributable to the PAC with-profits fund and deficit of £82 million (2007: deficit of £85 million) attributable to shareholder operations.

iii In addition to PSPS, there are two smaller schemes in the UK, the Scottish Amicable Pension Scheme, and the M&G Pension Scheme, with a combined deficit at 31 December 2008 of £67 million (2007: £71 million), gross of tax. There is also a small scheme in Taiwan, which at 31 December 2008 had a deficit of £17 million (2007: £10 million), gross of tax.

The movements in the deficit on the 'economic basis' between scheme assets and liabilities were:

	2008 %	2007 %
Current service cost	(19)	(19)
Curtailment credit	14	–
Other finance income	(2)	2
Cash costs and unwind of discount on opening provision for deficit funding for PSPS	(29)	(41)
Contributions	95	101
Actuarial and other gains and losses	(21)	(7)
Exchange translation difference	(4)	–
Net increase in deficit	34	36

Estimated pension scheme deficit attributable to shareholder operations – economic basis

Movements on the pension scheme deficit (determined on the 'economic basis'), to the extent attributable to shareholder operations are as follows:

	2008 £m					
	At beginning of year	Charge to operating results (based on longer-term investment returns) note i	Actuarial and other gains (losses) attributable to shareholders note ii	Contributions paid by shareholder operations	Exchange translation difference	At end of year
Gross of tax deficit	(85)	(26)	(14)	47	(4)	(82)
Related deferred tax	22	7	5	(13)	–	21
Net of tax deficit	(63)	(19)	(9)	34	(4)	(61)

	2007 £m				
	At beginning of year	Charge to operating results (based on longer-term investment returns) note i	Actuarial and other gains (losses) attributable to shareholders note ii	Contributions paid by shareholder operations	At end of year
Gross of tax deficit	(99)	(35)	(1)	50	(85)
Related deferred tax	27	8	1	(14)	22
Net of tax deficit	(72)	(27)	–	36	(63)

Notes

i Charge to operating results (based on longer-term investment returns)

This comprises:

	2008 £m	2007 £m
Current service cost	(19)	(19)
Curtailment credit	14	–
Finance income (expense):		
Interest on pension scheme liabilities	(39)	(31)
Expected return on pension scheme assets	37	33
	(2)	2
Total credit net of finance income	(7)	(17)
Cash cost and unwind of discount on opening provision for deficit funding for PSPS*	(29)	(41)
Less: amount attributable to PAC with-profits fund	10	23
Charge to operating results, based on longer-term investment returns, attributable to shareholders	(26)	(35)

* Consistent with the derecognition of the Company's interest in the underlying IAS 19 surplus of PSPS, the effect of the accounting policy change on the operating results, based on longer-term investment returns, is to replace the usual IAS 19 pension charges and credits with the cash cost of contributions for ongoing service of active members. In addition, the charge to the operating results also includes a charge for the unwind of discount on the opening provision for deficit funding for PSPS.

I1: Staff and pension plans continued

Notes continued

ii Actuarial and other gains and losses

This comprises:

	2008 £m	2007 £m
Actuarial gains and losses:		
Actual less expected return on pension scheme assets	(97)	4
Experience gains (losses) on scheme liabilities	18	(4)
Changes in assumptions underlying the present value of scheme liabilities[a]	71	(7)
Total actuarial losses	(8)	(7)
Less: amount attributable to PAC with-profits fund	(2)	6
	(10)	(1)
Other gains and losses:		
Change in the provision for deficit funding for PSPS[b]	(13)	–
Less: amount attributable to PAC with-profits fund	9	–
	(4)	–
Actuarial gains and losses attributable to shareholders, excluded from operating results based on longer-term investment returns, but included in profit before tax attributable to shareholders[b]	(14)	(1)

a The gains of £71 million relating to changes in assumptions comprise the gains due to the effect of an increase in the risk discount rate combined with the effect of decreases in inflation rates.

b The amounts of actuarial gains and losses shown in the table above relate to Scottish Amicable, M&G and a small Taiwan defined benefit pension scheme. Consistent with the derecognition of the underlying IAS 19 surplus of PSPS, the amounts do not include actuarial gains and losses for PSPS. In addition, as a result of the adoption of IFRIC 14, the Group has recognised a provision for deficit funding to 5 April 2010 in respect of PSPS. The change in the period in relation to this provision is recognised above as other gains and losses on defined benefit pension schemes.

Since shareholder profits in respect of the PAC with-profits fund are a function of the actuarially determined surplus for distribution, the overall income statement result is not directly affected by the level of pension cost or other expenses attributable to the fund.

Estimated pension scheme deficit attributable to PAC with-profits fund – economic basis

Movements on the pension scheme deficit determined on the 'economic basis' are as follows:

	2008 £m				
	At beginning of year	Pension charge (credit) note i above	Actuarial and other gains (losses) note ii above	Contributions paid by PAC with-profits fund	At end of year
Gross of tax deficit	(98)	(10)	(7)	48	(67)
Related deferred tax	10	1	1	(5)	7
Net of tax deficit	(88)	(9)	(6)	43	(60)

	2007 £m				
	At beginning of year	Pension charge (credit) note i above	Actuarial and other gains (losses) note ii above	Contributions paid by PAC with-profits fund	At end of year
Gross of tax deficit	(120)	(23)	(6)	51	(98)
Related deferred tax	12	2	1	(5)	10
Net of tax deficit	(108)	(21)	(5)	46	(88)

The pension charges and credits which comprise service costs less net finance income for the Scottish Amicable Scheme and the cash costs and unwind of discount on pension provision for deficit funding for PSPS, and actuarial and other gains and losses are included within the income statement but also taken account of in determining the charge in the income statement for the transfer to the liability for unallocated surplus of with-profits funds.

6 Movement in IAS 19 basis financial position

The change in the present value of the benefit obligation and the change in fair value of the assets for the total of the PSPS, Scottish Amicable, M&G and Taiwan schemes over the period were as follows:

	2008 £m					
	PSPS	Other schemes				Total
	Provision for deficit funding	IAS 19 basis: change in fair value of plan assets	Investments in Prudential insurance policies	Economic basis: total assets	IAS 19 basis: change in present value of benefit obligations	Economic basis: net obligations
Fair value of plan assets, beginning of year		401	172	573		573
Present value of benefit obligation, beginning of year					(654)	(654)
Provision for deficit funding for PSPS	(102)					(102)
	(102)	401	172	573	(654)	(183)
Service cost – current charge only					(19)	(19)
Curtailment credit					14	14
Interest cost					(39)	(39)
Expected return on plan assets		26	11	37		37
Employee contributions			1	1	(1)	–
Employer contributions	79	7	9	16		95
Actuarial gains (losses)		(67)	(31)	(98)	90	(8)
Benefit payments		(10)	(5)	(15)	15	–
Cash costs and unwind of discount on the opening provision for deficit funding for PSPS	(29)					(29)
Movement in the provision for deficit funding for PSPS	(13)					(13)
Exchange translation difference					(4)	(4)
Fair value of plan assets, end of year		357	157	514		514
Present value of benefit obligation, end of year					(598)	(598)
Provision for deficit funding of PSPS	(65)					(65)
Economic basis deficit						(149)

I1: Staff and pension plans continued

	2007 £m					
	PSPS	Other schemes				Total
	Provision for deficit funding	IAS 19 basis: change in fair value of plan assets	Investments in Prudential insurance policies	Economic basis: total assets	IAS 19 basis: change in present value of benefit obligations	Economic basis: net obligations
Fair value of plan assets, beginning of year		366	161	527		527
Present value of benefit obligation, beginning of year					(603)	(603)
Provision for deficit funding for PSPS	(143)					(143)
	(143)	366	161	527	(603)	(219)
Service cost – current charge only					(19)	(19)
Interest cost					(31)	(31)
Expected return on plan assets		23	10	33		33
Employee contributions			1	1	(1)	–
Employer contributions	82	10	9	19		101
Actuarial gains (losses)		9	(5)	4	(11)	(7)
Benefit payments		(7)	(4)	(11)	11	–
Cash costs and unwind of discount on the opening liability for deficit funding for PSPS	(41)					(41)
Fair value of plan assets, end of year		401	172	573		573
Present value of benefit obligation, end of year					(654)	(654)
Provision for deficit funding for PSPS	(102)					(102)
Economic basis deficit						(183)

7 IAS 19 basis financial position as consolidated

The IAS 19 basis pensions deficit can be summarised as follows:

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Fair value of plan assets, end of year	**5,057**	5,150	4,988	4,622	4,092
Present value of funded benefit obligation	**(4,493)**	(4,826)	(5,023)	(5,228)	(4,777)
Funded status	**564**	324	(35)	(606)	(685)
Present value of unfunded obligations (M&G scheme)*	**(180)**	(189)	(187)	(190)	(140)
	384	135	(222)	(796)	(825)
Effect of the change in accounting policy for pension schemes:					
Derecognition of PSPS' surplus	**(728)**	(528)	(141)	–	–
Set up obligation for deficit funding for PSPS until 5 April 2010	**(65)**	(102)	(143)	–	–
Adjustment in respect of investment of PSPS in Prudential policies	**103**	140	126	–	–
Deficit recognised in the balance sheet	**(306)**	(355)	(380)	(796)	(825)

* The M&G pension scheme assets are invested in Prudential insurance policies. For IFRS accounting purposes, the M&G scheme is in effect unfunded. Please see above for more details.

	2008 £m	2007 £m
Components of net periodic pension cost		
Current service cost	(45)	(58)
Curtailment credit	44	–
Interest cost	(289)	(265)
Expected return on assets – economic basis	336	309
Less: expected return on investments of scheme assets in Prudential insurance policies	(22)	(20)
Expected return on assets – IAS 19 basis†	314	289
	24	(34)
Effect of the adoption of IFRIC 14	(71)	(34)
Pension cost (as referred to in note I1a)	(47)	(68)
Actuarial gains and losses – economic basis	60	295
Less: actuarial losses on investments of scheme assets in Prudential insurance policies	79	1
	139	296
Effect of the adoption of IFRIC 14	(129)	(298)
Actuarial gains and losses – IAS 19 basis* (as referred to in note I1a)	10	(2)
Net periodic pension cost (included within acquisition and other operating expenditure in the income statement)	(37)	(70)

* Consistent with the derecognition of the Company's interest in the underlying IAS 19 surplus of PSPS, the effect on the net periodic pension cost for PSPS was to replace the usual IAS 19 pension charges and credits with the cash cost of contribution for ongoing services of active members and also not to report the actuarial gains and losses.

† In determining the expected return on scheme assets for 2008, the 5.9 per cent rate shown below has been applied to the opening assets.

The long-term expected rate of return has been taken to be the weighted average (by market value) of the long-term expected rates of return on each major asset class shown below:

	2008		2007		2006		2005		2004	
	£m	%	£m	%	£m	%	£m	%	£m	%
Scheme assets (IAS 19 basis before effect of adoption of IFRIC 14)										
Equity	875	17	1,332	26	1,432	29	2,376	51	2,516	61
Bonds	2,619	52	1,299	25	2,185	44	1,593	35	993	24
Properties	290	6	583	11	621	12	575	12	520	13
Cash-like investments	1,273	25	1,936	38	750	15	78	2	63	2
Total	5,057	100	5,150	100	4,988	100	4,622	100	4,092	100

	Prospectively for 2009 %	2008 %	2007 %
Long-term expected rate of return			
Equity	6.8	7.5	7.5
Bonds	4.8	5.4	4.8
Properties	6.05	6.75	6.8
Cash	2.0	5.5	5.0
Weighted average long-term expected rate of return	4.5	6.1	5.9

The expected rates of return have been determined by reference to long-term expectations, the carrying value of the assets and equity and other market conditions at the balance sheet date.

The actual return on scheme assets was a loss £20 million (2007: gain of £282 million) on an IAS 19 basis.

I1: Staff and pension plans continued

None of the scheme assets included shares in Prudential plc or property occupied by the Prudential Group.

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Fair value of scheme assets, end of year (IAS 19 basis)	5,057	5,150	4,988	4,622	4,092
Present value of the benefit obligation, end of year	(4,673)	(5,015)	(5,210)	(5,418)	(4,917)
Underlying scheme assets in surplus (deficit) of benefit obligation, before the effect of the adoption of IFRIC 14	384	135	(222)	(796)	(825)
Experience adjustments on scheme	**145**	(14)	18	1	(17)
Percentage of scheme liabilities at 31 December	**3.10%**	0.28%	(0.35)%	(0.02)%	0.35%
Experience adjustments on scheme assets (IAS 19 basis)	**(277)**	(7)	140	527	112
Percentage of scheme assets at 31 December	**(5.48)%**	(0.14)%	2.81%	11.42%	2.74%

The experience adjustments on scheme liabilities in 2008 of a gain of £145 million relate mainly to the 'true up' reflecting improvements in data consequent upon the ongoing triennial valuation of PSPS.

Total employer contributions expected to be paid into the Group defined benefit schemes for the year ending 31 December 2009 amounts to £98 million (2008: £90 million), subject to a reassessment when the valuation at 5 April 2008 is completed.

8 Sensitivity of the financial position of the PSPS, Scottish Amicable and M&G pension schemes to key variables

The table below shows the sensitivity of the underlying PSPS, Scottish Amicable and M&G pension scheme liabilities at 31 December 2008 of £4,075 million, £398 million and £180 million respectively (2007: £4,361 million, £454 million and £189 million) to changes in discount rates and inflation rates.

2008			
Assumption	**Change in assumption**	**Impact on scheme liabilities on IAS 19 basis**	
Discount rate	Decrease by 0.2% from 6.1% to 5.9%	Increase in scheme liabilities by:	
		PSPS	3.3%
		Scottish Amicable	4.9%
		M&G	4.5%
Discount rate	Increase by 0.2% from 6.1% to 6.3%	Decrease in scheme liabilities by:	
		PSPS	3.1%
		Scottish Amicable	4.6%
		M&G	4.2%
Rate of inflation	Decrease by 0.2% from 3.0% to 2.8% with consequent reduction in salary increases	Decrease in scheme liabilities by:	
		PSPS	0.8%
		Scottish Amicable	4.5%
		M&G	3.8%

2007			
Assumption	**Change in assumption**	**Impact on scheme liabilities on IAS 19 basis**	
Discount rate	Decrease by 0.2% from 5.9% to 5.7%	Increase in scheme liabilities by:	
		PSPS	3.5%
		Scottish Amicable	5.3%
		M&G	4.8%
Discount rate	Increase by 0.2% from 5.9% to 6.1%	Decrease in scheme liabilities by:	
		PSPS	3.4%
		Scottish Amicable	5.1%
		M&G	4.5%
Rate of inflation	Decrease by 0.2% from 3.3% to 3.1% with consequent reduction in salary increases	Decrease in scheme liabilities by:	
		PSPS	1.3%
		Scottish Amicable	5.0%
		M&G	4.4%

9 Transfer value of PSPS scheme

At 31 December 2008, it is estimated that the assets of the scheme are broadly sufficient to cover the liabilities of PSPS on a 'buyout' basis including an allowance for expenses. The 'buyout' basis refers to a basis that might apply in the circumstance of a transfer to another appropriate financial institution. In making this assessment it has been assumed that a more conservative investment strategy applies together with a more prudent allowance for future mortality improvements and no allowance for discretionary pension increases.

ii Other pension plans

The Group operates various defined contribution pension schemes including schemes in Jackson and Asia. As noted earlier, the cost of the Group's contributions for continuing operations to these schemes in 2008 was £31 million (2007: £28 million).

I2: Share-based payments

The Group maintains 10 main share award and share option plans relating to Prudential plc shares, which are described below.

The Group Performance Share Plan (GPSP) is the incentive plan in which all executive directors and other senior executives within the Group can participate. This scheme was established as a replacement for the Restricted Share Plan (RSP) under which no further awards could be made after March 2006. Awards are granted either in the form of a nil cost option, conditional right over shares, or such other form that shall confer to the participant an equivalent economic benefit, with a vesting period of three years. The performance measure for the awards is that Prudential's Total Shareholder Return (TSR) outperforms an index comprising of peer companies. Vesting of the awards between each performance point is on a straight line sliding scale basis. Participants are entitled to the value of reinvested dividends that would have accrued on the shares that vest. Shares are currently purchased in the open market by a trust for the benefit of qualifying employees.

The RSP was, until March 2006, the Group's long-term incentive plan for executive directors and other senior executives designed to provide rewards linked to shareholder return. Each year participants were granted a conditional option to receive a number of shares. There was a deferment period of three years at the end of which the award vested to an extent that depended on the performance of the Group's shares including notional reinvested dividends and on the Group's underlying financial performance. After vesting, the option may be exercised at zero cost at any time, subject to closed period rules, in the balance of a 10-year period. Shares are purchased in the open market by a trust for the benefit of qualifying employees. The RSP replaced the Executive Share Option Scheme in 1995 and all options under this plan had been exercised at 31 December 2005.

No rights were granted in the RSP if the Company's TSR performance as ranked against the comparator group is below 50th percentile. For performance at 50th percentile, an option of 25 per cent of the maximum award is made. The maximum grant is made only if the TSR ranking of the Company is 20th percentile or above. Between these points, the size of the grant of option made is calculated on a straight line sliding scale.

The BUPP is an incentive plan created to provide a common framework under which awards would be made to senior employees and in the UK, Jackson and Asia include the Chief Executive Officers. Awards under this plan in 2007 and 2008 were based on growth in Shareholder Capital Value on the European Embedded Value (EEV) basis with performance measured over three years. Upon vesting, half of the vested award is released as shares and the other half released in cash. Participants are entitled to receive the value of reinvested dividends over the performance period for those shares that vest. The growth parameters for the awards are relevant to each region and vesting of the awards between each performance point is on a straight line sliding scale basis.

UK-based executive directors are eligible to participate in the Prudential HM Revenue & Customs (HMRC) approved UK Savings Related Share Option Scheme (SAYE scheme) and the Asia-based executive directors can participate in the equivalent International SAYE scheme. The schemes allow employees to save towards the exercise of options over Prudential plc shares, at an option price set at the beginning of the savings period at a discount of up to 20 per cent to the market price. Savings contracts may be up to £250 per month for three or five years, or additionally in the UK scheme seven years. On maturity at the end of the set term, participants may exercise their options within six months of the end of the savings period and purchase Prudential plc shares. If an option is not exercised within six months, participants are entitled to a refund of their cash contributions plus interest if applicable under the rules. Shares are issued to satisfy options that are exercised. No options may be granted under the schemes if the grant would cause the number of shares which have been issued, or which remain issuable pursuant to options granted in the preceding 10 years under the scheme and other share option schemes operated by the Company, or which have been issued under any other share incentive scheme of the Company, to exceed 10 per cent of the Company's ordinary share capital at the proposed date of grant.

UK-based executive directors are also eligible to participate in the Company's HMRC approved Share Incentive Plan which allows all UK-based employees to purchase shares of Prudential plc (partnership shares) on a monthly basis out of gross salary. For every four partnership shares bought, an additional matching share is awarded, purchased on the open market. Dividend shares accumulate while the employee participates in the plan. Partnership shares may be withdrawn from the scheme at any time. If the employee withdraws from the plan within five years, the matching shares are forfeit and if within three years, dividend shares are forfeit.

I2: Share-based payments continued

Jackson operates a performance-related share award which, subject to the prior approval of the Jackson Remuneration Committee, may grant share awards to eligible Jackson employees in the form of a contingent right to receive shares or a conditional allocation of shares. These share awards have vesting periods of four years and are at nil cost to the employee. Award holders do not have any right to dividends or voting rights attaching to the shares. The shares are held in the employee share trust in the form of American Depository Receipts which are tradable on the New York Stock Exchange.

The new Prudential Corporation Asia Long-Term Incentive Plan (PCA LTIP) is an incentive plan for senior employees and Chief Executive Officers replacing the Asia Business Unit Performance Plan (BUPP). Awards under the new PCA LTIP will vest after three years subject to the employee being in employment at the time of vesting without any performance conditions. Awards will be discretionary and on a year by year basis determined by Prudential's full year financial results and the employee's contribution to the business. All awards will be in Prudential shares except for countries where share awards are not feasible due to securities and/or tax reasons, where awards will be replaced by the cash value of the shares that would otherwise have been transferred.

Certain senior executives have annual incentive plans with awards paid in cash up to the target level of their plan. The portion of any award for above target performance is made in the form of awards of shares deferred for three years, with the release of shares subject to close periods. The shares are held in the employee share trust and shares equivalent to dividends otherwise payable will accumulate for the benefit of award holders during the deferral period up to the release date.

In addition, there are other share awards which included the 1,000 Day Long Term Incentive Plan (LTIP) and other arrangements.

The 1,000 Day LTIP plan was a UK insurance operations performance-based plan in which the UK Remuneration Committee could, at any time up to 5 October 2005, select employees at its absolute discretion, for participation in the plan. The performance period was 1,000 days and, based on the final performance level being at, or above, the threshold level, the committee shall grant participants 10 per cent of the allocated award in 2005, 20 per cent in 2006 and the remaining 70 per cent in 2007. There are no beneficial interests, or any rights to dividends until such time as the awards are released, at nil cost, to participants. There are no outstanding shares awarded through this scheme.

The other arrangements relate to various awards that have been made without performance conditions to individual employees, typically in order to secure their appointment or ensure retention.

Movements in share options outstanding under the Group's share-based compensation plans relating to Prudential plc shares during 2008 and 2007 were as follows:

Options outstanding (including conditional options)	2008		2007	
	Number of options millions	Weighted average exercise price £	Number of options millions	Weighted average exercise price £
Beginning of year:	14.5	2.57	16.5	2.47
Granted	6.9	3.28	4.0	2.69
Exercised	(3.5)	2.73	(1.9)	3.42
Forfeited	(1.5)	0.69	(1.4)	1.37
Expired	(3.7)	4.94	(2.7)	2.13
End of year	12.7	2.44	14.5	2.57
Options immediately exercisable, end of year	0.6	2.29	0.2	3.35

The weighted average share price of Prudential plc for the year ended 31 December 2008 was £5.46 compared to £7.15 for the year ended 31 December 2007.

Movements in share awards outstanding under the Group's share-based compensation plans relating to Prudential plc shares at 31 December 2008 and 2007 were as follows:

Awards outstanding	2008 Number of awards millions	2007 Number of awards millions
Beginning of year:	8.0	6.6
Granted	3.5	3.8
Exercised	(1.7)	(1.3)
Forfeited	(0.9)	(1.1)
Expired	(0.3)	–
End of year	8.6	8.0

The following table provides a summary of the range of exercise prices for Prudential plc options (including conditional options) outstanding at 31 December 2008.

Range of exercise prices	Outstanding			Exercisable	
	Number outstanding millions	Weighted average remaining contractual life years	Weighted average exercise prices £	Number exercisable millions	Weighted average exercise prices £
Between £0 and £1	5.9	8.3	–	0.3	–
Between £1 and £2	–	–	–	–	–
Between £2 and £3	0.3	1.7	2.66	0.0	2.66
Between £3 and £4	0.5	1.4	3.56	0.0	3.65
Between £4 and £5	4.6	3.3	4.45	0.3	4.07
Between £5 and £6	1.4	2.8	5.59	–	–
Between £6 and £7	0.0	0.4	6.17	0.0	6.17
Between £7 and £8	–	–	–	–	–
	12.7	5.5	2.44	0.6	2.29

The following table provides a summary of the range of exercise prices for Prudential plc options (including conditional options) outstanding at 31 December 2007.

Range of exercise prices	Outstanding			Exercisable	
	Number outstanding millions	Weighted average remaining contractual life years	Weighted average exercise prices £	Number exercisable millions	Weighted average exercise prices £
Between £0 and £1	5.5	8.6	–	–	–
Between £1 and £2	–	–	–	–	–
Between £2 and £3	2.7	1.3	2.66	–	–
Between £3 and £4	1.2	1.7	3.62	0.2	3.37
Between £4 and £5	2.9	2.7	4.62	–	–
Between £5 and £6	2.2	3.5	5.62	–	–
Between £6 and £7	–	0.9	6.55	–	6.95
Between £7 and £8	–	–	–	–	–
	14.5	4.7	2.57	0.2	3.35

The years shown above for weighted average remaining contractual life include the time period from end of vesting period to expiration of contract.

The weighted average fair values of Prudential plc options and awards granted during the period are as follows:

2008 £			2007 £		
Weighted average fair value			Weighted average fair value		
GPSP	Other options	Awards	RSP and GPSP	Other options	Awards
4.16	2.14	5.69	4.78	2.55	7.33

The fair value amounts relating to all options including conditional nil cost options above were determined using the Black-Scholes and the Monte Carlo option-pricing models using the following assumptions:

	2008		2007	
	GPSP	Other options	RSP and GPSP	Other options
Dividend yield (%)	3.60	3.60	2.32	2.32
Expected volatility (%)	30.87	34.67	28.90	27.17
Risk-free interest rate (%)	4.23	4.46	5.46	5.25
Expected option life (years)	3.00	3.74	3.00	3.48
Weighted average exercise price (£)	–	4.74	–	5.62
Weighted average share price (£)	6.63	6.16	7.52	7.47

I2: Share-based payments continued

Under IFRS, compensation costs for all share-based compensation plans are determined using the Black-Scholes model and the Monte Carlo model. Share options and awards are valued using the share price at the date of grant. The compensation costs for all awards and options are recognised in net income over the plans' respective vesting periods. The Group uses the Black-Scholes model to value all options and awards other than the GPSP, for which the Group uses a Monte Carlo model in order to allow for the impact of the TSR performance conditions. These models are used to calculate fair values for share options and awards at the grant date based on the quoted market price of the stock at the measurement date, the amount, if any, that the employees are required to pay, the dividend yield, expected volatility, risk-free interest rates and exercise prices.

The expected volatility is measured as the standard deviation of expected share price returns based on statistical analysis of daily share prices over a period up to the grant date equal to the expected life of options. Risk-free interest rates are UK gilt rates with projections for three, five and seven year terms to match corresponding vesting periods. Dividend yield is determined as the average yield over the year of grant and expected dividends are not incorporated into the measurement of fair value. For the GPSP, volatility and correlation between Prudential and an index constructed from a simple average of the TSR growth of 11 companies is required. For grants in 2008, an average index volatility and correlation of 26 per cent and 82 per cent respectively, were used.

When options are granted or awards made to employees, an estimate is made of what percentage is more than likely to vest, be forfeited, lapse or cancelled based on historical information. Based on these estimates, compensation expense to be accrued at that date is calculated and amortised over the vesting period. For early exercises of options or release of awards due to redundancy, death or resignation, the compensation expense is immediately recognised and for forfeitures due to employees leaving the Group, any previously recognised expense is reversed. However, if an employee loses their award because of the Group's failure to meet the performance criteria, previously recognised expense is not reversed.

During the year, the Group granted share options to certain non-employee independent financial advisors. Those options were measured using the Black-Scholes option pricing model with assumptions consistent with those of other share options. These transactions were measured using an option model because the Group does not receive a separate and measurable benefit from those non-employees in exchange for the options granted. As such, the fair value of the options themselves is more readily determinable than the services received in return.

c Total share-based payment expense

Total expense recognised in the year in the consolidated financial statements related to share-based compensation is as follows:

	2008 £m	2007 £m
Share-based compensation expense	23	28
Amount accounted for as equity-settled	27	19
Carrying value at 31 December of liabilities arising from share-based payment transactions	12	18
Intrinsic value of above liabilities for which rights had vested at 31 December	4	4

I3: Key management remuneration

Key management constitutes the directors of Prudential plc as they have authority and responsibility for planning, directing and controlling the activities of the Group.

Total key management remuneration amounts to £18,122,000 (2007: £15,670,000). This comprises salaries and short-term benefits of £10,425,000 (2007: £9,496,000), post-employment benefits of £1,003,000 (2007: £967,000), leaving benefits of £507,000 (2007: £nil) and share-based payments of £6,187,000 (2007: £5,207,000).

Post-employment benefits comprise the change in the transfer value of the accrued benefit relating to directors' defined benefit pension schemes in the year and the total contributions made to directors' other pension arrangements.

The share-based payments charge is the sum of £4,624,000 (2007: £3,456,000), which is determined in accordance with IFRS 2, 'Share-Based Payments' (see note I2) and £1,563,000 (2007: £1,751,000) of deferred share awards.

Total key management remuneration includes total directors' emoluments of £12,683,000 (2006: £11,959,000) as shown in the directors' remuneration table and related footnotes in the directors' remuneration report, and additional amounts in respect of pensions and share-based payments. Further information on directors' remuneration is given in the directors' remuneration report.

I4: Fees payable to auditor

	2008 £m	2007 £m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	1.6	1.8
Fees payable to the Company's auditor and its associates for other services:		
Audit of subsidiaries and associates pursuant to legislation	5.0	4.4
Other services supplied pursuant to legislation	2.4	2.9
Other services relating to taxation	0.6	0.4
Valuation and actuarial services	0.7	0.7
Services relating to corporate finance transactions	–	0.2
All other services	0.5	1.0
Total	10.8	11.4

In addition, there were fees incurred of £0.2 million (2007: £0.2 million) for the audit of pension schemes.

The Audit Committee regularly monitors the non-audit services provided to the Group by its auditor and has developed a formal Auditor Independence Policy which sets out the types of services that the auditor may provide, consistent with the guidance in Sir Robert Smith's report 'Audit Committees – Combined Code Guidance' and with the provisions of the US Sarbanes-Oxley Act.

The Audit Committee annually reviews the auditor's objectivity and independence. More information on these issues is given in the corporate governance report within this Annual Report.

I5: Related party transactions

Transactions between the Company and its subsidiaries are eliminated on consolidation.

In addition, the Company has transactions and outstanding balances with certain unit trusts, OEICs, collateralised debt obligations and similar entities which are not consolidated and where a Group company acts as manager. These entities are regarded as related parties for the purposes of IAS 24. The balances are included in the Group's balance sheet at fair value or amortised cost in accordance with their IAS 39 classifications. The transactions are included in the income statement and include amounts paid on issue of shares or units, amounts received on cancellation of shares or units and paid in respect of the periodic charge and administration fee. Further details of the aggregate assets, liabilities, revenues, profits or losses and reporting dates of entities considered to be associates under IFRS are disclosed in note H8.

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

Apart from the transactions with directors referred to below, no director had interests in shares, transactions or arrangements that require disclosure, other than those given in the directors' remuneration report. Key management remuneration is disclosed in note I3.

In 2007, prior to disposal, three directors had credit cards with the discontinued banking operations. In 2008 and 2007, other transactions with directors were de-minimis both by virtue of their size and in the context of the directors' financial positions. As indicated above, all of these transactions are on terms broadly equivalent to those that prevail in arm's length transactions.

I6: Subsidiary undertakings

i Principal subsidiaries

The principal subsidiary undertakings of the Company at 31 December 2008, all wholly owned except PCA Life Assurance Company Limited, were:

	Main activity	Country of incorporation
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Annuities Limited*	Insurance	England and Wales
Prudential Retirement Income Limited (PRIL)*	Insurance	Scotland
M&G Investment Management Limited*	Asset management	England and Wales
Jackson National Life Insurance Company*	Insurance	US
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore
PCA Life Assurance Company Limited* (99% owned)	Insurance	Taiwan

* Owned by a subsidiary undertaking of the Company.

I6: Subsidiary undertakings continued

Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for PRIL which operates mainly in England and Wales.

On 20 February 2009, the Company announced that it had entered into an agreement to transfer the assets and liabilities of its agency distribution business and its agency force in Taiwan to China Life Insurance Company Ltd of Taiwan. The business being transferred represents 94 per cent of its in-force liabilities in Taiwan. Further details are set out in note I10.

ii Dividend restrictions and minimum capital requirements

Certain Group subsidiaries are subject to restrictions on the amount of funds they may transfer in the form of cash dividends or otherwise to the parent company. UK insurance companies are required to maintain solvency margins which must be supported by capital reserves and other resources, including unrealised gains on investments. Jackson can pay dividends on its capital stock only out of earned surplus unless prior regulatory approval is obtained. Furthermore, without the prior regulatory approval, dividends cannot be distributed if all dividends made within the preceding 12 months exceed the greater of Jackson's statutory net gain from operations or 10 per cent of Jackson's statutory surplus for the prior year. In 2009, the maximum amount of dividends that can be paid by Jackson without prior regulatory approval is US$290 million (£202 million) (in 2008: US$490 million (£246 million)). The Group's Asian subsidiaries, mainly the Singapore and Malaysia businesses, may remit dividends to the Group, in general, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations.

PAC and Jackson are the two principal insurance subsidiaries of the Group, which together comprise approximately 77 per cent (2007: 78 per cent) of total Group assets. At 31 December 2008, the PAC long-term fund's excess of available capital resources over its regulatory requirement (as per line 42 of Form 2 of the PAC FSA regulatory returns) was estimated to be £4.7 billion (2007: £10.5 billion) and the statutory capital and surplus of Jackson was US$3 billion (£2 billion) (2007: US$4.0 billion (£2.0 billion)). The Group capital position statement for life assurance businesses is set out in note D5.

iii Acquisition and disposal of subsidiaries

2007

On 1 May 2007, the Company completed the sale of Egg Banking plc to Citi. Additional details regarding the disposal are set out in note I9.

On 9 November 2007, the Company completed the sale of PPM Capital, its direct private equity business.

2008

There were no acquisitions or disposals of subsidiaries during the year. Subsequent to the year end, on 20 February 2009, the Company announced that it had entered into an agreement to transfer the assets and liabilities of its agency distribution business and its agency force in Taiwan to China Life Insurance Company Ltd of Taiwan, subject to regulatory approval. Additional details regarding this transfer are set out in note I10.

iv PAC with-profits fund acquisitions and disposals

The PAC with-profits fund acquired a number of venture capital holdings through PPM Capital and M&G. Prior to November 2007, the Group was deemed to have a controlling interest in these venture capital holdings, in aggregate with, if applicable, other holdings held by, for example, the Prudential Staff Pension Scheme. In November 2007, the Group disposed of PPM Capital following which the Group no longer had a controlling interest in venture fund investment subsidiaries that it managed and consequently ceased to consolidate these investments from that date. The Group continues to consolidate, where applicable, the venture capital holdings managed by M&G.

2007

The acquisitions made in 2007 were as follows:

- 71 per cent of the voting equity interest of Orizon AG, an employment hiring agency, which was managed by PPM Capital; and
- 78 per cent of the voting equity interest of Red Funnel, a ferry company, which was managed by M&G.

These acquisitions are considered individually immaterial and therefore all information relating to the acquisitions has been presented in aggregate in this note.

The results of the acquisitions have been included in the consolidated financial statements of the Group and contributed a loss of £8.3 million to earnings within the income statement.

The table below identifies the net assets of these acquisitions and minor business purchases by existing venture holdings and reconciles the net assets to the consideration paid:

	2007 £m Fair value on acquisition
Cash and cash equivalents	20
Other current assets	26
Property, plant and equipment	38
Intangible assets other than goodwill	1
Other non-current assets	3
Less liabilities, including current liabilities and borrowings	(304)
Net assets acquired	(216)
Goodwill	313
Cash consideration	97

Aggregate goodwill of £313 million was recognised for the excess of the cost over the Group's interest in the net fair value of the entities' assets, liabilities, and contingent liabilities acquired.

Following the disposal of PPM Capital, SUSPA, TJ Hughes, Sterigenics, Muller & Weygandt, TMF Group, JOST, Histoire D'or, Azzuri Communications, Paramount plc and Orizon AG ceased to be consolidated as subsidiary undertakings and goodwill and other intangible assets, net of amortisation, relating to these investments were derecognised accordingly.

2008

There were no new acquisitions or disposals of venture capital investments in 2008. However, during the year, the holding in the voting equity interest of Red Funnel increased from 78 per cent to 90 per cent.

I7: Commitments

i Operating leases

The Group leases various offices to conduct its business. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

	2008 £m	2007 £m
Future minimum lease payments for non-cancellable operating leases fall due during the following periods:		
Not later than 1 year	**86**	38
Later than 1 year and not later than 5 years	**199**	126
Later than 5 years	**140**	111

The total minimum future sublease rentals to be received on non-cancellable operating leases for land and buildings for the year ended 31 December 2008 was £0.2 million (2007: £0.4 million).

Minimum lease rental payments for the year ended 31 December 2008 of £84 million (2007: £50 million) are included in the consolidated income statement.

ii Capital commitments

The Group has provided, from time to time, certain guarantees and commitments to third-parties including funding the purchase or development of land and buildings and other related matters. At 31 December 2008, the aggregate amount of contractual obligations to purchase and develop investment properties amounted to £1 million (2007: £64 million).

I8: Cash flows

Structural borrowings of shareholder-financed operations comprise core debt of the parent company and Jackson surplus notes. Core debt excludes borrowings to support short-term fixed income securities programmes and non-recourse borrowings of investment subsidiaries and consolidated investment funds of shareholder-financed operations and other borrowings. Cash flows in respect of these borrowings are included within cash flows from operating activities.

Structural borrowings of with-profits operations relate solely to the £100 million 8.5 per cent undated subordinated guaranteed bonds which contribute to the solvency base of SAIF. Cash flows in respect of other borrowings of with-profits funds, which principally relate to consolidated investment funds are also included within cash flows from operating activities.

Cash flows relating to discontinued operations in 2007, as detailed in note I9, are inflows of £157 million for the period of ownership in 2007. All of these related to cash flows from operating activities.

I9: Discontinued banking operations

Discontinued banking operations in 2007 related entirely to UK banking operations following the sale on 1 May 2007 of Egg Banking plc to Citi. Consideration paid to the Company was, net of expenses, £527 million cash. Cash and cash equivalents disposed of in 2007 were £1,065 million. Accordingly, the cash outflow for the Group in 2007 arising from the disposal of Egg, as shown in the consolidated cash flow statement, was £538 million.

The profit included in the 2007 income statement in respect of discontinued banking operations for the period of ownership was as follows:

	2007 £m
Interest income	261
Interest expense	(148)
Net interest income	113
Fee and commission income	41
Fee and commission expense	(8)
Operating income	146
General administrative expenses	(56)
Impairment losses on loans and cash advances to customers	(149)
Other operating expenses	(9)
Operating loss based on longer-term investment returns	(68)
Profit on sale of Egg Banking plc	290
Profit before tax	222
Tax on operating loss based on longer-term investment returns	19
Tax on profit on sale of Egg Banking plc	0
Tax attributable to shareholders' profits	19
Profit for the year	241

The interest income on financial assets not at fair value through profit and loss for the period of ownership in 2007 was £241 million. The interest expense on financial liabilities not at fair value through profit and loss for the period of ownership in 2007 was £148 million.

Fee and commission income in 2007 includes £27 million relating to financial instruments held at amortised cost. These fees primarily related to balance transfer fees and late payment fees. Fee and commission expense in 2007 includes fee expenses relating to financial liabilities held at amortised cost of £4 million which related to treasury fees.

Of the loss for the period of ownership in 2007, no loss was attributable to minority interests in Egg.

I10: Post balance sheet events

i Intended sale of legacy agency book and agency force in Taiwan to China Life Insurance of Taiwan

On 20 February 2009, the Company announced that it had entered into an agreement to sell the assets and liabilities of its agency distribution business and its agency force in Taiwan to China Life Insurance Company Ltd of Taiwan ('China Life') for the nominal sum of NT$1, subject to regulatory approval.

In addition, the Company will invest £45 million to purchase a 9.95 per cent stake in China Life through a share placement. The business to be transferred represents 94 per cent of Prudential's in-force liabilities in Taiwan and includes its legacy interest rate guaranteed products with IFRS basis gross assets at 31 December 2008 of £4.5 billion. After taking account of IFRS shareholders' funds of the business at 31 December 2008 and restructuring and other costs, the Group's IFRS shareholders' funds are expected to decrease by approximately £595 million. In addition, on completion there will be a net increase in the Company's Insurance Groups Directive surplus of approximately £800 million.

The movement in shareholders' IFRS equity of the total Taiwan life business for 2008 comprised:

	£m
Operating profit based on longer-term investment returns	60
Short-term fluctuations in investment returns	(65)
Shareholders share of actuarial and other gains and losses on defined benefit pension schemes	(3)
Loss before tax	(8)
Total tax	(8)
Loss for the financial year	(16)
Minority interests	–
Investments by Parent Company*	93
Exchange and other reserve movements	111
Net movement	188
Equity brought forward at 1 January 2008	289
Equity carried forward at 31 December 2008	477

* Comprising £66 million for solvency capital and £27 million for business development.

The carrying value of the IFRS equity reflects the application of 'grandfathered' US GAAP under IFRS. This does not, and is not designed to include the cost of holding economic capital, to support the legacy interest rate guaranteed products as recognised under the Company's supplementary reporting basis under European Embedded Value principles.

ii Insurance Groups Directive – Group solvency position

The IGD group solvency position as at 31 December 2008 will be submitted to the FSA by 30 April 2009. At the time of preparation of these financial statements the surplus capital, under the IGD test of capital adequacy, was estimated to be around £1.7 billion before allowing for the 2008 final dividend, giving a solvency ratio of 160 per cent. This is composed of the Group's IGD surplus at 31 December 2008 which is estimated at £1.4 billion and of an additional £0.3 billion which the FSA has, after the year end, allowed the Group to include in the Group's IGD surplus going forward as a result of an innovative structure the Group has developed. The £0.3 billion additional capital reflects the ability to realise a portion of the shareholders' economic interest in the future transfers from the PAC with-profits fund.