

**Registered Number 2554213**

**Prudential Annuities Limited**

**Annual Report and Financial Statements  
For the year ended 31 December 2006**

# Prudential Annuities Limited

Incorporated and registered in England and Wales Registered Number 2554213  
Registered Office: Laurence Pountney Hill, London, EC4R 0HH

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# **Prudential Annuities Limited**

## **Directors**

D J Belsham  
T V Broadman  
H McKee  
N T E Prettejohn  
G Shaughnessy

## **Secretary**

Prudential Group Secretarial Services Limited

## **Auditors**

KPMG Audit Plc, London

# **Prudential Annuities Limited**

## **Directors' report for the year ended 31 December 2006**

### **Principal activity and business review**

The principal activity of the Company is the writing of pension annuity long term insurance business. This will continue in 2007.

The Company ceased to accept annuity business reassured from group companies during 2004. This represented the majority of the Company's new business. The amount of new business in future years is expected to be negligible.

The results of the Company for the year as set out on pages 8 and 9, show a profit on ordinary activities before tax of £49m (2005 : £340m).

The decrease in profits compared to 2005 is mainly due to:

- £40m - an increase in the provisions required for maintenance expenses.
- £10m - a significantly lower investment return on the surplus assets held by the Company as a result of an increase in interest rates over 2006.
  - during 2005 there were a number of one off reserve releases in respect of in-force business which have not been repeated in 2006.

The shareholders' funds of the Company total £1,625m (2005: £1,590m).

The assets and liabilities of the Company have reduced during 2006 as a result of an increase in interest rates and the payment of annuity claims.

The Company remained in a strong financial position at 31 December 2006.

### **Results and dividends**

The state of affairs of the Company at 31 December 2006 is shown in the balance sheet on pages 9 and 10. The profit and loss account appears on pages 7 and 8. No dividend for 2006 is proposed (2005: £Nil).

### **Post balance sheet events**

There have been no significant events affecting the Company since the balance sheet date.

### **Payment policy**

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

# Prudential Annuities Limited

## Directors' report for the year ended 31 December 2006 (continued)

### Share Capital

The authorised share capital of the Company is £800,000,000. There were no changes to the issued share capital in the year.

### Directors and their interests

The directors who served during the year were:

D J Belsham	
T V Boardman	
M E Tucker	Resigned 9 January 2006
N E T Prettejohn	Appointed 9 January 2006
T J W Tookey	Resigned 16 March 2006
K Coleman	Appointed 18 April 2006, resigned 15 December 2006
R C Ramsden	Resigned 31 May 2006
A D Briggs	Resigned 2 October 2006
G Shaughnessy	Appointed 14 December 2006
H McKee	Appointed 15 December 2006

The interests of Mr D J Belsham, Mr N E T Prettejohn and Mr G Shaughnessy who were directors in office at the end of the year and who were also directors of the immediate parent company, The Prudential Assurance Company Limited, are shown in the annual report and financial statements of that company.

- (i) The other directors in office at the end of the year had interests in shares of 5p each in Prudential plc as follows:
- (a) in shares, including rights granted under the Prudential Restricted Share Plan where the directors have yet to exercise their right to receive shares, and shares held in relevant Prudential Share Incentive plans:

	01/01/06 or later date of appointment	31/12/06
T V Boardman	37,740	35,314
H McKee	1,726	1,726

- (b) in conditional awards that have been made under the Prudential Restricted Share Plan, in which the shares are held in trust and represent the maximum awards for which rights may be granted, at the end of the relevant performance period, if the performance requirements of the Plan are met:

	01/01/06 or later date of appointment	31/12/06
T V Boardman	32,919	34,695
H McKee	15,425	15,425

## Prudential Annuities Limited

### Directors' report for the year ended 31 December 2006 (continued)

#### Directors and their interests (continued)

- (c) in conditional awards that have been made under the Prudential 1000 Day Long Term Incentive Plan, in which shares are held in trust and represent the maximum awards for which shares may be released, at the end of the relevant performance period, if the performance requirements of the Plan are met:

	01/01/06 or later date of appointment	31/12/06
T V Boardman	20,907	20,907
H McKee	10,510	10,510

- (d) in options to subscribe for shares under the Prudential Savings-Related Share Option Scheme:

	01/01/06 or later date of appointment	Granted	Exercised	Lapsed or cancelled	31/12/06
T V Boardman	5,162	-	2,865	-	2,297
H McKee	-	-	-	-	-

- (ii) Except as stated above, none of the directors in office at the end of the year:
- (a) had any interest in shares in, or debentures of, any Group company either at the beginning of the year or at the end of the year; or
- (b) were granted or exercised any right to subscribe for shares in, or debentures of, any Group company during the year, or up to the end of the year.

#### Financial risk management objectives, policies and exposure

The Company's objectives and policy in relation to the management of financial risk resulting from its financial assets and liabilities is to minimise any risk. The Company's exposure to financial risk through its financial assets and liabilities is provided in detail in note 7 of the notes to the financial statements.

#### Disclosure of information to auditors

The directors who held the office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

## **Prudential Annuities Limited**

### **Directors' report for the year ended 31 December 2006 (continued)**

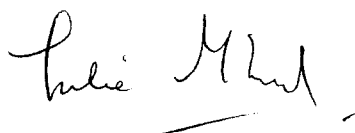
#### **Auditors**

In accordance with section 386 of the Companies Act 1985, an elective resolution has been passed by the Company dispensing with the need to appoint auditors annually. Accordingly, KPMG Audit Plc will be deemed to be re-appointed auditors of the Company for the current financial year.

#### **Qualifying third party indemnities**

The Articles of Association of the Company provide for the directors and officers of the Company to be indemnified in respect of liabilities incurred as a result of their office. Prudential plc also provides certain protections for its directors and senior managers of companies within the Prudential Group against personal financial exposure that they may incur in their capacity as such. These include qualifying third party indemnity provisions (as defined under section 309B of the Companies Act 1985) in force for the benefit of the directors of Prudential plc and of certain directors of associated companies (as defined under section 309A of the Companies Act 1985) at the time this directors' report was approved under section 234A of the Companies Act 1985 and during 2006.

On behalf of the board of directors.



Prudential Group Secretarial Services Limited  
Company Secretary  
22 March 2007

## Prudential Annuities Limited

### Profit and Loss Account for the year ended 31 December 2006

Long Term Business - Technical Account	Note	2006 £m	2005 £m
<b>Earned premiums, net of reinsurance</b>			
Gross premiums written	1	4	60
		<b>4</b>	<b>60</b>
<b>Investment income</b>			
Investment income	2	944	944
Unrealised (losses) / gains on investments		(651)	700
		<b>293</b>	<b>1,644</b>
<b>Claims incurred, net of reinsurance</b>			
Claims paid		(921)	(913)
<b>Change in other technical provisions, net of reinsurance</b>			
Long-term business provision, net of reinsurance	9	605	(405)
<b>Change in technical provision for linked liabilities, net of reinsurance</b>			
	9	90	(115)
		<b>695</b>	<b>(520)</b>
<b>Net operating expenses</b>			
- Acquisition costs		(1)	(1)
- Administrative expenses		(15)	(12)
- Investment expenses and charges		(12)	(9)
		<b>(28)</b>	<b>(22)</b>
<b>Tax attributable to the long term business</b>		<b>(11)</b>	<b>(75)</b>
<b>Balance on the technical account – long term business</b>		<b>32</b>	<b>174</b>

The amounts shown above are in respect of continuing operations.

The accounting policies and notes on pages 11 to 28 form an integral part of these financial statements.

## Prudential Annuities Limited

### Profit and Loss Account for the year ended 31 December 2006 (continued)

<b>Non-Technical Account</b>	Note	<b>2006 £m</b>	<b>2005 £m</b>
<b>Balance on the long term business technical account</b>		<b>32</b>	<b>174</b>
Tax credit attributable to the balance on the long term business technical account		<b>11</b>	<b>75</b>
Investment income	2	<b>62</b>	<b>83</b>
Unrealised (losses) /gains on investments		<b>(55)</b>	<b>9</b>
Investment management expenses		<b>(1)</b>	<b>(1)</b>
<b>Profit on ordinary activities before tax</b>		<b>49</b>	<b>340</b>
Tax on profit on ordinary activities	4	<b>(14)</b>	<b>(101)</b>
<b>Retained profit for the financial year transferred to reserves</b>	9	<b>35</b>	<b>239</b>

### Statement of total recognised gains and losses

Year ended 31 December 2006

	<b>2006 £m</b>	<b>2005 £m</b>
Retained profit for the financial year	<b>35</b>	<b>239</b>
<b>Total recognised gains and losses recognised since the last annual report</b>	<b>35</b>	<b>239</b>

### Reconciliation of movement in Shareholder's Funds

Year ended 31 December 2006

	<b>2006 £m</b>	<b>2005 £m</b>
Shareholders' capital and reserves at beginning of year	<b>1,590</b>	<b>1,351</b>
Retained profit for the financial year	<b>35</b>	<b>239</b>
<b>Shareholders' capital and reserves at end of year</b>	<b>1,625</b>	<b>1,590</b>

The amounts shown above are in respect of continuing operations.

The accounting policies and notes on pages 11 to 28 form an integral part of these financial statements.

# Prudential Annuities Limited

## Balance sheet as at 31 December 2006

<b>ASSETS</b>	Note	2006 £m	2005 £m
<b>Investments</b>			
Land and buildings		381	348
Other financial investments		12,913	13,464
	7	13,294	13,812
<b>Assets held to cover linked liabilities</b>	8	2,031	2,125
<b>Reinsurers' share of technical provisions</b>			
Long term business provision	9	4	4
Technical provision for linked liabilities	9	2	2
		6	6
<b>Debtors</b>			
Tax recoverable		10	-
Other debtors		21	25
		31	25
<b>Other assets</b>			
Cash at bank and in hand		123	120
<b>Prepayments and accrued income</b>			
Accrued interest and rent		221	220
<b>Total assets</b>	1(b)	15,706	16,308

The accounting policies and notes on pages 11 to 28 form an integral part of these financial statements.

# Prudential Annuities Limited

## Balance sheet as at 31 December 2006 (continued)

<b>LIABILITIES</b>	Note	2006 £m	2005 £m
<b>Capital and reserves</b>			
Called up share capital	14	550	550
Profit and loss account	9	1,075	1,040
<b>Total shareholders' funds</b>		<b>1,625</b>	<b>1,590</b>
<b>Technical provisions</b>			
Long term business provision	9	11,323	12,005
Claims outstanding	9	23	17
<b>Technical provisions for linked liabilities</b>	9	<b>2,033</b>	<b>2,127</b>
<b>Provision for other risks and charges</b>			
Deferred tax	11	216	206
<b>Creditors</b>			
Derivative liabilities		44	77
Amounts owed to credit institutions		411	218
Other creditors including taxation and social security	12	31	68
<b>Total liabilities</b>		<b>15,706</b>	<b>16,308</b>

The financial statements on pages 7 to 28 were approved by the board of directors on 22 March 2007.



N E T Prettejohn  
Chairman

The accounting policies and notes on pages 11 to 28 form an integral part of these financial statements.

# Prudential Annuities Limited

## Accounting Policies

### (a) Basis of preparation

The financial statements have been prepared in accordance with the provisions of Section 255 of, and Schedule 9A to, the Companies Act 1985, which cover the disclosures applicable to insurance companies.

The financial statements have been prepared in accordance with applicable accounting standards and with the Statement of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers in December 2005.

The Company has not presented a capital position statement with supporting disclosures under FRS 27 on the basis that the Company is more than 90 per cent owned within a group and the Company is included in the publicly available Prudential group financial statements which provide information on a group basis complying with this requirement. The process for setting assumptions and determining liabilities, as required to be disclosed by FRS 27, is described in note 10 of the financial statements (together with key assumptions).

#### Change in accounting policies

The Company has implemented the following accounting standards in preparing its results for the year ended 31 December 2006. These standards closely reflect the requirements of International Financial Reporting Standards (IFRS) and form part of the continuing implementation of IFRS in the UK.

FRS 23 "The effects of changes in foreign exchange rates", FRS 24 "Financial reporting in hyperinflationary economies", FRS 25 "Financial Instruments: Disclosures and Presentation" and FRS 26 "Financial instruments: Measurement"

These accounting standards are part of a package of standards comprising FRS 23, FRS 24, the disclosure requirements of FRS 25 and FRS 26. The Company adopted these standards on 1 January 2006. The presentation requirements of FRS25 were adopted by the Company from 1 January 2005.

The main impacts of the adoption of these standards are described below:

#### FRS 23 "The effects of changes in foreign exchange rates"

The adoption of this standard has no impact on the balance sheet or profit and loss account of the Company. However, certain changes have been made on the disclosures relating to foreign exchange differences as a result of adopting this standard.

#### FRS 24 "Financial reporting in hyperinflationary economies"

The adoption of this standard has no impact on the results of the Company.

#### FRS 25 "Financial instruments: disclosures and presentation"

FRS 25 is based on the text of IAS 32 "Financial instruments: disclosures and presentation" as at 31 March 2004, incorporating the revised version of IAS 32 issued by the IASB in December 2003 and includes amendments made by IFRS 4 "Insurance contracts".

# Prudential Annuities Limited

## Accounting Policies (continued)

### (a) Basis of preparation (continued)

The disclosures required under FRS 25 are set out in Note 7. The Company has taken advantage of the provisions within FRS 25 that allows the comparatives not to be restated to comply with this standard in the first year of adoption.

#### FRS 26 “Financial instruments: measurement”

FRS 26 is based on the text of IAS39, “Financial instruments: recognition and measurement” as at 31 March 2004, incorporating the revised version of IAS39 issued by the IASB in December 2003 together with the amendments to IAS39 on “Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk” and those made by IFRS 4 “Insurance contracts”.

As with FRS 25, the comparative information has not been restated to comply with this standard.

Certain provisions of the Statement of Recommended Practice, “Accounting for Insurance Business”, issued in December 2005 (as amended in December 2006) by the Association of British Insurers ABI SORP (“the ABI SORP”) relating to application of FRS 26 also became effective for the Company upon its adoption of FRS 26 in 2006. The principal effects of adopting FRS 26 arise in the Company’s long-term business contracts and financial assets.

#### Long-term business

On adoption of FRS 26, the measurement basis of assets and liabilities of long term business contracts is dependent upon the classification of the contracts as either insurance contracts, if the level of insurance risk is significant, or investment contracts if the risk is insignificant. The Company’s contracts are all classed as insurance contracts.

### (b) Long term business

Annuity considerations are accounted for when due. Annuities are accounted for when the annuity becomes due for payment. Surrenders are accounted for when paid. Death claims and all other claims are accounted for when notified. Index linked business has been disclosed as linked for the purposes of these financial statements.

Investment income and realised and unrealised investment gains attributable to long-term business are credited to the long term business technical account.

The costs of acquiring new business, principally commission and certain costs associated with policy issue and underwriting which are not matched by policy charges, are written off in the year they are incurred.

# Prudential Annuities Limited

## Accounting Policies (continued)

### (c) Investments

#### (i) *Land and buildings*

Land and buildings are valued annually by professional external valuers on an Fair Value basis, as defined in the Appraisal and Valuation Manual issued by the Royal Institute of Chartered Surveyors, in particular Practice Statement 3.2. No depreciation is provided on land and buildings, held for investment purposes, in accordance with Statement of Standard Accounting Practice 19, Accounting for Investment Properties.

On historical cost basis buildings are depreciated over 40 years. Leasehold buildings are depreciated over the 40 years or if the lease is less than 40 years over the length of the lease.

#### (ii) *Other financial investments valuation*

Listed investments are shown at fair value. Unlisted investments are valued on quotations provided by external fund managers, brokers, independent pricing services or values as determined by the directors.

#### (iii) *Realised gains and losses on investments*

Realised gains and losses on investments represent the difference between the value on disposal and the original cost.

#### (iv) *Unrealised gains and losses on investments*

Unrealised gains and losses on investments represent the difference between the fair value or directors' valuation (as appropriate) and the fair value at the previous balance sheet date or the original cost if acquired during the year.

An impact arising from the adoption of FRS 26 is in relation to recognition and measurement of financial instruments (other than long-term business contracts classified as financial instrument as described above). Upon initial recognition, financial investments are measured at fair value. Subsequently, the Company is permitted, subject to specific criteria, to designate its investments as either financial investments at fair value through profit and loss, financial investments held on an available-for-sale basis, financial investments held to maturity, or loans and receivables. The Company holds financial investments on the following bases:

#### (v) *Financial investments at fair value through profit and loss*

This comprises assets designated by management as fair value through profit and loss on inception. These investments and including all derivatives are valued at fair value with all changes thereon being recognised in the profit and loss account.

Under the previous UK GAAP, quoted financial investments are carried at market value at the mid-market prices. Upon the adoption of FRS 26, the Company uses bid prices to value its quoted financial investments.

#### (vi) *Loans and receivables*

This comprises investments that have fixed or determinable payments and are not designated as fair value through profit and loss or available-for-sale. These investments include loans secured by mortgages, deposits and other unsecured loans and receivables. These investments were held at fair value under the previous UK GAAP. Under FRS 26, these investments are carried at amortised cost using the effective interest method and subject to impairment reviews. The Company measures the amount of the impairment loss by comparing the amortised cost with the present value of its estimated future cash flows discounted at the original effective interest rate.

