PRUDENTIAL FINANCIAL INC
Form 10-Q
November 05, 2010
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended September 30, 2010**

**OR**

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Transition Period from to**

**Commission File Number 001-16707**

# Prudential Financial, Inc.

**(Exact Name of Registrant as Specified in its Charter)**

| **New Jersey** | **22-3703799** |
|---|---|
| **(State or Other Jurisdiction of Incorporation or Organization)** | **(I.R.S. Employer Identification Number)** |

**751 Broad Street**

**Newark, New Jersey 07102**

**(973) 802-6000**

**(Address and Telephone Number of Registrant s Principal Executive Offices)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of the Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of October 31, 2010, 465 million shares of the registrant s Common Stock (par value $0.01) were outstanding. In addition, 2 million shares of the registrant s Class B Stock, for which there is no established public trading market, were outstanding.

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**Forward-Looking Statements**

Certain of the statements included in this Quarterly Report on Form 10-Q, including but not limited to those in Management s Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995. Words such as expects, believes, anticipates, includes, plans, assumes, estimates, projects, should, will, shall or variations of such words are generally part of forward-looking statements. Forward-looking statements are made based on management s current expectations and beliefs concerning future developments and their potential effects upon Prudential Financial, Inc. and its subsidiaries. There can be no assurance that future developments affecting Prudential Financial, Inc. and its subsidiaries will be those anticipated by management. These forward-looking statements are not a guarantee of future performance and involve risks and uncertainties, and there are certain important factors that could cause actual results to differ, possibly materially, from expectations or estimates reflected in such forward-looking statements, including, among others: (1) general economic, market and political conditions, including the performance and fluctuations of fixed income, equity, real estate and other financial markets; (2) the availability and cost of additional debt or equity capital or external financing for our operations; (3) interest rate fluctuations or prolonged periods of low interest rates; (4) the degree to which we choose not to hedge risks, or the potential ineffectiveness or insufficiency of hedging or risk management strategies we do implement, with regard to variable annuity or other product guarantees; (5) any inability to access our credit facilities; (6) reestimates of our reserves for future policy benefits and claims; (7) differences between actual experience regarding mortality, morbidity, persistency, surrender experience, interest rates or market returns and the assumptions we use in pricing our products, establishing liabilities and reserves or for other purposes; (8) changes in our assumptions related to deferred policy acquisition costs, valuation of business acquired or goodwill; (9) changes in assumptions for retirement expense; (10) changes in our financial strength or credit ratings; (11) statutory reserve requirements associated with term and universal life insurance policies under Regulation XXX and Guideline AXXX; (12) investment losses, defaults and counterparty non-performance; (13) competition in our product lines and for personnel; (14) difficulties in marketing and distributing products through current or future distribution channels; (15) changes in tax law; (16) economic, political, currency and other risks relating to our international operations; (17) fluctuations in foreign currency exchange rates and foreign securities markets; (18) regulatory or legislative changes, including the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act; (19) inability to protect our intellectual property rights or claims of infringement of the intellectual property rights of others; (20) adverse determinations in litigation or regulatory matters and our exposure to contingent liabilities, including in connection with our divestiture or winding down of businesses; (21) domestic or international military actions, natural or man-made disasters including terrorist activities or pandemic disease, or other events resulting in catastrophic loss of life; (22) ineffectiveness of risk management policies and procedures in identifying, monitoring and managing risks; (23) effects of acquisitions, divestitures and restructurings, including possible difficulties in integrating and realizing the projected results of acquisitions, including risks associated with the proposed acquisition of certain insurance operations of American International Group, Inc. in Japan; (24) interruption in telecommunication, information technology or other operational systems or failure to maintain the security, confidentiality or privacy of sensitive data on such systems; (25) changes in statutory or U.S. GAAP accounting principles, practices or policies; (26) Prudential Financial, Inc. s primary reliance, as a holding company, on dividends or distributions from its subsidiaries to meet debt payment obligations and the ability of the subsidiaries to pay such dividends or distributions in light of our ratings objectives and/or applicable regulatory restrictions; and (27) risks due to the lack of legal separation between our Financial Services Businesses and our Closed Block Business. Prudential Financial, Inc. does not intend, and is under no obligation, to update any particular forward-looking statement included in this document. See Risk Factors included in this Quarterly Report on Form 10-Q for discussion of certain risks relating to our businesses and investment in our securities.

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*Throughout this Quarterly Report on Form 10-Q, Prudential Financial and the Registrant refer to Prudential Financial, Inc., the ultimate holding company for all of our companies. Prudential Insurance refers to The Prudential Insurance Company of America, before and after its demutualization on December 18, 2001. Prudential, the Company, we and our refer to our consolidated operations before and after demutualization.*

**PART I FINANCIAL INFORMATION**

**ITEM 1. Financial Statements**

**PRUDENTIAL FINANCIAL, INC.**

**Unaudited Interim Consolidated Statements of Financial Position**

**September 30, 2010 and December 31, 2009 (in millions, except share amounts)**

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| **ASSETS** | | |
| Fixed maturities, available for sale, at fair value (amortized cost: 2010 $184,586; 2009 $174,251)(1) | $ 197,189 | $ 175,225 |
| Fixed maturities, held to maturity, at amortized cost (fair value: 2010 $5,522; 2009 $5,198)(1) | 5,233 | 5,120 |
| Trading account assets supporting insurance liabilities, at fair value(1) | 17,750 | 16,020 |
| Other trading account assets, at fair value | 5,676 | 3,033 |
| Equity securities, available for sale, at fair value (cost: 2010 $6,368; 2009-$6,106) | 7,272 | 6,895 |
| Commercial mortgage and other loans (includes $418 and $479 measured at fair value under the fair value option at September 30, 2010 and December 31, 2009, respectively)(1) | 31,924 | 31,384 |
| Policy loans | 10,544 | 10,146 |
| Other long-term investments (includes $244 million and $0 million measured at fair value under the fair value option at September 30, 2010 and December 31, 2009, respectively)(1) | 6,130 | 5,904 |
| Short-term investments | 5,677 | 6,825 |
| Total investments | 287,395 | 260,552 |
| Cash and cash equivalents(1) | 11,973 | 13,164 |
| Accrued investment income(1) | 2,416 | 2,322 |
| Deferred policy acquisition costs | 15,054 | 14,578 |
| Other assets(1) | 15,623 | 15,513 |
| Separate account assets(1) | 194,463 | 174,074 |
| **Total Assets** | $ 526,924 | $ 480,203 |
| **LIABILITIES AND EQUITY** | | |
| **LIABILITIES** | | |
| Future policy benefits | $ 133,660 | $ 125,707 |
| Policyholders account balances | 105,298 | 101,666 |
| Policyholders dividends | 4,384 | 1,254 |
| Securities sold under agreements to repurchase | 5,934 | 6,033 |
| Cash collateral for loaned securities | 2,465 | 3,163 |

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| Income taxes | 7,058 | 4,014 |
| Short-term debt | 2,572 | 3,122 |
| Long-term debt (includes $0 and $429 measured at fair value under the fair value option at September 30, 2010 and December 31, 2009, respectively) | 22,337 | 21,037 |
| Other liabilities(1) | 14,685 | 14,404 |
| Separate account liabilities(1) | 194,463 | 174,074 |
| Total liabilities | 492,856 | 454,474 |
| **COMMITMENTS AND CONTINGENT LIABILITIES (See Note 15)** | | |
| **EQUITY** | | |
| Preferred Stock ($.01 par value; 10,000,000 shares authorized; none issued) | 0 | 0 |
| Common Stock ($.01 par value; 1,500,000,000 shares authorized; 641,762,159 and 641,762,089 shares issued at September 30, 2010 and December 31, 2009, respectively) | 6 | 6 |
| Class B Stock ($.01 par value; 10,000,000 shares authorized; 2,000,000 shares issued and outstanding at September 30, 2010 and December 31, 2009, respectively) | 0 | 0 |
| Additional paid-in capital | 23,222 | 23,235 |
| Common Stock held in treasury, at cost (176,812,357 and 179,650,931 shares at September 30, 2010 and December 31, 2009, respectively) | (11,205) | (11,390) |
| Accumulated other comprehensive income (loss) | 4,729 | (443) |
| Retained earnings | 16,794 | 13,787 |
| Total Prudential Financial, Inc. equity | 33,546 | 25,195 |
| Noncontrolling interests | 522 | 534 |
| Total equity | 34,068 | 25,729 |
| **TOTAL LIABILITIES AND EQUITY** | $ 526,924 | $ 480,203 |

(1) See Note 5 for details of balances associated with variable interest entities.

*See Notes to Unaudited Interim Consolidated Financial Statements*

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**PRUDENTIAL FINANCIAL, INC.**

**Unaudited Interim Consolidated Statements of Operations**

**Three and Nine Months Ended September 30, 2010 and 2009 (in millions, except per share amounts)**

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2010** | **2009** | **2010** | **2009** |
| **REVENUES** | | | | |
| Premiums | $ 4,654 | $ 4,100 | $ 13,500 | $ 12,321 |
| Policy charges and fee income | 761 | 613 | 2,436 | 2,052 |
| Net investment income | 3,018 | 2,854 | 8,806 | 8,534 |
| Asset management fees and other income | 1,500 | 1,420 | 3,362 | 3,617 |
| Realized investment gains (losses), net: | | | | |
| Other-than-temporary impairments on fixed maturity securities | (435) | (398) | (2,198) | (3,497) |
| Other-than-temporary impairments on fixed maturity securities transferred to Other Comprehensive Income | 345 | 38 | 1,715 | 2,033 |
| Other realized investment gains (losses), net | 119 | (84) | 2,687 | (1,113) |
| Total realized investment gains (losses), net | 29 | (444) | 2,204 | (2,577) |
| Total revenues | 9,962 | 8,543 | 30,308 | 23,947 |
| **BENEFITS AND EXPENSES** | | | | |
| Policyholders benefits | 4,538 | 3,925 | 13,668 | 12,152 |
| Interest credited to policyholders account balances | 1,174 | 1,317 | 3,640 | 3,585 |
| Dividends to policyholders | 512 | 566 | 1,547 | 842 |
| General and administrative expenses | 1,998 | 1,887 | 7,169 | 6,527 |
| Total benefits and expenses | 8,222 | 7,695 | 26,024 | 23,106 |
| **INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF OPERATING JOINT VENTURES** | 1,740 | 848 | 4,284 | 841 |
| Income tax expense (benefit) | 520 | (153) | 1,306 | (318) |
| **INCOME FROM CONTINUING OPERATIONS BEFORE EQUITY IN EARNINGS OF OPERATING JOINT VENTURES** | 1,220 | 1,001 | 2,978 | 1,159 |
| Equity in earnings of operating joint ventures, net of taxes | 14 | 31 | 33 | 30 |
| **INCOME FROM CONTINUING OPERATIONS** | 1,234 | 1,032 | 3,011 | 1,189 |
| Income from discontinued operations, net of taxes | 8 | 0 | 6 | 26 |
| **NET INCOME** | 1,242 | 1,032 | 3,017 | 1,215 |
| Less: Loss attributable to noncontrolling interests | (2) | (50) | (1) | (44) |
| **NET INCOME ATTRIBUTABLE TO PRUDENTIAL FINANCIAL, INC** | $ 1,244 | $ 1,082 | $ 3,018 | $ 1,259 |
| **EARNINGS PER SHARE (See Note 8)** | | | | |
| **Financial Services Businesses** | | | | |
| **Basic:** | | | | |

| | | | | |
|---|---|---|---|---|
| Income from continuing operations attributable to Prudential Financial, Inc. per share of Common Stock | $ 2.48 | $ 2.36 | $ 5.37 | $ 3.68 |
| Income from discontinued operations, net of taxes | 0.02 | 0.00 | 0.01 | 0.06 |
| Net income attributable to Prudential Financial, Inc. per share of Common Stock | $ 2.50 | $ 2.36 | $ 5.38 | $ 3.74 |
| **Diluted:** | | | | |
| Income from continuing operations attributable to Prudential Financial, Inc. per share of Common Stock | $ 2.45 | $ 2.35 | $ 5.30 | $ 3.66 |
| Income from discontinued operations, net of taxes | 0.01 | 0.00 | 0.01 | 0.06 |
| Net income attributable to Prudential Financial, Inc. per share of Common Stock | $ 2.46 | $ 2.35 | $ 5.31 | $ 3.72 |
| **Closed Block Business** | | | | |
| **Basic and Diluted:** | | | | |
| Income (loss) from continuing operations attributable to Prudential Financial, Inc. per share of Class B Stock | $ 33.50 | $ (10.00) | $ 243.50 | $ (199.00) |
| Income from discontinued operations, net of taxes | 0.50 | 0.00 | 0.50 | 0.00 |
| Net income (loss) attributable to Prudential Financial, Inc. per share of Class B Stock | $ 34.00 | $ (10.00) | $ 244.00 | $ (199.00) |

*See Notes to Unaudited Interim Consolidated Financial Statements*

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**PRUDENTIAL FINANCIAL, INC.**

**Unaudited Interim Consolidated Statements of Equity(1)**

**Nine Months Ended September 30, 2010 and 2009 (in millions)**

| | Prudential Financial, Inc. Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Common Stock | Additional Paid-in Capital | Retained Earnings | Common Stock Held In Treasury | Accumulated Other Comprehensive Income (loss) | Total Prudential Financial, Inc. Equity | Noncontrolling Interests | Total Equity |
| **Balance December 31, 2009** | $ 6 | $ 23,235 | $ 13,787 | $ (11,390) | $ (443) | $ 25,195 | $ 534 | $ 25,729 |
| Contributions from noncontrolling interests | | | | | | | 6 | 6 |
| Distributions to noncontrolling interests | | | | | | | (19) | (19) |
| Consolidations/deconsolidations of noncontrolling interests | | (2) | | | | (2) | (1) | (3) |
| Stock-based compensation programs | | (11) | (11) | 185 | | 163 | | 163 |
| Comprehensive income: | | | | | | | | |
| Net income | | | 3,018 | | | 3,018 | (1) | 3,017 |
| Other comprehensive income, net of tax | | | | | 5,172 | 5,172 | 3 | 5,175 |
| Total comprehensive income | | | | | | 8,190 | 2 | 8,192 |
| **Balance, September 30, 2010** | $ 6 | $ 23,222 | $ 16,794 | $ (11,205) | $ 4,729 | $ 33,546 | $ 522 | $ 34,068 |

| | Prudential Financial, Inc. Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Common Stock | Additional Paid-in Capital | Retained Earnings | Common Stock Held In Treasury | Accumulated Other Comprehensive Income (loss) | Total Prudential Financial, Inc. Equity | Noncontrolling Interests | Total Equity |
| **Balance, December 31, 2008** | $ 6 | $ 22,001 | $ 10,426 | $ (11,655) | $ (7,343) | $ 13,435 | $ 351 | $ 13,786 |
| Common Stock issued | | 1,391 | | | | 1,391 | | 1,391 |
| Contributions from noncontrolling interests | | | | | | | 275 | 275 |
| Distributions to noncontrolling interests | | | | | | | (16) | (16) |
| Stock-based compensation programs | | (44) | (57) | 213 | | 112 | | 112 |
| Impact of adoption of guidance for other-than-temporary impairments of debt securities, net of taxes | | | 659 | | (659) | 0 | | 0 |
| Comprehensive income: | | | | | | | | |
| Net income | | | 1,259 | | | 1,259 | (44) | 1,215 |
| Other comprehensive income (loss), net of tax | | | | | 8,101 | 8,101 | (17) | 8,084 |
| Total comprehensive income (loss) | | | | | | 9,360 | (61) | 9,299 |
| **Balance, September 30, 2009** | $ 6 | $ 23,348 | $ 12,287 | $ (11,442) | $ 99 | $ 24,298 | $ 549 | $ 24,847 |

(1) Class B Stock is not presented as the amounts are immaterial.

*See Notes to Unaudited Interim Consolidated Financial Statements*

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**PRUDENTIAL FINANCIAL, INC.**

**Unaudited Interim Consolidated Statements of Cash Flows**

**Nine Months Ended September 30, 2010 and 2009 (in millions)**

| | 2010 | 2009 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Net income | $ 3,017 | $ 1,215 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Realized investment (gains) losses, net | (2,204) | 2,577 |
| Policy charges and fee income | (705) | (850) |
| Interest credited to policyholders account balances | 3,639 | 3,585 |
| Depreciation and amortization | (56) | 158 |
| Gains on trading account assets supporting insurance liabilities, net | (720) | (1,527) |
| Change in: | | |
| Deferred policy acquisition costs | (829) | (824) |
| Future policy benefits and other insurance liabilities | 3,115 | 1,867 |
| Other trading account assets | (669) | 170 |
| Income taxes | (1,539) | (602) |
| Other, net | 1,555 | (1,066) |
| **Cash flows from operating activities** | 4,604 | 4,703 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Proceeds from the sale/maturity/prepayment of: | | |
| Fixed maturities, available for sale | 20,703 | 33,442 |
| Fixed maturities, held to maturity | 333 | 281 |
| Trading account assets supporting insurance liabilities and other trading account assets | 31,169 | 24,142 |
| Equity securities, available for sale | 1,898 | 1,422 |
| Commercial mortgage and other loans | 3,067 | 2,810 |
| Policy loans | 1,263 | 1,254 |
| Other long-term investments | 750 | 866 |
| Short-term investments | 16,522 | 21,182 |
| Payments for the purchase/origination of: | | |
| Fixed maturities, available for sale | (27,860) | (31,079) |
| Fixed maturities, held to maturity | (155) | (1,077) |
| Trading account assets supporting insurance liabilities and other trading account assets | (31,592) | (25,706) |
| Equity securities, available for sale | (1,872) | (887) |
| Commercial mortgage and other loans | (3,530) | (2,186) |
| Policy loans | (1,163) | (1,174) |
| Other long-term investments | (641) | (866) |
| Short-term investments | (15,436) | (23,611) |
| Other, net | 414 | (209) |
| **Cash flows used in investing activities** | (6,130) | (1,396) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Policyholders account deposits | 16,840 | 18,420 |
| Policyholders account withdrawals | (16,944) | (20,166) |
| Net change in securities sold under agreements to repurchase and cash collateral for loaned securities | (515) | (929) |
| Proceeds from the issuance of Common Stock | 0 | 1,391 |
| Cash dividends paid on Common Stock | (42) | (39) |
| Net change in financing arrangements (maturities 90 days or less) | 554 | (4,648) |
| Common Stock reissued for exercise of stock options | 78 | 39 |

| | | |
|---|---|---|
| Proceeds from the issuance of debt (maturities longer than 90 days) | 2,623 | 5,151 |
| Repayments of debt (maturities longer than 90 days) | (2,544) | (6,235) |
| Excess tax benefits from share-based payment arrangements | 11 | 0 |
| Other, net | 197 | 569 |
| **Cash flows from (used in) financing activities** | 258 | (6,447) |
| Effect of foreign exchange rate changes on cash balances | 77 | 83 |
| **NET DECREASE IN CASH AND CASH EQUIVALENTS** | (1,191) | (3,057) |
| **CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR** | 13,164 | 15,028 |
| **CASH AND CASH EQUIVALENTS, END OF PERIOD** | $ 11,973 | $ 11,971 |
| **NON-CASH TRANSACTIONS DURING THE PERIOD** | | |
| Treasury Stock shares issued for stock-based compensation programs | $ 70 | $ 97 |

*See Notes to Unaudited Interim Consolidated Financial Statements*

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements**

## 1. BUSINESS AND BASIS OF PRESENTATION

Prudential Financial, Inc. ( Prudential Financial ) and its subsidiaries (collectively, Prudential or the Company ) provide a wide range of insurance, investment management, and other financial products and services to both individual and institutional customers throughout the United States and in many other countries. Principal products and services provided include life insurance, annuities, retirement-related services, mutual funds, investment management, and real estate services. The Company has organized its principal operations into the Financial Services Businesses and the Closed Block Business. The Financial Services Businesses operate through three operating divisions: U.S. Retirement Solutions and Investment Management, U.S. Individual Life and Group Insurance, and International Insurance and Investments. The Company s real estate and relocation services business as well as businesses that are not sufficiently material to warrant separate disclosure and divested businesses, are included in Corporate and Other operations within the Financial Services Businesses. The Closed Block Business, which includes the Closed Block (see Note 6), is managed separately from the Financial Services Businesses. The Closed Block Business was established on the date of demutualization and includes the Company s in force participating insurance and annuity products and assets that are used for the payment of benefits and policyholders dividends on these products, as well as other assets and equity that support these products and related liabilities. In connection with the demutualization, the Company ceased offering these participating products.

***Basis of Presentation***

The Unaudited Interim Consolidated Financial Statements include the accounts of Prudential Financial, entities over which the Company exercises control, including majority-owned subsidiaries and minority-owned entities such as limited partnerships in which the Company is the general partner, and variable interest entities in which the Company is considered the primary beneficiary. See Note 5 for more information on the Company s consolidated variable interest entities. The Unaudited Interim Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( U.S. GAAP ) on a basis consistent with reporting interim financial information in accordance with instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission ( SEC ). Intercompany balances and transactions have been eliminated.

In the opinion of management, all adjustments necessary for a fair statement of the financial position and results of operations have been made. All such adjustments are of a normal, recurring nature. Interim results are not necessarily indicative of the results that may be expected for the full year. These financial statements should be read in conjunction with the Company s Audited Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2009.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant estimates include those used in determining deferred policy acquisition costs and related amortization; valuation of business acquired and its amortization; amortization of sales inducements; measurement of goodwill and any related impairment; valuation of investments including derivatives and the recognition of other-than-temporary impairments; future policy benefits including guarantees; pension and other postretirement benefits; provision for income taxes and valuation of deferred tax assets; and reserves for contingent liabilities, including reserves for losses in connection with unresolved legal matters.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*Reclassifications*

Certain amounts in prior periods have been reclassified to conform to the current period presentation.

## 2. SIGNIFICANT ACCOUNTING POLICIES AND PRONOUNCEMENTS

*Investments in Debt and Equity Securities*

The Company s investments in debt and equity securities include fixed maturities; trading account assets; equity securities; and short-term investments. The accounting policies related to these are as follows:

Fixed maturities are comprised of bonds, notes and redeemable preferred stock. Fixed maturities classified as available for sale are carried at fair value. See Note 13 for additional information regarding the determination of fair value. Fixed maturities that the Company has both the positive intent and ability to hold to maturity are carried at amortized cost and classified as held to maturity. The amortized cost of fixed maturities is adjusted for amortization of premiums and accretion of discounts to maturity. Interest income, as well as the related amortization of premium and accretion of discount, is included in Net investment income under the effective yield method. For mortgage-backed and asset-backed securities, the effective yield is based on estimated cash flows, including prepayment assumptions based on data from widely accepted third-party data sources or internal estimates. In addition to prepayment assumptions, cash flow estimates vary based on assumptions regarding the underlying collateral, including default rates and changes in value. These assumptions can significantly impact income recognition and the amount of other-than-temporary impairments recognized in earnings and other comprehensive income. For high credit quality mortgage-backed and asset-backed securities (those rated AA or above), cash flows are provided quarterly, and the amortized cost and effective yield of the security are adjusted as necessary to reflect historical prepayment experience and changes in estimated future prepayments. The adjustments to amortized cost are recorded as a charge or credit to net investment income in accordance with the retrospective method. For asset-backed and mortgage-backed securities rated below AA, the effective yield is adjusted prospectively for any changes in estimated cash flows. See the discussion below on realized investment gains and losses for a description of the accounting for impairments, as well as the impact of the Company s adoption on January 1, 2009 of new authoritative guidance for the recognition and presentation of other-than-temporary impairments for debt securities. Unrealized gains and losses on fixed maturities classified as available for sale, net of tax, and the effect on deferred policy acquisition costs, valuation of business acquired, deferred sales inducements, future policy benefits and policyholders dividends that would result from the realization of unrealized gains and losses, are included in Accumulated other comprehensive income (loss).

Trading account assets supporting insurance liabilities, at fair value includes invested assets that support certain products included in the Retirement segment, as well as certain products included in the International Insurance segment, which are experience rated, meaning that the investment results associated with these products are expected to ultimately accrue to contractholders. Realized and unrealized gains and losses

for these investments are reported in Asset management fees and other income. Interest and dividend income from these investments is reported in Net investment income.

Other trading account assets, at fair value consist primarily of investments and certain derivatives, including those used by the Company in its capacity as a broker-dealer and derivative hedging positions used in a non-broker or non-dealer capacity primarily to economically hedge the risks related to certain products. These instruments are carried at fair value. Realized and unrealized gains and losses on these investments and on derivatives used by the Company in its capacity as a broker-dealer are reported in Asset management fees and other income. Interest and dividend income from these investments is reported in Net investment income.

Equity securities available for sale are comprised of common stock, mutual fund shares, non-redeemable preferred stock, and perpetual preferred stock, and are carried at fair value. The associated unrealized gains and

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

losses, net of tax, and the effect on deferred policy acquisition costs, valuation of business acquired, deferred sales inducements, future policy benefits and policyholders dividends that would result from the realization of unrealized gains and losses, are included in Accumulated other comprehensive income (loss). The cost of equity securities is written down to fair value when a decline in value is considered to be other-than-temporary. See the discussion below on realized investment gains and losses for a description of the accounting for impairments. Dividends from these investments are recognized in Net investment income when declared.

Short-term investments primarily consist of highly liquid debt instruments with a maturity of greater than three months and less than twelve months when purchased, other than those debt instruments meeting this definition that are included in Trading account assets supporting insurance liabilities, at fair value. These investments are generally carried at fair value and include certain money market investments, short-term debt securities issued by government sponsored entities and other highly liquid debt instruments. Short-term investments held in our broker-dealer operations are marked-to-market through Asset management fees and other income.

Realized investment gains (losses) are computed using the specific identification method with the exception of some of the Company s International Insurance businesses portfolios, where the average cost method is used. Realized investment gains and losses are generated from numerous sources, including the sale of fixed maturity securities, equity securities, investments in joint ventures and limited partnerships and other types of investments, as well as adjustments to the cost basis of investments for net other-than-temporary impairments recognized in earnings. Realized investment gains and losses are also generated from prepayment premiums received on private fixed maturity securities, recoveries of principal on previously impaired securities, provisions for losses on commercial mortgage and other loans, fair value changes on commercial mortgage loans carried at fair value, and fair value changes on embedded derivatives and free-standing derivatives that do not qualify for hedge accounting treatment, except those derivatives used in the Company s capacity as a broker or dealer.

The Company s available for sale and held to maturity securities with unrealized losses are reviewed quarterly to identify other-than-temporary impairments in value. In evaluating whether a decline in value is other-than-temporary, the Company considers several factors including, but not limited to the following: (1) the extent and the duration of the decline; (2) the reasons for the decline in value (credit event, currency or interest-rate related, including general credit spread widening); and (3) the financial condition of and near-term prospects of the issuer. With regard to available-for-sale equity securities, the Company also considers the ability and intent to hold the investment for a period of time to allow for a recovery of value. When it is determined that a decline in value of an equity security is other-than-temporary, the carrying value of the equity security is reduced to its fair value, with a corresponding charge to earnings.

In addition, in April 2009, the Financial Accounting Standards Board ( FASB ) revised the authoritative guidance for the recognition and presentation of other-than-temporary impairments for debt securities. The Company early adopted this guidance on January 1, 2009. Prior to the adoption of this guidance the Company was required to record an other-than-temporary impairment for a debt security unless it could assert that it had both the intent and ability to hold the security for a period of time sufficient to allow for a recovery in its fair value to its amortized cost basis. The revised guidance indicates that an other-than-temporary impairment must be recognized in earnings for a debt security in an unrealized loss position when an entity either (a) has the intent to sell the debt security or (b) more likely than not will be required to sell the debt security before its anticipated recovery. For all debt securities in unrealized loss positions that do not meet either of these two criteria, the guidance requires that the Company analyze its ability to recover the amortized cost by comparing the net present value of projected future cash flows with the amortized cost of the security. The net present value is calculated by discounting the Company s best estimate of projected future cash flows at the effective interest rate implicit in the debt security prior to impairment. The Company may use the estimated fair value of collateral as a proxy for

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

the net present value if it believes that the security is dependent on the liquidation of collateral for recovery of its investment. If the net present value is less than the amortized cost of the investment, an other-than-temporary impairment is recognized. In addition to the above mentioned circumstances, the Company also recognizes an other-than-temporary impairment in earnings when a foreign currency denominated security in an unrealized loss position approaches maturity.

Under the authoritative guidance for the recognition and presentation of other-than-temporary impairments, when an other-than-temporary impairment of a debt security has occurred, the amount of the other-than-temporary impairment recognized in earnings depends on whether the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis. If the debt security meets either of these two criteria, the other-than-temporary impairment recognized in earnings is equal to the entire difference between the security s amortized cost basis and its fair value at the impairment measurement date. For other-than-temporary impairments of debt securities that do not meet these two criteria, the net amount recognized in earnings is equal to the difference between the amortized cost of the debt security and its net present value calculated as described above. Any difference between the fair value and the net present value of the debt security at the impairment measurement date is recorded in Other comprehensive income (loss). Unrealized gains or losses on securities for which an other-than-temporary impairment has been recognized in earnings is tracked as a separate component of Accumulated other comprehensive income (loss). Prior to the adoption of this guidance in 2009, an other-than-temporary impairment recognized in earnings for debt securities was equal to the total difference between amortized cost and fair value at the time of impairment.

For debt securities, the split between the amount of an other-than-temporary impairment recognized in other comprehensive income and the net amount recognized in earnings is driven principally by assumptions regarding the amount and timing of projected cash flows. For mortgage-backed and asset-backed securities, cash flow estimates consider the payment terms of the underlying assets backing a particular security, including prepayment assumptions, and are based on data from widely accepted third-party data sources or internal estimates. In addition to prepayment assumptions, cash flow estimates include assumptions regarding the underlying collateral including default rates and recoveries, which vary based on the asset type and geographic location, as well as the vintage year of the security. For structured securities, the payment priority within the tranche structure is also considered. For all other debt securities, cash flow estimates are driven by assumptions regarding probability of default and estimates regarding timing and amount of recoveries associated with a default. The Company has developed these estimates using information based on its historical experience as well as using market observable data, such as industry analyst reports and forecasts, sector credit ratings and other data relevant to the collectability of a security, such as the general payment terms of the security and the security s position within the capital structure of the issuer.

The new cost basis of an impaired security is not adjusted for subsequent increases in estimated fair value. In periods subsequent to the recognition of an other-than-temporary impairment, the impaired security is accounted for as if it had been purchased on the measurement date of the impairment. For debt securities, the discount (or reduced premium) based on the new cost basis may be accreted into net investment income in future periods, including increases in cash flow on a prospective basis.

***Derivative Financial Instruments***

Derivatives are financial instruments whose values are derived from interest rates, foreign exchange rates, financial indices or the values of securities or commodities. Derivative financial instruments generally used by the Company include swaps, futures, forwards and options and

may be exchange-traded or contracted in the over-the-counter market. Derivative positions are carried at fair value, generally by obtaining quoted market prices or through the use of valuation models. Values can be affected by changes in interest rates, foreign

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

exchange rates, financial indices, values of securities or commodities, credit spreads, market volatility, expected returns and liquidity. Values can also be affected by changes in estimates and assumptions, including those related to counterparty behavior and non-performance risk used in valuation models.

Derivatives are used in a non-dealer or broker capacity in insurance, investment and international businesses as well as treasury operations to manage the characteristics of the Company s asset/liability mix, to manage the interest rate and currency characteristics of assets or liabilities and to mitigate the risk of a diminution, upon translation to U.S. dollars, of expected non-U.S. earnings and net investments in foreign operations resulting from unfavorable changes in currency exchange rates. Additionally, derivatives may be used to seek to reduce exposure to interest rate, credit, foreign currency and equity risks associated with assets held or expected to be purchased or sold, and liabilities incurred or expected to be incurred. As discussed in detail below and in Note 14, all realized and unrealized changes in fair value of non-dealer or broker related derivatives, with the exception of the effective portion of cash flow hedges and effective hedges of net investments in foreign operations, are recorded in current earnings. Cash flows from these derivatives are reported in the operating, investing, or financing activities sections in the Unaudited Interim Consolidated Statements of Cash Flows.

Derivatives are also used in a derivative dealer or broker capacity in the Company s global commodities group to meet the needs of clients by structuring transactions that allow clients to manage their exposure to interest rates, foreign exchange rates, indices or prices of securities and commodities. Realized and unrealized changes in fair value of derivatives used in these dealer related operations are included in Asset management fees and other income in the periods in which the changes occur. Cash flows from such derivatives are reported in the operating activities section of the Unaudited Interim Consolidated Statements of Cash Flows.

Derivatives are recorded either as assets, within Other trading account assets, at fair value or Other long-term investments, or as liabilities, within Other liabilities, except for embedded derivatives which are recorded with the associated host contract. The Company nets the fair value of all derivative financial instruments with counterparties for which a master netting arrangement has been executed.

The Company designates derivatives as either (1) a hedge of the fair value of a recognized asset or liability or unrecognized firm commitment ( fair value hedge); (2) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability ( cash flow hedge); (3) a foreign-currency fair value or cash flow hedge ( foreign currency hedge); (4) a hedge of a net investment in a foreign operation; or (5) a derivative that does not qualify for hedge accounting.

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated risk of the hedged item. Effectiveness of the hedge is formally assessed at inception and throughout the life of the hedging relationship. Even if a derivative qualifies for hedge accounting treatment, there may be an element of ineffectiveness of the hedge. Under such circumstances, the ineffective portion is recorded in Realized investment gains (losses), net.

The Company formally documents at inception all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as fair value, cash

flow, or foreign currency hedges to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. Hedges of a net investment in a foreign operation are linked to the specific foreign operation.

When a derivative is designated as a fair value hedge and is determined to be highly effective, changes in its fair value, along with changes in the fair value of the hedged asset or liability (including losses or gains on firm

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

commitments), are reported on a net basis in the income statement, generally in Realized investment gains (losses), net. When swaps are used in hedge accounting relationships, periodic settlements are recorded in the same income statement line as the related settlements of the hedged items.

When a derivative is designated as a cash flow hedge and is determined to be highly effective, changes in its fair value are recorded in Accumulated other comprehensive income (loss) until earnings are affected by the variability of cash flows being hedged (e.g., when periodic settlements on a variable-rate asset or liability are recorded in earnings). At that time, the related portion of deferred gains or losses on the derivative instrument is reclassified and reported in the income statement line item associated with the hedged item.

When a derivative is designated as a foreign currency hedge and is determined to be highly effective, changes in its fair value are recorded either in current period earnings if the hedge transaction is a fair value hedge (e.g., a hedge of a recognized foreign currency asset or liability) or in Accumulated other comprehensive income (loss) if the hedge transaction is a cash flow hedge (e.g., a foreign currency denominated forecasted transaction). When a derivative is used as a hedge of a net investment in a foreign operation, its change in fair value, to the extent effective as a hedge, is recorded in the cumulative translation adjustment account within Accumulated other comprehensive income (loss).

If it is determined that a derivative no longer qualifies as an effective fair value or cash flow hedge or management removes the hedge designation, the derivative will continue to be carried on the balance sheet at its fair value, with changes in fair value recognized currently in Realized investment gains (losses), net. The asset or liability under a fair value hedge will no longer be adjusted for changes in fair value and the existing basis adjustment is amortized to the income statement line associated with the asset or liability. The component of Accumulated other comprehensive income (loss) related to discontinued cash flow hedges is amortized to the income statement line associated with the hedged cash flows consistent with the earnings impact of the original hedged cash flows.

When hedge accounting is discontinued because the hedged item no longer meets the definition of a firm commitment, or because it is probable that the forecasted transaction will not occur by the end of the specified time period, the derivative will continue to be carried on the balance sheet at its fair value, with changes in fair value recognized currently in Realized investment gains (losses), net. Any asset or liability that was recorded pursuant to recognition of the firm commitment is removed from the balance sheet and recognized currently in Realized investment gains (losses), net. Gains and losses that were in Accumulated other comprehensive income (loss) pursuant to the hedge of a forecasted transaction are recognized immediately in Realized investment gains (losses), net.

If a derivative does not qualify for hedge accounting, all changes in its fair value, including net receipts and payments, are included in Realized investment gains (losses), net without considering changes in the fair value of the economically associated assets or liabilities.

The Company is a party to financial instruments that contain derivative instruments that are embedded in the financial instruments. At inception, the Company assesses whether the economic characteristics of the embedded derivative are clearly and closely related to the economic characteristics of the remaining component of the financial instrument (i.e., the host contract) and whether a separate instrument with the same terms as the embedded instrument would meet the definition of a derivative instrument. When it is determined that (1) the embedded derivative

possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, and (2) a separate instrument with the same terms would qualify as a derivative instrument, the embedded derivative is separated from the host contract, carried at fair value, and changes in its fair value are included in Realized investment gains (losses), net. For certain financial

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

instruments that contain an embedded derivative that otherwise would need to be bifurcated and reported at fair value, the Company may elect to classify the entire instrument as a trading account asset and report it within Other trading account assets, at fair value.

***Adoption of New Accounting Pronouncements***

In March 2010, the FASB issued updated guidance that amends and clarifies the accounting for credit derivatives embedded in interests in securitized financial assets. This new guidance eliminates the scope exception for embedded credit derivatives (except for those that are created solely by subordination) and provides new guidance on how the evaluation of embedded credit derivatives is to be performed. This new guidance is effective for the first interim reporting period beginning after June 15, 2010. The Company s adoption of this guidance effective with the interim reporting period ending September 30, 2010 did not have a material effect on the Company s consolidated financial position, results of operations, and financial statement disclosures.

In January 2010, the FASB issued updated guidance that requires new fair value disclosures about significant transfers between Level 1 and 2 measurement categories and separate presentation of purchases, sales, issuances, and settlements within the roll forward of Level 3 activity. Also, this updated fair value guidance clarifies the disclosure requirements about level of disaggregation and valuation techniques and inputs. This new guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of Level 3 activity, which are effective for interim and annual reporting periods beginning after December 15, 2010. The Company adopted the effective portions of this guidance on January 1, 2010. The required disclosures are provided in Note 13. The Company will provide the required disclosures about purchases, sales, issuances, and settlements in the roll forward of Level 3 activity in the interim reporting period ending March 31, 2011.

In June 2009, the FASB issued authoritative guidance which changes the analysis required to determine whether or not an entity is a variable interest entity ( VIE ). In addition, the guidance changes the determination of the primary beneficiary of a VIE from a quantitative to a qualitative model. Under the new qualitative model, the primary beneficiary must have both the ability to direct the activities of the VIE and the obligation to absorb either losses or gains that could be significant to the VIE. This guidance also changes when reassessment is needed, as well as requires enhanced disclosures, including the effects of a company s involvement with a VIE on its financial statements. This guidance is effective for interim and annual reporting periods beginning after November 15, 2009. In February 2010, the FASB issued updated guidance which defers, except for disclosure requirements, the impact of this guidance for entities that (1) possess the attributes of an investment company, (2) do not require the reporting entity to fund losses, and (3) are not financing vehicles or entities that were formerly classified as qualified special purpose entities ( QSPE s ). The Company s adoption of this guidance effective January 1, 2010 did not have a material effect on the Company s consolidated financial position and results of operations. The disclosures required by this revised guidance are provided in Note 5.

In June 2009, the FASB issued authoritative guidance which changes the accounting for transfers of financial assets, and is effective for transfers of financial assets occurring in interim and annual reporting periods beginning after November 15, 2009. It removes the concept of a QSPE from the guidance for transfers of financial assets and removes the exception from applying the guidance for consolidation of variable interest entities to qualifying special-purpose entities. It changes the criteria for achieving sale accounting when transferring a financial asset and changes the initial recognition of retained beneficial interests. The guidance also defines participating interest to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale. The Company s adoption of this guidance effective January 1, 2010 did not have a material

effect on the Company s consolidated financial position, results of operations, and financial statement disclosures.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Future Adoption of New Accounting Pronouncements***

In October 2010, the FASB issued guidance to address diversity in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. Under the new guidance acquisition costs are to include only those costs that are directly related to the acquisition or renewal of insurance contracts by applying a model similar to the accounting for loan origination costs. An entity may defer incremental direct costs of contract acquisition that are incurred in transactions with independent third parties or employees as well as the portion of employee compensation costs related to underwriting, policy issuance and processing, medical inspection, and contract selling for successfully negotiated contracts. Additionally, an entity may capitalize as a deferred acquisition cost only those advertising costs meeting the capitalization criteria for direct-response advertising. This change is effective for fiscal years beginning after December 15, 2011 and interim periods within those years. Early adoption as of the beginning of a fiscal year is permitted. The guidance is to be applied prospectively upon the date of adoption, with retrospective application permitted, but not required. The Company will adopt this guidance effective January 1, 2012. The Company is currently assessing the impact of the guidance on the Company s consolidated financial position, results of operations, and financial statement disclosures.

In July 2010, the FASB issued updated guidance that requires enhanced disclosures related to the allowance for credit losses and the credit quality of a company s financing receivable portfolio. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The Company will provide the required disclosures in the annual reporting period ending December 31, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning after December 15, 2010. The Company will provide these required disclosures in the interim reporting period ending March 31, 2011.

In April 2010, the FASB issued guidance clarifying that an insurance entity should not consider any separate account interests in an investment held for the benefit of policyholders to be the insurer s interests, and should not combine those interests with its general account interest in the same investment when assessing the investment for consolidation, unless the separate account interests are held for a related party policyholder, whereby consolidation of such interests must be considered under applicable variable interest guidance. This guidance is effective for interim and annual reporting periods beginning after December 15, 2010 and retrospectively to all prior periods upon the date of adoption, with early adoption permitted. The Company s adoption of this guidance effective January 1, 2011 is not expected to have a material effect on the Company s consolidated financial position, results of operations, and financial statement disclosures.

**3. ACQUISITIONS AND DISPOSITIONS**

***Agreement to Acquire AIG Star Life Insurance Co., Ltd., AIG Edison Life Insurance Company and Related Entities from AIG***

On September 30, 2010, Prudential Financial entered into a stock purchase agreement with American International Group, Inc. ( AIG ), pursuant to which Prudential Financial agreed to acquire, directly or through one or more of its subsidiaries, all of the issued and outstanding shares of preferred and common stock of AIG Star Life Insurance Co., Ltd., AIG Edison Life Insurance Company, AIG Financial Assurance Japan K.K., and AIG Edison Service Co., Ltd. for a total purchase price of $4.8 billion. The total purchase price of $4.8 billion is comprised of approximately $4.2 billion in cash and $0.6 billion in assumed third party debt, substantially all of which is expected to be repaid with excess capital of the acquired entities. All acquired entities are Japanese corporations and their businesses are in Japan. The transaction, which is expected to close in the first quarter of 2011, is subject to certain governmental approvals, including Japanese anti-competition approvals (or expirations of waiting periods) and Japanese insurance regulatory approvals, as well as other customary conditions to closing, including the execution and delivery of related transaction documents.

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Sale of investment in Wachovia Securities***

On December 31, 2009, the Company completed the sale of its minority joint venture interest in Wachovia Securities Financial Holdings, LLC ( Wachovia Securities ), which includes Wells Fargo Advisors, to Wells Fargo & Company ( Wells Fargo ). The Company s minority joint venture interest in Wachovia Securities originated as a result of the Company combining its retail securities brokerage and clearing operations with those of Wachovia Corporation ( Wachovia ) in 2003. On December 31, 2008, Wachovia merged with and into Wells Fargo, which succeeded to Wachovia s rights and obligations under the joint venture arrangements. At the closing, the Company received $4.5 billion in cash as the purchase price of its joint venture interest and de-recognized the carrying value of its investment in the joint venture and the carrying value of the associated lookback option. The pre-tax gain on sale recognized by the Company was $2.247 billion and was reflected in Equity in earnings of operating joint ventures, net of taxes.

***Acquisition of Yamato Life***

On May 1, 2009, the Company s Gibraltar Life operations acquired Yamato Life, a Japanese life insurance company that declared bankruptcy in October 2008. Gibraltar Life served as the reorganization sponsor for Yamato and under the reorganization agreement acquired Yamato by contributing $72 million of capital to Yamato. At the date of acquisition the Company recognized $2.3 billion of assets and $2.3 billion of liabilities related to Yamato. Subsequent to the acquisition, the Company renamed the acquired company The Prudential Gibraltar Financial Life Insurance Company, Ltd.

***Discontinued Operations***

Income (loss) from discontinued businesses, including charges upon disposition, are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Korean asset management operations | $ 3 | $ 4 | $ 35 | $ 15 |
| Equity sales, trading and research operations | 0 | 1 | 0 | 2 |
| Real estate investments sold or held for sale | 1 | (6) | 5 | 22 |
| Mexican asset management operations | 6 | 0 | 6 | (1) |
| Healthcare operations | 1 | 0 | 1 | 0 |
| International securities operations | 0 | 0 | (1) | 1 |

| | | | | |
|---|---|---|---|---|
| Income (loss) from discontinued operations before income taxes | 11 | (1) | 46 | 39 |
| Income tax expense (benefit) | 3 | (1) | 40 | 13 |
| Income from discontinued operations, net of taxes | $ 8 | $ 0 | $ 6 | $ 26 |

In the first quarter of 2010, the Company signed a definitive agreement to sell Prudential Investment & Securities Co. Ltd. and Prudential Asset Management Co. Ltd., which together comprise the Company s Korean asset management operations. This transaction closed in the second quarter of 2010. Included within the table above for the nine months ended September 30, 2010, is an after-tax loss of $5 million recorded in connection with the sale of these operations, consisting of a pre-tax gain of $29 million and income tax expense of $34 million. Certain tax benefits related to the sale were recognized in the fourth quarter of 2009 as a result of the change in repatriation assumption of the earnings in these operations.

Real estate investments sold or held for sale reflects the income or loss from discontinued real estate investments.

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**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Charges recorded in connection with the disposals of businesses include estimates that are subject to subsequent adjustment.

The Company s Unaudited Interim Consolidated Statements of Financial Position include total assets and total liabilities related to discontinued businesses as follows:

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Total assets | $ 112 | $ 937 |
| Total liabilities | $ 62 | $ 556 |

**4. INVESTMENTS**

***Fixed Maturities and Equity Securities***

The following tables provide information relating to fixed maturities and equity securities (excluding investments classified as trading) as of the dates indicated:

| | September 30, 2010 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses (in millions) | Fair Value | Other-than-temporary impairments in AOCI(3) |
| **Fixed maturities, available for sale** | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 9,774 | $ 1,428 | $ 43 | $ 11,159 | $ 0 |
| Obligations of U.S. states and their political subdivisions | 1,895 | 145 | 3 | 2,037 | 0 |
| Foreign government bonds | 45,544 | 4,341 | 20 | 49,865 | 0 |
| Corporate securities | 93,631 | 9,284 | 1,935 | 100,980 | (28) |
| Asset-backed securities(1) | 12,379 | 240 | 2,124 | 10,495 | (1,679) |
| Commercial mortgage-backed securities | 11,526 | 858 | 61 | 12,323 | 3 |
| Residential mortgage-backed securities(2) | 9,837 | 562 | 69 | 10,330 | (12) |
| Total fixed maturities, available for sale | $ 184,586 | $ 16,858 | $ 4,255 | $ 197,189 | $ (1,716) |

| | | | | |
|---|---|---|---|---|
| **Equity securities, available for sale** | $ 6,368 | $ 1,083 | $ 179 | $ 7,272 |

(1) Includes credit tranched securities collateralized by sub-prime mortgages, auto loans, credit cards, education loans, and other asset types.
(2) Includes publicly traded agency pass-through securities and collateralized mortgage obligations.
(3) Represents the amount of other-than-temporary impairment losses in Accumulated other comprehensive income (loss), or AOCI, which were not included in earnings. Amount excludes $542 million of net unrealized gains on impaired securities relating to changes in the value of such securities subsequent to the impairment measurement date.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | September 30, 2010 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses (in millions) | Fair Value | Other-than-temporary impairments in AOCI(3) |
| **Fixed maturities, held to maturity** | | | | | |
| Foreign government bonds | $ 1,164 | $ 120 | $ 0 | $ 1,284 | $ 0 |
| Corporate securities | 1,011 | 8 | 94 | 925 | 0 |
| Asset-backed securities(1) | 1,185 | 62 | 0 | 1,247 | 0 |
| Commercial mortgage-backed securities | 474 | 116 | 0 | 590 | 0 |
| Residential mortgage-backed securities(2) | 1,399 | 77 | 0 | 1,476 | 0 |
| Total fixed maturities, held to maturity | $ 5,233 | $ 383 | $ 94 | $ 5,522 | $ 0 |

(1) Includes credit tranched securities collateralized by auto loans, credit cards, education loans, and other asset types.
(2) Includes publicly traded agency pass-through securities and collateralized mortgage obligations.
(3) Represents the amount of other-than-temporary impairment losses in Accumulated other comprehensive income (loss), or AOCI, which were not included in earnings.

| | December 31, 2009 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses (in millions) | Fair Value | Other-than-temporary impairments in AOCI(3) |
| **Fixed maturities, available for sale** | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 8,254 | $ 384 | $ 370 | $ 8,268 | $ 0 |
| Obligations of U.S. states and their political subdivisions | 1,389 | 28 | 42 | 1,375 | 0 |
| Foreign government bonds(4) | 40,627 | 1,569 | 142 | 42,054 | 0 |
| Corporate securities(4) | 89,083 | 4,357 | 2,739 | 90,701 | (43) |
| Asset-backed securities(1) | 12,587 | 155 | 2,504 | 10,238 | (1,716) |
| Commercial mortgage-backed securities | 11,036 | 202 | 220 | 11,018 | 1 |
| Residential mortgage-backed securities(2) | 11,275 | 428 | 132 | 11,571 | (11) |
| Total fixed maturities, available for sale | $ 174,251 | $ 7,123 | $ 6,149 | $ 175,225 | $ (1,769) |
| **Equity securities, available for sale** | $ 6,106 | $ 1,014 | $ 225 | $ 6,895 | |

(1) Includes credit tranched securities collateralized by sub-prime mortgages, auto loans, credit cards, education loans, and other asset types.

(2) Includes publicly traded agency pass-through securities and collateralized mortgage obligations.
(3) Represents the amount of other-than-temporary impairment losses in "Accumulated other comprehensive income (loss)," or "AOCI," which were not included in earnings. Amount excludes $540 million of net unrealized gains on impaired securities relating to changes in the value of such securities subsequent to the impairment measurement date.
(4) Includes reclassifications to conform to current period presentation.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | December 31, 2009 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses (in millions) | Fair Value | Other-than-temporary impairments in AOCI(3) |
| **Fixed maturities, held to maturity** | | | | | |
| Foreign government bonds | $ 1,058 | $ 25 | $ 1 | $ 1,082 | $ 0 |
| Corporate securities | 876 | 1 | 126 | 751 | 0 |
| Asset-backed securities(1) | 1,112 | 16 | 3 | 1,125 | 0 |
| Commercial mortgage-backed securities | 460 | 104 | 0 | 564 | 0 |
| Residential mortgage-backed securities(2) | 1,614 | 65 | 3 | 1,676 | 0 |
| Total fixed maturities, held to maturity | $ 5,120 | $ 211 | $ 133 | $ 5,198 | $ 0 |

(1) Includes credit tranched securities collateralized by auto loans, credit cards, education loans, and other asset types.
(2) Includes publicly traded agency pass-through securities and collateralized mortgage obligations.
(3) Represents the amount of other-than-temporary impairment losses in Accumulated other comprehensive income (loss), or AOCI, which were not included in earnings.

The amortized cost and fair value of fixed maturities by contractual maturities at September 30, 2010, are as follows:

| | Available for Sale | | Held to Maturity | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value (in millions) | Amortized Cost | Fair Value |
| Due in one year or less | $ 8,477 | $ 8,596 | $ 0 | $ 0 |
| Due after one year through five years | 36,709 | 38,431 | 0 | 0 |
| Due after five years through ten years | 37,666 | 41,136 | 218 | 222 |
| Due after ten years | 67,992 | 75,878 | 1,957 | 1,987 |
| Asset-backed securities | 12,379 | 10,495 | 1,185 | 1,247 |
| Commercial mortgage-backed securities | 11,526 | 12,323 | 474 | 590 |
| Residential mortgage-backed securities | 9,837 | 10,330 | 1,399 | 1,476 |
| Total | $ 184,586 | $ 197,189 | $ 5,233 | $ 5,522 |

Actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Asset-backed, commercial mortgage-backed, and residential mortgage-backed securities are shown separately in the table above, as they are not due at a single maturity date.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The following table depicts the sources of fixed maturity proceeds and related investment gains (losses), as well as losses on impairments of both fixed maturities and equity securities:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| **Fixed maturities, available for sale** | | | | |
| Proceeds from sales | $ 2,562 | $ 3,354 | $ 8,961 | $ 19,997 |
| Proceeds from maturities/repayments | 3,986 | 4,916 | 11,762 | 13,342 |
| Gross investment gains from sales, prepayments, and maturities | 218 | 150 | 485 | 779 |
| Gross investment losses from sales and maturities | (46) | (98) | (165) | (474) |
| **Fixed maturities, held to maturity** | | | | |
| Gross investment gains from prepayments | $ 0 | $ 0 | $ 0 | $ 0 |
| Proceeds from maturities/repayments | 108 | 113 | 332 | 281 |
| **Fixed maturity and equity security impairments** | | | | |
| Net writedowns for other-than-temporary impairment losses on fixed maturities recognized in earnings(1) | $ (90) | $ (360) | $ (483) | $ (1,464) |
| Writedowns for impairments on equity securities | (25) | (223) | (101) | (979) |

(1) Excludes the portion of other-than-temporary impairments recorded in Other comprehensive income (loss), representing any difference between the fair value of the impaired debt security and the net present value of its projected future cash flows at the time of impairment.

As discussed in Note 2, a portion of certain other-than-temporary impairment ( OTTI ) losses on fixed maturity securities are recognized in Other comprehensive income (loss) ( OCI ). For these securities the net amount recognized in earnings ( credit loss impairments ) represents the difference between the amortized cost of the security and the net present value of its projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment. Any remaining difference between the fair value and amortized cost is recognized in OCI. The following table sets forth the amount of pre-tax credit loss impairments on fixed maturity securities held by the Company as of the dates indicated, for which a portion of the OTTI loss was recognized in OCI, and the corresponding changes in such amounts.

| **Credit losses recognized in earnings on fixed maturity securities held by the Company for which a portion of the OTTI loss was recognized in OCI** | | |
|---|---|---|
| | Three Months Ended September 30, 2010 | Nine Months Ended September 30, 2010 |
| | (in millions) | |
| Balance, beginning of period | $ 1,775 | $ 1,747 |
| Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period | (42) | (290) |

| | | |
|---|---|---|
| Credit loss impairments previously recognized on securities impaired to fair value during the period(1) | (24) | (32) |
| Credit loss impairment recognized in the current period on securities not previously impaired | 4 | 134 |
| Additional credit loss impairments recognized in the current period on securities previously impaired | 26 | 157 |
| Increases due to the passage of time on previously recorded credit losses | 18 | 81 |
| Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected | (10) | (50) |
| Balance, September 30, 2010 | $ 1,747 | $ 1,747 |

(1) Represents circumstances where the Company determined in the current period that it intends to sell the security or it is more likely than not that it will be required to sell the security before recovery of the security s amortized cost.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | Three Months Ended September 30, 2009 | Nine Months Ended September 30, 2009 |
|---|---|---|
| | (in millions) | |
| Balance, beginning of period | $ 1,522 | $ 0 |
| Credit losses remaining in retained earnings related to adoption of new authoritative guidance on January 1, 2009 | 0 | 658 |
| Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period | (60) | (151) |
| Credit loss impairments previously recognized on securities impaired to fair value during the period(1) | (3) | (9) |
| Credit loss impairment recognized in the current period on securities not previously impaired | 81 | 639 |
| Additional credit loss impairments recognized in the current period on securities previously impaired | 209 | 603 |
| Increases due to the passage of time on previously recorded credit losses | 13 | 29 |
| Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected | (17) | (24) |
| Balance, September 30, 2009 | $ 1,745 | $ 1,745 |

(1) Represents circumstances where the Company determined in the current period that it intends to sell the security or it is more likely than not that it will be required to sell the security before recovery of the security s amortized cost.

***Trading Account Assets Supporting Insurance Liabilities***

The following table sets forth the composition of Trading account assets supporting insurance liabilities as of the dates indicated:

| | September 30, 2010 | | December 31, 2009 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (in millions) | | | |
| Short-term investments and cash equivalents | $ 777 | $ 777 | $ 725 | $ 725 |
| Fixed maturities: | | | | |
| Corporate securities | 9,636 | 10,449 | 9,202 | 9,502 |
| Commercial mortgage-backed securities | 2,186 | 2,272 | 1,899 | 1,893 |
| Residential mortgage-backed securities | 1,271 | 1,294 | 1,434 | 1,432 |
| Asset-backed securities | 1,090 | 956 | 1,022 | 857 |

| | | | | |
|---|---|---|---|---|
| Foreign government bonds | 533 | 553 | 508 | 517 |
| U.S. government authorities and agencies and obligations of U.S. states | 419 | 420 | 169 | 159 |
| Total fixed maturities | 15,135 | 15,944 | 14,234 | 14,360 |
| Equity securities | 1,144 | 1,029 | 1,033 | 935 |
| Total trading account assets supporting insurance liabilities | $ 17,056 | $ 17,750 | $ 15,992 | $ 16,020 |

The net change in unrealized gains (losses) from trading account assets supporting insurance liabilities still held at period end, recorded within Asset management fees and other income was $363 million and $692 million during the three months ended September 30, 2010 and 2009, respectively, and $666 million and $1,689 million during the nine months ended September 30, 2010 and 2009, respectively.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Other Trading Account Assets***

The following table sets forth the composition of the Other trading account assets as of the dates indicated:

| | September 30, 2010 | | December 31, 2009 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | | (in millions) | | |
| Short-term investments and cash equivalents | $ 5 | $ 5 | $ 5 | $ 5 |
| Fixed Maturities: | | | | |
| Asset-backed securities | 749 | 698 | 1,043 | 991 |
| U.S. government authorities and agencies and obligations of U.S. states | 354 | 357 | 90 | 95 |
| Residential mortgage-backed securities | 311 | 186 | 287 | 158 |
| Corporate securities | 315 | 321 | 345 | 359 |
| Commercial mortgage-backed securities | 152 | 102 | 239 | 136 |
| Foreign government bonds | 25 | 26 | 23 | 24 |
| Total fixed maturities | 1,906 | 1,690 | 2,027 | 1,763 |
| Other(1) | 26 | 30 | 25 | 29 |
| Equity securities | 470 | 484 | 456 | 471 |
| Subtotal | $ 2,407 | $ 2,209 | $ 2,513 | $ 2,268 |
| Derivative instruments | | 3,467 | | 765 |
| Total other trading account assets | $ 2,407 | $ 5,676 | $ 2,513 | $ 3,033 |

(1) Includes reclassifications to conform to current period presentation.

The net change in unrealized gains (losses) from other trading account assets, excluding derivative instruments, still held at period end, recorded within Asset management fees and other income was $73 million and $32 million during the three months ended September 30, 2010 and 2009, respectively, and $47 million and $80 million during the nine months ended September 30, 2010 and 2009, respectively.

***Concentrations of Financial Instruments***

The Company monitors its concentrations of financial instruments on an ongoing basis, and mitigates credit risk by maintaining a diversified investment portfolio which limits exposure to any one issuer.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

As of September 30, 2010 and December 31, 2009, the Company was not exposed to any concentrations of credit risk of any single issuer greater than 10% of the Company s stockholders equity, other than securities of the U.S. government, certain U.S. government agencies and certain securities guaranteed by the U.S. government, as well as the securities disclosed below.

| | September 30, 2010 | | December 31, 2009 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (in millions) | | | |
| **Investments in Japanese government and government agency securities:** | | | | |
| Fixed maturities, available for sale | $ 37,307 | $ 40,610 | $ 33,393 | $ 34,449 |
| Fixed maturities, held to maturity | 1,164 | 1,284 | 1,058 | 1,082 |
| Trading account assets supporting insurance liabilities | 406 | 421 | 361 | 368 |
| Other trading account assets | 16 | 16 | 22 | 23 |
| Short-term investments | 0 | 0 | 0 | 0 |
| Cash equivalents | 0 | 0 | 0 | 0 |
| Total | $ 38,893 | $ 42,331 | $ 34,834 | $ 35,922 |

| | September 30, 2010 | | December 31, 2009 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (in millions) | | | |
| **Investments in South Korean government and government agency securities:** | | | | |
| Fixed maturities, available for sale | $ 3,790 | $ 4,186 | $ 3,284 | $ 3,280 |
| Fixed maturities, held to maturity | 0 | 0 | 0 | 0 |
| Trading account assets supporting insurance liabilities | 17 | 18 | 17 | 18 |
| Other trading account assets | 2 | 2 | 1 | 1 |
| Short-term investments | 0 | 0 | 0 | 0 |
| Cash equivalents | 0 | 0 | 0 | 0 |
| Total | $ 3,809 | $ 4,206 | $ 3,302 | $ 3,299 |

| | September 30, 2010 | | December 31, 2009 | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (in millions) | | | |
| **Investments in Federal Home Loan Mortgage Corporation (FHLMC) securities:** | | | | |
| Fixed maturities, available for sale | $ 379 | $ 383 | $ 148 | $ 158 |
| Fixed maturities, held to maturity | 0 | 0 | 0 | 0 |
| Trading account assets supporting insurance liabilities | 165 | 165 | 161 | 161 |
| Other trading account assets | 0 | 0 | 0 | 0 |
| Short-term investments | 881 | 881 | 1,333 | 1,333 |
| Cash equivalents | 1,931 | 1,931 | 328 | 328 |

| | | | | |
|---|---|---|---|---|
| Total | $ 3,356 | $ 3,360 | $ 1,970 | $ 1,980 |

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Net Investment Income***

Net investment income for the three and nine months ended September 30, 2010 and 2009 was from the following sources:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Fixed maturities, available for sale | $ 2,109 | $ 2,014 | $ 6,229 | $ 6,115 |
| Fixed maturities, held to maturity | 32 | 37 | 100 | 105 |
| Equity securities, available for sale | 71 | 80 | 219 | 235 |
| Trading account assets | 218 | 203 | 615 | 613 |
| Commercial mortgage and other loans | 487 | 480 | 1,404 | 1,448 |
| Policy loans | 146 | 144 | 429 | 422 |
| Broker-dealer related receivables | 4 | 4 | 10 | 15 |
| Short-term investments and cash equivalents | 14 | 22 | 37 | 113 |
| Other long-term investments | 38 | (15) | 66 | (174) |
| Gross investment income | 3,119 | 2,969 | 9,109 | 8,892 |
| Less: investment expenses | (101) | (115) | (303) | (358) |
| Net investment income | $ 3,018 | $ 2,854 | $ 8,806 | $ 8,534 |

***Realized Investment Gains (Losses), Net***

Realized investment gains (losses), net, for the three and nine months ended September 30, 2010 and 2009 were from the following sources:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Fixed maturities | $ 82 | $ (308) | $ (163) | $ (1,159) |
| Equity securities | 29 | (123) | 128 | (942) |
| Commercial mortgage and other loans | 44 | (124) | 51 | (452) |
| Investment real-estate | 0 | (26) | 1 | (47) |
| Joint ventures and limited partnerships | (12) | 9 | (36) | (44) |

| | | | | |
|---|---|---|---|---|
| Derivatives(1) | (122) | 123 | 2,208 | 51 |
| Other | 8 | 5 | 15 | 16 |
| Realized investment gains (losses), net | $ 29 | $ (444) | $ 2,204 | $ (2,577) |

(1) Includes the offset of hedged items in qualifying effective hedge relationships prior to maturity or termination.

***Net Unrealized Investment Gains (Losses)***

Net unrealized investment gains and losses on securities classified as available for sale and certain other long-term investments and other assets are included in the Consolidated Statements of Financial Position as a component of Accumulated other comprehensive income (loss), or AOCI. Changes in these amounts include reclassification adjustments to exclude from Other comprehensive income (loss) those items that are included

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

as part of Net income for a period that had been part of Other comprehensive income (loss) in earlier periods. The amounts for the periods indicated below, split between amounts related to fixed maturity securities on which an OTTI loss has been recognized, and all other net unrealized investment gains and losses, are as follows:

*Net Unrealized Investment Gains and Losses on Fixed Maturity Securities on which an OTTI loss has been recognized*

| | Net Unrealized Gains (Losses) on Investments | Deferred Policy Acquisition Costs, Deferred Sales Inducements, and Valuation of Business Acquired | Future Policy Benefits | Policyholders Dividends | Deferred Income Tax (Liability) Benefit | Accumulated Other Comprehensive Income (Loss) Related To Net Unrealized Investment Gains (Losses) |
|---|---|---|---|---|---|---|
| | | | (in millions) | | | |
| Balance, December 31, 2009 | $ (1,229) | $ 193 | $ 2 | $ 0 | $ 355 | $ (679) |
| Net investment gains (losses) on investments arising during the period | (178) | | | | 62 | (116) |
| Reclassification adjustment for (gains) losses included in net income | 254 | | | | (89) | 165 |
| Reclassification adjustment for OTTI losses excluded from net income(1) | (34) | | | | 12 | (22) |
| Impact of net unrealized investment (gains) losses on deferred policy acquisition costs, deferred sales inducements and valuation of business acquired | | (144) | | | 50 | (94) |
| Impact of net unrealized investment (gains) losses on future policy benefits | | | (12) | | 4 | (8) |
| Impact of net unrealized investment (gains) losses on policyholders dividends | | | | 450 | (158) | 292 |
| Balance, September 30, 2010 | $ (1,187) | $ 49 | $ (10) | $ 450 | $ 236 | $ (462) |

(1) Represents transfers in related to the portion of OTTI losses recognized during the period that were not recognized in earnings for securities with no prior OTTI loss.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*All Other Net Unrealized Investment Gains and Losses in AOCI*

| | Net Unrealized Gains (Losses) on Investments(1) | Deferred Policy Acquisition Costs, Deferred Sales Inducements, and Valuation of Business Acquired | Future Policy Benefits | Policyholders Dividends | Deferred Income Tax (Liability) Benefit | Accumulated Other Comprehensive Income (Loss) Related To Net Unrealized Investment Gains (Losses) |
|---|---|---|---|---|---|---|
| | | | (in millions) | | | |
| Balance, December 31, 2009 | $ 2,885 | $ (803) | $ (509) | $ 0 | $ (383) | $ 1,190 |
| Net investment gains (losses) on investments arising during the period | 11,881 | | | | (4,066) | 7,815 |
| Reclassification adjustment for (gains) losses included in net income | (208) | | | | 73 | (135) |
| Reclassification adjustment for OTTI losses excluded from net income(2) | 34 | | | | (12) | 22 |
| Impact of net unrealized investment (gains) losses on deferred policy acquisition costs, deferred sales inducements and valuation of business acquired | | (612) | | | 214 | (398) |
| Impact of net unrealized investment (gains) losses on future policy benefits | | | (708) | | 248 | (460) |
| Impact of net unrealized investment (gains) losses on policyholders dividends | | | | (3,603) | 1,261 | (2,342) |
| Balance, September 30, 2010 | $ 14,592 | $ (1,415) | $ (1,217) | $ (3,603) | $ (2,665) | $ 5,692 |

(1) Includes cash flow hedges. See Note 14 for information on cash flow hedges.
(2) Represents transfers out related to the portion of OTTI losses recognized during the period that were not recognized in earnings for securities with no prior OTTI loss.

The table below presents net unrealized gains (losses) on investments by asset class as of the dates indicated:

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Fixed maturity securities on which an OTTI loss has been recognized | $ (1,187) | $ (1,229) |

| | | |
|---|---|---|
| Fixed maturity securities, available for sale all other | 13,790 | 2,203 |
| Equity securities, available for sale | 904 | 789 |
| Derivatives designated as cash flow hedges(1) | (293) | (317) |
| Other investments(2) | 191 | 210 |
| Net unrealized gains (losses) on investments | $ 13,405 | $ 1,656 |

(1) See Note 14 for more information on cash flow hedges.

(2) Includes $242 million of net unrealized losses on held to maturity securities that were transferred from available for sale. Also includes net unrealized gains on certain joint ventures that are strategic in nature and are included in Other assets.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Duration of Gross Unrealized Loss Positions for Fixed Maturities***

The following table shows the fair value and gross unrealized losses aggregated by investment category and length of time that individual fixed maturity securities have been in a continuous unrealized loss position, as of the dates indicated:

| | September 30, 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in millions) | | | | | |
| **Fixed maturities(1)** | | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 623 | $ 3 | $ 468 | $ 40 | $ 1,091 | $ 43 |
| Obligations of U.S. states and their political subdivisions | 55 | 2 | 49 | 1 | 104 | 3 |
| Foreign government bonds | 487 | 3 | 115 | 17 | 602 | 20 |
| Corporate securities | 5,489 | 266 | 10,603 | 1,763 | 16,092 | 2,029 |
| Commercial mortgage-backed securities | 132 | 2 | 382 | 59 | 514 | 61 |
| Asset-backed securities | 933 | 18 | 5,771 | 2,106 | 6,704 | 2,124 |
| Residential mortgage-backed securities | 331 | 3 | 501 | 66 | 832 | 69 |
| Total | $ 8,050 | $ 297 | $ 17,889 | $ 4,052 | $ 25,939 | $ 4,349 |

(1) Includes $600 million of fair value and $94 million of gross unrealized losses at September 30, 2010 on securities classified as held to maturity, a portion of which are not reflected in accumulated other comprehensive income.

| | December 31, 2009 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in millions) | | | | | |
| **Fixed maturities(2)** | | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 4,058 | $ 259 | $ 475 | $ 111 | $ 4,533 | $ 370 |
| Obligations of U.S. states and their political subdivisions | 936 | 42 | 7 | 0 | 943 | 42 |
| Foreign government bonds(1) | 5,251 | 101 | 515 | 42 | 5,766 | 143 |
| Corporate securities(1) | 10,164 | 346 | 17,397 | 2,519 | 27,561 | 2,865 |
| Commercial mortgage-backed securities | 1,471 | 40 | 3,216 | 180 | 4,687 | 220 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Asset-backed securities | 1,619 | 565 | 6,128 | 1,942 | 7,747 | 2,507 |
| Residential mortgage-backed securities | 1,567 | 21 | 1,150 | 114 | 2,717 | 135 |
| Total | $ 25,066 | $ 1,374 | $ 28,888 | $ 4,908 | $ 53,954 | $ 6,282 |

(1) Includes reclassifications to conform to current period presentation.

(2) Includes $1,216 million of fair value and $133 million of gross unrealized losses at December 31, 2009 on securities classified as held to maturity, a portion of which are not reflected in accumulated other comprehensive income.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The gross unrealized losses at September 30, 2010 and December 31, 2009 are composed of $2,734 million and $4,240 million related to high or highest quality securities based on NAIC or equivalent rating and $1,615 million and $2,042 million related to other than high or highest quality securities based on NAIC or equivalent rating. At September 30, 2010, $2,711 million of the gross unrealized losses represented declines in value of greater than 20%, $643 million of which had been in that position for less than six months, as compared to $3,594 million at December 31, 2009, that represented declines in value of greater than 20%, $588 million of which had been in that position for less than six months. At September 30, 2010, the $4,052 million of gross unrealized losses of twelve months or more were concentrated in asset-backed securities, and in the manufacturing, services, and finance sectors of the Company s corporate securities. At December 31, 2009, the $4,908 million of gross unrealized losses of twelve months or more were concentrated in asset-backed securities, and in the manufacturing and finance sectors of the Company s corporate securities. In accordance with its policy described in Note 2, the Company concluded that an adjustment to earnings for other-than-temporary impairments for these securities was not warranted at September 30, 2010 or December 31, 2009. These conclusions are based on a detailed analysis of the underlying credit and cash flows on each security. The gross unrealized losses are primarily attributable to credit spread widening and increased liquidity discounts. At September 30, 2010, the Company does not intend to sell the securities and it is not more likely than not that the Company will be required to sell the securities before the anticipated recovery of its remaining amortized cost basis.

***Duration of Gross Unrealized Loss Positions for Equity Securities***

The following table shows the fair value and gross unrealized losses aggregated by length of time that individual equity securities have been in a continuous unrealized loss position, as of the following dates:

| | September 30, 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in millions) | | | | | |
| Equity securities, available for sale | $ 1,447 | $ 142 | $ 348 | $ 37 | $ 1,795 | $ 179 |

| | December 31, 2009 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in millions) | | | | | |
| Equity securities, available for sale | $ 1,159 | $ 142 | $ 754 | $ 83 | $ 1,913 | $ 225 |

At September 30, 2010, $58 million of the gross unrealized losses represented declines of greater than 20%, $42 million of which had been in that position for less than six months. At December 31, 2009, $62 million of the gross unrealized losses represented declines of greater than 20%, $37 million of which had been in that position for less than six months. Perpetual preferred securities have characteristics of both debt and equity securities. Since an impairment model similar to fixed maturity securities is applied to these securities, an other-than-temporary impairment has not been recognized on certain perpetual preferred securities that have been in a continuous unrealized loss position for twelve months or more as of September 30, 2010, and December 31, 2009. In accordance with its policy described in Note 2, the Company concluded that an adjustment for other-than-temporary impairments for these equity securities was not warranted at September 30, 2010 or December 31, 2009.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

**5. VARIABLE INTEREST ENTITIES**

In the normal course of its activities, the Company enters into relationships with various special purpose entities and other entities that are deemed to be variable interest entities ( VIEs ). A VIE is an entity that either (1) has equity investors that lack certain essential characteristics of a controlling financial interest (including the ability to control activities of the entity, the obligation to absorb the entity s expected losses and the right to receive the entity s expected residual returns) or (2) lacks sufficient equity to finance its own activities without financial support provided by other entities, which in turn would be expected to absorb at least some of the expected losses of the VIE.

If the Company determines that it is the VIE s primary beneficiary it consolidates the VIE. There are currently two models for determining whether or not the Company is the primary beneficiary of a VIE. The first relates to those VIE s that have the characteristics of an investment company and for which certain other conditions are true. These conditions are that (1) the Company does not have the implicit or explicit obligation to fund losses of the VIE and (2) the VIE is not a securitization entity, asset-backed financing entity or an entity that was formerly considered a qualified special-purpose entity. In this model the Company is the primary beneficiary if it stands to absorb a majority of the VIE s expected losses or to receive a majority of the VIE s expected residual returns and would be required to consolidate the VIE.

For all other VIE s, the Company is the primary beneficiary if the Company has (1) the power to direct the activities of the VIE that most significantly impact the economic performance of the entity and (2) the obligation to absorb losses of the entity that could be potentially significant to the VIE or the right to receive benefits from the entity that could be potentially significant. If both conditions are present the Company would be required to consolidate the VIE.

***Consolidated Variable Interest Entities for which the Company is the Sponsor***

The Company is the sponsor of certain asset-backed investment vehicles (commonly referred to as collateralized debt obligations, or CDOs ) and certain other vehicles for which the Company earns fee income for investment management services, including certain investment structures which the Company s asset management business invests with other co-investors in investment funds referred to as feeder funds. The Company sells or syndicates investments through these vehicles, principally as part of the proprietary investing activity of the Company s asset management businesses. Additionally, the Company may invest in debt or equity securities issued by these vehicles. CDOs raise capital by issuing debt securities, and use the proceeds to purchase investments, typically interest-bearing financial instruments. The Company analyzes these relationships to determine whether it has (1) the power to direct the activities of the VIE that most significantly impact the economic performance of the entity and (2) the obligation to absorb losses of the entity that could be potentially significant to the VIE or the right to receive benefits from the entity that could be potentially significant and thus is the primary beneficiary. This analysis includes a review of (1) the Company s rights and responsibilities as sponsor, (2) fees received by the Company and (3) other interests (if any) held by the Company. The Company is not required to provide, and has not provided, material financial or other support to any VIE for which it is the sponsor.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The Company has determined that it is the primary beneficiary of certain VIEs that it sponsors, including one CDO and certain other investment structures, as it meets both conditions listed above. The table below reflects the carrying amount and balance sheet caption in which the assets and liabilities of consolidated VIEs for which the Company is the sponsor are reported. The assets of these VIE s are restricted and must be used first to settle liabilities of the VIE. The creditors of these VIEs do not have recourse to the Company in excess of the assets contained within the VIE.

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Fixed maturities, available for sale | $ 58 | $ 68 |
| Trading account assets supporting insurance liabilities | 9 | 7 |
| Commercial mortgage and other loans | 356 | 412 |
| Other long-term investments | 3 | 10 |
| Cash and cash equivalents | 88 | 44 |
| Accrued investment income | 2 | 2 |
| Other assets | 3 | 4 |
| Separate account assets | 19 | 38 |
| Total assets of consolidated VIEs | $ 538 | $ 585 |
| Other liabilities | 380 | 413 |
| Separate account liabilities | 19 | 38 |
| Total liabilities of consolidated VIEs | $ 399 | $ 451 |

The Company also consolidates a VIE whose beneficial interests are wholly owned by consolidated subsidiaries. This VIE is not included in the table above and the Company does not currently intend to sell these beneficial interests to third parties.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Other Consolidated Variable Interest Entities***

The Company is the primary beneficiary of certain VIEs in which the Company has invested, as part of its investment activities. Included among these structured investments are structured investments issued by a VIE that manages yen-denominated investments coupled with cross-currency coupon swap agreements thereby creating synthetic dual currency investments. The Company s involvement in the structuring of these investments combined with its economic interest indicates that the Company is the primary beneficiary. The Company has not provided material financial or other support that was not contractually required to these VIEs. The table below reflects the carrying amount and balance sheet caption in which the assets and liabilities of consolidated VIEs for which the Company is not the sponsor are reported. These liabilities primarily comprise obligations under debt instruments issued by the VIEs that are non-recourse to the Company. The creditors of each consolidated VIE have recourse only to the assets of that VIE.

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Fixed maturities, available for sale | $ 119 | $ 107 |
| Fixed maturities, held to maturity | 1,097 | 985 |
| Other trading account assets | 0 | 0 |
| Other long-term investments | (40) | (48) |
| Cash and cash equivalents | 0 | 0 |
| Accrued investment income | 4 | 4 |
| Other assets | 0 | 0 |
| Total assets of consolidated VIEs | $ 1,180 | $ 1,048 |
| Total liabilities of consolidated VIEs | $ 0 | $ 0 |

In addition, not reflected in the table above, the Company has created a trust that is a VIE, to facilitate Prudential Insurance s Funding Agreement Notes Issuance Program ( FANIP ). The trust issues medium-term notes secured by funding agreements issued to the trust by Prudential Insurance with the proceeds of such notes. The trust is the beneficiary of an indemnity agreement with the Company that provides that the Company is responsible for costs related to the notes issued with limited exception. As a result, the Company has determined that it is the primary beneficiary of the trust, which is therefore consolidated.

The funding agreements represent an intercompany transaction that is eliminated upon consolidation. However, in recognition of the security interest in such funding agreements, the trust s medium-term note liability of $3,509 million and $4,927 million at September 30, 2010 and December 31, 2009, respectively, is classified within Policyholders account balances. Creditors of the trust have recourse to Prudential Insurance if the trust fails to make contractual payments on the medium-term notes. The Company has not provided material financial or other support that was not contractually required to the trust.

***Unconsolidated Variable Interest Entities***

The Company has determined that it is not the primary beneficiary of certain VIEs that it sponsors, including certain CDOs and other investment structures, as it does not have both (1) the power to direct the activities of the VIE that most significantly impact the economic performance of the entity and (2) the obligation to absorb losses of the entity that could be potentially significant to the VIE or the right to receive benefits from the entity that could be potentially significant. The Company s maximum exposure to loss resulting from its relationship with unconsolidated VIEs it sponsors is limited to its investment in the VIEs, which was $507

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

million and $452 million at September 30, 2010 and December 31, 2009, respectively. These investments are reflected in Fixed maturities, available for sale, Other trading account assets, at fair value and Other long-term investments. The fair value of assets held within these unconsolidated VIEs was $8,163 million and $8,194 million as of September 30, 2010 and December 31, 2009, respectively. There are no liabilities associated with these unconsolidated VIEs on the Company s balance sheet.

In the normal course of its activities, the Company will invest in joint ventures and limited partnerships. These ventures include hedge funds, private equity funds and real estate related funds and may or may not be VIEs. The Company s maximum exposure to loss on these investments, both VIEs and non-VIEs, is limited to the amount of its investment. The Company has determined that it is not required to consolidate these entities because either (1) it does not control them or (2) it does not have the obligation to absorb losses of the entities that could be potentially significant to the entities or the right to receive benefits from the entities that could be potentially significant. The Company classifies these investments as Other long-term investments and its maximum exposure to loss associated with these entities was $3,403 million and $3,251 million as of September 30, 2010 and December 31, 2009, respectively.

In addition, in the normal course of its activities, the Company will invest in structured investments including VIEs for which it is not the sponsor. These structured investments typically invest in fixed income investments and are managed by third parties and include asset-backed securities, commercial mortgage-backed securities and residential mortgage-backed securities. The Company s maximum exposure to loss on these structured investments, both VIEs and non-VIEs, is limited to the amount of its investment. See Note 4 for details regarding the carrying amounts and classification of these assets. The Company has not provided material financial or other support that was not contractually required to these structures. The Company has determined that it is not the primary beneficiary of these structures due to the fact that it does not control these entities.

Included among these structured investments are asset-backed securities issued by VIEs that manage investments in the European market. In addition to a stated coupon, each investment provides a return based on the VIE s portfolio of assets and related investment activity. The market value of these VIEs was approximately $6.1 billion and $7.5 billion as of September 30, 2010 and December 31, 2009, respectively, and these VIEs were financed primarily through the issuance of notes similar to those purchased by the Company. The Company generally accounts for these investments as available for sale fixed maturities containing embedded derivatives that are bifurcated and marked-to-market through Realized investment gains (losses), net, based upon the change in value of the underlying portfolio. The Company s variable interest in each of these VIEs represents less than 50% of the only class of variable interests issued by the VIE. The Company s maximum exposure to loss from these interests was $750 million and $723 million at September 30, 2010 and December 31, 2009, respectively, which includes the fair value of the embedded derivatives.

**6. CLOSED BLOCK**

On the date of demutualization, Prudential Insurance established a Closed Block for certain individual life insurance policies and annuities issued by Prudential Insurance in the U.S. The recorded assets and liabilities were allocated to the Closed Block at their historical carrying amounts. The Closed Block forms the principal component of the Closed Block Business.

The policies included in the Closed Block are specified individual life insurance policies and individual annuity contracts that were in force on the effective date of the Plan of Reorganization and for which Prudential Insurance is currently paying or expects to pay experience-based policy dividends. Assets have been allocated to the Closed Block in an amount that has been determined to produce cash flows which, together with revenues from policies included in the Closed Block, are expected to be sufficient to support obligations and liabilities

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

relating to these policies, including provision for payment of benefits, certain expenses, and taxes and to provide for continuation of the policyholder dividend scales in effect in 2000, assuming experience underlying such scales continues. To the extent that, over time, cash flows from the assets allocated to the Closed Block and claims and other experience related to the Closed Block are, in the aggregate, more or less favorable than what was assumed when the Closed Block was established, total dividends paid to Closed Block policyholders may be greater than or less than the total dividends that would have been paid to these policyholders if the policyholder dividend scales in effect in 2000 had been continued. Any cash flows in excess of amounts assumed will be available for distribution over time to Closed Block policyholders and will not be available to stockholders. If the Closed Block has insufficient funds to make guaranteed policy benefit payments, such payments will be made from assets outside of the Closed Block. The Closed Block will continue in effect as long as any policy in the Closed Block remains in force unless, with the consent of the New Jersey insurance regulator, it is terminated earlier.

The excess of Closed Block Liabilities over Closed Block Assets at the date of the demutualization (adjusted to eliminate the impact of related amounts in Accumulated other comprehensive income (loss) ) represented the estimated maximum future earnings at that date from the Closed Block expected to result from operations attributed to the Closed Block after income taxes. In establishing the Closed Block, the Company developed an actuarial calculation of the timing of such maximum future earnings. If actual cumulative earnings of the Closed Block from inception through the end of any given period are greater than the expected cumulative earnings, only the expected earnings will be recognized in income. Any excess of actual cumulative earnings over expected cumulative earnings will represent undistributed accumulated earnings attributable to policyholders, which are recorded as a policyholder dividend obligation. The policyholder dividend obligation represents amounts to be paid to Closed Block policyholders as an additional policyholder dividend unless otherwise offset by future Closed Block performance that is less favorable than originally expected. If the actual cumulative earnings of the Closed Block from its inception through the end of any given period are less than the expected cumulative earnings of the Closed Block, the Company will recognize only the actual earnings in income. However, the Company may reduce policyholder dividend scales, which would be intended to increase future actual earnings until the actual cumulative earnings equaled the expected cumulative earnings.

As of September 30, 2010, the Company did not recognize a cumulative earnings policyholder dividend obligation since actual cumulative earnings were below the expected cumulative earnings by $64 million. However, accumulated net unrealized investment gains that have arisen subsequent to the establishment of the Closed Block have been reflected as a policyholder dividend obligation of $3.149 billion at September 30, 2010, to be paid to Closed Block policyholders unless offset by future experience, with an offsetting amount reported in Accumulated other comprehensive income (loss). As of December 31, 2009, actual cumulative earnings were below the expected cumulative earnings, thereby eliminating the policyholder dividend obligation. Furthermore, the accumulation of net unrealized investment gains as of December 31, 2009 that had arisen subsequent to the establishment of the Closed Block, were not sufficient to overcome the cumulative earnings shortfall. See the table below for changes in the components of the policyholder dividend obligation for the nine months ended September 30, 2010.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Closed Block Liabilities and Assets designated to the Closed Block, as well as maximum future earnings to be recognized from Closed Block Liabilities and Closed Block Assets, are as follows:

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| **Closed Block Liabilities** | | |
| Future policy benefits | $ 51,597 | $ 51,774 |
| Policyholders dividends payable | 971 | 926 |
| Policyholders dividend obligation | 3,149 | 0 |
| Policyholders account balances | 5,545 | 5,588 |
| Other Closed Block liabilities | 4,607 | 4,300 |
| Total Closed Block Liabilities | 65,869 | 62,588 |
| **Closed Block Assets** | | |
| Fixed maturities, available for sale, at fair value | 41,744 | 38,448 |
| Other trading account assets, at fair value | 156 | 166 |
| Equity securities, available for sale, at fair value | 3,200 | 3,037 |
| Commercial mortgage and other loans | 7,814 | 7,751 |
| Policy loans | 5,397 | 5,418 |
| Other long-term investments | 1,660 | 1,597 |
| Short-term investments | 995 | 1,218 |
| Total investments | 60,966 | 57,635 |
| Cash and cash equivalents | 758 | 662 |
| Accrued investment income | 643 | 608 |
| Other Closed Block assets | 474 | 307 |
| Total Closed Block Assets | 62,841 | 59,212 |
| Excess of reported Closed Block Liabilities over Closed Block Assets | 3,028 | 3,376 |
| Portion of above representing accumulated other comprehensive income: | | |
| Net unrealized investment gains (losses) | 3,175 | 231 |
| Allocated to policyholder dividend obligation | (3,149) | 0 |
| Future earnings to be recognized from Closed Block Assets and Closed Block Liabilities | $ 3,054 | $ 3,607 |

Information regarding the policyholder dividend obligation is as follows:

| | Nine Months Ended September 30, 2010 (in millions) |
|---|---|
| Balance, January 1 | $ 0 |
| Impact from earnings allocable to policyholder dividend obligation | 0 |
| Change in net unrealized investment gains (losses) allocated to policyholder dividend obligation | 3,149 |
| Balance, September 30 | $ 3,149 |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Closed Block revenues and benefits and expenses for the three and nine months ended September 30, 2010 and 2009 were as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| **Revenues** | | | | |
| Premiums | $ 684 | $ 738 | $ 2,191 | $ 2,378 |
| Net investment income | 751 | 733 | 2,226 | 2,161 |
| Realized investment gains (losses), net | 66 | (22) | 766 | (1,250) |
| Other income | 32 | 36 | 31 | 88 |
| Total Closed Block revenues | 1,533 | 1,485 | 5,214 | 3,377 |
| **Benefits and Expenses** | | | | |
| Policyholders benefits | 811 | 839 | 2,572 | 2,743 |
| Interest credited to policyholders account balances | 35 | 36 | 105 | 106 |
| Dividends to policyholders | 480 | 539 | 1,462 | 795 |
| General and administrative expenses | 136 | 139 | 407 | 427 |
| Total Closed Block benefits and expenses | 1,462 | 1,553 | 4,546 | 4,071 |
| Closed Block revenues, net of Closed Block benefits and expenses, before income taxes and discontinued operations | 71 | (68) | 668 | (694) |
| Income tax expense (benefit) | (41) | (6) | 116 | (8) |
| Closed Block revenues, net of Closed Block benefits and expenses and income taxes, before discontinued operations | 112 | (62) | 552 | (686) |
| Income from discontinued operations, net of taxes | 1 | 0 | 1 | 0 |
| Closed Block revenues, net of Closed Block benefits and expenses, income taxes and discontinued operations | $ 113 | $ (62) | $ 553 | $ (686) |

**7. EQUITY**

The Company has outstanding two classes of common stock: the Common Stock and the Class B Stock. The changes in the number of shares issued, held in treasury and outstanding are as follows for the periods indicated:

| | Common Stock | | | Class B Stock |
|---|---|---|---|---|
| | Issued | Held In Treasury | Outstanding | Issued and Outstanding |
| | (in millions) | | | |
| Balance, December 31, 2009 | 641.8 | 179.7 | 462.1 | 2.0 |
| Common Stock issued | 0.0 | 0.0 | 0.0 | 0.0 |
| Common Stock acquired | 0.0 | 0.0 | 0.0 | 0.0 |
| Stock-based compensation programs(1) | 0.0 | (2.9) | 2.9 | 0.0 |
| Balance, September 30, 2010 | 641.8 | 176.8 | 465.0 | 2.0 |

(1) Represents net shares issued from treasury pursuant to the Company s stock-based compensation program.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Comprehensive Income***

The components of comprehensive income (loss) are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Net income | $ 1,242 | $ 1,032 | $ 3,017 | $ 1,215 |
| Other comprehensive income (loss), net of taxes: | | | | |
| Change in foreign currency translation adjustments | 509 | 333 | 415 | 193 |
| Change in net unrealized investments gains (losses)(1) | 1,997 | 4,763 | 4,719 | 7,865 |
| Change in pension and postretirement unrecognized net periodic benefit | 3 | 8 | 41 | 26 |
| Other comprehensive income(2) | 2,509 | 5,104 | 5,175 | 8,084 |
| Comprehensive income | 3,751 | 6,136 | 8,192 | 9,299 |
| Comprehensive (income) loss attributable to noncontrolling interests | 22 | 42 | (2) | 61 |
| Comprehensive income attributable to Prudential Financial, Inc. | $ 3,773 | $ 6,178 | $ 8,190 | $ 9,360 |

(1) Includes cash flow hedges of $(119) million and $(36) million for the three months ended September 30, 2010 and 2009, respectively and $16 million and $(66) million for the nine months ended September 30, 2010 and 2009, respectively. See Note 4 for additional information regarding unrealized investment gains (losses), including the split between amounts related to fixed maturity securities on which an other-than-temporary impairment loss has been recognized, and all other unrealized investment gains (losses).

(2) Amounts are net of tax expense of $1,084 million and $2,578 million for the three months ended September 30, 2010 and 2009, respectively and $2,507 million and $4,070 million for the nine months ended September 30, 2010 and 2009, respectively.

The balance of and changes in each component of Accumulated other comprehensive income (loss) attributable to Prudential Financial, Inc. for the nine months ended September 30, 2010 and 2009 are as follows (net of taxes):

| Accumulated Other Comprehensive Income (Loss) Attributable to Prudential Financial, Inc. | | | |
|---|---|---|---|
| Foreign Currency Translation Adjustment | Net Unrealized Investment Gains | Pension and Postretirement Unrecognized Net | Total Accumulated Other Comprehensive |

| | | (Losses)(1) | Periodic Benefit (Cost) | Income (Loss) |
|---|---|---|---|---|
| | | | (in millions) | |
| Balance, December 31, 2009 | $ 674 | $ 511 | $ (1,628) | $ (443) |
| Change in component during period | 412 | 4,719 | 41 | 5,172 |
| Balance, September 30, 2010 | $ 1,086 | $ 5,230 | $ (1,587) | $ 4,729 |

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

| | Accumulated Other Comprehensive Income (Loss) Attributable to Prudential Financial, Inc. | | | |
|---|---|---|---|---|
| | Foreign Currency Translation Adjustment | Net Unrealized Investment Gains (Losses)(1) | Pension and Postretirement Unrecognized Net Periodic Benefit (Cost) | Total Accumulated Other Comprehensive Income (Loss) |
| | | (in millions) | | |
| Balance, December 31, 2008 | $ 375 | $ (6,735) | $ (983) | $ (7,343) |
| Change in component during period | 210 | 7,865 | 26 | 8,101 |
| Impact of adoption of guidance for other-than-temporary impairments of debt securities(2) | 0 | (659) | 0 | (659) |
| Balance, September 30, 2009 | $ 585 | $ 471 | $ (957) | $ 99 |

(1) Includes cash flow hedges of $(189) million and $(205) million as of September 30, 2010 and December 31, 2009, respectively and $(213) million and $(147) million as of September 30, 2009 and December 31, 2008, respectively. See Note 4 for additional information regarding unrealized investment gains (losses), including the split between amounts related to fixed maturity securities on which an other-than-temporary impairment loss has been recognized, and all other unrealized investment gains (losses).

(2) See Note 2 for additional information on the adoption of guidance for other-than-temporary impairments of debt securities.

## 8. EARNINGS PER SHARE

The Company has outstanding two separate classes of common stock. The Common Stock reflects the performance of the Financial Services Businesses and the Class B Stock reflects the performance of the Closed Block Business. Accordingly, earnings per share is calculated separately for each of these two classes of common stock.

Net income for the Financial Services Businesses and the Closed Block Business is determined in accordance with U.S. GAAP and includes general and administrative expenses charged to each of the respective businesses based on the Company s methodology for the allocation of such expenses. Cash flows between the Financial Services Businesses and the Closed Block Business related to administrative expenses are determined by a policy servicing fee arrangement that is based upon insurance and policies in force and statutory cash premiums. To the extent reported administrative expenses vary from these cash flow amounts, the differences are recorded, on an after tax basis, as direct equity adjustments to the equity balances of the businesses.

The direct equity adjustments modify the earnings available to each of the classes of common stock for earnings per share purposes.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Common Stock***

A reconciliation of the numerators and denominators of the basic and diluted per share computations is as follows:

| | Three Months Ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | 2009 | | |
| | Income | Weighted Average Shares | Per Share Amount | Income | Weighted Average Shares | Per Share Amount |
| | (in millions, except per share amounts) | | | | | |
| **Basic earnings per share** | | | | | | |
| Income from continuing operations attributable to the Financial Services Businesses | $ 1,158 | | | $ 1,040 | | |
| Direct equity adjustment | 9 | | | 12 | | |
| Less: Income (loss) attributable to noncontrolling interests | (2) | | | (50) | | |
| Less: Earnings allocated to participating unvested share-based payment awards | 15 | | | 12 | | |
| Income from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment | $ 1,154 | 464.8 | $ 2.48 | $ 1,090 | 461.2 | $ 2.36 |
| **Effect of dilutive securities and compensation programs** | | | | | | |
| Add: Earnings allocated to participating unvested share-based payment awards Basic | $ 15 | | | $ 12 | | |
| Less: Earnings allocated to participating unvested share-based payment awards Diluted | 15 | | | 12 | | |
| Stock options | | 2.9 | | | 2.4 | |
| Deferred and long-term compensation programs | | 0.4 | | | 0.3 | |
| Exchangeable Surplus Notes | 4 | 5.1 | | 1 | 0.7 | |
| **Diluted earnings per share** | | | | | | |
| Income from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment | $ 1,158 | 473.2 | $ 2.45 | $ 1,091 | 464.6 | $ 2.35 |

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | Nine Months Ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | 2009 | | |
| | Income | Weighted Average Shares | Per Share Amount | Income | Weighted Average Shares | Per Share Amount |
| | (in millions, except per share amounts) | | | | | |
| **Basic earnings per share** | | | | | | |
| Income from continuing operations attributable to the Financial Services Businesses | $ 2,495 | | | $ 1,553 | | |
| Direct equity adjustment | 29 | | | 34 | | |
| Less: Income (loss) attributable to noncontrolling interests | (1) | | | (44) | | |
| Less: Earnings allocated to participating unvested share-based payment awards | 33 | | | 18 | | |
| Income from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment | $ 2,492 | 464.0 | $ 5.37 | $ 1,613 | 438.8 | $ 3.68 |
| **Effect of dilutive securities and compensation programs** | | | | | | |
| Add: Earnings allocated to participating unvested share-based payment awards Basic | $ 33 | | | $ 18 | | |
| Less: Earnings allocated to participating unvested share-based payment awards Diluted | 32 | | | 18 | | |
| Stock options | | 3.1 | | | 1.2 | |
| Deferred and long-term compensation programs | | 0.5 | | | 0.6 | |
| Exchangeable Surplus Notes | 13 | 5.1 | | 0 | 0.0 | |
| **Diluted earnings per share** | | | | | | |
| Income from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment | $ 2,506 | 472.7 | $ 5.30 | $ 1,613 | 440.6 | $ 3.66 |

Unvested share-based payment awards that contain nonforfeitable rights to dividends are participating securities and included in the computation of earnings per share pursuant to the two-class method. Under this method, earnings of the Financial Services Businesses attributable to Prudential Financial, Inc. are allocated between Common Stock and the participating awards, as if the awards were a second class of stock. Undistributed earnings allocated to participating unvested share-based payment awards for the three months ended September 30, 2010 and 2009 were based on 6.2 million and 5.3 million of such awards, respectively, weighted for the period they were outstanding. Undistributed earnings allocated to participating unvested share-based payment awards for the nine months ended September 30, 2010 and 2009 were based on 6.1 million and 4.9 million of such awards, respectively, weighted for the period they were outstanding. The computation of earnings per share of Common Stock excludes the dilutive impact of participating unvested share-based awards based on the application of the two-class method.

For the three months ended September 30, 2010 and 2009, 11.2 million and 10.4 million options, respectively, weighted for the portion of the period they were outstanding, with a weighted average exercise price of $70.65 and $72.65 per share, respectively, were excluded from the computation of diluted earnings per share because the options, based on application of the treasury stock method, were antidilutive. For the nine months ended September 30, 2010 and 2009, 10.3 million and 14.1 million options, respectively, weighted for the

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

portion of the period they were outstanding, with a weighted average exercise price of $72.00 and $62.87 per share, respectively, were excluded from the computation of diluted earnings per share because the options, based on application of the treasury stock method, were antidilutive.

In September 2009, the Company issued $500 million of surplus notes with an interest rate of 5.36% per annum which are exchangeable at the option of the note holders for shares of Common Stock. The exchange rate used in the diluted earnings per share calculation for the surplus notes is 10.1235 shares of Common Stock per each $1,000 principal amount of surplus notes. In calculating diluted earnings per share under the if-converted method, the potential shares that would be issued assuming a hypothetical exchange, weighted for the period the notes are outstanding, is added to the denominator, and interest expense, net of tax, is added to the numerator, if the overall effect is dilutive. For the nine months ended September 30, 2009, the hypothetical impact of these shares was antidilutive and therefore excluded from the computation of diluted earnings per share.

The Company s convertible senior notes provide for the Company to issue shares of its Common Stock as a component of the conversion of the notes. As of September 30, 2010, $2 million of senior notes related to the $2.0 billion December 2006 issuance remain outstanding. These will be dilutive to earnings per share if the average market price of the Common Stock for a particular period is above the initial conversion price of $104.21. As of September 30, 2010, $0.2 million of senior notes related to the $3.0 billion December 2007 issuance remain outstanding. These senior notes will be dilutive to earnings per share if the average market price of the Common Stock for a particular period is above the initial conversion price of $132.39.

***Class B Stock***

Income (loss) from continuing operations per share of Class B Stock for the three and nine months ended September 30, are presented below. There are no potentially dilutive shares associated with the Class B Stock.

| | Three Months Ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | 2009 | | |
| | Income | Weighted Average Shares | Per Share Amount | Income | Weighted Average Shares | Per Share Amount |
| | (in millions, except per share amounts) | | | | | |
| **Basic earnings per share** | | | | | | |
| Income (loss) from continuing operations attributable to the Closed Block Business | $ 76 | | | $ (8) | | |
| Less: Direct equity adjustment | 9 | | | 12 | | |
| Income (loss) from continuing operations attributable to the Closed Block Business available to holders of Class B Stock after direct equity adjustment | $ 67 | 2.0 | $ 33.50 | $ (20) | 2.0 | $ (10.00) |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | Nine Months Ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | 2009 | | |
| | Income | Weighted Average Shares | Per Share Amount | Income | Weighted Average Shares | Per Share Amount |
| | (in millions, except per share amounts) | | | | | |
| **Basic earnings per share** | | | | | | |
| Income (loss) from continuing operations attributable to the Closed Block Business | $ 516 | | | $ (364) | | |
| Less: Direct equity adjustment | 29 | | | 34 | | |
| Income (loss) from continuing operations attributable to the Closed Block Business available to holders of Class B Stock after direct equity adjustment | $ 487 | 2.0 | $ 243.50 | $ (398) | 2.0 | $ (199.00) |

**9. SHORT-TERM AND LONG-TERM DEBT**

***Commercial Paper***

The Company issues commercial paper under the two programs described below primarily to manage operating cash flows and existing commitments, to meet working capital needs and to take advantage of current investment opportunities. At September 30, 2010 and December 31, 2009, the weighted average maturity of total commercial paper outstanding was 35 and 27 days, respectively.

Prudential Financial has a commercial paper program rated A-1 by Standard & Poor s Rating Services ( S&P ), P-2 by Moody s Investors Service, Inc. ( Moody s ) and F2 by Fitch Ratings Ltd. ( Fitch ) as of September 30, 2010.

Prudential Funding, LLC, a wholly owned subsidiary of Prudential Insurance has a commercial paper program, rated A-1+ by S&P, P-2 by Moody s and F1 by Fitch as of September 30, 2010. Prudential Financial has issued a subordinated guarantee covering Prudential Funding s domestic commercial paper program.

Both commercial paper programs are backed by our unsecured committed lines of credit. As of September 30, 2010, Prudential Financial, Prudential Insurance and Prudential Funding had unsecured committed lines of credit totaling $3.9 billion, which reflects a reduction from $4.3 billion effective July 15, 2010, in connection with an amendment to certain terms and conditions of the credit facilities. There were no outstanding borrowings under these facilities as of September 30, 2010.

The table below presents the Company s total outstanding commercial paper borrowings as of the dates indicated:

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Prudential Financial | $ 249 | $ 146 |
| Prudential Funding, LLC | 1,092 | 730 |
| Total outstanding commercial paper borrowings | $ 1,341 | $ 876 |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Medium-term Notes***

On January 14, 2010, Prudential Financial issued under its Medium-term Notes, Series D program $500 million of 2.75% notes due January 2013 and $750 million of 3.875% notes due January 2015. On June 21, 2010, Prudential Financial issued under its Medium-term Notes, Series D program $650 million of 5.375% notes due June 2020 and $350 million of 6.625% notes due June 2040.

***Retail Medium-term Notes***

Prudential Financial also maintains a retail medium-term notes program, including the InterNotes® program, under its shelf registration statement with an authorized issuance capacity of $5.0 billion. As of September 30, 2010, the outstanding balance of retail notes was $2.8 billion, a decrease of $432 million from December 31, 2009, resulting primarily from maturities and redemptions at the request of the Company.

***Federal Home Loan Bank of New York***

Prudential Insurance is a member of the Federal Home Loan Bank of New York, or FHLBNY. Membership allows Prudential Insurance access to the FHLBNY s financial services, including the ability to obtain collateralized loans and to issue collateralized funding agreements that can be used as an alternative source of liquidity. FHLBNY borrowings and funding agreements are collateralized by qualifying mortgage-related assets or U.S. Treasury securities, the fair value of which must be maintained at certain specified levels relative to outstanding borrowings, depending on the type of asset pledged. FHLBNY membership requires Prudential Insurance to own member stock and borrowings require the purchase of activity-based stock in an amount equal to 4.5% of outstanding borrowings. Under FHLBNY guidelines, if Prudential Insurance s financial strength ratings decline below A/A2/A Stable by S&P/Moody s/Fitch, respectively, and the FHLBNY does not receive written assurances from the New Jersey Department of Banking and Insurance, or NJDOBI, regarding Prudential Insurance s solvency, new borrowings from the FHLBNY would be limited to a term of 90 days or less. Currently there are no restrictions on the term of borrowings from the FHLBNY.

NJDOBI permits Prudential Insurance to pledge collateral to the FHLBNY in an amount up to 7% of its prior year-end statutory net admitted assets, excluding separate account assets. This limitation resets to 5% on December 31, 2010 unless extended by NJDOBI. NJDOBI has also limited the aggregate amount of assets that Prudential Insurance may pledge for any loans, including FHLBNY borrowings, to up to 10% of its prior year-end statutory net admitted assets, excluding separate account assets; however, this limitation excludes certain activities, such as the asset-based financing transactions described above. Based on Prudential Insurance s statutory net admitted assets as of December 31, 2009, the 7% limitation equates to a maximum amount of pledged assets of $10.4 billion and an estimated maximum borrowing capacity (after taking into account required collateralization levels and purchases of activity-based stock) of approximately $8.7 billion. Nevertheless, FHLBNY borrowings are subject to the FHLBNY s discretion and to the availability of qualifying assets at Prudential Insurance.

As of September 30, 2010, Prudential Insurance had pledged qualifying assets with a fair value of $2.8 billion, which supported outstanding collateralized advances of $1.0 billion and collateralized funding agreements of $1.5 billion. The fair value of qualifying assets that were available to Prudential Insurance but not pledged amounted to $6.2 billion as of September 30, 2010.

As of September 30, 2010, the $1.0 billion of FHLBNY outstanding advances are reflected in Short-term debt and represent a $1.0 billion decrease from December 31, 2009, reflecting the repayment of collateralized advances that matured on June 4, 2010. The outstanding $1.0 billion collateralized advance matures on December 6, 2010. The funding agreements issued to the FHLBNY, which are reflected in Policyholders account balances, have priority claim status above debt holders of Prudential Insurance.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Federal Home Loan Bank of Boston***

Prudential Retirement Insurance and Annuity Company, or PRIAC, became a member of the Federal Home Loan Bank of Boston, or FHLBB, in December 2009. Membership allows PRIAC access to collateralized advances which will be classified in short-term debt or long-term debt, depending on the maturity date of the obligation. PRIAC s membership in FHLBB requires the ownership of member stock and borrowings from FHLBB require the purchase of activity-based stock in an amount between 3.0% and 4.5% of outstanding borrowings depending on the maturity date of the obligation. As of September 30, 2010, PRIAC had no advances outstanding under the FHLBB facility.

The Connecticut Department of Insurance, or CTDOI, permits PRIAC to pledge up to $2.6 billion in qualifying assets to secure FHLBB borrowings through December 31, 2011. PRIAC must seek re-approval from CTDOI prior to borrowing additional funds after that date. Based on available eligible assets as of September 30, 2010, PRIAC had an estimated maximum borrowing capacity, after taking into consideration required collateralization levels and required purchases of activity based FHLBB stock, of approximately $0.9 billion.

***Term Asset-Backed Securities Loan Facility***

During 2009, the Company purchased securities under the Federal Reserve s Term Asset-Backed Securities Loan Facility ( TALF ). The TALF is designed to provide secured financing for the acquisition of certain types of asset-backed securities, including certain high-quality commercial mortgage-backed securities issued before January 1, 2009. TALF financing is non-recourse to the borrower, is collateralized by the purchased securities and provides financing for the purchase price of the securities, less a haircut that varies based on the type of collateral. Borrowers under the program can deliver the collateralized securities to a special purpose vehicle created by the Federal Reserve in full defeasance of the loan.

During 2009, the Company obtained $1,167 million of secured financing from the Federal Reserve under this program. In 2009, the Company sold a portion of the securities purchased under the program and used the proceeds to repay $738 million of the borrowings. In 2010, the Company sold a portion of the remaining securities purchased under the program and used the proceeds, as well as internal sources of cash, to repay the remaining $429 million of the borrowings.

**10. EMPLOYEE BENEFIT PLANS**

***Pension and Other Postretirement Plans***

The Company has funded and non-funded contributory and non-contributory defined benefit pension plans, which cover substantially all of its employees. For some employees, benefits are based on final average earnings and length of service, while benefits for other employees are based on an account balance that takes into consideration age, service and earnings during their career.

The Company provides certain health care and life insurance benefits for its retired employees, their beneficiaries and covered dependents ( other postretirement benefits ). The health care plan is contributory; the life insurance plan is non-contributory. Substantially all of the Company s U.S. employees may become eligible to receive other postretirement benefits if they retire after age 55 with at least 10 years of service or under certain circumstances after age 50 with at least 20 years of continuous service.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Net periodic (benefit) cost included in General and administrative expenses includes the following components:

| | Three Months Ended September 30, | | | |
|---|---|---|---|---|
| | Pension Benefits | | Other Postretirement Benefits | |
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| **Components of net periodic (benefit) cost** | | | | |
| Service cost | $ 45 | $ 40 | $ 3 | $ 3 |
| Interest cost | 118 | 115 | 28 | 29 |
| Expected return on plan assets | (186) | (182) | (27) | (27) |
| Amortization of prior service cost | 6 | 7 | (3) | (3) |
| Amortization of actuarial (gain) loss, net | 10 | 8 | 10 | 11 |
| Net periodic (benefit) cost(1) | $ (7) | $ (12) | $ 11 | $ 13 |

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| | Pension Benefits | | Other Postretirement Benefits | |
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Service cost | $ 134 | $ 122 | $ 9 | $ 9 |
| Interest cost | 352 | 345 | 84 | 87 |
| Expected return on plan assets | (558) | (546) | (81) | (81) |
| Amortization of prior service cost | 18 | 21 | (9) | (9) |
| Amortization of actuarial (gain) loss, net | 30 | 24 | 30 | 33 |
| Curtailments | (6) | 0 | 0 | 0 |
| Special termination benefits | 2 | 0 | 0 | 0 |
| Net periodic (benefit) cost(1) | $ (28) | $ (34) | $ 33 | $ 39 |

(1) Includes net periodic (benefit) cost for pensions of $0 million and $1 million for the three months ended September 30, 2010 and September 30, 2009, respectively and $(4) million and $4 million for the nine months ended September 30, 2010 and September, 2009, respectively, that have been classified as discontinued operations.

The Company made a discretionary cash contribution in July of 2010 of $95 million to an irrevocable trust, commonly referred to as a rabbi trust, which holds assets of the Company to be used to satisfy its obligations with respect to certain non-qualified retirement plans.

The Company has evaluated the impact of the Patient Protection and Affordable Care Act ( PPACA ) and Health Care and Education Reconciliation Act ( HCERA ) signed into law in March 2010 on its Retiree Medical obligations and has concluded the impact is not material. The effects of the Acts will be included in the next measurement of the obligation at December 31, 2010.

**11. SEGMENT INFORMATION**

***Segments***

The Company has organized its principal operations into the Financial Services Businesses and the Closed Block Business. Within the Financial Services Businesses, the Company operates through three divisions, which together encompass seven reportable segments. The Company s real estate and relocation services business, as

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

well as businesses that are not sufficiently material to warrant separate disclosure and divested businesses are included in Corporate and Other operations within the Financial Services Businesses. Collectively, the businesses that comprise the three operating divisions and Corporate and Other are referred to as the Financial Services Businesses.

***Adjusted Operating Income***

In managing the Financial Services Businesses, the Company analyzes the operating performance of each segment using adjusted operating income. Adjusted operating income does not equate to income from continuing operations before income taxes and equity in earnings of operating joint ventures or net income as determined in accordance with U.S. GAAP but is the measure of segment profit or loss used by the Company to evaluate segment performance and allocate resources, and consistent with authoritative guidance, is the measure of segment performance presented below.

Adjusted operating income is calculated by adjusting each segment s income from continuing operations before income taxes and equity in earnings of operating joint ventures for the following items, which are described in greater detail below:

- realized investment gains (losses), net, and related charges and adjustments;
- net investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes;
- the contribution to income/loss of divested businesses that have been or will be sold or exited but that did not qualify for discontinued operations accounting treatment under U.S. GAAP; and
- equity in earnings of operating joint ventures and earnings attributable to noncontrolling interests.

These items are important to an understanding of overall results of operations. Adjusted operating income is not a substitute for income determined in accordance with U.S. GAAP, and the Company s definition of adjusted operating income may differ from that used by other companies. However, the Company believes that the presentation of adjusted operating income as measured for management purposes enhances the understanding of results of operations by highlighting the results from ongoing operations and the underlying profitability factors of the Financial Services Businesses.

Effective with the third quarter of 2010, the Company has amended its definition of adjusted operating income as it relates to certain variable annuity contracts and defined contribution accounts that contain optional guaranteed living benefit features. Changes in the fair value of these

optional living benefit features, which are accounted for as embedded derivatives, are primarily driven by changes in the policyholders account balance and changes in the capital market and policyholder behavior assumptions used in the valuation of the embedded derivatives, including equity market returns, interest rates, market volatility, benefit utilization, contract lapses, contractholder mortality, and withdrawal rates. The changes in fair value of the embedded derivative liabilities also reflect an increase or decrease in the market-perceived risk of the Company s non-performance. The Company hedges or limits its exposure to certain risks associated with these living benefit features through a combination of product design elements and externally purchased hedging instruments. In addition, beginning in the second quarter of 2009, the Company expanded its hedging program to include a portion of the market exposure related to the overall capital position of the variable annuity business. During the second quarter of 2010, the equity component of the capital hedge within the variable annuity business was replaced with a new capital hedge program that more broadly addressed equity market exposure of the statutory capital within the Financial Services Businesses as a whole. Changes in the value of the embedded derivatives inclusive of the

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

market-perceived risk of the Company s non-performance, and the related hedge positions are reported in Realized investment gains (losses), net. Historically, adjusted operating income included the changes in fair value of these embedded derivatives and related hedge positions, in the period they occurred, and also included the related impact to amortization of deferred policy acquisition and other costs.

Adjusted operating income under the amended definition excludes any amounts related to changes in the market value of the embedded derivatives and related hedge positions, and the related impact to amortization of deferred policy acquisition and other costs. Adjusted operating income for all periods presented has been revised to conform to the amended definition. The Company views adjusted operating income under the amended definition as a more meaningful presentation of its results for purposes of analyzing the operating performance of, and allocating resources to, its business segments, as the amended definition presents results on a basis more consistent with the economics of the businesses. The accounting for these products and associated derivatives under U.S. GAAP has not changed.

The following table presents amounts included within the U.S. GAAP results of the Individual Annuities and Retirement segments and Corporate and Other operations that have been excluded from adjusted operating income under the amended definition for the periods indicated:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Net benefit/(charge) excluded from adjusted operating income under the amended definition: | | | | |
| Individual Annuities: | | | | |
| Decrease/(increase) in the fair value of the embedded derivative liabilities(1) | $ (69) | $ 274 | $ (1,922) | $ 2,062 |
| Change in fair value of hedge positions | 139 | (166) | 2,056 | (1,761) |
| Subtotal | 70 | 108 | 134 | 301 |
| Decrease/(increase) in the embedded derivative liabilities resulting from updates to inputs used in the valuation of the liability | (152) | (197) | 912 | 454 |
| Net benefit/(charge) from the mark-to-market of embedded derivatives and related hedge positions | (82) | (89) | 1,046 | 755 |
| Related benefit/(charge) to amortization of deferred policy acquisition and other costs | 187 | 80 | (509) | (558) |
| Net impact living benefit guarantees and hedging activities and related costs | 105 | (9) | 537 | 197 |
| Impact of capital hedge program | (22) | (140) | (21) | (142) |
| Subtotal Individual Annuities | 83 | (149) | 516 | 55 |
| Retirement(2) | 3 | 2 | 9 | 15 |
| Corporate and Other(3) | 3 | (4) | (3) | 25 |
| Net benefit/(charge) excluded from adjusted operating income under the amended definition | $ 89 | $ (151) | $ 522 | $ 95 |

(1) Represents the change in fair value of the embedded derivative liabilities, excluding the impact resulting from updates to inputs used in the valuation of the liability and the market-perceived risk of the Company s non-performance.
(2) Represents the net impact of living benefit guarantees, hedging activities, and related amortization of deferred policy acquisition and other costs associated with certain defined contribution accounts, which are excluded from adjusted operating income under the amended definition.
(3) Represents the net impact of capital hedge related activities and consolidating adjustments associated with these living benefit guarantees, which are excluded from adjusted operating income under the amended definition.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*Realized investment gains (losses), net, and related charges and adjustments.* Adjusted operating income excludes realized investment gains (losses), net, except as indicated below. A significant element of realized investment gains and losses are impairments and credit-related and interest rate-related gains and losses from sales of securities. Impairments and losses from sales of credit-impaired securities, the timing of which depends largely on market credit cycles, can vary considerably across periods. The timing of other sales that would result in gains or losses, such as interest rate-related gains or losses, is largely subject to the Company s discretion and influenced by market opportunities, as well as the Company s tax and capital profile. Trends in the underlying profitability of the Company s businesses can be more clearly identified without the fluctuating effects of these transactions.

Charges that relate to realized investment gains (losses), net, are also excluded from adjusted operating income. The related charges are associated with: policyholder dividends; amortization of deferred policy acquisition costs, valuation of business acquired ( VOBA ), unearned revenue reserves and deferred sales inducements; interest credited to policyholders account balances; reserves for future policy benefits; and payments associated with the market value adjustment features related to certain of the annuity products the Company sells. The related charges associated with policyholder dividends include a percentage of the net increase in the fair value of specified assets included in Gibraltar Life s reorganization plan that was paid as a special dividend to Gibraltar Life policyholders. The liability related to this special dividend was fully paid as of June 30, 2010. Deferred policy acquisition costs, VOBA, unearned revenue reserves and deferred sales inducements for certain products are amortized based on estimated gross profits, which include net realized investment gains and losses on the underlying invested assets including certain portions of the net realized investment gains and losses related to the embedded derivatives and related hedging positions associated with the living benefit features related to certain products as discussed above. The related charge for these items represents the portion of this amortization associated with net realized investment gains and losses. The related charges for interest credited to policyholders account balances relate to certain group life policies that pass back certain realized investment gains and losses to the policyholder. The reserves for certain policies are adjusted when cash flows related to these policies are affected by net realized investment gains and losses, and the related charge for reserves for future policy benefits represents that adjustment. Certain of the Company s annuity products contain a market value adjustment feature that requires us to pay to the contractholder or entitles us to receive from the contractholder, upon surrender, a market value adjustment based on the crediting rates on the contract surrendered compared to crediting rates on newly issued contracts or based on an index rate at the time of purchase compared to an index rate at time of surrender, as applicable. These payments mitigate the net realized investment gains or losses incurred upon the disposition of the underlying invested assets. The related charge represents the payments or receipts associated with these market value adjustment features.

Adjustments to Realized investment gains (losses), net, for purposes of calculating adjusted operating income, include the following:

Gains and losses pertaining to derivative contracts that do not qualify for hedge accounting treatment, other than derivatives used in the Company s capacity as a broker or dealer, are included in Realized investment gains (losses), net. This includes mark-to-market adjustments of open contracts as well as periodic settlements. As discussed further below, adjusted operating income includes a portion of realized gains and losses pertaining to certain derivative contracts.

Adjusted operating income of the International Insurance segment and International Investments segment, excluding the global commodities group, reflect the impact of an intercompany arrangement with Corporate and Other operations pursuant to which the segments non-U.S. dollar denominated earnings in all countries for a particular year, including its interim reporting periods, are translated at fixed currency exchange

rates. The fixed rates are determined in connection with a currency hedging program designed to mitigate the risk that

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

unfavorable rate changes will reduce the segments U.S. dollar equivalent earnings. Pursuant to this program, the Company s Corporate and Other operations execute forward currency contracts with third parties to sell the net exposure of projected earnings from the hedged currency in exchange for U.S. dollars at a specified exchange rate. The maturities of these contracts correspond with the future periods in which the identified non-U.S. dollar denominated earnings are expected to be generated. These contracts do not qualify for hedge accounting under U.S. GAAP and, as noted above, all resulting profits or losses from such contracts are included in Realized investment gains (losses), net. When the contracts are terminated in the same period that the expected earnings emerge, the resulting positive or negative cash flow effect is included in adjusted operating income (net losses of $27 million and $13 million for the three months ended September 30, 2010 and 2009, respectively, and net losses of $58 million and $14 million for the nine months ended September 30, 2010 and 2009, respectively). As of September 30, 2010 and December 31, 2009, the fair value of open contracts used for this purpose were net liabilities of $203 million and $16 million, respectively.

The Company uses interest rate and currency swaps and other derivatives to manage interest and currency exchange rate exposures arising from mismatches between assets and liabilities, including duration mismatches. For the derivative contracts that do not qualify for hedge accounting treatment, mark-to-market adjustments of open contracts as well as periodic settlements are included in Realized investment gains (losses), net. However, the periodic swap settlements, as well as other derivative related yield adjustments, are included in adjusted operating income to reflect the after-hedge yield of the underlying instruments. In certain instances, when these derivative contracts are terminated or offset before their final maturity, the resulting realized gains or losses recorded within Realized investment gains (losses), net are recognized in adjusted operating income over periods that generally approximate the expected terms of the derivatives or underlying instruments in order for adjusted operating income to reflect the after-hedge yield of the underlying instruments. Adjusted operating income includes net gains of $49 million and $43 million for the three months ended September 30, 2010 and 2009, respectively, due to periodic settlements and yield adjustments of such contracts, and includes net gains of $9 million and $7 million, respectively, related to derivative contracts that were terminated or offset in prior periods. Adjusted operating income includes net gains of $180 million and $100 million for the nine months ended September 30, 2010 and 2009, respectively, due to periodic settlements and yield adjustments of such contracts, and includes net gains of $24 million and $18 million, respectively, related to derivative contracts that were terminated or offset in prior periods. The table below reflects the total deferred gain (loss) as of September 30, 2010, related to derivative contracts that were terminated or offset in prior periods that will be recognized in adjusted operating income in future periods for each segment, as well as the weighted average period over which these deferred amounts will be recognized.

| | Deferred Amount | Weighted Average Period |
|---|---|---|
| | (in millions) | |
| **Segment:** | | |
| International Insurance | $ 723 | 30 years |
| Asset Management | 27 | 9 years |
| Corporate and Other | (50) | 7 years |
| Total deferred gain (loss) | $ 700 | |

Adjustments are also made for the purposes of calculating adjusted operating income for the following items:

The Company conducts certain activities for which Realized investment gains (losses), net are a principal source of earnings for its businesses and therefore included in adjusted operating income, particularly within the Company s Asset Management segment. For example, Asset Management s proprietary investing business

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

makes investments for sale or syndication to other investors or for placement or co-investment in the Company s managed funds and structured products. The Realized investment gains (losses), net associated with the sale of these proprietary investments, as well as related derivative results, are a principal activity for this business and included in adjusted operating income. In addition, the Realized investment gains (losses), net associated with loans originated by the Company s commercial mortgage operations, as well as related derivative results and retained mortgage servicing rights, are a principal activity for this business and included in adjusted operating income. Net realized investment losses of $1 million and $33 million for the three months ended September 30, 2010 and 2009, respectively, and net gains of $9 million and losses of $175 million for the nine months ended September 30, 2010 and 2009, respectively, related to these and other businesses were included in adjusted operating income as an adjustment to Realized investment gains (losses), net.

The Company has certain investments in its general account portfolios that are classified as trading. These trading investments are carried at fair value and included in Other trading account assets, at fair value on the Company s statements of financial position. Realized and unrealized gains and losses for these investments are recorded in Asset management fees and other income, and interest and dividend income for these investments is recorded in Net investment income. Consistent with the exclusion of realized investment gains and losses with respect to other investments managed on a consistent basis, the net gains or losses on these investments, which is recorded within Asset management fees and other income, is excluded from adjusted operating income and is reflected as an adjustment to Realized investment gains (losses), net. In addition, prior to the Company s repayment of the obligation in 2010, the secured financing received from the Federal Reserve under TALF was reflected within Long-term debt, and carried at fair value under the fair value option under authoritative guidance around fair value. The changes in the fair value of this debt, which were recorded within Asset management fees and other income, was also excluded from adjusted operating income and reflected as an adjustment to Realized investment gains (losses), net. This is consistent with the securities purchased with the proceeds from this financing, which were carried at fair value and included in Other trading account assets, at fair value as discussed above. The net impact of these adjustments was to exclude from adjusted operating income net gains of $23 million and $31 million, for the three months ended September 30, 2010 and 2009, respectively, and net gains of $18 million and $14 million for the nine months ended September 30, 2010 and 2009, respectively.

The Company has certain assets and liabilities for which, under GAAP, the change in value due to changes in foreign currency exchange rates during the period is recorded in Asset management fees and other income. To the extent the foreign currency exposure on these assets and liabilities is economically hedged, the change in value included in Asset management fees and other income is excluded from adjusted operating income and is reflected as an adjustment to Realized investment gains (losses), net. The net impact of these adjustments was to exclude from adjusted operating income net gains of $192 million, and losses of $23 million for the three months ended September 30, 2010 and 2009, respectively, and net gains of $150 million and gains of $56 million for the nine months ended September 30, 2010 and 2009, respectively.

*Investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes.* Certain products included in the Retirement and International Insurance segments, are experience-rated in that investment results associated with these products are expected to ultimately accrue to contractholders. The investments supporting these experience-rated products, excluding commercial mortgage and other loans, are classified as trading and are carried at fair value. These trading investments are reflected on the statements of financial position as Trading account assets supporting insurance liabilities, at fair value. Realized and unrealized gains and losses for these investments are reported in Asset management fees and other income. Interest and dividend income for these investments is reported in Net investment income. Commercial mortgage and other loans that support these experience-rated products are carried at unpaid principal, net of unamortized discounts and an allowance for losses, and are reflected on the statements of financial position as Commercial mortgage and other loans.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Adjusted operating income excludes net investment gains and losses on trading account assets supporting insurance liabilities. This is consistent with the exclusion of realized investment gains and losses with respect to other investments supporting insurance liabilities managed on a consistent basis. In addition, to be consistent with the historical treatment of charges related to realized investment gains and losses on investments, adjusted operating income also excludes the change in contractholder liabilities due to asset value changes in the pool of investments (including changes in the fair value of commercial mortgage and other loans) supporting these experience-rated contracts, which are reflected in Interest credited to policyholders account balances. The result of this approach is that adjusted operating income for these products includes net fee revenue and interest spread the Company earns on these experience-rated contracts, and excludes changes in fair value of the pool of investments, both realized and unrealized, that are expected to ultimately accrue to the contractholders.

*Divested businesses.* The contribution to income/loss of divested businesses that have been or will be sold or exited, but that did not qualify for discontinued operations accounting treatment under U.S. GAAP, are excluded from adjusted operating income as the results of divested businesses are not relevant to understanding the Company s ongoing operating results.

*Equity in earnings of operating joint ventures and earnings attributable to noncontrolling interests*. Equity in earnings of operating joint ventures, on a pre-tax basis, are included in adjusted operating income as these results are a principal source of earnings. These earnings are reflected on a U.S. GAAP basis on an after-tax basis as a separate line on the Company s Unaudited Interim Consolidated Statements of Operations.

Earnings attributable to noncontrolling interests are excluded from adjusted operating income. Earnings attributable to noncontrolling interests represents the portion of earnings from consolidated entities that relates to the equity interests of minority investors, and are reflected on a U.S. GAAP basis as a separate line on the Company s Unaudited Interim Consolidated Statements of Operations.

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The summary below reconciles adjusted operating income before income taxes for the Financial Services Businesses to income from continuing operations before income taxes and equity in earnings of operating joint ventures:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Adjusted Operating Income before income taxes for Financial Services Businesses by Segment: | | | | |
| Individual Annuities | $ 588 | $ 315 | $ 701 | $ 560 |
| Retirement | 119 | 117 | 425 | 362 |
| Asset Management | 148 | 29 | 355 | 61 |
| Total U.S. Retirement Solutions and Investment Management Division | 855 | 461 | 1,481 | 983 |
| Individual Life | 190 | 243 | 369 | 421 |
| Group Insurance | 61 | 64 | 146 | 262 |
| Total U.S. Individual Life and Group Insurance Division | 251 | 307 | 515 | 683 |
| International Insurance | 530 | 500 | 1,473 | 1,390 |
| International Investments | 1 | 7 | 32 | 25 |
| Total International Insurance and Investments Division | 531 | 507 | 1,505 | 1,415 |
| Corporate Operations | (279) | (209) | (662) | (521) |
| Real Estate and Relocation Services | 19 | 6 | 22 | (54) |
| Total Corporate and Other | (260) | (203) | (640) | (575) |
| Adjusted Operating Income before income taxes for Financial Services Businesses | 1,377 | 1,072 | 2,861 | 2,506 |
| Reconciling items: | | | | |
| Realized investment gains (losses), net, and related adjustments | 160 | (406) | 1,481 | (1,101) |
| Charges related to realized investment gains (losses), net | 118 | 29 | (641) | (561) |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net | 388 | 694 | 719 | 1,525 |
| Change in experience-rated contractholder liabilities due to asset value changes | (367) | (458) | (831) | (850) |
| Divested businesses | (32) | 25 | (46) | (31) |
| Equity in earnings of operating joint ventures and earnings attributable to noncontrolling interests | (18) | (92) | (36) | (75) |

| | | | | |
|---|---|---|---|---|
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures for Financial Services Businesses | 1,626 | 864 | 3,507 | 1,413 |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures for Closed Block Business | 114 | (16) | 777 | (572) |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | $ 1,740 | $ 848 | $ 4,284 | $ 841 |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The U.S. Retirement Solutions and Investment Management Division and U.S. Individual Life and Group Insurance Division results reflect deferred policy acquisition costs as if the individual annuity business and group insurance business were stand-alone operations. The elimination of intersegment costs capitalized in accordance with this policy is included in consolidating adjustments within Corporate and Other operations.

The summary below presents revenues for the Company s reportable segments:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| | (in millions) | | | |
| Financial Services Businesses: | | | | |
| Individual Annuities | $ 807 | $ 653 | $ 2,334 | $ 1,818 |
| Retirement | 1,376 | 1,100 | 3,875 | 3,525 |
| Asset Management | 493 | 291 | 1,366 | 896 |
| Total U.S. Retirement Solutions and Investment Management Division | 2,676 | 2,044 | 7,575 | 6,239 |
| Individual Life | 638 | 656 | 2,076 | 2,039 |
| Group Insurance | 1,466 | 1,356 | 4,093 | 3,992 |
| Total U.S. Individual Life and Group Insurance Division | 2,104 | 2,012 | 6,169 | 6,031 |
| International Insurance | 3,008 | 2,668 | 8,849 | 7,738 |
| International Investments | 84 | 74 | 256 | 225 |
| Total International Insurance and Investments Division | 3,092 | 2,742 | 9,105 | 7,963 |
| Corporate Operations | (62) | (62) | (166) | (154) |
| Real Estate and Relocation Services | 66 | 62 | 167 | 113 |
| Total Corporate and Other | 4 | 0 | 1 | (41) |
| Total | 7,876 | 6,798 | 22,850 | 20,192 |
| Reconciling items: | | | | |
| Realized investment gains (losses), net, and related adjustments | 160 | (406) | 1,481 | (1,101) |
| Charges related to realized investment gains (losses), net | (42) | (80) | (115) | (141) |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net | 388 | 694 | 719 | 1,525 |
| Divested businesses | 4 | 32 | 6 | (10) |
| | (16) | (43) | (35) | (31) |

| | | | | |
|---|---|---|---|---|
| Equity in earnings of operating joint ventures and earnings attributable to noncontrolling interests | | | | |
| Total Financial Services Businesses | 8,370 | 6,995 | 24,906 | 20,434 |
| Closed Block Business | 1,592 | 1,548 | 5,402 | 3,513 |
| Total per Unaudited Interim Consolidated Financial Statements | $ 9,962 | $ 8,543 | $ 30,308 | $ 23,947 |

The Asset Management segment revenues include intersegment revenues primarily consisting of asset-based management and administration fees as follows:

| | **Three Months Ended September 30,** | | **Nine Months Ended September 30,** | |
|---|---|---|---|---|
| | **2010** | **2009** | **2010** | **2009** |
| | | **(in millions)** | | |
| Asset Management segment intersegment revenues | $ 102 | $ 88 | $ 290 | $ 257 |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Management has determined the intersegment revenues with reference to market rates. Intersegment revenues are eliminated in consolidation in Corporate and Other.

The summary below presents total assets for the Company s reportable segments as of the dates indicated:

| | September 30, 2010 | December 31, 2009 |
|---|---|---|
| | (in millions) | |
| Individual Annuities | $ 101,969 | $ 84,064 |
| Retirement | 129,845 | 123,625 |
| Asset Management | 32,181 | 30,185 |
| Total U.S. Retirement Solutions and Investment Management Division | 263,995 | 237,874 |
| Individual Life | 40,002 | 36,917 |
| Group Insurance | 34,927 | 32,935 |
| Total U.S. Individual Life and Group Insurance Division | 74,929 | 69,852 |
| International Insurance | 100,806 | 87,590 |
| International Investments | 5,779 | 4,997 |
| Total International Insurance and Investments Division | 106,585 | 92,587 |
| Corporate Operations | 12,080 | 14,368 |
| Real Estate and Relocation Services | 634 | 590 |
| Total Corporate and Other | 12,714 | 14,958 |
| Total Financial Services Businesses | 458,223 | 415,271 |
| Closed Block Business | 68,701 | 64,932 |
| Total | $ 526,924 | $ 480,203 |

**12. INCOME TAXES**

The Company s liability for income taxes includes the liability for unrecognized tax benefits, interest and penalties which relate to tax years still subject to review by the Internal Revenue Service ( IRS ) or other taxing authorities. Audit periods remain open for review until the statute of limitations has passed. Generally, for tax years which produce net operating losses, capital losses or tax credit carryforwards ( tax attributes ), the statute of limitations does not close, to the extent of these tax attributes, until the expiration of the statute of limitations for the tax year in which they are fully utilized. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to the liability for income taxes. The statute of limitations for the 2002 tax year expired on April 30, 2009. The statute of limitations for the 2003 tax year expired on July 31, 2009. The statute of limitations for the 2004, 2005, and 2006 tax years will expire in April 2011, unless extended. Tax years 2007 through 2009 are still open for IRS examination. The Company does not anticipate any significant changes within the next 12 months to its total unrecognized tax benefits related to tax years for which the statute of limitations has not expired.

The dividends received deduction ( DRD ) reduces the amount of dividend income subject to U.S. tax and is a significant component of the difference between the Company s effective tax rate and the federal statutory tax rate of 35%. The DRD for the current period was estimated using information from 2009, current year results, and was adjusted to take into account the current year s equity market performance. The actual current year DRD can vary from the estimate based on factors such as, but not limited to, changes in the amount of dividends received that are eligible for the DRD, changes in the amount of distributions received from mutual fund investments, changes in the account balances of variable life and annuity contracts, and the Company s taxable income before the DRD.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

In August 2007, the IRS released Revenue Ruling 2007-54, which included, among other items, guidance on the methodology to be followed in calculating the DRD related to variable life insurance and annuity contracts. In September 2007, the IRS released Revenue Ruling 2007-61. Revenue Ruling 2007-61 suspended Revenue Ruling 2007-54 and informed taxpayers that the U.S. Treasury Department and the IRS intend to address through new regulations the issues considered in Revenue Ruling 2007-54, including the methodology to be followed in determining the DRD related to variable life insurance and annuity contracts. On February 1, 2010, the Obama Administration released the General Explanations of the Administration s Revenue Proposals. Although the Administration has not released proposed statutory language, one proposal would change the method used to determine the amount of the DRD. A change in the DRD, including the possible retroactive or prospective elimination of this deduction through regulation or legislation, could increase actual tax expense and reduce the Company s consolidated net income. The IRS recently issued an Industry Director Directive ( IDD ) stating that the methodology for calculating the DRD set forth in Revenue Ruling 2007-54 should not be followed. The IDD also confirmed that the IRS guidance issued before Revenue Ruling 2007-54, which guidance the Company relied upon in calculating its DRD, should be used to determine the DRD. These activities had no impact on the Company s 2009 or the first nine months of 2010 results.

In December 2006, the IRS completed all fieldwork with respect to its examination of the consolidated federal income tax returns for tax years 2002 and 2003. The final report was initially submitted to the Joint Committee on Taxation for their review in April 2007. The final report was resubmitted in March 2008 and again in April 2008. The Joint Committee returned the report to the IRS for additional review of an industry issue regarding the methodology for calculating the DRD related to variable life insurance and annuity contracts. The IRS completed its review of the issue and proposed an adjustment with respect to the calculation of the DRD. In order to expedite receipt of an income tax refund related to the 2002 and 2003 tax years, the Company agreed to such adjustment. The report, with the adjustment to the DRD, was submitted to the Joint Committee on Taxation in October 2008. The Company was advised on January 2, 2009 that the Joint Committee completed its consideration of the report and took no exception to the conclusions reached by the IRS. Accordingly, the final report was processed and a $157 million refund was received in February 2009. The Company believes that its return position with respect to the calculation of the DRD is technically correct. Therefore, the Company filed protective refund claims on October 1, 2009 to recover the taxes associated with the agreed upon adjustment and to pursue such other actions as appropriate. The Company is working with its IRS audit team to bring the DRD issue to a close in accordance with the IDD. These activities had no impact on the Company s 2009 or the first nine months of 2010 results.

In January 2007, the IRS began an examination of tax years 2004 through 2006. For tax years 2007 through 2010, the Company is participating in the IRS s Compliance Assurance Program ( CAP ). Under CAP, the IRS assigns an examination team to review completed transactions contemporaneously during these tax years in order to reach agreement with the Company on how they should be reported in the tax returns. If disagreements arise, accelerated resolutions programs are available to resolve the disagreements in a timely manner before the tax returns are filed. It is management s expectation this program will shorten the time period between the filing of the Company s federal income tax returns and the IRS s completion of its examination of the returns.

The Company s affiliates in Japan file separate tax returns and are subject to audits by the local taxing authority. The general statute of limitations is five years from when the return is filed. During 2009, the Tokyo Regional Taxation Bureau concluded a routine tax audit of the tax returns of Prudential Life Insurance Company Ltd. for its tax years ending March 31, 2004 to March 31, 2008. These activities had no material impact on the Company s 2009 or the first nine months of 2010 results.

The Company s affiliates in South Korea file separate tax returns and are subject to audits by the local taxing authority. The general statute of limitations is five years from when the return is filed. During 2009, a

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

local district office in the South Korean tax authority concluded a routine tax audit of the local taxes for tax years ending March 31, 2004 through March 31, 2007 of Prudential Life Insurance Company of Korea, Ltd. ( POK ). During 2010, South Korea s National Tax Service concluded a general tax audit of POK s tax years ending March 31, 2006 to March 31, 2010. These activities had no material impact on the Company s 2009 or the first nine months of 2010 results.

On March 23, 2010, President Obama signed into law the Patient Protection and Affordable Care Act, which was modified by the Health Care and Education Reconciliation Act of 2010 signed into law on March 30, 2010, (together, the Healthcare Act ). The federal government provides a subsidy to companies that provide certain retiree prescription drug benefits (the Medicare Part D subsidy ), including the Company. The Medicare Part D subsidy was previously provided tax-free. However, as currently adopted, the Healthcare Act includes a provision that would reduce the tax deductibility of retiree health care costs to the extent of any Medicare Part D subsidy received. In effect, this provision of the Healthcare Act makes the Medicare Part D subsidy taxable beginning in 2013. Therefore, the Company incurred a charge in the first quarter of 2010 for the reduction of deferred tax assets of $94 million, which reduces net income and is reflected in Income tax expense (benefit).

The Healthcare Act also amended Section 162(m) of the Internal Revenue Code to limit the tax deductibility of compensation paid to certain employees of covered health insurance providers. Pursuant to this new provision, the Company could be considered a covered health insurance provider and could be subject to the limitation on the tax deductibility of certain compensation earned in 2010 but payable after 2012. As a result, the Company incurred a charge in the third quarter of 2010 of $12 million to reflect a portion of the Company s compensation expense that would not be deductible.

**13. FAIR VALUE OF ASSETS AND LIABILITIES**

**Fair Value Measurement** Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The authoritative guidance around fair value established a framework for measuring fair value that includes a hierarchy used to classify the inputs used in measuring fair value. The hierarchy prioritizes the inputs to valuation techniques into three levels. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The levels of the fair value hierarchy are as follows:

Level 1 Fair value is based on unadjusted quoted prices in active markets that are accessible to the Company for identical assets or liabilities. These generally provide the most reliable evidence and are used to measure fair value whenever available. Active markets are defined as having the following characteristics for the measured asset/liability: (i) many transactions, (ii) current prices, (iii) price quotes not varying substantially among market makers, (iv) narrow bid/ask spreads and (v) most information publicly available. The Company s Level 1 assets and liabilities primarily include certain cash equivalents and short term investments, equity securities and derivative contracts that are traded in an active exchange market. Prices are obtained from readily available sources for market transactions involving identical assets or liabilities.

Level 2 Fair value is based on significant inputs, other than Level 1 inputs, that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability through corroboration with observable market data. Level 2 inputs include

quoted market prices in active markets for similar assets and liabilities, quoted market prices in markets that are not active for identical or similar assets or liabilities, and other market observable inputs. The Company s Level 2 assets and liabilities include: fixed maturities (corporate public and private bonds, most government securities, certain asset-backed and mortgage-

**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

backed securities, etc.), certain equity securities (mutual funds, which do not actively trade and are priced based on a net asset value) and commercial mortgage loans, short-term investments and certain cash equivalents (primarily commercial paper), and certain over-the-counter derivatives. Valuations are generally obtained from third party pricing services for identical or comparable assets or liabilities or through the use of valuation methodologies using observable market inputs. Prices from services are validated through comparison to trade data and internal estimates of current fair value, generally developed using market observable inputs and economic indicators.

Level 3 Fair value is based on at least one or more significant unobservable inputs for the asset or liability. These inputs reflect the Company s assumptions about the inputs market participants would use in pricing the asset or liability. The Company s Level 3 assets and liabilities primarily include: certain private fixed maturities and equity securities, certain manually priced public equity securities and fixed maturities, certain highly structured over-the-counter derivative contracts, certain commercial mortgage loans, certain consolidated real estate funds for which the Company is the general partner, and embedded derivatives resulting from certain products with guaranteed benefits. Prices are determined using valuation methodologies such as option pricing models, discounted cash flow models and other similar techniques. Non-binding broker quotes, which are utilized when pricing service information is not available, are reviewed for reasonableness based on the Company s understanding of the market, and are generally considered Level 3. Under certain conditions, based on its observations of transactions in active markets, the Company may conclude the prices received from independent third party pricing services or brokers are not reasonable or reflective of market activity. In those instances, the Company may choose to over-ride the third-party pricing information or quotes received and apply internally developed values to the related assets or liabilities. To the extent the internally developed valuations use significant unobservable inputs, they are classified as Level 3. As of September 30, 2010 and December 31, 2009, these over-rides on a net basis were not material.

**Inactive Markets** During 2009 and continuing through the first quarter of 2010, the Company observed that the volume and level of activity in the market for asset-backed securities collateralized by sub-prime mortgages remained at historically low levels. This stood in particular contrast to the markets for other structured products with similar cash flow and credit profiles. The Company also observed significant implied relative liquidity risk premiums, yields, and weighting of worst case cash flows for asset-backed securities collateralized by sub-prime mortgages in comparison with its own estimates for such securities. In contrast, the liquidity of other spread-based asset classes, such as corporate bonds, high yield and consumer asset-backed securities, such as those collateralized by credit cards or autos, which were previously more correlated with sub-prime securities, improved beginning in the second quarter of 2009. Based on this information, the Company concluded as of June 30, 2009, and continuing through March 31, 2010 that the market for asset-backed securities collateralized by sub-prime mortgages was inactive and also determined the pricing quotes it received were based on limited market transactions, calling into question their representation of observable fair value. As a result, the Company considered both third-party pricing information and an internally developed price based on a discounted cash flow model in determining the fair value of certain of these securities as of June 30, 2009 through March 31, 2010. Based on the unobservable inputs used in the discounted cash flow model and the limited observable market activity, the Company classified these securities within Level 3 as of June 30, 2009 through March 31, 2010.

Beginning in the second quarter of 2010, the Company observed an increasingly active market, as evidence of orderly transactions in asset-backed securities collateralized by sub-prime mortgages became more apparent. Additionally, the valuation based on the pricing the Company received from independent pricing services was not materially different from its internal estimates of current market value for these securities. As a result, where third party pricing information based on observable inputs was used to fair value the security, and based on the

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

assessment that the market has been becoming increasingly active, the Company reported fair values for these asset-backed securities collateralized by sub-prime mortgages in Level 2 since June 30, 2010. As of September 30, 2010, the fair value of these securities included in Level 2 were $4,627 million included in Fixed Maturities Available for Sale Asset-Backed Securities and $212 million included in Trading Account Assets Supporting Insurance Liabilities Asset-Backed Securities.

**Assets and Liabilities by Hierarchy Level** The tables below present the balances of assets and liabilities measured at fair value on a recurring basis, as of the dates indicated.

| | As of September 30, 2010 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 (in millions) | Netting(2) | Total |
| Fixed maturities, available for sale: | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 0 | $ 11,159 | $ 0 | $ | $ 11,159 |
| Obligations of U.S. states and their political subdivisions | 0 | 2,037 | 0 | | 2,037 |
| Foreign government bonds | 0 | 49,833 | 32 | | 49,865 |
| Corporate securities | 5 | 100,238 | 737 | | 100,980 |
| Asset-backed securities | 0 | 8,812 | 1,683 | | 10,495 |
| Commercial mortgage-backed securities | 0 | 12,180 | 143 | | 12,323 |
| Residential mortgage-backed securities | 0 | 10,306 | 24 | | 10,330 |
| Subtotal | 5 | 194,565 | 2,619 | | 197,189 |
| Trading account assets supporting insurance liabilities: | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | 0 | 245 | 0 | | 245 |
| Obligations of U.S. states and their political subdivisions | 0 | 175 | 0 | | 175 |
| Foreign government bonds | 0 | 553 | 0 | | 553 |
| Corporate securities | 0 | 10,407 | 42 | | 10,449 |
| Asset-backed securities | 0 | 780 | 176 | | 956 |
| Commercial mortgage-backed securities | 0 | 2,267 | 5 | | 2,272 |
| Residential mortgage-backed securities | 0 | 1,275 | 19 | | 1,294 |
| Equity securities | 794 | 231 | 4 | | 1,029 |
| Short-term investments and cash equivalents | 624 | 153 | 0 | | 777 |
| Subtotal | 1,418 | 16,086 | 246 | | 17,750 |
| Other trading account assets: | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | 0 | 244 | 0 | | 244 |
| Obligations of U.S. states and their political subdivisions | 0 | 113 | 0 | | 113 |
| Foreign government bonds | 2 | 24 | 0 | | 26 |
| Corporate securities | 8 | 282 | 31 | | 321 |
| Asset-backed securities | 0 | 638 | 60 | | 698 |
| Commercial mortgage-backed securities | 0 | 84 | 18 | | 102 |
| Residential mortgage-backed securities | 0 | 166 | 20 | | 186 |
| Equity securities | 314 | 142 | 28 | | 484 |
| All other activity | 91 | 11,249 | 203 | (8,041) | 3,502 |
| Subtotal | 415 | 12,942 | 360 | (8,041) | 5,676 |
| Equity securities, available for sale | 4,004 | 2,921 | 347 | | 7,272 |
| Commercial mortgage and other loans | 0 | 89 | 308 | | 397 |
| Other long-term investments | 42 | 149 | 756 | | 947 |

| | | | | | |
|---|---|---|---|---|---|
| Short-term investments | 3,980 | 1,447 | 0 | | 5,427 |
| Cash equivalents | 1,967 | 6,560 | 0 | | 8,527 |
| Other assets | 1,743 | 360 | 21 | | 2,124 |
| Subtotal excluding separate account assets | 13,574 | 235,119 | 4,657 | (8,041) | 245,309 |
| Separate account assets(1) | 38,674 | 141,047 | 14,742 | | 194,463 |
| Total assets | $ 52,248 | $ 376,166 | $ 19,399 | $ (8,041) | $ 439,772 |
| Future policy benefits | $ 0 | $ 0 | $ 1,291 | $ | $ 1,291 |
| Long-term debt | 0 | 0 | 0 | | 0 |
| Other liabilities | 30 | 7,721 | 2 | (7,060) | 693 |
| Total liabilities | $ 30 | $ 7,721 | $ 1,293 | $ (7,060) | $ 1,984 |

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

| | As of December 31, 2009(3) | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Netting(2) | Total |
| | | | (in millions) | | |
| Fixed maturities, available for sale: | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | $ 0 | $ 8,268 | $ 0 | $ | $ 8,268 |
| Obligations of U.S. states and their political subdivisions | 0 | 1,375 | 0 | | 1,375 |
| Foreign government bonds | 0 | 42,007 | 47 | | 42,054 |
| Corporate securities | 5 | 89,794 | 902 | | 90,701 |
| Asset-backed securities | 0 | 3,875 | 6,363 | | 10,238 |
| Commercial mortgage-backed securities | 0 | 10,713 | 305 | | 11,018 |
| Residential mortgage-backed securities | 0 | 11,467 | 104 | | 11,571 |
| Subtotal | 5 | 167,499 | 7,721 | | 175,225 |
| Trading account assets supporting insurance liabilities: | | | | | |
| U.S. Treasury securities and obligations of U.S. government authorities and agencies | 0 | 128 | 0 | | 128 |
| Obligations of U.S. states and their political subdivisions | 0 | 31 | 0 | | 31 |
| Foreign government bonds | 0 | 517 | 0 | | 517 |
| Corporate securities | 0 | 9,419 | 83 | | 9,502 |
| Asset-backed securities | 0 | 576 | 281 | | 857 |
| Commercial mortgage-backed securities | 0 | 1,888 | 5 | | 1,893 |
| Residential mortgage-backed securities | 0 | 1,412 | | | |