PRUDENTIAL FINANCIAL INC
Form 10-Q
August 07, 2014
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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 June 30, 2014

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	**(I.R.S. Employer**
Incorporation or Organization)	**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 July 31, 2014, 458 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, longevity, 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, value 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 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 projected results of acquisitions; (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 the Annual Report on Form 10-K for the year ended December 31, 2013 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. Prudential, the Company, we and our refer to our consolidated operations.

PART I - FINANCIAL INFORMATION

ITEM 1. ***Financial Statements***

PRUDENTIAL FINANCIAL, INC.

Unaudited Interim Consolidated Statements of Financial Position

June 30, 2014 and December 31, 2013 (in millions, except share amounts)

	June 30, 2014	December 31, 2013
ASSETS		
Fixed maturities, available-for-sale, at fair value (amortized cost: 2014-$277,756; 2013-$268,727)(1)	$ 304,472	$ 286,866
Fixed maturities, held-to-maturity, at amortized cost (fair value: 2014-$3,464; 2013-$3,553)(1)	3,171	3,312
Trading account assets supporting insurance liabilities, at fair value(1)	21,273	20,827
Other trading account assets, at fair value(1)	8,665	6,453
Equity securities, available-for-sale, at fair value (cost: 2014-$7,218; 2013-$7,003)	10,222	9,910
Commercial mortgage and other loans (includes $204 and $158 measured at fair value under the fair value option at June 30, 2014 and December 31, 2013, respectively)(1)	42,964	41,008
Policy loans	11,966	11,766
Other long-term investments (includes $944 and $873 measured at fair value under the fair value option at June 30, 2014 and December 31, 2013, respectively)(1)	10,923	10,328
Short-term investments	5,663	7,703
Total investments	419,319	398,173
Cash and cash equivalents(1)	12,160	11,439
Accrued investment income(1)	3,162	3,089
Deferred policy acquisition costs	16,669	16,512
Value of business acquired	3,499	3,675
Other assets(1)	13,927	13,833
Separate account assets	296,801	285,060
TOTAL ASSETS	$ 765,537	$ 731,781
LIABILITIES AND EQUITY		
LIABILITIES		
Future policy benefits	$ 215,219	$ 206,859
Policyholders account balances(1)	138,545	136,657
Policyholders dividends	7,186	5,515
Securities sold under agreements to repurchase	8,786	7,898
Cash collateral for loaned securities	4,889	5,040
Income taxes	8,504	5,422
Short-term debt	3,804	2,669
Long-term debt	23,488	23,553

Other liabilities(1)	11,935	13,925
Notes issued by consolidated variable interest entities (includes $4,539 and $3,254 measured at fair value under the fair value option at June 30, 2014 and December 31, 2013, respectively)(1)	4,573	3,302
Separate account liabilities	296,801	285,060
Total liabilities	723,730	695,900
COMMITMENTS AND CONTINGENT LIABILITIES (See Note 15)		
EQUITY		
Preferred Stock ($.01 par value; 10,000,000 shares authorized; none issued)	0	0
Common Stock ($.01 par value; 1,500,000,000 shares authorized; 660,111,337 and 660,111,319 shares issued at June 30, 2014 and December 31, 2013, respectively)	6	6
Class B Stock ($.01 par value; 10,000,000 shares authorized; 2,000,000 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively)	0	0
Additional paid-in capital	24,478	24,475
Common Stock held in treasury, at cost (201,707,340 and 199,056,067 shares at June 30, 2014 and December 31, 2013, respectively)	(12,723)	(12,415)
Accumulated other comprehensive income (loss)	13,077	8,681
Retained earnings	16,357	14,531
Total Prudential Financial, Inc. equity	41,195	35,278
Noncontrolling interests	612	603
Total equity	41,807	35,881
TOTAL LIABILITIES AND EQUITY	$ 765,537	$ 731,781

(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 Six Months Ended June 30, 2014 and 2013 (in millions, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
REVENUES				
Premiums	$ 6,068	$ 6,922	$ 11,936	$ 14,006
Policy charges and fee income	1,520	1,375	3,021	2,731
Net investment income	3,754	3,711	7,592	7,349
Asset management and service fees	928	880	1,832	1,700
Other income	267	(1,823)	802	(3,827)
Realized investment gains (losses), net:				
Other-than-temporary impairments on fixed maturity securities	(32)	(180)	(111)	(488)
Other-than-temporary impairments on fixed maturity securities transferred to Other Comprehensive Income	6	147	69	385
Other realized investment gains (losses), net	635	(991)	859	(1,644)
Total realized investment gains (losses), net	609	(1,024)	817	(1,747)
Total revenues	13,146	10,041	26,000	20,212
BENEFITS AND EXPENSES				
Policyholders benefits	6,466	7,024	12,852	14,243
Interest credited to policyholders account balances	1,178	394	2,193	1,444
Dividends to policyholders	711	445	1,311	1,005
Amortization of deferred policy acquisition costs	482	220	919	438
General and administrative expenses	2,802	2,727	5,500	5,410
Total benefits and expenses	11,639	10,810	22,775	22,540
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF OPERATING JOINT VENTURES	1,507	(769)	3,225	(2,328)
Income tax expense (benefit)	404	(275)	877	(1,102)
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE EQUITY IN EARNINGS OF OPERATING JOINT VENTURES	1,103	(494)	2,348	(1,226)
Equity in earnings of operating joint ventures, net of taxes	6	5	6	51
INCOME (LOSS) FROM CONTINUING OPERATIONS	1,109	(489)	2,354	(1,175)
Income (loss) from discontinued operations, net of taxes	4	2	8	3
NET INCOME (LOSS)	1,113	(487)	2,362	(1,172)
Less: Income (loss) attributable to noncontrolling interests	23	27	34	62
NET INCOME (LOSS) ATTRIBUTABLE TO PRUDENTIAL FINANCIAL, INC	$ 1,090	$ (514)	$ 2,328	$ (1,234)
EARNINGS PER SHARE (See Note 8)				
Financial Services Businesses				
Basic earnings per share-Common Stock:				

Income (loss) from continuing operations attributable to Prudential Financial, Inc.	$ 2.25	$ (1.12)	$ 4.87	$ (2.70)
Income (loss) from discontinued operations, net of taxes	0.01	0.00	0.02	0.01
Net income (loss) attributable to Prudential Financial, Inc.	$ 2.26	$ (1.12)	$ 4.89	$ (2.69)
Diluted earnings per share-Common Stock:				
Income (loss) from continuing operations attributable to Prudential Financial, Inc.	$ 2.21	$ (1.12)	$ 4.79	$ (2.70)
Income (loss) from discontinued operations, net of taxes	0.01	0.00	0.02	0.01
Net income (loss) attributable to Prudential Financial, Inc.	$ 2.22	$ (1.12)	$ 4.81	$ (2.69)
Dividends declared per share of Common Stock	$ 0.53	$ 0.40	$ 1.06	$ 0.80
Closed Block Business				
Basic and Diluted earnings per share-Class B Stock:				
Income (loss) from continuing operations attributable to Prudential Financial, Inc.	$ 22.00	$ 1.00	$ 29.50	$ 6.50
Income (loss) from discontinued operations, net of taxes	0.00	0.00	0.00	0.00
Net income (loss) attributable to Prudential Financial, Inc.	$ 22.00	$ 1.00	$ 29.50	$ 6.50
Dividends declared per share of Class B Stock	$ 2.41	$ 2.41	$ 4.82	$ 4.82

See Notes to Unaudited Interim Consolidated Financial Statements

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PRUDENTIAL FINANCIAL, INC.

Unaudited Interim Consolidated Statements of Comprehensive Income

Three and Six Months Ended June 30, 2014 and 2013 (in millions)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
NET INCOME (LOSS)	$ 1,113	$ (487)	$ 2,362	$ (1,172)
Other comprehensive income (loss), before tax:				
Foreign currency translation adjustments for the period	167	(505)	247	(1,406)
Net unrealized investment gains (losses)	3,251	(5,430)	6,319	(1,152)
Defined benefit pension and postretirement unrecognized periodic benefit	20	43	43	93
Total	3,438	(5,892)	6,609	(2,465)
Less: Income tax expense (benefit) related to other comprehensive income (loss)	1,158	(1,933)	2,205	(710)
Other comprehensive income (loss), net of taxes	2,280	(3,959)	4,404	(1,755)
Comprehensive income (loss)	3,393	(4,446)	6,766	(2,927)
Less: Comprehensive income (loss) attributable to noncontrolling interests	24	37	42	72
Comprehensive income (loss) attributable to Prudential Financial, Inc.	$ 3,369	$ (4,483)	$ 6,724	$ (2,999)

See Notes to Unaudited Interim Consolidated Financial Statements

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PRUDENTIAL FINANCIAL, INC.

Unaudited Interim Consolidated Statements of Equity(1)

Six Months Ended June 30, 2014 and 2013 (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, 2013	$ 6	$ 24,475	$ 14,531	$ (12,415)	$ 8,681	$ 35,278	$ 603	$ 35,881
Common Stock acquired				(500)		(500)		(500)
Contributions from noncontrolling interests		(3)				(3)	2	(1)
Distributions to noncontrolling interests							(54)	(54)
Consolidations/(deconsolidations) of noncontrolling interests							19	19
Stock-based compensation programs		6	0	192		198		198
Dividends declared on Common Stock			(493)			(493)		(493)
Dividends declared on Class B Stock			(9)			(9)		(9)
Comprehensive income:								
Net income (loss)			2,328			2,328	34	2,362
Other comprehensive income (loss), net of tax					4,396	4,396	8	4,404
Total comprehensive income (loss)						6,724	42	6,766
Balance, June 30, 2014	$ 6	$ 24,478	$ 16,357	$ (12,723)	$ 13,077	$ 41,195	$ 612	$ 41,807

	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, 2012	$ 6	$ 24,380	$ 16,066	$ (12,163)	$ 10,214	$ 38,503	$ 609	$ 39,112
Common Stock acquired				(250)		(250)		(250)
Contributions from noncontrolling interests							1	1
Distributions to noncontrolling interests							(72)	(72)
Consolidations/(deconsolidations) of noncontrolling interests							28	28
Stock-based compensation programs		3	(39)	237		201		201
Dividends declared on Common Stock			(376)			(376)		(376)
Dividends declared on Class B Stock			(10)			(10)		(10)
Comprehensive income:								
Net income (loss)			(1,234)			(1,234)	62	(1,172)
Other comprehensive income (loss), net of tax					(1,765)	(1,765)	10	(1,755)
Total comprehensive income (loss)						(2,999)	72	(2,927)
Balance, June 30, 2013	$ 6	$ 24,383	$ 14,407	$ (12,176)	$ 8,449	$ 35,069	$ 638	$ 35,707

(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

Six Months Ended June 30, 2014 and 2013 (in millions)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ 2,362	$ (1,172)
Adjustments to reconcile net income to net cash provided by operating activities:		
Realized investment (gains) losses, net	(817)	1,747
Policy charges and fee income	(1,032)	(856)
Interest credited to policyholders account balances	2,193	1,444
Depreciation and amortization	179	161
Gains on trading account assets supporting insurance liabilities, net	(324)	378
Change in:		
Deferred policy acquisition costs	(429)	(1,131)
Future policy benefits and other insurance liabilities	3,251	4,774
Other trading account assets	(1)	(39)
Income taxes	898	(2,681)
Other, net	(725)	(239)
Cash flows from operating activities	5,555	2,386
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from the sale/maturity/prepayment of:		
Fixed maturities, available-for-sale	26,535	26,806
Fixed maturities, held-to-maturity	232	275
Trading account assets supporting insurance liabilities and other trading account assets	6,098	12,639
Equity securities, available-for-sale	2,483	2,082
Commercial mortgage and other loans	1,673	2,737
Policy loans	1,096	1,176
Other long-term investments	350	805
Short-term investments	35,249	21,896
Payments for the purchase/origination of:		
Fixed maturities, available-for-sale	(32,670)	(30,252)
Fixed maturities, held-to-maturity	(23)	(37)
Trading account assets supporting insurance liabilities and other trading account assets	(7,563)	(14,019)
Equity securities, available-for-sale	(2,289)	(1,982)
Commercial mortgage and other loans	(3,527)	(3,753)
Policy loans	(969)	(905)
Other long-term investments	(1,148)	(1,522)
Short-term investments	(33,301)	(23,090)
Acquisition of business, net of cash acquired	(23)	(488)
Other, net	272	(221)
Cash flows used in investing activities	(7,525)	(7,853)
CASH FLOWS FROM FINANCING ACTIVITIES		
Policyholders account deposits	12,226	12,245
Policyholders account withdrawals	(11,617)	(12,957)
Net change in securities sold under agreements to repurchase and cash collateral for loaned securities	736	2,914
Cash dividends paid on Common Stock	(495)	(397)
Cash dividends paid on Class B Stock	(10)	(10)
Net change in financing arrangements (maturities 90 days or less)	324	496
Common Stock acquired	(500)	(237)
Common Stock reissued for exercise of stock options	138	116
Proceeds from the issuance of debt (maturities longer than 90 days)	2,817	2,091

Repayments of debt (maturities longer than 90 days)	(971)	(2,848)
Excess tax benefits from share-based payment arrangements	16	13
Other, net	(47)	(161)
Cash flows from financing activities	2,617	1,265
Effect of foreign exchange rate changes on cash balances	74	(853)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	721	(5,055)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	11,439	18,100
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 12,160	$ 13,045
NON-CASH TRANSACTIONS DURING THE PERIOD		
Treasury Stock shares issued for stock-based compensation programs	$ 94	$ 102
Acquisition of Gibraltar BSN Life Berhad (See Note 3):		
Assets acquired, excluding cash and cash equivalents acquired	$ 656	$ 0
Liabilities assumed	586	0
Noncontrolling interest assumed	47	0
Net cash paid on acquisition	$ 23	$ 0
Acquisition of The Hartford s individual life business (See Note 3):		
Assets acquired, excluding cash and cash equivalents acquired	$ 0	$ 11,056
Liabilities assumed	0	10,568
Net cash paid on acquisition	$ 0	$ 488

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, and investment management. 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. The Company s 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, 2013.

The Company s Gibraltar Life Insurance Company, Ltd. (Gibraltar Life) consolidated operations use a November 30 fiscal year end for purposes of inclusion in the Company s Consolidated Financial Statements. Therefore, the Unaudited Interim Consolidated Financial Statements as of June 30, 2014, include the assets and liabilities of Gibraltar Life and its results of operations as of, and for the three and six months ended, May 31, 2014, respectively.

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.

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The most significant estimates include those used in determining deferred policy acquisition costs and related amortization; value 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.

Reclassifications

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

2. SIGNIFICANT ACCOUNTING POLICIES AND PRONOUNCEMENTS

This section supplements, and should be read in conjunction with, Note 2 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2013.

Adoption of New Accounting Pronouncements

In December 2013, the Financial Accounting Standards Board (FASB) issued updated guidance establishing a single definition of a public entity for use in financial accounting and reporting guidance. This new guidance is effective for all current and future reporting periods and did not have a significant effect on the Company s consolidated financial position, results of operations or financial statement disclosures.

In July 2013, the FASB issued new guidance regarding derivatives. The guidance permits the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) to be used as a U.S. benchmark interest rate for hedge accounting in addition to the United States Treasury rate and London Inter-Bank Offered Rate (LIBOR). The guidance also removes the restriction on using different benchmark rates for similar hedges. The guidance is effective for qualifying new or redesignated hedging relationships entered into on or after July 17, 2013, and was applied prospectively. Adoption of the guidance did not have a significant effect on the Company s consolidated financial position, results of operations or financial statement disclosures.

In July 2013, the FASB issued updated guidance regarding the presentation of unrecognized tax benefits when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. This new guidance became effective for interim or annual reporting periods that began after December 15, 2013, and was applied prospectively. Adoption of the guidance did not have a significant effect on the Company s consolidated financial position, results of operations or financial statement disclosures.

In June 2013, the FASB issued updated guidance clarifying the characteristics of an investment company and requiring new disclosures. Under the guidance, all entities regulated under the Investment Company Act of 1940 automatically qualify as investment companies, while all other entities need to consider both the fundamental and typical characteristics of an investment company in determining whether they qualify as investment companies. This new guidance became effective for interim or annual reporting periods that began after December 15, 2013, and was applied prospectively. Adoption of the guidance did not have a significant effect on the Company s consolidated financial position, results of operations or financial statement disclosures.

In March 2013, the FASB issued updated guidance regarding the recognition in net income of the cumulative translation adjustment upon the sale or loss of control of a business or group of assets residing in a foreign subsidiary, or a loss of control of a foreign investment. This guidance became effective for interim or annual reporting periods that began after December 15, 2013, and was applied prospectively. The amendments

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

require an entity that ceases to have a controlling financial interest in a subsidiary or group of assets within a foreign entity to release any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. For an equity method investment that is a foreign entity, the partial sale guidance still applies. As such, a pro rata portion of the cumulative translation adjustment should be released into net income upon a partial sale of such an equity method investment. Adoption of the guidance did not have a significant effect on the Company s consolidated financial position, results of operations or financial statement disclosures.

In February 2013, the FASB issued updated guidance regarding the presentation of comprehensive income. Under the guidance, an entity is required to separately present information about significant items reclassified out of accumulated other comprehensive income by component as well as changes in accumulated other comprehensive income balances by component in either the financial statements or the notes to the financial statements. The guidance does not change the items that are reported in other comprehensive income, does not change when an item of other comprehensive income must be reclassified to net income, and does not amend any existing requirements for reporting net income or other comprehensive income. The guidance became effective for interim or annual reporting periods that began after December 15, 2012, and was applied prospectively. The disclosures required by this guidance are included in Note 7.

In December 2011 and January 2013, the FASB issued updated guidance regarding the disclosure of recognized derivative instruments (including bifurcated embedded derivatives), repurchase agreements and securities borrowing/lending transactions that are offset in the statement of financial position or are subject to an enforceable master netting arrangement or similar agreement (irrespective of whether they are offset in the statement of financial position). This new guidance requires an entity to disclose information on both a gross and net basis about instruments and transactions within the scope of this guidance. This new guidance became effective for interim or annual reporting periods that began on or after January 1, 2013, and was applied retrospectively for all comparative periods presented. The disclosures required by this guidance are included in Note 14.

Future Adoption of New Accounting Pronouncements

In January 2014, the FASB issued updated guidance regarding investments in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit. Under the guidance, an entity is permitted to make an accounting policy election to amortize the initial cost of its investment in proportion to the tax credits and other tax benefits received and recognize the net investment performance in the statement of operations as a component of income tax expense (benefit) if certain conditions are met. The new guidance is effective for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014, and should be applied retrospectively to all periods presented. 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 January 2014, the FASB issued updated guidance for troubled debt restructurings clarifying when an in substance repossession or foreclosure occurs, and when a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan. The new guidance is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2014. This guidance can be elected for prospective adoption or by using a modified retrospective transition method. This guidance is not expected to have a significant impact on the Company s consolidated financial position, results of operations or financial statement disclosures.

In April 2014, the FASB issued updated guidance that changes the criteria for reporting discontinued operations and introduces new disclosures. The new guidance is effective prospectively to new disposals and new

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

classifications of disposal groups as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within those annual periods. Early adoption is permitted for new disposals or new classifications as held for sale that have not been reported in financial statements previously issued or available for issuance. This guidance is not expected to have a significant impact on the Company s consolidated financial position, results of operations or financial statement disclosures.

In May 2014, the FASB issued updated guidance on accounting for revenue recognition. The guidance is based on the core principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance also requires additional disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from cost incurred to obtain or fulfill a contract. Revenue recognition for insurance contracts is explicitly scoped out of the guidance. The new guidance is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2016, and must be applied using one of two retrospective application methods. Early adoption is not permitted. 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 August 2014, the FASB issued updated guidance for measuring the financial assets and the financial liabilities of a consolidated collateralized financing entity. Under the guidance, an entity within scope is permitted to measure both the financial assets and financial liabilities of a consolidated collateralized financing entity based on either the fair value of the financial assets or the financial liabilities, whichever is more observable. If elected, the guidance will eliminate the measurement difference that exists when both are measured at fair value. The new guidance is effective for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2015. Early adoption will be permitted. This guidance can be elected for modified retrospective or full retrospective adoption. The Company is currently assessing the impact of the guidance on the Company s consolidated financial position, results of operations and financial statement disclosures.

3. ACQUISITIONS AND DISPOSITIONS

Acquisition of UniAsia Life Assurance

On January 2, 2014, the Company completed the acquisition of UniAsia Life Assurance Berhad, an established life insurance company in Malaysia, through the formation of a joint venture with Bank Simpanan Nasional (BSN), a bank owned by the Malaysian government. The joint venture paid cash consideration of $158 million, 70% of which was provided by Prudential Insurance and 30% of which was provided by BSN. This acquisition is part of the Company s strategic initiative to further expand its business into Southeast Asian markets. Subsequent to the acquisition, the Company renamed the acquired company Gibraltar BSN Life Berhad.

The assets acquired and the liabilities assumed have been included in the Company s Unaudited Interim Consolidated Financial Statements as of the acquisition date. After adjustments, total assets acquired were $744 million, including $88 million of cash and cash equivalents and $19 million of goodwill, none of which is deductible for local tax purposes, and total liabilities assumed were $586 million.

Prudential Financial intends to make a Section 338(g) election under the Internal Revenue Code with respect to this acquisition, resulting in the acquired entity being treated for U.S. tax purposes as a newly-incorporated company. Under such election, the U.S. tax basis of the assets acquired and liabilities assumed of UniAsia Life Assurance Berhad was adjusted as of January 2, 2014, to reflect the consequences of the Section 338(g) election.

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Acquisition of The Hartford s Individual Life Insurance Business

On January 2, 2013, the Company acquired The Hartford Financial Services Group s (The Hartford) individual life insurance business through a reinsurance transaction. Under the agreement, the Company paid The Hartford cash consideration of $615 million, primarily in the form of a ceding commission, to provide reinsurance for approximately 700,000 life insurance policies with net retained face amount in force of approximately $141 billion. The acquisition increased the Company s scale in the U.S. individual life insurance market, particularly universal life products, and provides complementary distribution opportunities through expanded wirehouse and bank distribution channels.

The assets acquired and liabilities assumed have been included in the Company s Unaudited Interim Consolidated Financial Statements as of the acquisition date. Total assets acquired were $11.2 billion, including $1.4 billion of value of business acquired and $0.1 billion of cash, and total liabilities assumed were $10.6 billion. There is no goodwill, including tax deductible goodwill, associated with the acquisition.

Sale of Wealth Management Solutions Business

In April 2013, the Company signed a definitive agreement to sell its wealth management solutions business to Envestnet Inc. The transaction, which does not have a material impact to the Company s financial results, closed on July 1, 2013. Due to the existence of an ongoing contractual relationship between the Company and these operations, this disposition did not qualify for discontinued operations treatment under U.S. GAAP.

Discontinued Operations

Income from discontinued operations, including charges upon disposition, are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Real estate investments sold or held for sale(1)	$ 6	$ 2	$ 12	$ 2
Global commodities business	0	0	0	2
Income from discontinued operations before income taxes	6	2	12	4
Income tax expense	2	0	4	1
Income from discontinued operations, net of taxes	$ 4	$ 2	$ 8	$ 3

(1) Reflects the income from discontinued real estate investments.

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 operations as follows:

	June 30, 2014	December 31, 2013
	(in millions)	
Total assets	$ 5	$ 15
Total liabilities	$ 7	$ 7

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

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:

	June 30, 2014				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Other-than-temporary Impairments in AOCI(3)
			(in millions)		
Fixed maturities, available-for-sale					
U.S. Treasury securities and obligations of U.S. government authorities and agencies	$ 14,348	$ 2,759	$ 8	$ 17,099	$ 0
Obligations of U.S. states and their political subdivisions	4,766	566	20	5,312	0
Foreign government bonds	79,407	8,869	138	88,138	1
Corporate securities	148,552	14,935	1,206	162,281	(6)
Asset-backed securities(1)	10,577	289	150	10,716	(626)
Commercial mortgage-backed securities	14,040	460	58	14,442	0
Residential mortgage-backed securities(2)	6,066	427	9	6,484	(6)
Total fixed maturities, available-for-sale	$ 277,756	$ 28,305	$ 1,589	$ 304,472	$ (637)
Equity securities, available-for-sale	$ 7,218	$ 3,030	$ 26	$ 10,222	

	June 30, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(in millions)		
Fixed maturities, held-to-maturity				
Foreign government bonds	$ 972	$ 149	$ 0	$ 1,121
Corporate securities(4)	879	71	17	933
Asset-backed securities(1)	641	45	0	686
Commercial mortgage-backed securities	114	11	0	125
Residential mortgage-backed securities(2)	565	34	0	599

Total fixed maturities, held-to-maturity(4)	$ 3,171	$ 310	$ 17	$ 3,464

(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 (AOCI), which were not included in earnings. Amount excludes $921 million of net unrealized gains on impaired available-for-sale securities and less than $1 million of net unrealized gains on impaired held-to-maturity securities relating to changes in the value of such securities subsequent to the impairment measurement date.
(4) Excludes notes with amortized cost of $3,588 million (fair value, $3,859 million) which have been offset with the associated payables under a netting agreement.

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

	December 31, 2013				
	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	$ 13,754	$ 1,742	$ 96	$ 15,400	$ 0
Obligations of U.S. states and their political subdivisions	3,598	274	137	3,735	0
Foreign government bonds	75,595	7,459	266	82,788	1
Corporate securities	145,091	12,095	3,408	153,778	(4)
Asset-backed securities(1)	10,691	214	316	10,589	(755)
Commercial mortgage-backed securities	13,633	403	163	13,873	0
Residential mortgage-backed securities(2)	6,365	379	41	6,703	(7)
Total fixed maturities, available-for-sale	$ 268,727	$ 22,566	$ 4,427	$ 286,866	$ (765)
Equity securities, available-for-sale	$ 7,003	$ 2,931	$ 24	$ 9,910	

	December 31, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses (in millions)	Fair Value
Fixed maturities, held-to-maturity				
Foreign government bonds	$ 938	$ 117	$ 0	$ 1,055
Corporate securities(4)	904	50	24	930
Asset-backed securities(1)	693	46	0	739
Commercial mortgage-backed securities	166	18	0	184
Residential mortgage-backed securities(2)	611	34	0	645
Total fixed maturities, held-to-maturity(4)	$ 3,312	$ 265	$ 24	$ 3,553

(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 AOCI, which were not included in earnings. Amount excludes $875 million of net unrealized gains on impaired available-for-sale securities and $1 million of net unrealized gains on impaired held-to-maturity securities relating to changes in the value of such securities subsequent to the impairment measurement date.
(4) Excludes notes with amortized cost of $2,400 million (fair value, $2,461 million) which have been offset with the associated payables under a netting agreement.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The amortized cost and fair value of fixed maturities by contractual maturities at June 30, 2014, are as follows:

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in millions)			
Due in one year or less	$ 12,289	$ 12,760	$ 0	$ 0
Due after one year through five years	50,192	55,136	21	22
Due after five years through ten years	57,901	63,722	323	335
Due after ten years(1)	126,691	141,212	1,507	1,697
Asset-backed securities	10,577	10,716	641	686
Commercial mortgage-backed securities	14,040	14,442	114	125
Residential mortgage-backed securities	6,066	6,484	565	599
Total	$ 277,756	$ 304,472	$ 3,171	$ 3,464

(1) Excludes notes with amortized cost of $3,588 million (fair value, $3,859 million) which have been offset with the associated payables under a netting agreement.

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.

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 June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Fixed maturities, available-for-sale				
Proceeds from sales	$ 7,460	$ 8,139	$ 16,038	$ 14,634
Proceeds from maturities/repayments	5,847	6,705	10,706	12,444
Gross investment gains from sales, prepayments, and maturities	476	413	901	642
Gross investment losses from sales and maturities	(83)	(88)	(235)	(194)
Fixed maturities, held-to-maturity				
Gross investment gains from prepayments	$ 0	$ 0	$ 0	$ 0
Proceeds from maturities/repayments	138	148	232	273
Equity securities, available-for-sale				

Proceeds from sales	$ 1,316	$ 1,137	$ 2,481	$ 2,185
Gross investment gains from sales	198	124	331	231
Gross investment losses from sales	(22)	(29)	(60)	(52)
Fixed maturity and equity security impairments				
Net writedowns for other-than-temporary impairment losses on fixed maturities recognized in earnings(1)	$ (26)	$ (33)	$ (42)	$ (103)
Writedowns for impairments on equity securities	(7)	(1)	(17)	(8)

(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.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

As discussed in Note 2 to the Company s Consolidated Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2013, 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 tables set 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 June 30, 2014	Six Months Ended June 30, 2014
	(in millions)	
Balance, beginning of period	$ 838	$ 968
Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period	(59)	(199)
Credit loss impairments previously recognized on securities impaired to fair value during the period(1)	0	0
Credit loss impairment recognized in the current period on securities not previously impaired	10	12
Additional credit loss impairments recognized in the current period on securities previously impaired	0	4
Increases due to the passage of time on previously recorded credit losses	9	18
Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected	(4)	(9)
Balance, end of period	$ 794	$ 794

	Three Months Ended June 30, 2013	Six Months Ended June 30, 2013
	(in millions)	
Balance, beginning of period	$ 1,089	$ 1,166
Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period	(53)	(150)
Credit loss impairments previously recognized on securities impaired to fair value during the period(1)	0	0
Credit loss impairment recognized in the current period on securities not previously impaired	7	8
Additional credit loss impairments recognized in the current period on securities previously impaired	27	39

Increases due to the passage of time on previously recorded credit losses	14	26
Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected	(4)	(9)
Balance, end of period	$ 1,080	$ 1,080

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

(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:

	June 30, 2014		December 31, 2013	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in millions)			
Short-term investments and cash equivalents	$ 726	$ 726	$ 697	$ 697
Fixed maturities:				
Corporate securities	12,097	12,829	12,109	12,616
Commercial mortgage-backed securities	2,450	2,498	2,417	2,441
Residential mortgage-backed securities(1)	1,772	1,795	1,857	1,830
Asset-backed securities(2)	1,159	1,181	1,096	1,107
Foreign government bonds	639	659	579	596
U.S. government authorities and agencies and obligations of U.S. states	302	353	303	341
Total fixed maturities	18,419	19,315	18,361	18,931
Equity securities	1,005	1,232	913	1,199
Total trading account assets supporting insurance liabilities	$ 20,150	$ 21,273	$ 19,971	$ 20,827

(1) Includes publicly-traded agency pass-through securities and collateralized mortgage obligations.
(2) Includes credit-tranched securities collateralized by sub-prime mortgages, auto loans, credit cards, education loans and other asset types.

The net change in unrealized gains (losses) from trading account assets supporting insurance liabilities still held at period end, recorded within Other income , was $201 million and ($596) million during the three months ended June 30, 2014 and 2013, respectively, and $267 million and ($493) million during the six months ended June 30, 2014 and 2013, respectively.

Other Trading Account Assets

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

	June 30, 2014		December 31, 2013	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in millions)			
Short-term investments and cash equivalents	$ 85	$ 86	$ 105	$ 106
Fixed maturities	6,265	6,361	4,653	4,723
Equity securities	1,026	1,160	1,051	1,177
Other	8	13	3	7
Subtotal	$ 7,384	7,620	$ 5,812	6,013
Derivative instruments		1,045		440
Total other trading account assets		$ 8,665		$ 6,453

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The net change in unrealized gains (losses) from other trading account assets, excluding derivative instruments, still held at period end, recorded within Other income was $9 million and $13 million during the three months ended June 30, 2014 and 2013, respectively, and $35 million and $87 million during the six months ended June 30, 2014 and 2013, respectively.

Concentrations of Financial Instruments

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

As of both June 30, 2014 and December 31, 2013, the Company s exposure to concentrations of credit risk of single issuers greater than 10% of the Company s stockholders equity included 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.

	June 30, 2014		December 31, 2013	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in millions)			
Investments in Japanese government and government agency securities:				
Fixed maturities, available-for-sale	$ 61,968	$ 68,248	$ 59,775	$ 65,389
Fixed maturities, held-to-maturity	949	1,096	916	1,032
Trading account assets supporting insurance liabilities	490	498	451	458
Other trading account assets	39	39	38	39
Short-term investments	0	0	0	0
Cash equivalents	296	296	107	107
Total	$ 63,742	$ 70,177	$ 61,287	$ 67,025

	June 30, 2014		December 31, 2013	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in millions)			
Investments in South Korean government and government agency securities:				
Fixed maturities, available-for-sale	$ 7,257	$ 8,322	$ 6,672	$ 7,277
Fixed maturities, held-to-maturity	0	0	0	0
Trading account assets supporting insurance liabilities	61	62	61	61
Other trading account assets	0	0	0	0
Short-term investments	0	0	0	0
Cash equivalents	0	0	0	0

Total	$ 7,318	$ 8,384	$ 6,733	$ 7,338

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Commercial Mortgage and Other Loans

The Company s commercial mortgage and other loans are comprised as follows, as of the dates indicated:

	June 30, 2014		December 31, 2013	
	Amount (in millions)	% of Total	Amount (in millions)	% of Total
Commercial and agricultural mortgage loans by property type:				
Office	$ 8,455	20.6%	$ 7,762	19.9%
Retail	8,458	20.6	8,698	22.3
Apartments/Multi-Family	8,883	21.6	7,492	19.2
Industrial	7,372	17.9	7,390	18.9
Hospitality	2,068	5.0	2,050	5.2
Other	3,691	9.0	3,464	8.9
Total commercial mortgage loans	38,927	94.7	36,856	94.4
Agricultural property loans	2,173	5.3	2,183	5.6
Total commercial and agricultural mortgage loans by property type	41,100	100.0%	39,039	100.0%
Valuation allowance	(192)		(195)	
Total net commercial and agricultural mortgage loans by property type	40,908		38,844	
Other loans				
Uncollateralized loans	1,232		1,306	
Residential property loans	512		544	
Other collateralized loans	328		335	
Total other loans	2,072		2,185	
Valuation allowance	(16)		(21)	
Total net other loans	2,056		2,164	
Total commercial mortgage and other loans(1)	$ 42,964		$ 41,008	

(1) Includes loans held at fair value.

The commercial mortgage and agricultural property loans are geographically dispersed throughout the United States, Canada, Europe, Mexico and Asia with the largest concentrations in California (26%), New York (10%), and Texas (9%) at June 30, 2014.

Activity in the allowance for losses for all commercial mortgage and other loans, as of the dates indicated, is as follows:

	June 30, 2014					
	Commercial Mortgage Loans	Agricultural Property Loans	Residential Property Loans	Other Collateralized Loans	Uncollateralized Loans	Total
	(in millions)					
Allowance for losses, beginning of year	$ 188	$ 7	$ 6	$ 3	$ 12	$ 216
Addition to / (release of) allowance of losses	4	0	0	(1)	(2)	1
Charge-offs, net of recoveries	(7)	0	0	(2)	0	(9)
Change in foreign exchange	0	0	0	0	0	0
Total ending balance	$ 185	$ 7	$ 6	$ 0	$ 10	$ 208

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

	December 31, 2013					
	Commercial Mortgage Loans	Agricultural Property Loans	Residential Property Loans	Other Collateralized Loans	Uncollateralized Loans	Total
	(in millions)					
Allowance for losses, beginning of year	$ 209	$ 20	$ 11	$ 12	$ 17	$ 269
Addition to / (release of) allowance of losses	12	(7)	(3)	(9)	(2)	(9)
Charge-offs, net of recoveries	(33)	(6)	0	0	0	(39)
Change in foreign exchange	0	0	(2)	0	(3)	(5)
Total ending balance	$ 188	$ 7	$ 6	$ 3	$ 12	$ 216

The following tables set forth the allowance for credit losses and the recorded investment in commercial mortgage and other loans as of the dates indicated:

	June 30, 2014					
	Commercial Mortgage Loans	Agricultural Property Loans	Residential Property Loans	Other Collateralized Loans	Uncollateralized Loans	Total
	(in millions)					
Allowance for Credit Losses:						
Ending balance: individually evaluated for impairment	$ 11	$ 0	$ 0	$ 0	$ 0	$ 11
Ending balance: collectively evaluated for impairment	174	7	6	0	10	197
Ending balance: loans acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending balance	$ 185	$ 7	$ 6	$ 0	$ 10	$ 208
Recorded Investment:(1)						
Ending balance gross of reserves: individually evaluated for impairment	$ 400	$ 4	$ 0	$ 4	$ 2	$ 410
Ending balance gross of reserves: collectively evaluated for impairment	38,527	2,169	512	324	1,230	42,762
Ending balance gross of reserves: loans acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending balance, gross of reserves	$ 38,927	$ 2,173	$ 512	$ 328	$ 1,232	$ 43,172

(1) Recorded investment reflects the balance sheet carrying value gross of related allowance.

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

	December 31, 2013					
	Commercial Mortgage Loans	Agricultural Property Loans	Residential Property Loans	Other Collateralized Loans	Uncollateralized Loans	Total
	(in millions)					
Allowance for Credit Losses:						
Ending balance: individually evaluated for impairment	$ 16	$ 0	$ 0	$ 3	$ 0	$ 19
Ending balance: collectively evaluated for impairment	172	7	6	0	12	197
Ending balance: loans acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending balance	$ 188	$ 7	$ 6	$ 3	$ 12	$ 216
Recorded Investment:(1)						
Ending balance gross of reserves: individually evaluated for impairment	$ 429	$ 5	$ 0	$ 7	$ 2	$ 443
Ending balance gross of reserves: collectively evaluated for impairment	36,427	2,178	544	328	1,304	40,781
Ending balance gross of reserves: loans acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending balance, gross of reserves	$ 36,856	$ 2,183	$ 544	$ 335	$ 1,306	$ 41,224

(1) Recorded investment reflects the balance sheet carrying value gross of related allowance.

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Impaired loans include those loans for which it is probable that all amounts due will not be collected according to the contractual terms of the loan agreement. Impaired commercial mortgage and other loans identified in management s specific review of probable loan losses and the related allowance for losses, as of the dates indicated, are as follows:

	June 30, 2014				
	Recorded Investment(1)	Unpaid Principal Balance	Related Allowance	Average Recorded Investment Before Allowance(2)	Interest Income Recognized(3)
	(in millions)				
With no related allowance recorded:					
Commercial mortgage loans	$ 14	$ 14	$ 0	$ 24	$ 0
Agricultural property loans	1	1	0	3	0
Residential property loans	0	0	0	0	0
Other collateralized loans	0	0	0	0	0
Uncollateralized loans	0	2	0	0	0
Total with no related allowance	$ 15	$ 17	$ 0	$ 27	$ 0
With an allowance recorded:					
Commercial mortgage loans	$ 114	$ 115	$ 11	$ 73	$ 3
Agricultural property loans	2	2	0	1	0
Residential property loans	0	0	0	0	0
Other collateralized loans	3	3	0	4	0
Uncollateralized loans	0	0	0	0	0
Total with related allowance	$ 119	$ 120	$ 11	$ 78	$ 3
Total:					
Commercial mortgage loans	$ 128	$ 129	$ 11	$ 97	$ 3
Agricultural property loans	3	3	0	4	0
Residential property loans	0	0	0	0	0
Other collateralized loans	3	3	0	4	0
Uncollateralized loans	0	2	0	0	0
Total	$ 134	$ 137	$ 11	$ 105	$ 3

(1) Recorded investment reflects the balance sheet carrying value gross of related allowance.
(2) Average recorded investment represents the average of the beginning-of-period and end-of-period balances.
(3) The interest income recognized is for the year-to-date income regardless of when the impairments occurred.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

	December 31, 2013				
	Recorded Investment(1)	Unpaid Principal Balance	Related Allowance	Average Recorded Investment Before Allowance(2)	Interest Income Recognized(3)
	(in millions)				
With no related allowance recorded:					
Commercial mortgage loans	$ 33	$ 33	$ 0	$ 30	$ 1
Agricultural property loans	5	5	0	2	0
Residential property loans	0	0	0	0	0
Other collateralized loans	0	0	0	0	0
Uncollateralized loans	0	2	0	0	0
Total with no related allowance	$ 38	$ 40	$ 0	$ 32	$ 1
With an allowance recorded:					
Commercial mortgage loans	$ 54	$ 55	$ 16	$ 121	$ 1
Agricultural property loans	0	0	0	10	0
Residential property loans	0	0	0	0	0
Other collateralized loans	5	5	3	8	3
Uncollateralized loans	0	0	0	0	0
Total with related allowance	$ 59	$ 60	$ 19	$ 139	$ 4
Total:					
Commercial mortgage loans	$ 87	$ 88	$ 16	$ 151	$ 2
Agricultural property loans	5	5	0	12	0
Residential property loans	0	0	0	0	0
Other collateralized loans	5	5	3	8	3
Uncollateralized loans	0	2	0	0	0
Total	$ 97	$ 100	$ 19	$ 171	$ 5

(1) Recorded investment reflects the balance sheet carrying value gross of related allowance.
(2) Average recorded investment represents the average of the beginning-of-period and all subsequent quarterly end-of-period balances.
(3) The interest income recognized is for the year-to-date income regardless of when the impairments occurred.

The net carrying value of commercial and other loans held for sale by the Company as of June 30, 2014 and December 31, 2013 was $204 million and $158 million, respectively. In all of these transactions, the Company pre-arranges that it will sell the loan to an investor. As of both June 30, 2014 and December 31, 2013, all of the Company s commercial and other loans held for sale were collateralized, with collateral primarily consisting of apartment complexes.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The following tables set forth certain key credit quality indicators as of June 30, 2014, based upon the recorded investment gross of allowance for credit losses.

Commercial mortgage loans

	Debt Service Coverage Ratio June 30, 2014			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total
		(in millions)		
Loan-to-Value Ratio				
0%-59.99%	$ 20,299	$ 560	$ 354	$ 21,213
60%-69.99%	11,675	436	268	12,379
70%-79.99%	4,099	479	41	4,619
Greater than 80%	354	183	179	716
Total commercial mortgage loans	$ 36,427	$ 1,658	$ 842	$ 38,927

Agricultural property loans

	Debt Service Coverage Ratio June 30, 2014			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total
		(in millions)		
Loan-to-Value Ratio				
0%-59.99%	$ 2,027	$ 134	$ 2	$ 2,163
60%-69.99%	10	0	0	10
70%-79.99%	0	0	0	0
Greater than 80%	0	0	0	0
Total agricultural property loans	$ 2,037	$ 134	$ 2	$ 2,173

Total commercial and agricultural mortgage loans

	Debt Service Coverage Ratio June 30, 2014			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total

		(in millions)		
Loan-to-Value Ratio				
0%-59.99%	$ 22,326	$ 694	$ 356	$ 23,376
60%-69.99%	11,685	436	268	12,389
70%-79.99%	4,099	479	41	4,619
Greater than 80%	354	183	179	716
Total commercial and agricultural mortgage loans	$ 38,464	$ 1,792	$ 844	$ 41,100

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The following tables set forth certain key credit quality indicators as of December 31, 2013, based upon the recorded investment gross of allowance for credit losses.

Commercial mortgage loans

	Debt Service Coverage Ratio December 31, 2013			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total
	(in millions)			
Loan-to-Value Ratio				
0%-59.99%	$ 19,089	$ 597	$ 179	$ 19,865
60%-69.99%	11,101	379	95	11,575
70%-79.99%	4,005	422	216	4,643
Greater than 80%	325	173	275	773
Total commercial mortgage loans	$ 34,520	$ 1,571	$ 765	$ 36,856

Agricultural property loans

	Debt Service Coverage Ratio December 31, 2013			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total
	(in millions)			
Loan-to-Value Ratio				
0%-59.99%	$ 2,023	$ 137	$ 0	$ 2,160
60%-69.99%	23	0	0	23
70%-79.99%	0	0	0	0
Greater than 80%	0	0	0	0
Total agricultural property loans	$ 2,046	$ 137	$ 0	$ 2,183

Total commercial and agricultural mortgage loans

	Debt Service Coverage Ratio December 31, 2013			
	Greater than 1.2X	1.0X to <1.2X	Less than 1.0X	Total

		(in millions)		
Loan-to-Value Ratio				
0%-59.99%	$ 21,112	$ 734	$ 179	$ 22,025
60%-69.99%	11,124	379	95	11,598
70%-79.99%	4,005	422	216	4,643
Greater than 80%	325	173	275	773
Total commercial and agricultural mortgage loans	$ 36,566	$ 1,708	$ 765	$ 39,039

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The following tables provide an aging of past due commercial mortgage and other loans as of the dates indicated, based upon the recorded investment gross of allowance for credit losses, as well as the amount of commercial mortgage loans on nonaccrual status as of the dates indicated.

	June 30, 2014							
	Current	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days - Accruing	Greater Than 90 Days - Not Accruing	Total Past Due	Total Commercial Mortgage and Other Loans	Non Accrual Status
	(in millions)							
Commercial mortgage loans	$ 38,918	$ 5	$ 3	$ 0	$ 1	$ 9	$ 38,927	$ 9
Agricultural property loans	2,172	0	0	0	1	1	2,173	1
Residential property loans	493	7	4	0	8	19	512	9
Other collateralized loans	328	0	0	0	0	0	328	3
Uncollateralized loans	1,232	0	0	0	0	0	1,232	2
Total	$ 43,143	$ 12	$ 7	$ 0	$ 10	$ 29	$ 43,172	$ 24

	December 31, 2013							
	Current	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days - Accruing	Greater Than 90 Days - Not Accruing	Total Past Due	Total Commercial Mortgage and Other Loans	Non Accrual Status
	(in millions)							
Commercial mortgage loans	$ 36,821	$ 16	$ 0	$ 0	$ 19	$ 35	$ 36,856	$ 154
Agricultural property loans	2,182	0	0	0	1	1	2,183	2
Residential property loans	520	11	3	0	10	24	544	10
Other collateralized loans	334	0	0	0	1	1	335	5
Uncollateralized loans	1,306	0	0	0	0	0	1,306	2
Total	$ 41,163	$ 27	$ 3	$ 0	$ 31	$ 61	$ 41,224	$ 173

See Note 2 to the Company s Consolidated Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2013, for further discussion regarding nonaccrual status loans.

For both the three and six months ended June 30, 2014, there were no new commercial mortgage and other loans acquired, other than those through direct origination, nor were there any new commercial mortgage and other loans sold, other than those classified as held-for-sale. For the three months ended June 30, 2013, there were no new commercial mortgage and other loans acquired, other than those through direct origination, and there were $7 million of commercial mortgage and other loans sold, other than those classified as held-for-sale. For the six months ended June 20, 2013, there were $718 million of commercial mortgage and other loans acquired, other than those through direct origination and $7 million of commercial mortgage and other loans sold, other than those classified as held-for-sale.

The Company s commercial mortgage and other loans may occasionally be involved in a troubled debt restructuring. As of both June 30, 2014 and December 31, 2013, the Company had no significant commitments to fund to borrowers that have been involved in a troubled debt restructuring. During the three months and six months ended June 30, 2014 and 2013, respectively, there were no new troubled debt restructurings related to commercial mortgage and other loans, and no payment defaults on commercial mortgage and other loans that were modified as a troubled debt restructuring within the 12 months preceding each respective period. For

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

additional information relating to the accounting for troubled debt restructurings, see Note 2 to the Company s Consolidated Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2013.

Net Investment Income

Net investment income for the three and six months ended June 30, 2014 and 2013, was from the following sources:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Fixed maturities, available-for-sale	$ 2,669	$ 2,641	$ 5,286	$ 5,292
Fixed maturities, held-to-maturity	42	30	82	61
Equity securities, available-for-sale	105	94	189	172
Trading account assets	259	234	517	472
Commercial mortgage and other loans	522	492	1,020	982
Policy loans	158	150	312	298
Short-term investments and cash equivalents	8	11	17	21
Other long-term investments	175	199	517	332
Gross investment income	3,938	3,851	7,940	7,630
Less: investment expenses	(184)	(140)	(348)	(281)
Net investment income	$ 3,754	$ 3,711	$ 7,592	$ 7,349

Realized Investment Gains (Losses), Net

Realized investment gains (losses), net, for the three and six months ended June 30, 2014 and 2013, were from the following sources:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Fixed maturities	$ 367	$ 291	$ 624	$ 344
Equity securities	169	94	254	171
Commercial mortgage and other loans	8	24	16	37

Investment real-estate	0	0	0	0
Joint ventures and limited partnerships	0	(5)	1	(6)
Derivatives(1)	60	(1,430)	(85)	(2,300)
Other	5	2	7	7
Realized investment gains (losses), net	$ 609	$ (1,024)	$ 817	$ (1,747)

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

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Net Unrealized Gains (Losses) on Investments by Asset Class

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

	June 30, 2014	December 31, 2013
	(in millions)	
Fixed maturity securities on which an OTTI loss has been recognized	$ 284	$ 110
Fixed maturity securities, available-for-sale all other	26,432	18,029
Equity securities, available-for-sale	3,004	2,907
Derivatives designated as cash flow hedges(1)	(533)	(446)
Other investments(2)	15	4
Net unrealized gains (losses) on investments	$ 29,202	$ 20,604

(1) See Note 14 for more information on cash flow hedges.
(2) As of June 30, 2014, includes $11 million of net unrealized losses on held-to-maturity securities that were previously transferred from available-for-sale.

Duration of Gross Unrealized Loss Positions for Fixed Maturities and Equity Securities

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

	June 30, 2014					
	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	$ 1,225	$ 5	$ 83	$ 3	$ 1,308	$ 8
Obligations of U.S. states and their political subdivisions	53	0	587	20	640	20
Foreign government bonds	967	26	2,046	112	3,013	138
Corporate securities	5,037	65	22,766	1,158	27,803	1,223
Commercial mortgage-backed securities	423	2	1,984	56	2,407	58

Asset-backed securities	1,358	7	2,883	143	4,241	150
Residential mortgage-backed securities	2	0	413	9	415	9
Total	$ 9,065	$ 105	$ 30,762	$ 1,501	$ 39,827	$ 1,606
Equity securities, available-for-sale	$ 492	$ 26	$ 1	$ 0	$ 493	$ 26

(1) Includes $174 million of fair value and $17 million of gross unrealized losses at June 30, 2014, on securities classified as held-to-maturity, a portion of which is not reflected in AOCI.

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

	December 31, 2013					
	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	$ 3,913	$ 95	$ 6	$ 1	$ 3,919	$ 96
Obligations of U.S. states and their political subdivisions	1,187	129	43	8	1,230	137
Foreign government bonds	3,260	211	438	55	3,698	266
Corporate securities	29,574	1,618	14,094	1,814	43,668	3,432
Commercial mortgage-backed securities	4,267	128	605	35	4,872	163
Asset-backed securities	3,007	42	2,556	274	5,563	316
Residential mortgage-backed securities	1,590	34	239	7	1,829	41
Total	$ 46,798	$ 2,257	$ 17,981	$ 2,194	$ 64,779	$ 4,451
Equity securities, available-for-sale	$ 586	$ 24	$ 1	$ 0	$ 587	$ 24

(1) Includes $210 million of fair value and $24 million of gross unrealized losses at December 31, 2013, on securities classified as held-to-maturity, a portion of which is not reflected in AOCI.

The gross unrealized losses on fixed maturity securities at June 30, 2014 and December 31, 2013, are composed of $1,484 million and $4,178 million, respectively, related to high or highest quality securities based on the National Association of Insurance Commissioners (NAIC) or equivalent rating and $122 million and $274 million, respectively, related to other than high or highest quality securities based on NAIC or equivalent rating. At June 30, 2014, the $1,501 million of gross unrealized losses of twelve months or more were concentrated in the consumer non-cyclical, utility, capital goods, and finance sectors of the Company s corporate securities. At December 31, 2013, the $2,194 million of gross unrealized losses of twelve months or more were concentrated in the consumer non-cyclical, utility, and capital goods sectors of the Company s corporate securities. In accordance with its policy described in Note 2 to the Company s Consolidated Financial Statements included in its 2013 Annual Report on Form 10-K, the Company concluded that an adjustment to earnings for other-than-temporary impairments for these securities was not warranted at June 30, 2014 or December 31, 2013. 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 foreign currency movements, credit spread widening and increased liquidity discounts. At June 30, 2014, the Company does not intend to sell these securities and it is not more likely than not that the Company will be required to sell these securities before the anticipated recovery of their remaining amortized cost bases.

At June 30, 2014, $2 million of the gross unrealized losses on equity securities represented declines in value of greater than 20%, all of which had been in that position for less than six months. At December 31, 2013, $4 million of the gross unrealized losses on equity securities represented declines in value of greater than 20%, all of which had been in that position for less than six months. In accordance with its policy described in Note 2 to the Company s Consolidated Financial Statements included in its 2013 Annual Report on Form 10-K, the Company concluded that an adjustment for other-than-temporary impairments for these equity securities was not warranted at June 30, 2014 or December 31, 2013.

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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 (the Investment Company Model) relates to those VIEs 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.

For all other VIEs, 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.

Consolidated Variable Interest Entities

The Company is the investment manager of certain asset-backed investment vehicles (commonly referred to as collateralized loan obligations, or CLOs) and certain other vehicles for which the Company earns fee income for investment management services, including certain investment structures in which the Company s asset management business invests with other co-investors in investment funds referred to as feeder funds. The Company may sell or syndicate investments through these vehicles, principally as part of the strategic investing activity of the Company s asset management businesses. Additionally, the Company may invest in securities issued by these vehicles. CLOs raise capital by issuing debt securities, and use the proceeds to purchase investments, typically interest-bearing financial instruments. The Company has analyzed these relationships and determined that for certain CLOs and other investment structures it is the primary beneficiary and consolidates these entities. This analysis includes a review of (1) the Company s rights and responsibilities as investment manager, (2) fees received by the Company and (3) other interests (if any) held by the Company. The assets of these VIEs are restricted and must be used first to settle liabilities of the VIE. The Company is not required to provide, and has not provided, material financial or other support to any of these VIEs.

Additionally, the Company is the primary beneficiary of certain VIEs in which the Company has invested, as part of its investment activities, but for which it is not the investment manager. These include 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 support or other support that was not contractually required to these VIEs.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

The table below reflects the carrying amount and balance sheet caption in which the assets and liabilities of consolidated VIEs are reported. The liabilities primarily comprise obligations under debt instruments issued by the VIEs that are non-recourse to the Company. The creditors of these VIE do not have recourse to the Company in excess of the assets contained within the VIE.

	Consolidated VIEs for Which the Company is the Investment Manager		Other Consolidated VIEs	
	June 30, 2014	December 31, 2013	June 30, 2014	December 31, 2013
	(in millions)			
Fixed maturities, available-for-sale	$ 54	$ 68	$ 115	$ 108
Fixed maturities, held-to-maturity	0	0	903	871
Trading account assets supporting insurance liabilities	0	0	10	11
Other trading account assets	5,473	3,832	0	0
Commercial mortgage and other loans	13	23	300	300
Other long-term investments	0	0	86	87
Cash and cash equivalents	493	566	0	(3)
Accrued investment income	26	19	4	4
Other assets	171	132	0	0
Total assets of consolidated VIEs	$ 6,230	$ 4,640	$ 1,418	$ 1,378
Notes issued by consolidated VIEs	$ 4,573	$ 3,302	$ 0	$ 0
Other liabilities	554	631	1	1
Total liabilities of consolidated VIEs	$ 5,127	$ 3,933	$ 1	$ 1

As included in the table above, notes issued by consolidated VIEs are classified in the line item on the Consolidated Statements of Financial Position titled, Notes issued by consolidated VIEs. Recourse is limited to the assets of the respective VIE and does not extend to the general credit of Prudential Financial. As of June 30, 2014, the maturities of these obligations were greater than five years.

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 $2,203 million and $2,381 million at June 30, 2014 and December 31, 2013, 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 to the trust that was not contractually required.

Unconsolidated Variable Interest Entities

The Company has determined that it is not the primary beneficiary of certain VIEs for which it is the investment manager. These VIEs consist primarily of investment funds for which the Company utilizes the

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Investment Company Model to assess consolidation. Accordingly, the Company has determined that it is not the primary beneficiary of these entities because it does not stand to absorb a majority of the VIE s expected losses or to receive a majority of the VIE s expected residual returns. For all other investment structures, the Company has determined that it is not the primary beneficiary 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 for which it is the investment manager is limited to its investment in the VIEs, which was $154 million and $489 million at June 30, 2014 and December 31, 2013, 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 $8,185 million and $9,426 million as of June 30, 2014 and December 31, 2013, 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 $7,541 million and $7,244 million as of June 30, 2014 and December 31, 2013, 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 investment manager. 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.

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 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

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

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 AOCI) 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 June 30, 2014 and December 31, 2013, the Company recognized a policyholder dividend obligation of $1,187 million and $887 million, respectively, to Closed Block policyholders for the excess of actual cumulative earnings over the expected cumulative earnings. Additionally, 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 $4,939 million and $3,624 million at June 30, 2014 and December 31, 2013, respectively, to be paid to Closed Block policyholders unless offset by future experience, with an offsetting amount reported in AOCI. See the table below for changes in the components of the policyholder dividend obligation for the six months ended June 30, 2014.

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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:

	June 30, 2014	December 31, 2013
	(in millions)	
Closed Block Liabilities		
Future policy benefits	$ 50,040	$ 50,258
Policyholders dividends payable	902	907
Policyholders dividend obligation	6,126	4,511
Policyholders account balances	5,328	5,359
Other Closed Block liabilities	5,774	4,281
Total Closed Block Liabilities	68,170	65,316
Closed Block Assets		
Fixed maturities, available-for-sale, at fair value	41,402	39,169
Other trading account assets, at fair value	261	291
Equity securities, available-for-sale, at fair value	3,789	3,884
Commercial mortgage and other loans	9,073	8,762
Policy loans	4,945	5,013
Other long-term investments	2,607	2,085
Short-term investments	1,333	1,790
Total investments	63,410	60,994
Cash and cash equivalents	765	544
Accrued investment income	537	542
Other Closed Block assets	530	296
Total Closed Block Assets	65,242	62,376
Excess of reported Closed Block Liabilities over Closed Block Assets	2,928	2,940
Portion of above representing accumulated other comprehensive income:		
Net unrealized investment gains (losses)	4,931	3,615
Allocated to policyholder dividend obligation	(4,939)	(3,624)
Future earnings to be recognized from Closed Block Assets and Closed Block Liabilities	$ 2,920	$ 2,931

Information regarding the policyholder dividend obligation is as follows:

		Six Months Ended June 30, 2014 (in millions)
Balance, January 1	$	4,511
Impact from earnings allocable to policyholder dividend obligation		300
Change in net unrealized investment gains (losses) allocated to policyholder dividend obligation		1,315
Balance, June 30	$	6,126

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Closed Block revenues and benefits and expenses for the three and six months ended June 30, 2014 and 2013 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Revenues				
Premiums	$ 711	$ 711	$ 1,350	$ 1,358
Net investment income	683	714	1,404	1,421
Realized investment gains (losses), net	369	(20)	504	76
Other income	19	5	34	15
Total Closed Block revenues	1,782	1,410	3,292	2,870
Benefits and Expenses				
Policyholders benefits	911	870	1,703	1,685
Interest credited to policyholders account balances	33	34	67	68
Dividends to policyholders	688	408	1,265	911
General and administrative expenses	111	118	225	237
Total Closed Block benefits and expenses	1,743	1,430	3,260	2,901
Closed Block revenues, net of Closed Block benefits and expenses, before income taxes and discontinued operations	39	(20)	32	(31)
Income tax expense (benefit)	33	(25)	21	(41)
Closed Block revenues, net of Closed Block benefits and expenses and income taxes, before discontinued operations	6	5	11	10
Income (loss) from discontinued operations, net of taxes	0	0	0	0
Closed Block revenues, net of Closed Block benefits and expenses, income taxes and discontinued operations	$ 6	$ 5	$ 11	$ 10

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, 2013	660.1	199.0	461.1	2.0
Common Stock issued	0.0	0.0	0.0	0.0
Common Stock acquired	0.0	5.9	(5.9)	0.0
Stock-based compensation programs(1)	0.0	(3.2)	3.2	0.0
Balance, June 30, 2014	660.1	201.7	458.4	2.0

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

In June 2013, Prudential Financial s Board of Directors authorized the Company to repurchase at management s discretion up to $1.0 billion of its outstanding Common Stock from July 1, 2013 through June 30

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

2014. As of June 30, 2014, 12.0 million shares of the Company s common stock were repurchased under this authorization at a total cost of $1.0 billion, of which 5.9 million shares were repurchased in the first six months of 2014 at a total cost of $500 million.

In June 2014, Prudential Financial s Board of Directors authorized the Company to repurchase at management s discretion up to $1.0 billion of its outstanding Common Stock from July 1, 2014 through June 30, 2015. The timing and amount of share repurchases are determined by management based upon market conditions and other considerations, and repurchases may be effected in the open market, through derivative, accelerated repurchase and other negotiated transactions and through prearranged trading plans complying with Rule 10b5-1(c) under the Securities Exchange Act of 1934 (the Exchange Act). Numerous factors could affect the timing and amount of any future repurchases under the share repurchase authorization, including increased capital needs of the Company due to changes in regulatory capital requirements, opportunities for growth and acquisitions, and the effect of adverse market conditions on the segments.

Accumulated Other Comprehensive Income (Loss)

The balance of and changes in each component of Accumulated other comprehensive income (loss) attributable to Prudential Financial, Inc. for the six months ended June 30, 2014 and 2013 are as follows:

	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, 2013	$ (113)	$ 10,344	$ (1,550)	$ 8,681
Change in other comprehensive income before reclassifications	241	7,175	(3)	7,413
Amounts reclassified from AOCI	(2)	(856)	46	(812)
Income tax benefit (expense)	(47)	(2,142)	(16)	(2,205)
Balance, June 30, 2014	$ 79	$ 14,521	$ (1,523)	$ 13,077

	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	Total Accumulated Other Comprehensive

			Benefit (Cost)	Income (Loss)
		(in millions)		
Balance, December 31, 2012	$ 928	$ 11,402	$ (2,116)	$ 10,214
Change in other comprehensive income before reclassifications	(1,416)	(628)	30	(2,014)
Amounts reclassified from AOCI	0	(524)	63	(461)
Income tax benefit (expense)	401	342	(33)	710
Balance, June 30, 2013	$ (87)	$ 10,592	$ (2,056)	$ 8,449

(1) Includes cash flow hedges of $(533) million and $(446) million as of June 30, 2014 and December 31, 2013, respectively, and $(98) million and $(257) million as of June 30, 2013 and December 31, 2012, respectively.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Reclassifications out of Accumulated Other Comprehensive Income (Loss)

	Three Months Ended June 30,		Six Months Ended June 30,		Affected line item in Consolidated Statement of Operations
	2014	2013	2014	2013	
	(in millions)				
Amounts reclassified from AOCI(1)(2):					
Foreign currency translation adjustment:					
Foreign currency translation adjustments	$ 1	$ 1	$ 2	$ 0	Realized investment gains (losses), net
Total foreign currency translation adjustment	1	1	2	0	
Net unrealized investment gains (losses):					
Cash flow hedges Interest Rate	(6)	(8)	(12)	(12)	(3)
Cash flow hedges Currency/Interest rate	(6)	(26)	(10)	(44)	(3)
Net unrealized investment gains (losses) on available-for-sale securities	536	384	878	514	
Net unrealized investment gains (losses) all other	0	0	0	66	
Total net unrealized investment gains (losses)	524	350	856	524	(4)
Amortization of defined benefit pension items:					
Prior service cost	5	5	11	11	(5)
Actuarial gain (loss)	(29)	(37)	(57)	(74)	(5)
Total amortization of defined benefit pension items	(24)	(32)	(46)	(63)	
Total reclassifications for the period	$ 501	$ 319	$ 812	$ 461	

(1) All amounts are shown before tax.
(2) Positive amounts indicate gains/benefits reclassified out of AOCI. Negative amounts indicate losses/costs reclassified out of AOCI.
(3) See Note 14 for additional information on cash flow hedges.
(4) See table below for additional information on unrealized investment gains (losses), including the impact on deferred policy acquisition and other costs, future policy benefits and policyholders dividends.
(5) See Note 10 for information on employee benefit plans.

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

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 Company s Unaudited Interim Consolidated Statements of Financial Position as a component of AOCI. Changes in these amounts include reclassification adjustments to exclude from Other comprehensive income (loss) those items that are included 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 Value of Business Acquired	Future Policy Benefits and Policyholders Account Balances	Policyholders Dividends	Deferred Income Tax (Liability) Benefit	Accumulated Other Comprehensive Income (Loss) Related To Net Unrealized Investment Gains (Losses)
			(in millions)			
Balance, December 31, 2013	$ 110	$ (5)	$ 4	$ 64	$ (60)	$ 113
Net investment gains (losses) on investments arising during the period	134				(47)	87
Reclassification adjustment for (gains) losses included in net income	41				(14)	27
Reclassification adjustment for OTTI losses excluded from net income(1)	(1)				0	(1)
Impact of net unrealized investment (gains) losses on deferred policy acquisition costs, deferred sales inducements and value of business acquired		(1)			0	(1)
Impact of net unrealized investment (gains) losses on future policy benefits and policyholders account balances			(3)		1	(2)
Impact of net unrealized investment (gains) losses on				(97)	34	(63)

policyholders dividends						
Balance, June 30, 2014	$ 284	$ (6)	$ 1	$ (33)	$ (86)	$ 160

(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 Cost, Deferred Sales Inducements, and Value of Business Acquired	Future Policy Benefits and Policyholders Account Balances	Policyholders Dividends	Deferred Income Tax (Liability) Benefit	Accumulated Other Comprehensive Income (Loss) Related To Net Unrealized Investment Gains (Losses)
	(in millions)					
Balance, December 31, 2013	$ 20,494	$ (719)	$ (679)	$ (3,694)	$ (5,171)	$ 10,231
Net investment gains (losses) on investments arising during the period	9,320				(3,194)	6,126
Reclassification adjustment for (gains) losses included in net income	(897)				314	(583)
Reclassification adjustment for OTTI losses excluded from net income(2)	1				0	1
Impact of net unrealized investment (gains) losses on deferred policy acquisition costs, deferred sales inducements and value of business acquired		(398)			139	(259)
Impact of net unrealized investment (gains) losses on future policy benefits and policyholders account balances			(554)		195	(359)
Impact of net unrealized investment (gains) losses on policyholders dividends				(1,222)	426	(796)
Balance, June 30, 2014	$ 28,918	$ (1,117)	$ (1,233)	$ (4,916)	$ (7,291)	$ 14,361

(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.

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

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PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

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.

Common Stock

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

	Three Months Ended June 30,					
	2014			2013		
	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 Financial Services Businesses	$ 1,068			$ (492)		
Direct equity adjustment	(3)			1		
Less: Income (loss) attributable to noncontrolling interests	23			27		
Less: Dividends and undistributed earnings allocated to participating unvested share-based payment awards	10			2		
Income (loss) from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment	$ 1,032	459.4	$ 2.25	$ (520)	464.1	$ (1.12)
Effect of dilutive securities and compensation programs(1)						
Add: Dividends and undistributed earnings allocated to participating unvested share-based payment awards Basic	$ 10			$ 2		
Less: Dividends and undistributed earnings allocated to participating unvested share-based payment awards Diluted	10			2		
Stock options		3.0			0.0	
Deferred and long-term compensation programs		0.7			0.0	
Exchangeable Surplus Notes	5	5.4		0	0.0	
Diluted earnings per share(1)						
Income (loss) from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment	$ 1,037	468.5	$ 2.21	$ (520)	464.1	$ (1.12)

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	Six Months Ended June 30,					
	2014			2013		
	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 Financial Services Businesses	$ 2,300			$ (1,193)		
Direct equity adjustment	(5)			5		
Less: Income (loss) attributable to noncontrolling interests	34			62		
Less: Dividends and undistributed earnings allocated to participating unvested share-based payment awards	21			4		
Income (loss) from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment	$ 2,240	460.1	$ 4.87	$ (1,254)	464.2	$ (2.70)
Effect of dilutive securities and compensation programs(1)						
Add: Dividends and undistributed earnings allocated to participating unvested share-based payment awards Basic	$ 21			$ 4		
Less: Dividends and undistributed earnings allocated to participating unvested share-based payment awards Diluted	21			4		
Stock options		3.1			0.0	
Deferred and long-term compensation programs		0.8			0.0	
Exchangeable Surplus Notes	9	5.4		0	0.0	
Diluted earnings per share(1)						
Income (loss) from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment	$ 2,249	469.4	$ 4.79	$ (1,254)	464.2	$ (2.70)

(1) For the three and six months ended June 30, 2013, weighted average shares for basic earnings per share is also used for calculating diluted earnings per share because dilutive shares and dilutive earnings per share are not applicable when a loss from continuing operations is reported. As a result of the loss from continuing operations available to holders of Common Stock after direct equity adjustment for the three and six months ended June 30, 2013, all potential stock options and compensation programs were considered antidilutive.

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 are allocated between Common Stock and the participating awards, as if the awards were a second class of stock. During periods of income from continuing operations available to holders of Common Stock after direct equity adjustment, the calculation of earnings per share excludes the income attributable to participating securities in the numerator and the dilutive impact of these securities from the denominator. In the event of loss from continuing operations

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

available to holders of Common Stock after direct equity adjustment, undistributed earnings are not allocated to participating securities and the denominator excludes the dilutive impact of these securities as they do not share in the losses of the Company. For the three and six months ended June 30, 2013, undistributed earnings were not allocated to participating unvested share-based payment awards as these awards do not participate in losses. Undistributed earnings allocated to participating unvested share-based payment awards for the three and six months ended June 30, 2014 were based on 4.3 million and 4.3 million of such awards, respectively, weighted for the period they were outstanding.

Stock options and shares related to deferred and long-term compensation programs that are considered antidilutive are excluded from the computation of dilutive earnings per share. Stock options are considered antidilutive based on application of the treasury stock method or in the event of loss from continuing operations available to holders of Common Stock after direct equity adjustment. Shares related to deferred and long-term compensation programs are considered antidilutive in the event of loss from continuing operations available to holders of Common Stock after direct equity adjustment. For the three and six months ended June 30, 2014 and 2013, the number of stock options and shares related to deferred and long-term compensation programs that were considered antidilutive and were excluded from the computation of diluted earnings per share, weighted for the portion of the period they were outstanding, are as follows:

	Three Months Ended June 30,			
	2014		2013	
	Shares	Exercise Price Per Share	Shares	Exercise Price Per Share
	(in millions, except per share amounts, based on weighted average)			
Antidilutive stock options based on application of the treasury stock method	2.3	$ 89.48	9.1	$ 72.64
Antidilutive stock options due to loss from continuing operations available to holders of Common Stock after direct equity adjustment	0.0		11.3	
Antidilutive shares due to loss from continuing operations available to holders of Common Stock after direct equity adjustment	0.0		5.2	
Total antidilutive stock options and shares	2.3		25.6	

	Six Months Ended June 30,			
	2014		2013	
	Shares	Exercise Price Per Share	Shares	Exercise Price Per Share
	(in millions, except per share amounts, based on weighted average)			
Antidilutive stock options based on application of the treasury stock method	2.1	$ 89.88	11.2	$ 70.73
Antidilutive stock options due to loss from continuing operations available to holders of Common Stock after direct equity adjustment	0.0		9.2	
Antidilutive shares due to loss from continuing operations available to holders of Common Stock after direct equity adjustment	0.0		5.2	
Total antidilutive stock options and shares	2.1		25.6	

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 initial

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exchange rate for the surplus notes was 10.1235 shares of Common Stock per each $1,000 principal amount of surplus notes, which represents an initial exchange price per share of Common Stock of $98.78; however, the exchange rate is subject to customary anti-dilution adjustments. 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, are added to the denominator, and interest expense, net of tax, is added to the numerator, if the overall effect is dilutive.

Prudential Financial may, at its option, at any time, subject to a notification period, exchange all outstanding shares of Class B Stock into such number of shares of Common Stock as have an aggregate average market value equal to 120% of the appraised fair market value of the outstanding shares of Class B Stock. Holders of Class B Stock will be permitted to convert their shares of Class B Stock into such number of shares of Common Stock as have an aggregate average market value equal to 100% of the appraised fair market value of the outstanding shares of Class B Stock in the holder s sole discretion, beginning on January 1, 2016, or earlier upon certain specified events. Any conversion may have a dilutive effect on holders of Common Stock.

Class B Stock

Income from continuing operations per share of Class B Stock for the three and six months ended June 30 are presented below. There are no potentially dilutive shares associated with the Class B Stock.

	Three Months Ended June 30,					
	2014			2013		
	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	$ 41			$ 3		
Less: Direct equity adjustment	(3)			1		
Income (loss) from continuing operations attributable to the Closed Block Business available to holders of Class B Stock after direct equity adjustment	$ 44	2.0	$ 22.00	$ 2	2.0	$ 1.00

	Six Months Ended June 30,					
	2014			2013		
	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	$ 54			$ 18		
Less: Direct equity adjustment	(5)			5		
Income (loss) from continuing operations attributable to the Closed Block Business available to holders of Class B Stock after direct equity adjustment	$ 59	2.0	$ 29.50	$ 13	2.0	$ 6.50

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9. SHORT-TERM AND LONG-TERM DEBT

Short-term Debt

The table below presents the Company s short-term debt as of the dates indicated:

	June 30, 2014	December 31, 2013
	(in millions)	
Commercial paper:		
Prudential Financial	$ 268	$ 190
Prudential Funding, LLC	710	460
Subtotal commercial paper	978	650
Other notes payable	326	0
Current portion of long-term debt(1)	2,500	2,019
Total short-term debt(2)	$ 3,804	$ 2,669
Supplemental short-term debt information:		
Portion of commercial paper borrowings due overnight	$ 357	$ 466
Daily average commercial paper outstanding	$ 1,366	$ 1,309
Weighted average maturity of outstanding commercial paper, in days	35	18
Weighted average interest rate on outstanding short-term debt(3)	0.23%	0.17%

(1) Includes limited and non-recourse borrowings of Prudential Holdings, LLC attributable to the Closed Block Business of $75 million at both June 30, 2014 and December 31, 2013.
(2) Includes Prudential Financial debt of $2,589 million and $1,721 million at June 30, 2014 and December 31, 2013, respectively.
(3) Excludes the current portion of long-term debt.

Commercial Paper

Prudential Financial has a commercial paper program with an authorized capacity of $3.0 billion. Prudential Financial s commercial paper borrowings have generally been used to fund the working capital needs of Prudential Financial s subsidiaries and provide short-term liquidity at Prudential Financial.

Prudential Funding, LLC (Prudential Funding), a wholly-owned subsidiary of Prudential Insurance, has a commercial paper program with an authorized capacity of $7.0 billion. Prudential Funding commercial paper borrowings generally have served as an additional source of financing to meet the working capital needs of Prudential Insurance and its subsidiaries. Prudential Funding also lends to other subsidiaries of Prudential Financial up to limits agreed with the New Jersey Department of Banking and Insurance (NJDOBI). Prudential Funding maintains a support agreement with Prudential Insurance whereby Prudential Insurance has agreed to maintain Prudential Funding s tangible net worth at a positive level. Additionally, Prudential Financial has issued a subordinated guarantee covering Prudential Funding s $7.0 billion commercial paper program.

Federal Home Loan Bank of New York

Prudential Insurance is a member of the Federal Home Loan Bank of New York (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. Under applicable law, the funding agreements issued to the FHLBNY have priority claim status above debt holders of Prudential Insurance. 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

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

borrowings. 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 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 of up to 5% of its prior year-end statutory net admitted assets, excluding separate account assets. Based on Prudential Insurance s statutory net admitted assets as of December 31, 2013, the 5% limitation equates to a maximum amount of pledged assets of $8.6 billion and an estimated maximum borrowing capacity (after taking into account required collateralization levels) of approximately $7.2 billion. Nevertheless, FHLBNY borrowings are subject to the FHLBNY s discretion and to the availability of qualifying assets at Prudential Insurance.

As of June 30, 2014, Prudential Insurance had pledged assets with a fair value of $2.7 billion supporting aggregate outstanding collateralized advances and collateralized funding agreements of $2.2 billion. As of June 30, 2014, an outstanding advance of $0.3 billion is in Long-term debt and matures in December 2015 and outstanding funding agreements, totaling $1.9 billion are included in Policyholders account balances. The fair value of qualifying assets that were available to Prudential Insurance but not pledged amounted to $4.1 billion as of June 30, 2014.

Federal Home Loan Bank of Boston

Prudential Retirement Insurance and Annuity Company (PRIAC) is a member of the Federal Home Loan Bank of Boston (FHLBB). 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 June 30, 2014, PRIAC had no advances outstanding under the FHLBB facility.

Under Connecticut state insurance law, without the prior consent of the Connecticut Insurance Department, the amount of assets insurers may pledge to secure debt obligations is limited to the lesser of 5% of prior-year statutory admitted assets or 25% of prior-year statutory surplus, resulting in a maximum borrowing capacity for PRIAC under the FHLBB facility of approximately $0.2 billion.

Credit Facilities

The Company s syndicated, unsecured committed credit facilities at June 30, 2014 are as follows:

Borrower	Original Term	Expiration Date	Capacity	Outstanding
			(in millions)	
Prudential Financial	5-year	Nov-2018	$ 2,000	$ 0
Prudential Financial and Prudential Funding	3-year	Nov-2016	1,750	0
			$ 3,750	$ 0

The above credit facilities may be used for general corporate purposes, including as backup liquidity for the Company s commercial paper programs discussed above. As of June 30, 2014, there were no outstanding

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borrowings under either credit facility. Prudential Financial expects that it may borrow under the five-year credit facility from time to time to fund its working capital needs and those of its subsidiaries. In addition, up to $300 million of the five-year facility may be drawn in the form of standby letters of credit that can be used to meet the Company s operating needs.

The credit facilities contain representations and warranties, covenants and events of default that are customary for facilities of this type; however, borrowings under the facilities are not contingent on the Company s credit ratings nor subject to material adverse change clauses. Borrowings under the credit facilities are conditioned on the continued satisfaction of other customary conditions, including the maintenance at all times of consolidated net worth, relating to the Company s Financial Services Businesses only, of at least $18,985 million, which for this purpose is calculated as U.S. GAAP equity, excluding AOCI and excluding equity of noncontrolling interests. As of June 30, 2014, the consolidated net worth of the Company s Financial Services Businesses exceeded the minimum amount required to borrow under the credit facilities.

Put Option Agreement for Senior Debt Issuance

In November 2013, Prudential Financial entered into a ten-year put option agreement with a Delaware trust upon the completion of the sale of $1.5 billion of trust securities by that Delaware trust in a Rule 144A private placement. The trust invested the proceeds from the sale of the trust securities in a portfolio of principal and interest strips of U.S. Treasury securities. The put option agreement provides Prudential Financial the right to sell to the trust at any time up to $1.5 billion of 4.419% senior notes due November 2023 and receive in exchange a corresponding amount of the principal and interest strips of the U.S. Treasury securities held by the trust. In return, the Company agreed to pay a semi-annual put premium to the trust at a rate of 1.777% per annum applied to the unexercised portion of the put option. The put option agreement with the trust provides Prudential Financial with a source of liquid assets.

The put option described above will be exercised automatically in full upon the Company s failure to make certain payments to the trust, such as paying the put option premium or reimbursing the trust for its expenses, if the Company s failure to pay is not cured within 30 days, and upon an event involving its bankruptcy. The Company is also required to exercise the put option if its consolidated stockholders equity, calculated in accordance with GAAP but excluding AOCI, falls below $7 billion, subject to adjustment in certain cases. The Company has a one-time right to unwind a prior voluntary exercise of the put option by repurchasing all of the senior notes then held by the trust in exchange for principal and interest strips of U.S. Treasury securities. Finally, any of the 4.419% senior notes that Prudential Financial issues may be redeemed prior to their maturity at par or, if greater, a make-whole price, following a voluntary exercise in full of the put option.

Long-term Debt

Surplus Notes

From 2011 through 2013, a captive reinsurance subsidiary of Prudential Insurance entered into agreements providing for the issuance and sale of up to $2.0 billion of ten-year fixed-rate surplus notes for the purpose of financing non-economic reserves under a regulation entitled Valuation of Life Insurance Policies Model Regulation, commonly known as Regulation XXX. Under these agreements, the captive receives in exchange for the surplus notes one or more credit-linked notes issued by a special-purpose subsidiary of the Company in an aggregate principal amount equal to the surplus notes issued. At June 30, 2014, $1,750 million of surplus notes were outstanding under these agreements, an increase of $250 million from December 31, 2013.

In December 2013, another captive reinsurance subsidiary entered into a twenty-year financing facility with external counterparties providing for the issuance and sale of a surplus note in an aggregate principal amount of

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

up to $2.0 billion in order to finance non-economic reserves under a supporting guideline entitled The Application of the Valuation of Life Insurance Policies Model Regulation, commonly known as Guideline AXXX. In June 2014, the facility was amended to increase the current financing capacity available under the facility from $2.0 billion to $3.5 billion, increase the maximum potential size of the facility to $4.0 billion and add additional external counterparties. Similar to the agreements described above, the captive receives in exchange for the surplus note one or more credit linked notes issued by a special-purpose affiliate in an aggregate principal amount equal to the surplus note. As of June 30, 2014, an aggregate of $1,838 million of surplus notes were outstanding under the facility, an increase of $938 million from December 31, 2013.

Under each of the above transactions for the captive reinsurance subsidiaries, because valid rights of set-off exist, interest and principal payments on the surplus notes and the credit-linked notes issued are settled on a net basis, and the surplus notes are reflected in the Company s total consolidated borrowings on a net basis.

Senior Notes

Medium-term notes. Prudential Financial maintains a medium-term notes program under its shelf registration statement with an authorized issuance capacity of $20 billion. As of June 30, 2014, the outstanding amount of medium-term notes issued under this program was $13.4 billion, an increase of $0.7 billion from December 31, 2013, due to $1.2 billion of issuances, as presented in the following table, offset by maturities of $0.5 billion.

Issue Date	Principal Amount (in millions)	Interest Rate	Maturity Date
May 15, 2014	$ 500	4.600%	May 15, 2044
May 15, 2014	$ 700	3.500%	May 15, 2024

10. EMPLOYEE BENEFIT PLANS

Pension and Other Postretirement Plans

The Company has funded and non-funded 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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Net periodic (benefit) cost included in General and administrative expenses includes the following components:

	Three Months Ended June 30,			
	Pension Benefits		Other Postretirement Benefits	
	2014	2013	2014	2013
	(in millions)			
Components of net periodic (benefit) cost				
Service cost	$ 59	$ 62	$ 4	$ 4
Interest cost	121	109	24	22
Expected return on plan assets	(179)	(192)	(29)	(21)
Amortization of prior service cost	(2)	(2)	(3)	(3)
Amortization of actuarial (gain) loss, net	22	23	7	14
Settlements	1	0	0	0
Special termination benefits	0	0	0	0
Net periodic (benefit) cost	$ 22	$ 0	$ 3	$ 16

	Six Months Ended June 30,			
	Pension Benefits		Other Postretirement Benefits	
	2014	2013	2014	2013
	(in millions)			
Service cost	$ 118	$ 127	$ 8	$ 8
Interest cost	241	219	48	44
Expected return on plan assets	(356)	(384)	(58)	(42)
Amortization of prior service cost	(5)	(5)	(6)	(6)
Amortization of actuarial (gain) loss, net	43	46	14	28
Settlements	2	0	0	0
Special termination benefits	0	2	0	0
Net periodic (benefit) cost	$ 43	$ 5	$ 6	$ 32

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 six reportable segments. 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 (loss) 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

PRUDENTIAL FINANCIAL, INC.

Notes to Unaudited Interim Consolidated Financial Statements (Continued)

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 (loss) 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, including businesses that have been placed in wind down status, 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.

Realized investment gains (losses), net, and related charges and adjustments

Realized investment gains (losses), net

Adjusted operating income excludes Realized investment gains (losses), net, except for certain items described below. Significant activity excluded from adjusted operating income includes impairments and credit-related gains and losses from sales of securities, the timing of which depends largely on market credit cycles and can vary considerably across periods, and interest rate-related gains and losses from sales of securities, which are largely subject to the Company s discretion and influenced by market opportunities, as well as the Company s tax and capital profile. Additionally, certain gains and losses pertaining to derivative contracts that do not qualify for hedge accounting treatment are also excluded from adjusted operating income. Trends in the underlying profitability of the Company s businesses can be more clearly identified without the fluctuating effects of these transactions.

The following table sets forth the significant components of "Realized investment gains (losses), net" that are included in adjusted operating income and, as a result, are reflected as adjustments to "Realized investment gains (losses), net" for purposes of calculating adjusted operating income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in millions)			
Net gains (losses) from:(1)				
Terminated hedges of foreign currency earnings	$ 66	$ 67	$ 144	$ 103
Current period yield adjustments	$ 122	$ 103	$ 246	$ 205
Principal source of earnings	$ 13	$ 43	$ 27	$ 69

(1) In addition to the items in the table above, "Realized investment gains (losses), net, and related charges and adjustments" also includes an adjustment to reflect "Realized investment gains (losses), net" related to divested businesses as results of "Divested businesses", discussed below.

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Notes to Unaudited Interim Consolidated Financial Statements (Continued)

Terminated Hedges of Foreign Currency Earnings. The amounts shown in the table above primarily reflect the impact of an intercompany arrangement between Corporate and Other operations and the International Insurance segment, pursuant to which the 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 unfavorable rate changes will reduce the segment s U.S. dollar equivalent earnings. Pursuant to this program, the Company s Corporate and Other operations may 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, so the resulting profits or losses are recorded 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.

Current Period Yield Adjustments. 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 derivative contracts that do not qualify for hedge accounting treatment, the periodic swap settlements, as well as certain other derivative related yield adjustments are recorded in Realized investment gains (losses), net , and 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 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. Included in the amounts shown in the table above are gains on certain derivatives contracts that were terminated or offset before their final maturity of $34 million and $18 million for the three months ended June 30, 2014 and 2013, respectively, and $52 million and $36 million for the six months ended June 30, 2014 and 2013, respectively. Additionally, as of June 30, 2014, there was a $362 million deferred net gain related to certain derivative contracts that were terminated or offset before their final maturity, primarily in the International Insurance segment.

Principal Source of Earnings. The Company conducts certain activities for which realized investment gains and losses 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 strategic investing business 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 and losses associated with the sale of these strategic 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 and losses 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.

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Other items reflected as adjustments to Realized investment gains (losses), net

The following table sets forth certain other items excluded from adjusted operating income and reflected as an adjustment to Realized investment gains (losses), net for purposes of calculating adjusted operating income:

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
	(in millions)			
Net gains (losses) from:				
Other trading account assets	$ 11	$ 36	$ 33	$ 85
Foreign currency exchange movements	$ (231)	$ (1,560)	$ 0	$ (4,025)
Other activities	$ 9	$ 1	$ 13	$ 112

Other Trading Account Assets. 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 Other 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 are excluded from adjusted operating income.

Foreign Currency Exchange Movements. The Company has certain assets and liabilities for which, under U.S. GAAP, the changes in value, including those associated with changes in foreign currency exchange rates during the period, are recorded in Other income. To the extent the foreign currency exposure on these assets and liabilities is economically hedged or considered part of the Company s capital funding strategies for its international subsidiaries, the change in value included in Other income is excluded from adjusted operating income. The amounts in the table above are largely driven by non-yen denominated insurance liabilities in the Company s Japanese insurance operations. The insurance liabilities are supported by investments denominated in corresponding currencies, including a significant portion designated as available-for-sale. While these non-yen denominated assets and liabilities are economically hedged, unrealized gains and losses on available-for-sale investments, including those arising from foreign currency exchange rate movements, are recorded in Accumulated other comprehensive income (loss) under U.S. GAAP, while the non-yen denominated liabilities are re-measured for foreign currency exchange rate movements, and the related change in value is recorded in earnings within Other income. Due to this non-economic volatility that is reflected in U.S. GAAP earnings, the change in value recorded within Other income is excluded from adjusted operating income.

Other Activities. The Company excludes certain other items from adjusted operating income that are consistent with similar adjustments described above. The significant items within other activities shown in the table above included the following:

In connection with disputes arising out of the Chapter 11 bankruptcy petition filed by Lehman Brothers Holdings Inc., the Company previously recorded losses related to a portion of its counterparty exposure on derivative transactions it had previously held with Lehman Brothers and its affiliates. The Company recorded estimated recoveries related to this matter of $9 million and $16 million in the three and six months ended June 30, 2014, respectively, and $117 million in the six months ended June 30, 2013. These recoveries are recorded within Other income within the Company s Corporate and Other operations. Consistent with the exclusion of credit-related losses recorded in Realized investment gains (losses), net , the impact of this estimated recovery is excluded from adjusted operating income.

The Company records valuation adjustments for non-performance risk that relates to the uncollateralized portion of certain derivative contracts between a subsidiary of the Company and third parties and liquidity risk

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associated with certain derivatives. These adjustments are recorded within Other income. Consistent with the exclusion of the mark-to-market on derivatives recorded in Realized investment gains (losses), net , the impact of these risks is excluded from adjusted operating income. The net impact of these risks was to exclude from adjusted operating income net losses of less than $1 million and net gains of $4 million for the three months ended June 30, 2014 and 2013, respectively, and net losses of $2 million and net gains of $2 million for the six months ended June 30, 2014 and 2013, respectively.

Related charges

Charges that relate to realized investment gains and losses are also excluded from adjusted operating income, and include the following:

- the portion of the amortization of deferred policy acquisition costs, value of business acquired, unearned revenue reserves and deferred sales inducements for certain products that is related to net realized investment gains and losses.

- policyholder dividends and interest credited to policyholders account balances that relate to certain life policies that pass back certain realized investment gains and losses to the policyholder, and reserves for future policy benefits for certain policies that are affected by net realized investment gains and losses.

- market value adjustments paid or received upon a contractholder s surrender of certain of the Company s annuity products as these amounts mitigate the net realized investment gains or losses incurred upon the disposition of the underlying invested assets.

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 majority of investments supporting these experience-rated products are classified as trading and are carried at fair value, with realized and unrealized gains and losses reported in Other income. To a lesser extent, these experience-rated products are also supported by derivatives and commercial mortgage and other loans. The derivatives are carried at fair value, with realized and unrealized gains and losses reported in Realized investment gains (losses), net. The commercial mortgage and other loans are carried at unpaid principal, net of unamortized discounts and an allowance for losses, with gains and losses on sales and changes in the valuation allowance for commercial mortgage and other loans reported in Realized investment gains (losses), net.

Adjusted operating income excludes net investment gains and losses on trading account assets supporting insurance liabilities, which 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. These adjustments are in addition to the exclusion from adjusted operating income of net investment gains and losses on the related derivatives and commercial mortgage and other loans through Realized investment gains (losses), net, and related charges and adjustments, as discussed above. 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.