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Committee of European Banking Supervisors
Working Group on Own Funds
Floor 18, Tower 42
25 Old Broad Street
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Dear Sirs

RESPONSE TO CEBS DRAFT PROPOSAL FOR A COMMON EU DEFINITION OF TIER 1 HYBRIDS

Prudential plc is a leading international financial services group providing retail financial services and fund management in the UK and Europe, the US and twelve Asian jurisdictions. Prudential considers hybrid capital instruments, particularly hybrid Tier 1, important long-term components of its capital structure and its financial planning. We have raised significant amounts of Tier 1 hybrid capital.

We appreciate that CEBS' efforts are focused on banking. However, the regulatory framework for banks and insurers is converging in Europe as evidenced by the development of Solvency II and the ongoing discussions between the industry and the Interim Working Committee on Financial Conglomerates, in which we have participated. We support this direction in principle and we note that in the UK, in particular, convergence has already been achieved.

In view of this, we have a vital interest in the development of the regulatory requirements for bank hybrid capital and are grateful for the opportunity to comment on CEBS' proposed technical advice to the European Commission on this issue.

We fully accept the three basic principles underlying the requirements for hybrid capital instruments: permanence, ability to absorb losses and the ability to suspend cash payments. However, the draft advice contains two specific requirements for hybrid Tier 1 capital which cause us significant concern: the requirement for principal write-down and the requirements for the Alternative Coupon Settlement Mechanism (ACSM).

In our opinion, these requirements are likely to undermine future issues by (i) affecting the tax treatment of instruments in the UK to such an extent that interest will not be treated as an allowable expense for tax purposes; and (ii) affecting the ability and willingness of investors to purchase hybrid capital instruments.

We believe it is questionable whether the suggested requirements for principal write-down and the structure of the ACSM achieve the stated objectives of improving the quality of hybrid capital, increasing the ability to absorb losses and removing obstacles to a recapitalisation of issuers in distress. In view of their negative impact on issuers and holders of hybrid capital instruments, we believe that these requirements could actually be counter-productive.

If the draft advice was implemented in its current form, an eventual harmonisation with the requirements for insurers would severely curtail our ability to issue hybrid capital instruments. Hybrid Tier 1 issues would become virtually impossible for us.

I attach a short paper setting out a more detailed explanation of our concerns and possible solutions. In general terms, given the number of involved parties in each jurisdiction, including issuers and holders of hybrid instruments, regulators and tax authorities, we think that CEBS's principles for own funds may be achieved most effectively by setting out the desired outcome in a principle which can be implemented taking into account the distinct regulatory, tax and legal framework in each jurisdiction.

We trust that this is a useful contribution to this debate and to the preparation of the impact assessment. My colleagues would be happy to discuss this further.

In view of the potential implications for insurers, I am copying this letter and our response to Sarah Varney at the FSA's Solvency II Office and to Karel van Hulle at the European Commission's Insurance and Pensions Unit.

Yours faithfully



Philip Broadley
Group Finance Director

cc Sarah Varney, FSA
Karel van Hulle, European Commission