



Merchant Navy Officers Pension Fund

Peter McEwen, Chairman

MNOFP Trustees Limited

2009 Actuarial Valuation

11 February 2010



Agenda

- 2009 Actuarial Valuation Chairman
 - Consultation process
 - Assumptions
 - Timetable

- Deficit Contribution Collection Chief Executive
 - Employer Covenant
 - Debt Recovery

Consultation Process

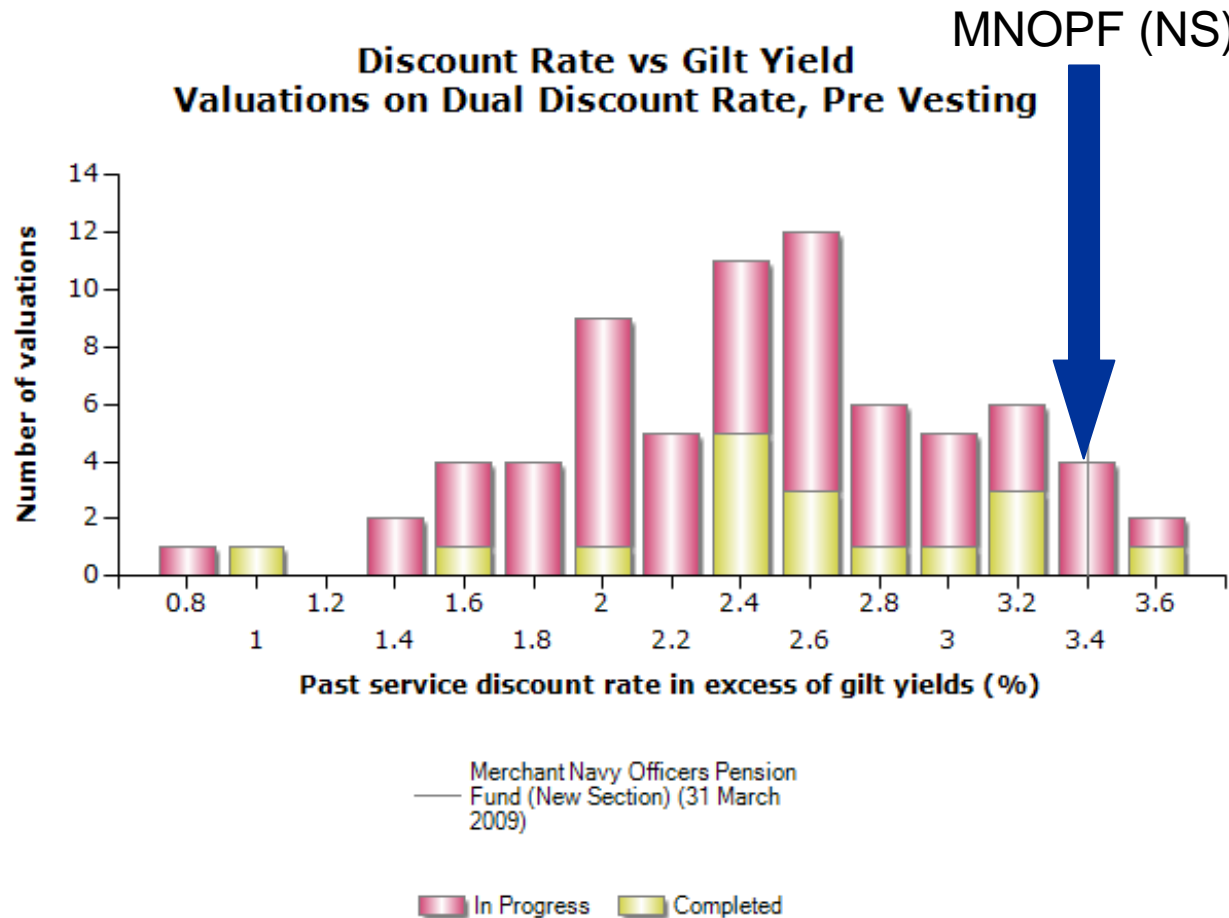
- Trustee must consult with employers on assumptions and contributions
- 30 November 2009 – Preliminary results sent to employers for consultation
- 13 January 2010 – Employers response to consultation
- 02 February 2010 – Trustee's reply sent to employers
- Decision on assumptions and contributions ultimately lies with the Trustee
- Trustee sets the required contributions having regard to Actuary's advice

Assumptions

Discount rates: Pre-Retirement

- Based on equity portfolio
- Proposed assumption 7.25% pa
 - 62% probability of being met or exceeded ('confidence level', over 15 years, based on Towers Watson asset model (TW - previously Watson Wyatt))
- Based on survey of TW valuations around 31 March 2009
 - Lower confidence level than the average of 66%
 - Range of pre-retirement discount rates in excess of 15 year gilt yield is 0.8% to 3.6%
 - MNOFP proposed of 7.25% is 3.4% above the 15 year gilt yield
 - MNOFP assumption is in the highest 5% of pre-retirement discount rates, as shown in the chart on the following slide

Discount rates: Pre-Retirement



This chart relates to 72 valuations for which a dual discount rate approach is used. It shows the difference between the past service pre-retirement discount rate used for each valuation and the annualised fixed-interest (15 year) gilt yield as at the quarter end on or prior to each valuation date. The lower section of each bar is for valuations which have been completed; the upper section represents preliminary assumptions for other valuations.

Discount rates: Post-Retirement

- Based on bond portfolio (50% gilts / 50% corporate bonds)
- Proposed assumption 4.75% pa consistent with: 4.0% pa gilt return + 5.5% pa corporate bond return
- 4.75% assumption is in line with the expected return (based on TW model over 15 years)
- Corporate bond return at 31 March 2009 includes a significant allowance for defaults and downgrades. Yields at the time were very high: included substantial illiquidity and credit risk premiums
- For non-pensioners there is a re-investment risk. 'Current' terms for bonds may not be available. No reduction to discount rate has been made for this
- Proportion of corporate bonds held in the future is likely to be less than 50%
- Regulator's survey for valuations up to late 2008 showed average post-retirement discount assumption was 0.6% pa over gilt returns – MNOPF proposed assumption is marginally higher

Mortality

- Proposed assumptions give male life expectancy from age 65 of 21.6 years
- Just under median from survey of TW valuations around 31 March 2009
- Current rates of mortality:
- The Pensions Regulator's view: regulatory requirement for prudence means "taking a margin below best estimate rates"
- Proposed assumption set equal to rates from pensioner experience in the Section over the last 3 years (930 deaths and £4.0m of annual pension extinguished) less a very small margin for prudence
- Recent mortality experience in the Fund lighter than previously, in line with general UK trend

Mortality

Allowance for future improvements in mortality:

- Extra years of male life expectancy at various ages shown in following table
- Compared with the Pensions Regulator's a 'trigger' of long cohort 'with some form of underpin' (commonly considered to be around 1% pa)

Extra years of male life expectancy				
	Age now	61	71	81
MNOPF NS 09 proposal		2.9	1.7	0.7
Regulator trigger		3.0	2.2	1.2

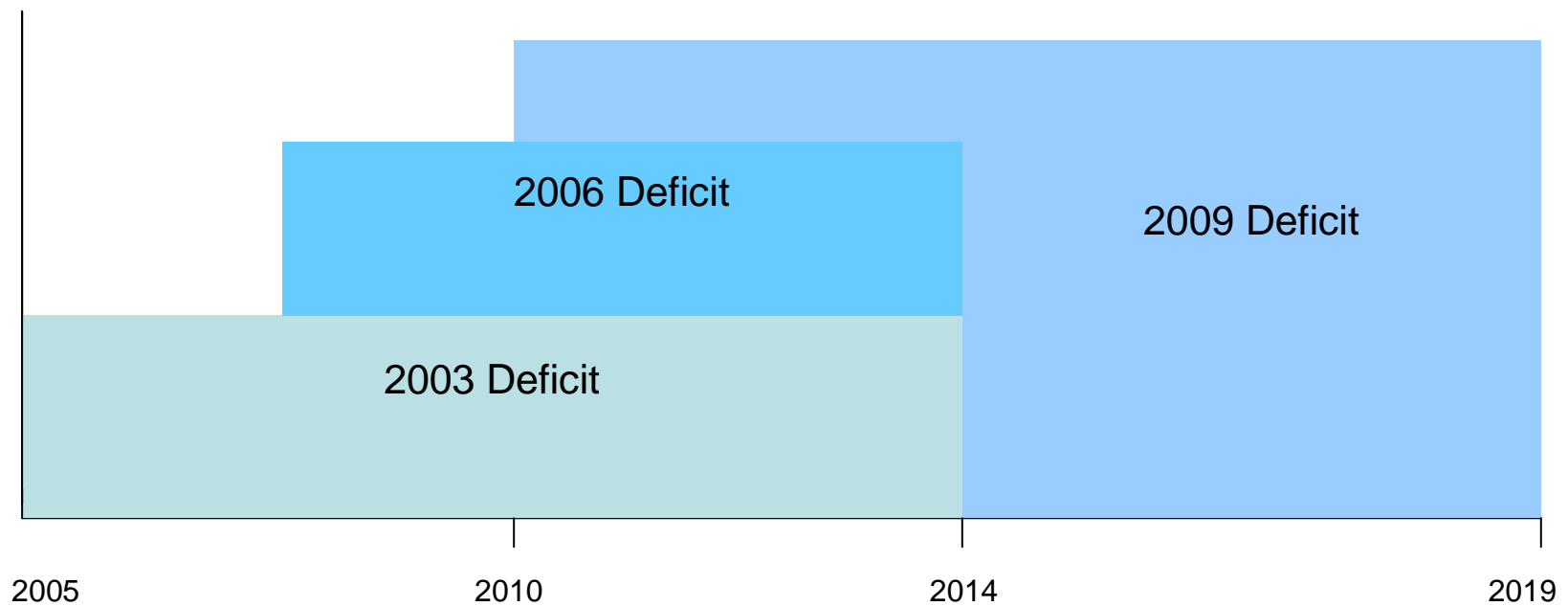
Recovery Plan

- Flexibility available in constructing the Recovery Plan
- Payment terms might vary between employers depending on creditworthiness
- 10 year period preferred
- Threshold for credit
- Cost of providing credit arrangements
- Future contribution rate
- Section 75 issues

Recovery Plan

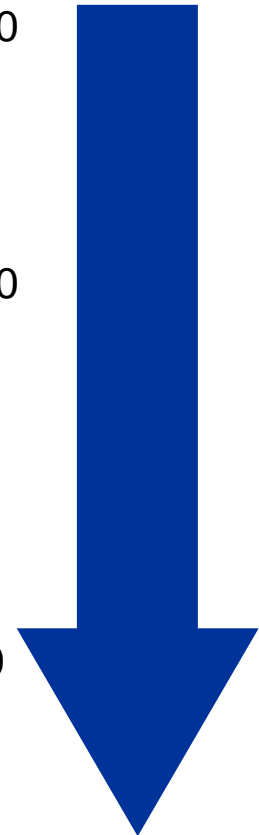
Many options including:

- Everything upfront
- Everything in Year 10 (not a prudent approach to funding the deficit)
- Possible back-end loading of instalment payments



Timetable

- Formal decisions made on Technical Provisions, Deficit, Recovery Plan and deficit contribution collection policy 26 March 2010
- Allocate deficit contributions to employers April 2010
- Communicate formal decisions to employers and set out process for giving credit April/May 2010
- Sign valuation reports, schedules of contributions etc May 2010
- Review Statement of Investment Principle July 2010
- Communicate valuation outcome to members July/Aug 2010
- Issue invoice / payment terms for deficit contributions to all New Section Employers for payment on 30 September 2010 and setting out the terms of any instalment option Thereafter





Merchant Navy Officers Pension Fund

Andrew Waring, Chief Executive

MNOFP Trustees Limited

Employer Covenant and
Credit Management
11 February 2010



The Employer Covenant Review

“An objective and independent assessment of the overall financial strength of the scheme employer(s)”

The Pensions Regulator's Guidance

“It is essential for the trustees to form an objective assessment of the employer's financial position and prospects as well as his willingness to continue to fund the scheme's benefits (the employer's covenant). This will inform decisions on both the technical provisions and any recovery plan needed.”

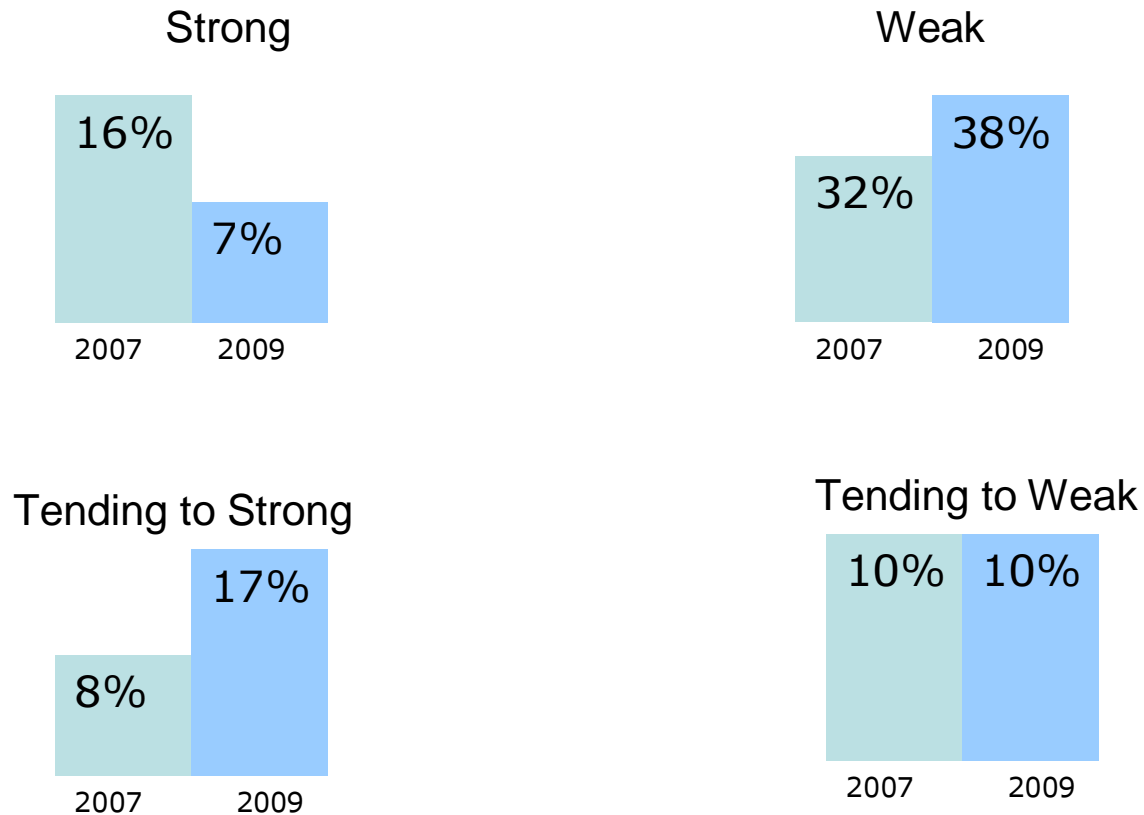
“The cornerstone of a good working relationship between trustees and the sponsoring employer is clear and open communication. As a trustee, you should put procedures in place to ensure that the employer keeps you informed about its financial position and of any plans that will change or impact upon the pension scheme.”

Assessing the covenant

How to assess the covenant of a “last man standing” scheme with c.400 participating employers?

1) Large deficit employers	2) “Strong” employers	3) Deficit coverage
Top 10 participating employers by deficit size account for c.40% of the deficit	Top 20 participating employers by net asset value have a combined NAV of over £15bn	Top 50 participating employers by deficit size account for c.70% of the deficit

Employer Covenant Comparison between 2007 and 2009

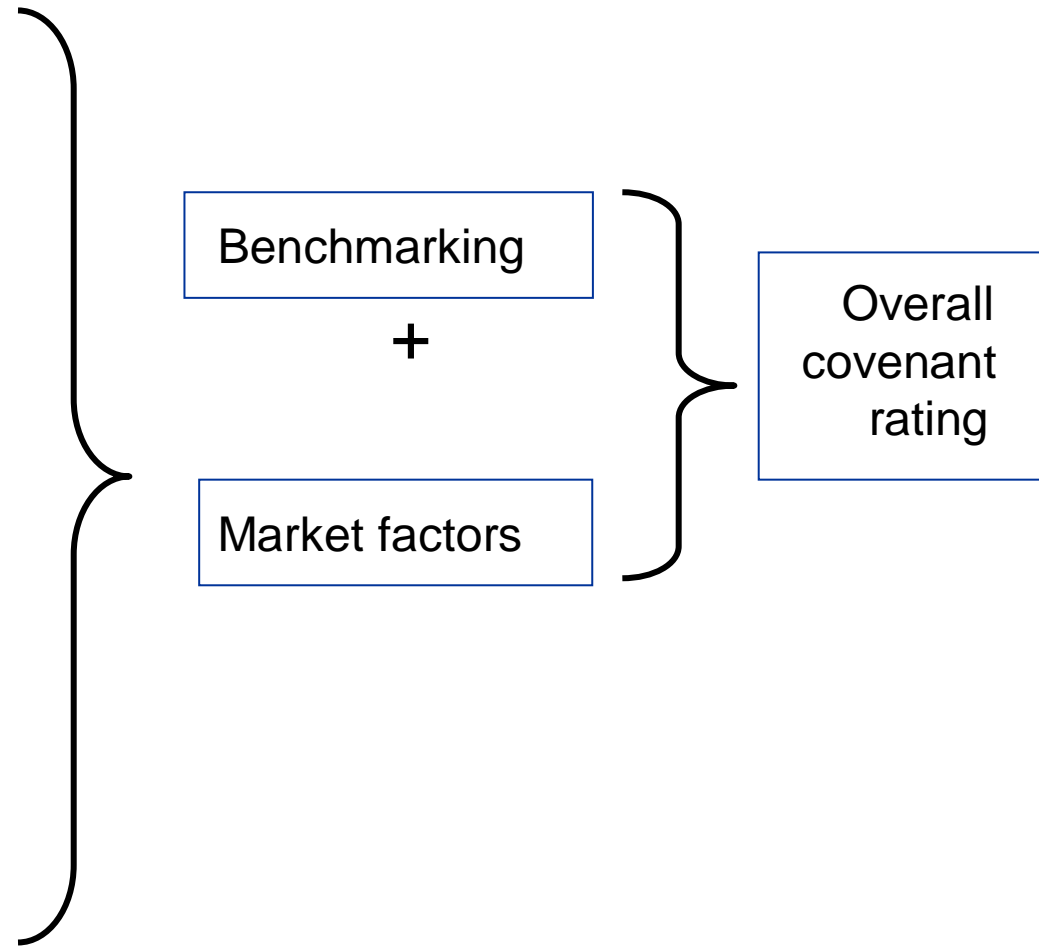


Sample covers largest 50 employers by deficit share and largest 20 employers by net asset value (with some overlap). Total deficit share covered over 70%

Assessing individual employers

Key drivers

- 1) Group structure
- 2) Pension deficit
- 3) Willingness to support
- 4) Balance sheet
- 5) P&L and cash flow
- 6) Forecasts

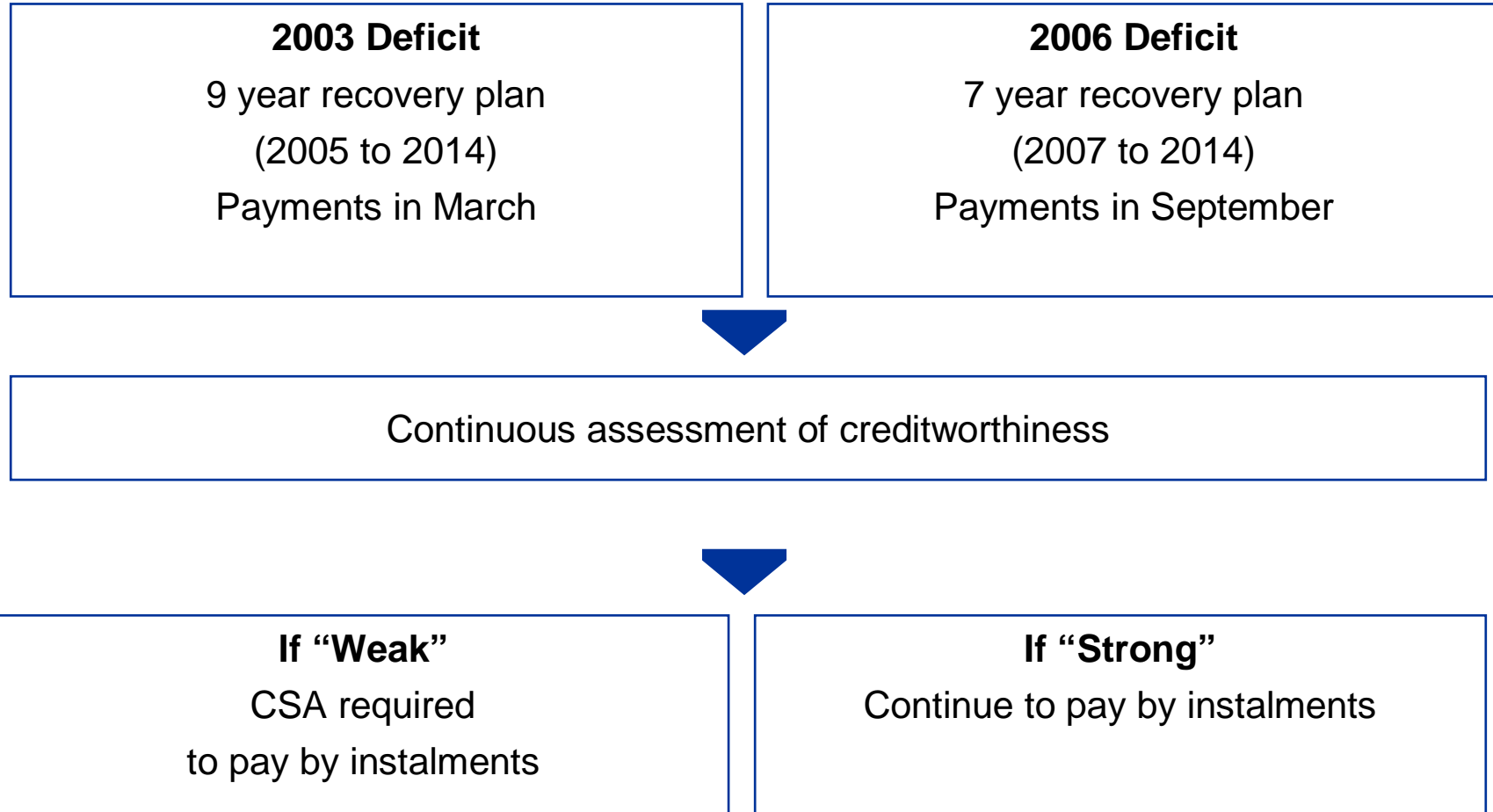


Employer covenant overview

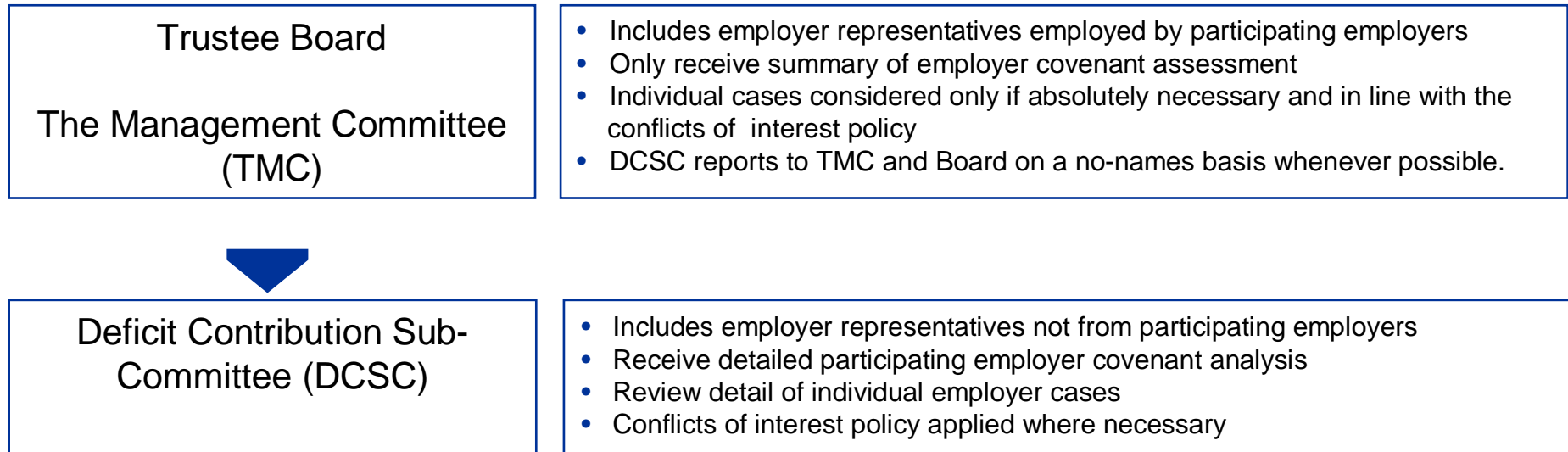
- Understanding the employer covenant is a complex exercise
- The Trustee gains comfort from the “last man standing” status of the scheme, however:
 - the covenant strength of the scheme is changing over time; and
 - the Trustee needs to ensure that all employers are treated fairly and equitably
 - the Trustee does not consider it reasonable to build the funding plan based on the last man standing
- Key to this is ensuring that the MNOFF and other employers are adequately protected against employers becoming insolvent
- If a participating employer is weak and there are deficit instalments outstanding, an appropriate credit support arrangement (“CSA”) needs to be in place
- The Trustee is prepared to listen and work with employers to ascertain what that CSA should be
- Failure to put in place a suitable CSA will result in the outstanding deficit being invoiced



Deficit collection



Maintaining confidentiality



- Professional Advisers appointed by the Trustee are obliged to maintain confidentiality
- If employers are required to disclose commercially sensitive information which is not publically available – Trustee will consider confidentiality agreement

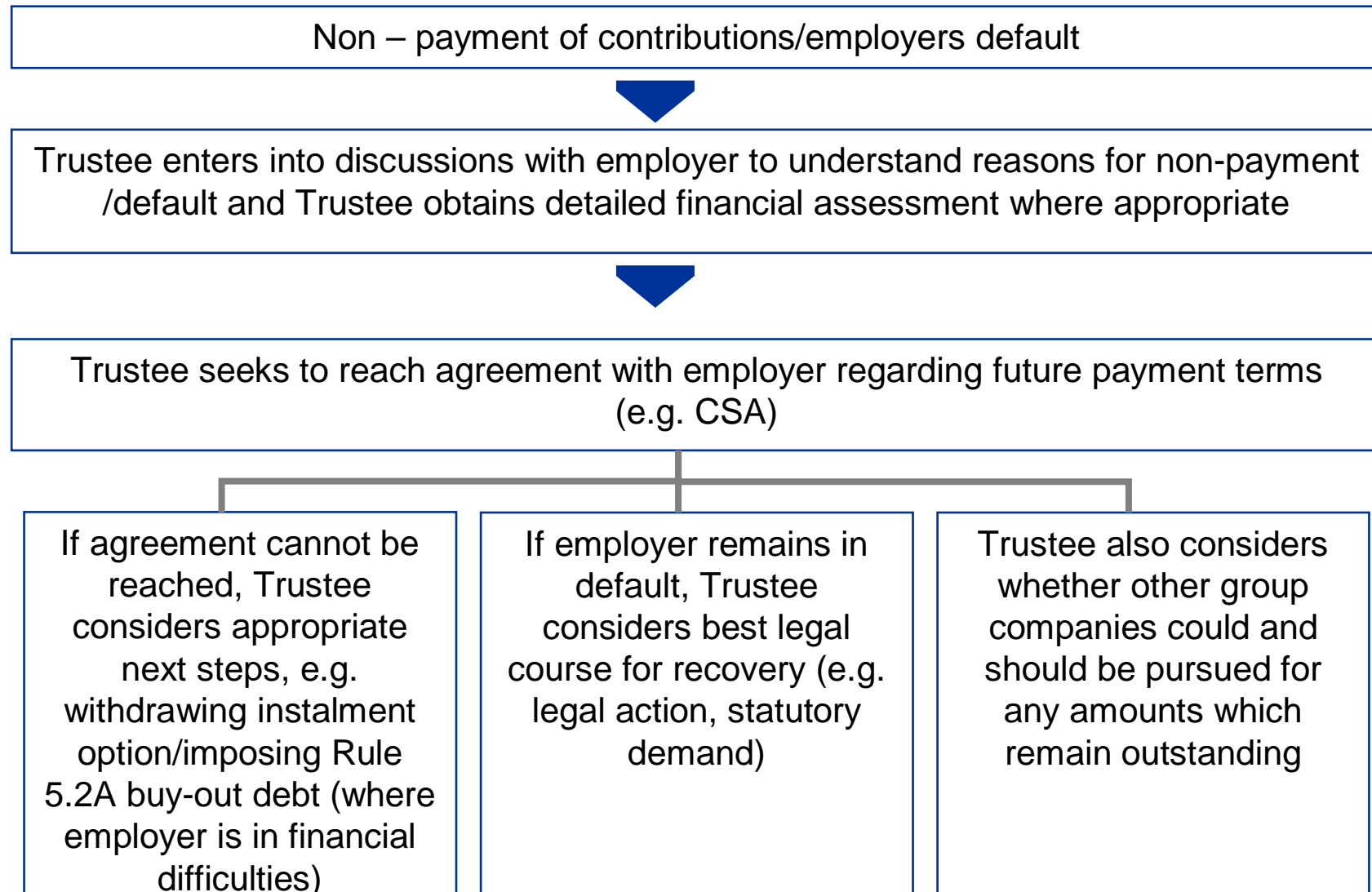
Conflicts of Interest Policy

- All Directors of the Trustee Board sign
- Agree not to disclose confidential information
- Agree not to participate in discussions or votes relating to an employer who
 - is their own employer
 - in the same corporate group
 - in an analogous position in another corporate group
- Papers and minutes withheld

Role of the DCSC

- Actuarial Valuations
 - Obtain assessments of the employer covenant and monitor in between valuations
 - Determine which debts are unrecoverable (orphan liabilities)
- Deficit Contribution Collection
 - Monitor receipt of payments due
 - Decide on action where employer defaults
- Statutory Debts
 - Consider and agree payment proposals
- Develop policies (for approval by the Board) and apply those policies in a consistent manner

DCSC: Debt Recovery Process



Why do we need to provide a CSA given that:

1. It is a last man standing scheme and the overall employer covenant is strong?

The Trustee needs to ensure all employers are treated fairly and equitably and the MNOFP does not just rely on the strong employers to support the scheme

2. We have kept up to date with our payments?

This does not provide sufficient protection for the MNOFP – some employers that have kept up to date with payments have subsequently become insolvent

3. If things go wrong, you could go to the Pensions Regulator?

The Pensions Regulator will not want the MNOFP to rely on its intervention to recover the MNOFP deficit

Taking preventative action now is better than taking time consuming and costly action later. This will be in the best interest of all employers and members.

Key messages

- The Trustee measures the employer covenant to help determine:
 - the actuarial assumptions;
 - the deficit recovery plan;
 - payment terms for individual employers; and
 - any actions the DCSC should take to protect the Scheme
- The Trustee is looking to ensure that:
 - member's benefits are protected;
 - a consistent approach is used for working with employers; and
 - all employers are treated fairly
- The Trustee will work with employers to ensure their concerns are taken into consideration and that solutions are appropriate

Important Information

- This presentation was produced to provide summary information to the participating employers of the MNOPF
- The information contained within this presentation is confidential and should not be distributed further without the prior written consent of the Trustee
- Any figures or graphs in this presentation have been produced for reference only and should not be relied upon
- No decisions should be based on the information contained in this report, and the Trustee accepts no responsibility, duty of care or liability for any decisions taken on the basis of the information contained in this report