

**QUESTIONS AND ANSWERS ON CURRENT TOPICS
AFFECTING THE MNOFP – AUGUST 2009**

(A) 2009 ACTUARIAL VALUATION

A1. Q. What will the future service contribution rate be?

A. The current contribution rate is 19.2% of pensionable salaries (members 7.3% and employers 11.9%). The rate calculated in the 2006 valuation was 24.3% but the rate was held at 19.2% by making an allowance for additional returns of 0.2% p.a. of the assets each year. To the extent that this additional return is not achieved, then the deficit resulting would be apportioned between employers with contributing members since 31 March 2006. The maximum amount in question is about £11m.

There is no information currently available on the contribution rate required in future as this will depend on the data and assumptions used in the 2009 actuarial valuation.

A2. Q. Will there be a New Section deficit?

A. The decrease in asset values combined with the increased valuation of liabilities due to more cautious mortality assumptions and lower investment return assumptions means that there will almost certainly be an additional deficit. A recent statement by the Pensions Regulator has emphasised the need for liabilities to be valued prudently. It is therefore likely that the deficit disclosed will be significant.

However, the Pensions Regulator has also indicated that there is flexibility in setting recovery plans to repair deficits. Trustees will be expected to take a realistic approach to setting and agreeing recovery plans.

A3. Q. Will there be an Old Section deficit?

A. We cannot know for certain until the actuarial calculations have been done. Although the Old Section has a relatively low risk investment strategy, return seeking assets still account for about 20% of the portfolio. The Old Section has a large allocation to bonds which have tended to reduce in value due to the large increases in credit spreads. Liabilities however will not have reduced in line with the fall in asset values.

A4. Q. Why did the Trustees grant a 4% bonus on Old Section pensions after the 2006 valuation?

A. At the time there was a surplus of about £100m on assumptions which were very cautious. Approximately £50m of that was used to

finance a 4% bonus effective 1 April 2007. It should be noted that previous bonuses in recent years have been limited to 2.5% (1 April 1998), 3% (1 April 2002) and 4% (1 January 2005). The bonus at 1 April 2007 was arrived at after consideration of the downside risk, which was considered to be sufficiently small so as not to preclude the award of the bonus. In the event, the very small risk that the £50m buffer would vanish has materialised due to the recent extraordinary economic conditions.

A5. Q. When will employers be consulted on the 31 March 2009 actuarial valuation?

A. The Trustee will receive preliminary valuation results from the actuary at in early October 2009. The timing of a consultation letter to the employers will depend on the amount of initial discussion required by the Trustees but it is expected that the consultation process will begin from late October or in November 2009. It is expected that the consultation will take place through the Chamber of Shipping although the Trustee may well also communicate directly with all employers. The consultation will take place separately in respect of the New Section and the Old Section as there will be different issues to consider in each.

The Trustee will consider the responses to the consultation in December 2009 and January 2010. At that point, the Trustee will need to be formulating its final decisions for approval by the Trustee Board in March 2010. It is therefore unlikely that there will be a second round of consultations.

(B) DEFICIT CONTRIBUTIONS

B1. Q. How will employers be informed of the Trustee's decision on deficit contributions?

A. The Trustees are likely to make formal decisions on the actuarial valuations and recovery plans during March 2010. These general decisions will be communicated to employers during April 2010. By that time it is expected that the recalculation as at 31 March 2009 of each employer's share of New Section liabilities will be complete and it is hoped that it will be possible to communicate this information to employers at the same time. Employers can then see what their additional liability for deficit contributions as a result of the 31 March 2009 valuation is likely to be. The due date of payment will be 30 September 2010 and it is likely that formal invoices will be distributed to employers in August 2010.

Prior to the distribution of invoices, the Trustee will review its Deficit Contribution Collection Policy and determine how to apply that Policy in respect of each employer. To the extent that the Trustee decides that

deficit contributions can be met by instalments, the Trustee will determine the procedure for assessing the credit worthiness of employers and obtaining security from employers if appropriate. Where the required security cannot be obtained, the full amount of deficit contributions outstanding will become payable.

B2. Q. What action is the Trustee taking to recover unpaid deficit contributions?

A. Following the 2003 actuarial valuation, deficit contributions of £234m were invoiced to employers for payment at 30 September 2005 and following the 2006 actuarial valuation, deficit contributions of £164.6m were invoiced to employers for payment at 30 September 2007. Employers whose deficit contributions amounted to over £100,000 were allowed to pay by annual instalments over the period to 2014 provided they were sufficiently creditworthy. Thus, there remains a significant portion of the deficit contributions yet to be paid in instalments over the five years to 2014.

With regard to the future instalments of deficit contributions, the Trustee continues to undertake regular financial reviews of the employers concerned and has put in place extra security where appropriate in the form of guarantees from adequately resourced parent companies or letters of credit from a bank etc.

The Trustee has taken strong action to pursue any deficit contributions that have already become due but have not been paid. Where it was clear that an employer could afford to pay, the Trustee has pursued payment, taking legal action if appropriate. In a number of cases, employers have been in liquidation and the Trustee has taken steps to obtain as large a share of the distribution of assets by the liquidator as possible. In general, whilst the preferred approach is an open constructive discussion with employers who have defaulted on payment, where this has not proved possible, statutory demands have been issued and if necessary winding up proceedings started. In a few cases, legal action through the courts has been initiated and been successful.

In 2007, the Trustee concluded that of the amount uncollected in relation to the deficit disclosed by the 2003 actuarial valuation, approximately £28m was very unlikely to be recovered and this was re-invoiced amongst the remaining employers. As a result, most of the original £234m is expected to be accounted for. With regard to the deficit disclosed by the 2006 valuation, it is expected that approximately £10m cannot be recovered and this will effectively form part of any further deficit disclosed by the 2009 actuarial valuation.

In conclusion, the Trustee has made and will continue to make all reasonable efforts to recover outstanding deficit contributions but of

course will have regard to the balance between the cost of pursuing unpaid deficit contributions and the amount that might be recovered.

B3. Q. Why do the existing employers have to meet the liabilities of employers that no longer exist?

A. The MNOPF is a multi-employer scheme for employers that are not associated in business (although there are some corporate groups with a number of participating employers who are associated) and in which the assets and liabilities are not segregated by employer.

In 2005, the Trustee obtained a ruling from the High Court which stated that all employers who had ever contributed to the MNOPF remained participating employers irrespective of whether they continued to employ active members and could be required by the Trustee to pay contributions to the scheme. Thus, all participating employers are jointly and severally responsible for the liabilities of the scheme. This applied equally to the Old Section and the New Section although in relation to the 2003 and 2006 Actuarial Valuations, the Trustee decided that the New Section deficit would be apportioned amongst New Section employers only. Of course, some New Section employers no longer exist but Rule 5.2A of the MNOPF Trust Deed and Rules gives the Trustee power to take into account in apportioning the deficit to the employers, those debts which cannot be recovered. As a result, the Trustee has decided to reapportion the unrecoverable deficit contributions amongst the remaining New Section employers.

Liabilities associated to employers that no longer exist are known as "orphan liabilities". As at 31 March 2006, approximately 17% of New Section liabilities were orphan liabilities. This percentage is likely to increase in the apportionment of the 2009 deficit and to increase further in future as, inevitably, more employers become insolvent. As time goes on, the liabilities will pass to a decreasing number of employers until, at least in principle, there is only one left and for this reason the MNOPF is known as a "last man standing" scheme.

Thus, it is in the interests of all employers to ensure that individual employers do not exit the fund so as to impose liabilities on the remaining employers.

As far as members are concerned, the joint and several obligation of employers provides a strong covenant and high level of security for their benefits. Thus, even if the employer for which they worked becomes insolvent, their full benefits become the responsibility of the remaining employers. Even if the last man standing becomes insolvent, then under current regulations, the Pension Protection Fund run by the government would apply although this might not cover full benefits for all members.

B4. Q. When does a Section 75 debt apply and how is it calculated?

A. Under Section 75 of the Pensions Act 1995, an employer becomes liable for a debt to the scheme on the occurrence of an "employment cessation event". This is defined in the legislation as meaning the cessation of employment of active members at a time at which at least one other employer continues to employ active members.

In the New Section of the MNOF, a Section 75 debt is calculated by reference to the deficiency in the New Section on a buy-out basis (i.e. the cost of purchasing annuities). The regulations require that only the employers of active members are liable for a Section 75 debt. Thus, an individual employer's Section 75 debt is calculated by reference to its share of the liabilities of active employers rather than its share of the liabilities of all employers (which would be a smaller proportion). At present, active employers account for approximately 30% of the total New Section liabilities.

A Section 75 debt is triggered as above provided at least one active employer remains. In the event that no active employer remains, the debt is not triggered immediately but is deferred until the scheme winds up.

(C) STRATEGIC REVIEW

C1. Q. What is the Old Section strategic review?

A. During 2008 the Trustee commenced a strategic review of the Old Section investigating the possibility of securing all Old Section benefits by means of a buy-in. A buy-in is the purchase of a bulk annuity held by the Trustee as an investment of the scheme. It is an insurance policy issued by an FSA authorised insurer. The purpose is to match some or all of the scheme's liabilities and therefore reduce the level of risk although it does not change the contractual liability of participating employers.

The buy-in potentially reduces the risk that members' benefits will not be paid in full. Members' benefits are protected under the MNOF by the employer covenant and ultimately the Pension Protection Fund. An insurance buy-in policy provides additional security through the Financial Services Authority and the Financial Services Compensation Scheme and may be combined with collateral arrangements that are put in place in case the insurer's financial strength reduces.

The recent economic crisis has reduced the value of Old Section assets and there are insufficient liquid assets available to purchase a buy-in policy to secure members benefits in full. However, a journey plan for securing Old Section liabilities has been developed whereby a partial buy-in using about 40% of the assets can be undertaken and the remaining assets managed in future with a view to ultimately achieving

a position whereby the remaining liabilities can be secured. Such a proposed partial buy-in would cover a significant portion of the pensioner liabilities.

The Trustee is currently working towards selecting an insurer which meets the key requirements of ensuring a high degree of security to protect members benefits and a premium for the policy which fits the expectations of the journey plan. A final decision will then be taken as to whether to proceed.

C2. Q. Why have the Trustees not secured Old Section benefits in the past when the actuarial valuations disclosed surpluses?

A. The Old Section was set up on the basis that members paid contributions based on an age related table of rates calculated at a relatively low rate of interest. Members effectively bought deferred pensions payable from normal pension age to which bonuses would be added if investment returns were sufficiently in excess of the interest rates inherent in the contribution tables. Thus, distribution of surpluses in the form of bonuses has always had to be a prime consideration of the Trustees in their governance of the Old Section.

As the Old Section has matured, the question of removing risk and ultimately securing members' benefits has increased in importance. The question of settling members' benefits by the purchase of annuities was first considered in 2001. At that time the market for pension fund annuities was very limited. Investigations indicated that although it might be possible to secure members' guaranteed benefits, there would be little, if any, surplus to enhance benefits and there were significant and, at that time, insoluble issues regarding settling the benefits of members with whom contact had been lost where it was not known whether a liability continued to exist. The Trustees took the decision that it was in members' interests to continue running the Old Section with some return seeking assets in order to generate future surpluses out of which bonuses could be paid.

Following the actuarial valuations in 2003 and 2006, the Trustees saw no reason to change the above strategy until the recent changes in the annuity market occurred due to more providers entering the market and premiums for annuity policies considerably reducing.

C3. Q. What is the New Section strategic review?

A. The Trustee has considered ways of reducing risk within the New Section and during 2008 undertook consultations with employers representing over 65% of New Section liabilities. Various options were discussed with employers including ideas on employers securing their own share of liabilities and whether it was possible to secure some of the orphan liability risk. The possibility of a number of employers forming a consortium to secure all liabilities (requiring the consortium to

pay in advance on behalf of any employers not in the consortium and then put in place arrangements for recouping such payments) was also discussed.

Although some employers showed an interest in securing their own share of liabilities in 2008, the cost of securing benefits (e.g. through a buy-in policy) is substantially greater than the assets and the recent economic crisis has adversely impacted on the affordability of achieving such settlements. With regard to insuring future orphan liability risk, there currently is no market. With regard to the consortium, this was not an idea that most employers were able to support.

The action most favoured by employers was to continue to operate the New Section by continued management of investment, mortality and other risks.

The Trustee will continue the risk management process in conjunction with the 2009 actuarial valuation.

C4. Q. Has the Trustee considered providing members with the facility of enhanced transfer values?

A. In the normal course of events, an employee might transfer benefits from a previous pension arrangement to the pension arrangement of a new employer or to a personal pension scheme if they so decide. This might be for the member's administrative convenience (to consolidate pension in one place) or it might be because there is a financial advantage. MNOPF members who make enquiries about transferring their benefits are always advised to obtain the services of an independent financial advisor so that they can understand the financial implications of making a transfer.

The purpose of an enhanced transfer value exercise is to offer an inducement to members to make such transfers. This removes the liability from the transferring scheme which from an actuarial point of view can be beneficial to the transferring scheme. This is because the actuarial factors used to value a member's benefits on transfer have no need to include the element of caution which the actuary has allowed for in the reserve held in the fund in respect of that member's benefits. The member is encouraged to make the transfer by an additional amount being added to the transfer value. This amount would normally be for the employer to provide by a top-up contribution to add to the transfer value.

The Trustee has given consideration as to whether an enhanced transfer value exercise is feasible in the MNOPF and decided not to proceed for the following reasons:

- Most members of the MNOFF have had a number of different employers during their MNOFF membership. Many of these employers no longer exist and any enhancement provided by an employer would have to be increased to account for such employers. A further complication is that if a transfer takes place, it would ideally be in respect of the whole of the member's benefit and thus every employer of that member would have to agree to pay the required share of the enhancement for that transfer to take place. If not, the result would be a partial transfer which might be inconvenient for the member and administratively expensive for the MNOFF. Furthermore, a rule amendment would be required to permit partial transfers. Thus, in a scheme such as the MNOFF, such an exercise becomes administratively very difficult and expensive and, depending on employer participation, may be limited in its effect.
- There is concern that such an arrangement is not in the interests of all members of the MNOFF. In the first place, the offer of an enhanced transfer value might encourage a member to transfer without the full considerations being given by the member to the implications. In order to circumvent this, it would be necessary for the Trustee to insist on the member obtaining independent financial advice which may have to be paid for by the employer or employers concerned. Secondly, such an exercise in a multi-employer scheme would be selective depending on whether any given employer is prepared to participate which would result in some members having access to a transfer value on better terms than would be available to other members.

C5. Q. Can an employer withdraw from the MNOFF?

A. Under Rule 5.2A of the MNOFF's Trust Deed and Rules, an employer can request withdrawal but can only cease to be a participating employer if the Trustee consents and provided it has made such contributions as the Trustee, having regard to the advice of the actuary, shall determine so as reasonably to protect the interests of members.

The Trustee has determined a policy in relation to employer withdrawal. The Trustee's general policy is that it will not allow participating employers to cease to be participating employers for the following reasons:

- the assets and liabilities fluctuate and it is therefore difficult to determine the amount of contributions that would be required;
- employers have a joint and several liability in relation to the MNOFF. The Trustee is not able to predict which employers will become unable to contribute in future and cannot therefore

- predict the extent to which liabilities will need to be reapportioned to other participating employers in future;
- the cessation of one participating employer is likely to have an impact on the extent of contributions due from other participating employers in future; and
- the Trustee does not wish to dilute the strength of the employer covenant by allowing participating employers to cease participation.

C6. Q. Will the Trustee consider a request from an employer to transfer its MNOFF members to its own pension scheme?

A. The Trustee has already received some such requests and given consideration to them. The primary issue relates to the security of members' benefits. The joint and several liability of MNOFF participating employers means that there is a very strong employer covenant in place and it is normally unlikely that this level of security would be matched in an employer's own pension scheme. It is also necessary to have regard to the interests to other employers and the transferring employer would have to remain as a participating employer with an obligation to fund its share of future orphan liabilities. There are also considerable administrative difficulties in that most members will have worked for several employers. No such bulk transfers have taken place but the Trustee will consider approaches on a case by case basis.

IMPORTANT INFORMATION

- These Questions and Answers were produced to provide summary information to the participating employers of the MNOFF.
- The information contained within these Questions and Answers is confidential and should not be distributed further without the prior written consent of the Trustee.
- No decisions should be based on the information contained in these Questions and Answers, and the Trustee accepts no responsibility, duty of care or liability for any decisions taken on the basis of the information contained in these Questions and Answers.