

Dear Member

November 2006

Actuarial Valuation as at 31 March 2006

Every three years an actuarial valuation of the MNOFP is carried out with separate valuations for the Old Section and the New Section. An actuarial valuation assesses how much money a scheme needs to have to pay pensions and other benefits accrued to date (the liabilities) and compares it with the value of its investments (the assets). If the assets are

more than sufficient to meet the liabilities the scheme is in surplus and if they are less than sufficient, it is in deficit. The valuation also looks at the rate of contributions required from active members and employers to pay for future service benefits.

General developments affecting valuations

Over recent years there has been a significant increase in life expectancy. This means that once a pension comes into payment it is likely to be paid for longer on average than previously assumed and this increases the cost of providing pensions.

A further factor affecting all pension schemes is that there are new funding requirements overseen by the Pensions Regulator. In order to reduce the risk of a pension scheme having to wind up without sufficient assets because its employer can no longer support it due to insolvency, the Regulator wishes to see schemes funded more strongly.

Old Section

The last Old Section valuation as at 31 March 2003 disclosed a surplus of £167m. This represented a 15% excess of assets over liabilities. The Old Section is predominantly invested in fixed interest investments which are more secure but in general have a lower return than investments in the stock market. Over the last three years, the Old Section has benefited from good investment returns. However, set against this is the cost of the 4% bonus paid in January 2005, the allowance for increasing life expectancy and an expectation that investment returns will be lower in the future.

Overall, the expectation is that the surplus in the Old Section will be of a similar order to the surplus disclosed in 2003. Once the results have been finalised, the Trustee will be able to give consideration to the level of bonus that can be granted on Old Section pensions (both to Old Section pensioners and to Old Section members who have not yet retired).

New Section

The previous valuation as at 31 March 2003 disclosed a deficit of £194m in the New Section. This represented a 14% shortfall in assets compared to liabilities. A significant proportion of the New Section's assets are invested in the stock market which has risen strongly over the last three years so the investment return has been very good. Another positive factor has been the collection of additional contributions from employers towards the deficit disclosed in the 2003 valuation. On the negative side, there is the allowance for improved life expectancy, the expectation that investment returns will be lower in future because of changed market conditions and the need to build in a stronger funding basis in order to meet the Regulator's requirements. It is likely that these negative factors will outweigh the positive factors.

The overall result will be that a significant additional deficit is likely to be disclosed in the New Section by the 2006 valuation and further contributions will be required from employers to meet this extra deficit. Furthermore, there will have to be a small increase in the joint contribution rate paid by members in service and their employers.

Given the financial position of the New Section and publicity in the media about underfunded pension schemes, it is reasonable for members to ask how safe their pension is. This issue is addressed in a series of questions and answers attached to this letter. In summary, however, the Trustee believes that the nature of the MNOFP and the support which its very wide-ranging group of employers is legally required to give to it means that your pension is very secure.

Consultation

The Trustee is required to consult with employers on the valuations. This process has recently commenced and is being undertaken through the Chamber of Shipping over the next few weeks. Also, the Officers Union (Nautilus UK - formerly NUMAST) will be providing information to members and inviting views.

Future Action

Once the consultations have been completed, the Trustee will determine what additional deficit contributions will be required and invoice employers accordingly. The Trustee will also determine the contribution rate required from active members and their employers to pay for future service benefits.

When these decisions have been made (which is expected to be in the first quarter of 2007) the Trustee will send a further communication to members.

Further Information

This letter and the attached questions and answers will be put on the MNOPF's web site (mnopf.co.uk) under Announcements. You will also find on the website a copy of the preliminary results of the New Section actuarial valuation under Publications. If you have any further questions, contact details can be found on the back of this leaflet.



Peter McEwen
Chairman
MNOPF Trustees Limited

Questions and Answers

New Section

1 Q Given that there is likely to be a further deficit on top of the deficit in 2003, how will the new deficit be made good?

A The Rules of the MNOPF give the Trustee power to require employers to pay deficit contributions. The Trustee has already invoiced employers for their share of the contributions required to meet the 2003 valuation deficit. Similarly employers will be invoiced for the further deficit contributions required following the 2006 actuarial valuation.

2 Q What happens if employers go bust and cannot pay the deficit contributions?

A In March 2005, the Trustee obtained a judgement from the Court that all employers who have participated in the MNOPF are liable for contributions towards a deficit. There are over 400 such employers who have participated in the New Section from whom deficit contributions are required. These employers have joint liability so that when employers become insolvent, their liabilities are spread over the remaining employers.

3 Q What if all the employers go bust?

A As there are over 400 employers in the MNOPF, the chance of them all going bust is very remote.

Also, some of the participating employers are very major companies or subsidiaries within major corporate groups and it is unlikely that the employers participating in the MNOPF would not have sufficient assets to support it.

In the extremely unlikely event that all employers become insolvent, support is likely to be provided by the Pension Protection Fund. This is a centralised scheme set up by the Government to provide some compensation to members of pension schemes where the employer has become insolvent.

4 Q Will there be further deficits?

A An actuarial valuation will be carried out every three years. The results of each valuation will depend on the experience of the scheme at the date of the valuation, including the improving life expectancy of members and the expectation for future investment returns at the time.

As more members retire and receive pensions, the need to invest in more secure fixed interest investments rather than invest in the stock market will increase. However the more secure investments will tend to produce lower investment returns. It is therefore possible that further deficits could be disclosed in future actuarial valuations.

5 Q Does the expected deficit in 2006 include the deficit disclosed in 2003?

A No, it is in addition. It is presumed that all the 2003 deficit will be made good by employers' deficit contributions. Employers will be required to pay extra deficit contributions on top of what they have already paid.

6 Q Have all the employers paid their 2003 deficit contributions?

A The deficit contributions already received, plus those expected to be received from employers who are paying by instalments, will meet a high proportion of the 2003 deficit. However, there are a number of employers who are no longer trading or who are in liquidation or do not have sufficient assets to meet the contribution requirements.

Where it proves impossible to recover unpaid deficit contributions or it is not viable to pursue payment any further, the shortfall will be recouped by increasing the deficit contributions required from the remaining employers.

7 Q Why isn't there a surplus given the rise in share values since 2003?

A The good investment returns since 2003 have had a positive effect over the last three years. However, the stock market is now at a higher level and the outlook for future investment returns over the next 30 or 40 years is lower. Also people are living longer and the Pensions Regulator requires Trustees to take a more prudent approach to funding. The net effect of these positive and negative influences is a deficit.

8 Q If an employer I worked for whilst contributing to the MNOFF goes bust, does that affect my pension?

A No, the assets of the MNOFF are entirely separate from those of the employers and the liabilities of the MNOFF are met jointly by all participating employers.

9 Q I am in receipt of a New Section pension. Will it be cut back because of the deficit?

A There will be no cut back in New Section pensions as a result of the deficit.

10 Q I am in receipt of a New Section pension. What increases will I get on my New Section pension in future?

A The MNOFF's Rules do not provide for any guaranteed increases to pensions in payment. However, some pensions have to be increased by law ("statutory increases"). Any other increase is at the discretion of the Trustee ("discretionary increases").

Statutory increases are due on pensions built up for service after April 1997 and on an element of your pension (known as the Guaranteed Minimum Pension) to which you are entitled for service after April 1988 if you were contracted out of the State Earnings Related Pension Scheme.

Discretionary increases are awarded only if the Trustee decides there is sufficient surplus available in the scheme, having taken advice from the Actuary. In the circumstances of the New Section being in deficit there is no current prospect of any discretionary increases being granted.

11 Q I am currently contributing to the MNOFF. Will the benefits I build up in future be affected?

A No, there is no change in the rate at which pension builds up. However, the stronger funding basis will require an increase in the contributions paid by yourself and your employer. The exact increase is not yet known. The Officers Union (Nautilus UK – previously NUMAST) will be providing information to members and inviting views. Members whose contracts of employment provide for the "Two Tier" system to operate (where the employer's contribution serves to reduce the officer's total remuneration) will be advised of the changes required once the contribution rates have been determined.

12 Q Is it possible to say how much the deficit is?

A The figures in the actuarial valuations are calculated using assumptions – principally, the rate of return on investments in future. Clearly, this cannot be known for certain and the Actuary therefore produces figures on a number of different assumptions. Using assumptions that are more likely to be achieved in reality should result in a stronger funding position. Thus, a range of figures can be produced depending on the strength of the assumptions used.

The Trustee is required to consult with employers on the results of an actuarial valuation. This consultation is currently being undertaken. Although the Trustee has the power to set the level of contributions required from employers, the law requires that the views of employers have to be taken into account to strike a balance between how strongly the scheme is funded and what employers can pay without creating excessive commercial difficulties.

Once these consultations have been completed, the Trustee will decide on the deficit contributions to be collected from employers.

Old Section

- 1 Q** As there is a surplus in the Old Section, will I get an increase on my pension?
- A** The Trustee reviews the position of Old Section pension discretionary increases after each triennial actuarial valuation and also carries out an interim review each year. The Trustee's policy is to grant a discretionary increase only if it is prudent to do so. The Trustee will consider early in 2007 whether an increase can be granted following the 2006 valuation results and will notify members.
- 2 Q** The surplus was £167m at the 2003 valuation. Why was the increase granted from January 2005 only 4% instead of sharing out the whole surplus?
- A** Each 1% increase cost the Old Section about £12m (now £13m), so a 4% increase cost £48m. The Trustee did not consider it prudent to use up any more of the assets in granting increases at that time.
- 3 Q** Could the Old Section go into deficit?
- A** In theory, yes. Improvements in life expectancy mean that pensions cost more. Also, granting increases to pensions reduces the surplus. The Trustee therefore has to be cautious when granting increases to ensure there is an adequate cushion against future unknown liabilities.
- 4 Q** Can the surplus in the Old Section be used to meet the deficit in the New Section?
- A** Under the Trust Deed and Rules of the MNOPF the assets and liabilities of the New Section and Old Section are completely separate. The surplus in the Old Section cannot therefore be used to meet the deficit in the New Section.

Further Questions

If you have any further questions you can contact us in one of the following ways:

- telephoning the MNPA Member Liaison Service on: 01372 200200
- sending an e-mail to: mnopf@mnpa.co.uk
- writing to the MNOPF Director of Pensions at the address on this letter.

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