The Pensions Regulator

Annual report and accounts
2005-2006

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Report presented to Parliament by the Secretary of State for Work and Pensions with the approval of the Treasury, in accordance with Section 11(5) of the Pensions Act 2004. The Accounts are prepared under paragraph 27 of Schedule 1 of the Pensions Act 2004, and presented by the Comptroller and Auditor General.

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Contents

The Pensions Regulator

The Pensions Regulator (the regulator) commenced operations in April 2005, having been established under the Pensions Act 2004. It is an executive non-departmental public body, accountable to the Secretary of State for Work and Pensions. The act gives the regulator four objectives:

- to protect the benefits of members of occupational pension schemes;
- to protect the benefits of members of work-based personal pension schemes;
- to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (PPF); and
- to promote, and to improve understanding of, the good administration of work-based pension schemes.

The regulator is funded by grant-in-aid from the Department for Work and Pensions (DWP) and the running costs are recovered through the general levy on pension schemes. This levy imposed on schemes covers the cost of the regulator, the Pensions Ombudsman and the Pensions Advisory Service. The Pension Protection Fund is funded via a separate levy.

While the organisation commenced operations on 6 April 2005, it was brought into being by a Commencement Order with effect from 17 December 2004.

The Pensions Regulator supersedes the Occupational Pensions Regulatory Authority (Opra), which was dissolved with effect from 5 April 2005. Under the provisions of the act, the Pensions Regulator inherits Opra's assets and liabilities as well as residual duties and powers.

The Pensions Act 2004 gives the Pensions Regulator a significantly wider range of powers and responsibilities than Opra. This necessitated a major programme of work, throughout 2005 and continuing into 2006, under the governance of the DWP, to design and build business processes for the new organisation and to manage the transition from Opra to the Pensions Regulator.

A report was published in September 2005, covering the period from 17 December 2004 to 31 March 2005. During this period, while the Pensions Regulator had legal existence, it was not operational and had no funds of its own. Its activities were encompassed within the Pensions Regulator Programme, which was funded directly by the DWP within a formal governance and control structure. For this reason, the Secretary of State issued an accounts direction on 2 August 2005, waiving the requirement to produce accounts. The report included a narrative statement confirming that there were no financial transactions or balances to report for the period.

1 Chair's foreword

This has been an exceptionally busy year and this report sets out the work we have done under the five themes of our business plan. There have been some notable achievements and I would like to touch on three things: the organisation, clearance and scheme funding.

First the organisation. We took over from Opra, which I believe did a good job within its limited powers. However, the task and powers shaped the organisation, and the more active and risk-based role of the regulator required a major reshaping. Tony Hobman and the three new executive directors have rightly seen this as a key task, building on the work undertaken by Opra and the Department for Work and Pensions in 2004-05 in preparing for the new regulator. There has been a significant programme of investment to help deliver the objectives Parliament has set us. We're deliberately bringing in people on secondment and on contract to supplement our core capacity, because we see it as important to have a regular injection of new ideas and experience to keep us up to date and sharp, rather like the Takeover Panel.

Second our clearance function. This came out of the need for moral hazard powers to protect the Pension Protection Fund from companies seeking to avoid their pension liabilities. Business rightly saw the potential for these powers to inhibit proper commercial activity and asked for a clearance procedure. This is an unusual role for a government body since regulators mostly step in when something is going wrong. We are asked to say something is acceptable and to bind ourselves for the future. The breadth of this remit in itself had the potential to hamper commercial activity, so we have tried to give broad guidance on how we would work, and to work from principle rather than lists, in this case the principle that the pension scheme should be treated like a material unsecured creditor.

In our first year we have granted clearance in almost 150 cases and refused it in only two. Also there have been many hundreds of enquiries and exploratory cases considering the nature and materiality of transactions and whether they fall within the scope of the clearance process. In the majority of clearance cases there has been sufficient mitigation offered to protect the scheme and the trustees have agreed to it. These are early days of course, and there is some evidence that as shareholder expectations adjust to reflect pension scheme liabilities and as our guidance and decisions get factored in, transactions are going through in discussion with trustees without necessarily coming to us for clearance.

And finally scheme funding. Here the Pensions Act 2004 asks us to set funding targets and recovery plans where employers and trustees cannot agree, and to receive and therefore evaluate recovery plans. Again we thought it right to consult about our approach to these roles. Our consultation closed in January 2006 and we issued a regulatory statement on scheme funding in May. The statement took into account the responses to our consultation and was well received.

We aim to follow the principles of better regulation, working in a risk-based way. We also want to go with the grain of the markets, because pension deficits will be best tackled through market pressures alongside the work of trustees and managements. Overall our assessment of progress is: so far, so good. The more gloomy predictions of some commentators have not come to pass, and the team in Brighton have contributed substantially to the progress being made in tackling the issues facing work-based pensions.

David Norgrove
chair, the Pensions Regulator
10 July 2006

2 Chief executive's summary

The Pensions Regulator's first year of operation has been characterised throughout by the dual requirement of providing an effective operational capability from day one, while developing appropriate plans and processes for the future.

As well as highlighting the progress we have made in developing the organisation and in responding to complex challenges, such as the clearance process and scheme specific funding, the chair has also emphasised in his foreword, the extent to which we have sought to work in partnership with the regulated community as a whole. In addition to engaging in a dialogue on funding we have, for example, consulted widely on all of our statutory codes of practice that range from reporting breaches to trustee knowledge and understanding and which are a key component of the new regulatory framework. We fully recognise the front line role that trustees play in the protection of members' benefits and believe that the free, interactive e-learning programme we launched in February 2006 will provide them with further practical support. Raising standards of governance, particularly in smaller schemes, remains an important focus for our work in 2006-07.

One of our core organisational values is to achieve worthwhile results and a great deal of thought has gone into defining success indicators which will be both relevant and durable in the years ahead. Despite the pace and complexity of organisational development over the course of the last 12 months, many, though not all, of our initial assumptions about performance measures have held good and these are detailed in the main body of this report. We have also been able to establish baselines for a number of the key targets that we will use going forward and these are also detailed below.

A year of intense transition and change has given the regulator a strong platform on which to build for the future and this could not have been achieved without the commitment and engagement of our staff. We know that much more needs to be done in the year ahead, but welcome the prospect of further embedding a risk-based and flexible approach to the regulation of occupational pensions.

An overview of the occupational pensions environment is provided in *section 3 – The pensions environment and the regulated community.* Section 4.1 – *Developing the organisation* – summarises the work of our internal culture change programme and *section 4.2 – A review of our activities during the year* – reports on our achievements against the five themes that were set out in our business plan for the year. Our key priorities for the year 2006-07 are set out in *section 4.4 – Looking ahead.*

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

3 The pensions environment and the regulated community

Work-based pensions are part of a wider pensions landscape which also comprises the basic state pension, the state earnings-related scheme (SERPS/S2P) and individual personal pensions. The Pensions Regulator regulates only employer-sponsored or work-based pension schemes. These comprise both trust-based and personal arrangements (see figure 3a below). Occupational schemes are governed by trustees; group personal pensions (GPPs) are an individual contract between the employee and the provider (typically an insurance company) although payments of contributions are made through the employer.

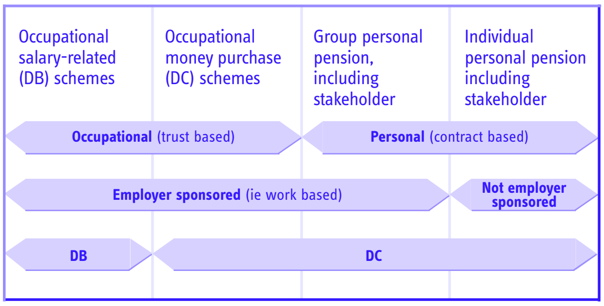


Figure 3a:
Types of pension arrangement

Source: Based on diagram on page 80 of *Pensions Commission, Pensions: Challenges and Choices*, The First Report of the Pensions Commission

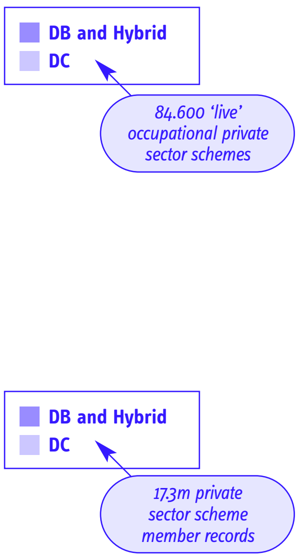
Profile of scheme membership

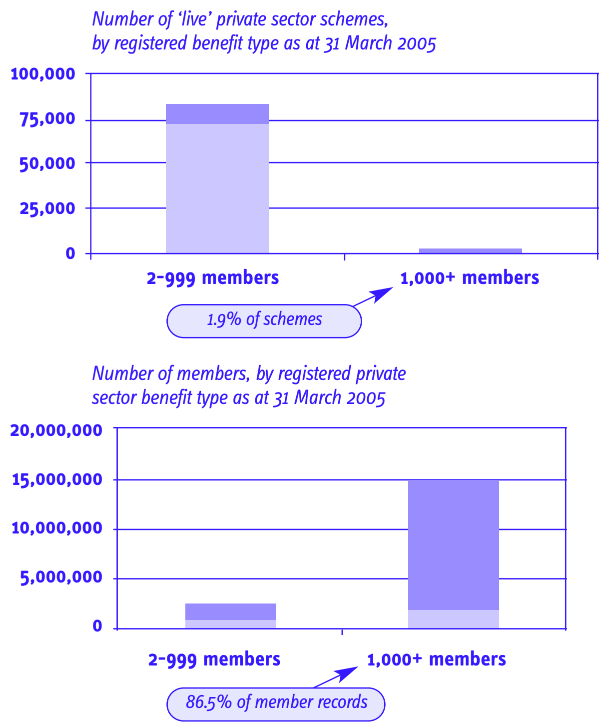
Most members of occupational pension schemes belong to a small number of schemes. At 31 March 2005 there were approximately 17.3 million members of 84,600 private sector occupational schemes (see figure 3b below). Of these members, over 85 per cent belonged to 1,600 schemes that had 1,000 or more members. The largest 1,600 schemes comprise just 1.9 per cent of all schemes; 1,000 were DB, 300 were hybrid and 300 were DC schemes.

Of the approximately 83,000 schemes with fewer than 1,000 members, approximately 72,000 were DC schemes and 11,000 were DB or hybrid. Of these 72,000 DC schemes, over 56,000 had between two and four members only.

Figure 3b:
The number of pension schemes and the number of members of pension schemes

Source: The Pensions Regulator *(Pension schemes in the UK, 2005)*

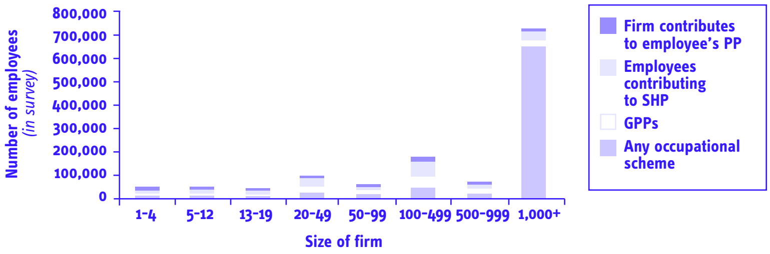




An estimated[1] 1.37 million employees contribute to group personal pensions (GPPs). While the membership of occupational pensions is concentrated in the schemes operated by large firms, DWP research[2] suggests the employees who contribute to GPPs are distributed more evenly between medium and large firms, especially among firms with 20-49 employees and 100-499 staff.

Figure 3c:
Active pension members, by type of pension provision and size of organisation

Source: *DWP Employers Pension Provision Survey, 2005*



The changing environment

The shift from DB to DC

A development that has been much commented on has been the closure of many defined benefit schemes to new members. As sponsors look for alternatives to traditional 'final salary' DB schemes, there has been a growth in trust-based DC arrangements and also GPP contract-based arrangements.

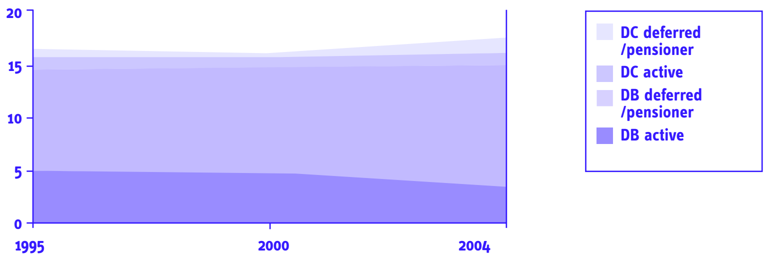
Research[3] estimates that in 2005, a GPP was offered by 6 per cent of private sector firms, employing one-third of employees. Membership of a GPP is estimated to represent around one in five (19 per cent) employees in any type of private sector employer's pension arrangement.

With the number of active members of DB schemes in decline, we estimate that if trends continue at current rates there will be equal numbers of active members of occupational DB and DC schemes by 2012. This estimate excludes the members of GPP arrangements (which are not occupational pension schemes).

However, even with a continuation of the current rate of decline of active members in occupational DB schemes, they will remain prominent for many years to come. Figure 3d below shows that there has been little change in the overall membership of DB schemes over the last ten years. By contrast, many DC schemes are relatively new and their membership drawn only from new employees.

Figure 3d:
Breakdown of membership of occupational pensions (1995-2004) – (excluding members of group personal pension arrangements)

Source: *GAD Occupational Pension Schemes Survey*



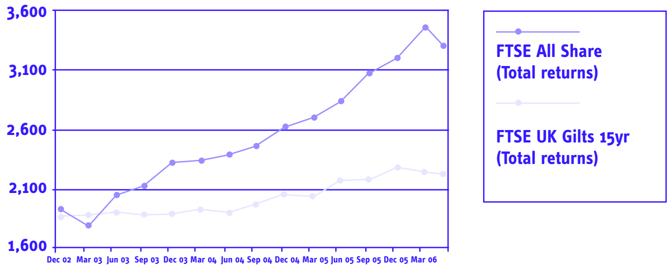
[1] Office of National Statistics, Annual survey of hours and earnings, 2004
[2+3] DWP Employers' Pension Provision Survey, 2005

The level of scheme underfunding

The driving force for the closure of DB schemes has been the increasing recognition of the extent to which such schemes expose the sponsoring employer to non-business related, and in some cases uncontrollable, risks, particularly in relation to investment volatility and increasing longevity. Some key risks have materialised in recent years resulting in substantial deficits.

During the period of this report, we have seen rising equity markets and changing conditions in relation to bonds (with a reversal towards the end of the period of the trend of falling yields).

Figure 3e:
Gilts and equities performance



Recent estimates[4] that take into account changes in investment market conditions suggest that the projected assets of the FTSE350 company pension schemes were £411.7bn and that the IAS19/FRS17 pension deficits of these pension schemes had reduced to £42.5 billion at the end of the April 2006.

Other factors that may have a significant impact on pension scheme deficits during 2006 include the extent to which companies are making substantial one-off payments to reduce deficits.

From our analysis of a sample of scheme return data collected in 2005-06, uprated for the most significant market changes, we estimate that the overall funding position for schemes is:

- Full Buy Out – Assets £675bn, Liabilities £925-1,025bn, Deficit £250-350bn
- IAS19/FRS17 – Assets £675bn, Liabilities £725-775bn, Deficit £50-100bn

It should be emphasised that these figures are estimates based on a sample of the available data, which reflected a range of valuation dates between 2002 and 2005, to which approximate assumptions about changes in asset and liability values have been applied. They take no account of deficit repayments made since the valuation date. The buy-out estimates represent the funding that would be needed to buy out the liabilities with an insurance company – not the cost of funding the liabilities on an ongoing basis, which would be substantially less. Reliable figures on that basis will only become available as schemes undertake their triennial valuations between 2006 and 2009.

[4] Watson Wyatt Pension Deficit Index

The governance of schemes

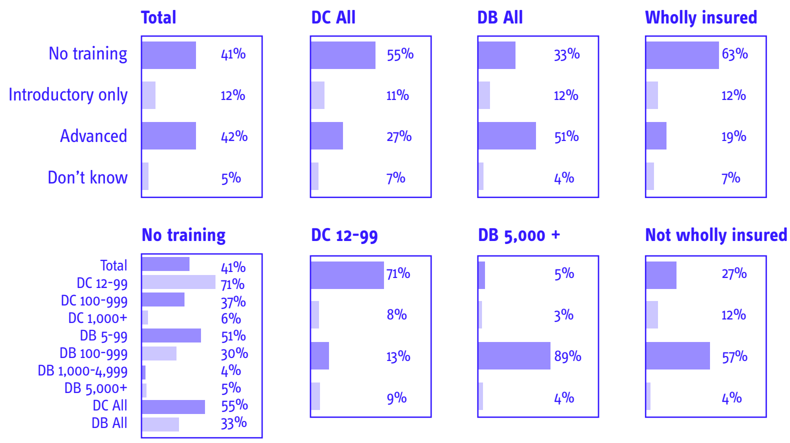
Well-governed pension schemes are likely to be better administered, have greater awareness of financial risk, and to represent well the interests of scheme members. This is true for DB, DC and hybrid schemes alike.

In the first quarter of 2006, we undertook the largest survey of occupational pension scheme governance in the UK. Early findings from this research provide a broadly encouraging picture of governance standards, and a number of areas where additional research is needed. We plan to publish a report of the findings in the summer and use the findings from the initial survey as a springboard for developing a governance strategy and to track further progress in governance standards. Among the findings, the research indicates scope for further activity from trustee boards in important areas such as identifying and managing risks. For example, less than half of schemes (42 per cent) had a formal process in place to identify risks. The management of conflicts of interest/duty amongst scheme trustees is also an important area, particularly among DB schemes with scheme funding responsibilities.

The research has shown correlations between schemes whose trustees undertake advanced training and greater confidence in a number of areas of scheme governance activities. However, a large number of schemes have trustees that have not undertaken any form of structured training – see figure 3f.

Figure 3f:
Formal structured training undertaken by one or more scheme trustee during the past 12 months

Source: *The Pensions Regulator's annual governance survey – Jan to March 2006*



Note: All percentages are rounded

Trustee learning is clearly an important area and our web-based e-learning modules **www.trusteetoolkit.com** provide all scheme trustees with a free and user-friendly learning resource.

4 Management commentary

4.1 Developing the organisation – the culture change programme

The regulator opened its doors on 6 April 2005. Its operational capacity at that stage was the result of a programme of development activity in 2004-05 managed by the Department for Work and Pensions (DWP) and involving staff from Opra. In addition to the review and development of core Opra business functions and processes taken over by the regulator, the programme developed new processes to support the regulator's wider powers.

Beginning in July 2005, a second organisational development programme – *the culture change programme* – was established by the regulator, under joint governance with the DWP. The new programme has continued the *design and build* activity of the earlier programme, to complete the implementation of business processes, policies, and IT and other support systems that are needed to deliver the full range of the regulator's functions.

The key achievement of the programme has been the design and implementation of the business processes associated with the development of policy and the delivery of regulation, and their embedding within the new organisational structure shown in the chart on page 38. More information on programme achievements is reported under *Theme 5* on page 19. Details of programme governance and funding are set out under *section 4.5 – Accountability and governance*.

4.2 A review of our activities during the year

This review reports on the key outcomes under each of the five themes from our business plan for 2005-06:

Theme 1	Demonstrating a proactive and proportionate response to risk
Theme 2	Becoming an authoritative voice in the industry
Theme 3	Working with the Pension Protection Fund (PPF) to protect pension scheme members from employer default
Theme 4	Supporting the strengthening of scheme funding
Theme 5	Strengthening the regulator and its people

Theme 1
Demonstrating a proactive and proportionate response to risk

Working towards the following outcomes:

- Schemes with the most significant risks are identified
- The most significant risks to members' benefits have been reduced in identified schemes, in a proportionate manner
- The Pensions Regulator can demonstrate that it is working to reduce the risks to members of DC schemes and personal pension (PP) arrangements
- The pensions industry and employers recognise that the Pensions Regulator's regulation is risk-based and proportionate

Risk-based management

We began the year having developed a model for assessing risks to pension schemes and responding according to the assessed risk. As work progressed to identify a pipeline for handling customer contact, processing incoming information, and identifying the appropriate regulatory response, the model was refined and an organisational structure built around it, using a *triage* approach to allocate work to one of three *regulatory practices*.

In the early part of the year we focused on the *corporate risk management* (clearance) practice and developing the *triage* function. Later in the year we commenced development of business processes to support a new practice team to address the new regulatory requirements for scheme funding – our *scheme specific funding practice*. Our third regulatory practice, dealing with *pensions administration and governance*, was also established during the year and focused initially on dealing with a significant volume of regulatory cases inherited from Opra, our predecessor body.

Full implementation of our *risk-based management* model is dependent on the completion of our *culture change programme*, but initial assessments of scheme risk have been undertaken, primarily using data from the scheme returns. The model also generated wider business rules for our regulatory practices to help us determine where we will intervene in an identified scheme risk. These rules take into consideration not only the scheme return information, but also Dunn & Bradstreet data, any corporate transactions that we are aware of, the risks identified from the data we have on the wider pensions landscape and any other knowledge we have from casework and intelligence sources.

We have implemented processes for receiving and recording whistleblowing and notifiable events reports within the risk framework, including e-reporting using webforms.

In our approach to risk mitigation plans we have sought to make allowance for the resources available to schemes in the choice and design of interventions, and to be consistent with the *Better Regulation Task Force* principles of good regulation.

We have published information on our new approach targeted at the pensions industry and employers including the risk-based nature of regulation and the deployment of our new powers. This has included mailing literature, placing articles, creating web pages, making presentations to industry conferences and running national roadshow events throughout the year.

Scheme specific funding

Within the programme of work to implement the new scheme funding requirements, initial contact was made with a number of the largest schemes. Our target in 2006-07 is to have established contact with schemes that have over 1000 members, and those companies in the FTSE 100 where valuations of their DB schemes fall between 22 September 2005 and 31 March 2007.

Scheme returns

The scheme return is designed to enable us to collect the key information about pension schemes that we and the Pension Protection Fund require to fulfil our roles. Returns were dispatched to defined benefit schemes with five or more members and over 88 per cent were returned by 31 March 2006.

During the year we consulted on scheme return arrangements for personal pension and stakeholder schemes, and prepared a further version of the return aimed at small and DC schemes. Clarification of our data requirements during the year enabled us to streamline the return, significantly reducing the number of items of data requested.

Environmental scanning

We have implemented a process to analyse risks apparent across a number of schemes or within specific sectors ('special themes'), by establishing an *environmental scanning* team. The team has gathered data about the defined benefit (DB) scheme landscape and trends in pensions provision, analysed sectoral risks to DB schemes and risks faced by defined contribution (DC) schemes and closed schemes, and looked at the implications of changes to the pensions tax regime.

Scheme wind-ups

Since April 2002 schemes in wind-up have been sending annual reports to the regulator (formerly Opra). These have been in three-year age bands with the oldest schemes reporting first. From 2007, all schemes will be due to report in the three months following the date that they have been in wind-up for three years.

As part of our risk-based approach, we identified from a sample of scheme returns some 130 schemes that were still in wind up after four years, with the aim of ensuring that trustees put in place robust project plans to conclude wind-up more quickly than originally notified. We are also looking to see that the level of fees they are charging is reasonable. Further research and analysis of the results will help determine our future approach to winding up.

In addition, we are working closely with a number of interested parties, such as the DWP's working group on winding up of pension schemes, to further explore the areas that act as a barrier to speedy action, with a view to developing joint approaches to tackle these issues.

Trustee knowledge and understanding

To improve TKU in risk identification and management, we issued regulatory guidance on risk (for trustees) in September. We also published a code of practice on TKU, and designed and implemented the first elements of a free e-learning programme aimed primarily at lay trustees.

We have ensured that the TKU regime, including the code of practice and the e-learning programme, is tailored for trustees of DC schemes, including fully-insured schemes, as well as for trustees of DB schemes.

Risks to defined contribution schemes

We undertook a review of risks to defined contribution (DC) schemes and personal pension (PP) arrangements. Having considered possible regulatory and resource strategies to mitigate these risks with our advisory group and our board, we set out a proposed approach for addressing these risks in our medium term strategy and 2006-07 business plan, and intend to consult on this in the coming year.

Regulation of stakeholder pensions

We have maintained a fully functional register of stakeholder schemes and their status and have responded to reports that access by employers is not being granted.

Theme 2

Becoming an authoritative voice in the industry

Working towards the following outcomes:

- The Pensions Regulator is a trusted source of information and comment on pensions and their regulation
- The Pensions Regulator uses its authoritative position to influence improvements in the governance and administration of pension schemes
- The Pensions Regulator builds partnerships

Research

The findings of our Occupational Pensions Schemes (OPS) research (covering market and scheme characteristics as well as key governance and funding issues), and the conclusions of research we commissioned from PwC on the corporate impact of clearance activity, were published as the first in our intended programme of reports about the regulatory environment.

Trustee knowledge and understanding

The code of practice on trustee knowledge and understanding (TKU) received ministerial approval and the first two modules of our e-learning programme were launched in February 2006. We continue to work with the QCA and Financial Sector Skills Council on the development of a TKU syllabus. E-Learning modules covering funding and investment issues are scheduled for development and issue in the year ahead.

We now have a baseline measure from which we can track changes in lay trustees' self-perception of their knowledge, from a *scheme governance survey* that we carried out in early 2006. (Detailed results from the survey will be published in summer 2006).

Pensions reform

During the year we worked closely with the DWP on pensions information and education in support of the government's pensions reform programme. We contributed to the Department's preparation for the government White Paper on Pensions, helping to identify potential improvements to pensions legislation and evaluating the regulatory implications of the *Pensions Commission* report.

Europe

We also worked closely with the DWP on the application of the EU Pensions Directive to the regulation of cross-border schemes. We are an active member of the European Committee for Insurance and Occupational Pension Supervisers (CEIOPS) and have played a significant role in developing the EU regulators' protocol ('the Budapest protocol') for cross-border schemes. We have consulted on, issued guidance for and are now operating live, the process for authorisation and approval of cross-border schemes.

Working with the PPF and other UK regulators

We have developed and strengthened our links with other UK regulators and overseas regulators. We established a memorandum of understanding (MoU) with the FSA, and agreed a tripartite MoU with the DWP and the Pension Protection Fund. With the PPF we developed service level agreements to govern the key areas of collaboration. Regular meetings were held with the PPF at operational and senior management levels, and the PPF and Pensions Regulator boards met together twice during the year.

List of key publications in the year:

06/04/05	Reporting breaches code of practice and guidance published
30/06/05	Notifiable events code of practice published
31/10/05	Consultation document on scheme funding published
14/11/05	Consultation document on cross-border schemes published
23/11/05	Guidance on multi-employer schemes published
15/02/06	Scheme funding code of practice published
07/03/06	Reporting late payments code of practice published
08/03/06	Anti-avoidance and clearance: the bigger picture

Theme 3
Working with the PPF to protect pension scheme members from employer default

Working towards the following outcomes:

- There is a clear understanding of how the Pensions Regulator will support the PPF and the PPF is confident in the service provided
- The pensions industry and employers understand: the respective roles of trustees, employers, the Pensions Regulator and the PPF; and the framework for powers relating to corporate transactions
- The Pensions Regulator reduces the risks to members and the PPF of employer avoidance of their liabilities for DB pensions

The last of these outcomes reflects our statutory objective 'to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund'.

We have sought to fulfil this statutory objective by increasing awareness of scheme funding issues, and through our regulatory oversight of the clearance of corporate transactions, and scheme specific funding.

During the year we established the corporate risk management practice and issued initial guidance on clearance in April 2005 and on withdrawal from multi-employer schemes in November 2005. We also issued a code of practice and guidance on scheme funding.

In addition, the TKU code of practice and e-learning material has addressed the need to strengthen trustees' knowledge and understanding of their role in respect of scheme debts on employers.

We have liaised with the PPF in clearance cases where they may be taking in pension scheme liabilities, as well as during the assessment period following a corporate insolvency.

Together with the DWP, we and the PPF are parties to a tripartite memorandum of understanding which helps to facilitate effective working. Bilateral service level agreements between ourselves and the PPF were developed during the year to cover specific areas of operation, such as levy collection. A letter of agreement covering consultation on policy and organisational change was subsequently signed to help ensure that the two bodies' regulatory approach remains consistent.

Further information on clearance activity is given under *section 4.3 – Facts and figures*.

Theme 4
Supporting the strengthening of scheme funding

Working towards the following outcomes:

- Trustees and advisers of DB schemes understand the new scheme specific funding arrangements and the Pensions Regulator's role
- Underfunded schemes have recovery plans in place that commit employers to achieving a funding level appropriate to securing benefits for members
- The Pensions Regulator's interventions in scheme funding issues do not increase the risk of employers reducing their commitment to work-based pensions

The move from the *minimum funding requirement* (MFR) to *scheme specific funding* places new requirements on trustees and employers to value scheme liabilities on the basis of prudent assumptions in a way that is appropriate to protecting the benefits of scheme members, and to put in place robust plans to make good any deficits.

It is our responsibility to ensure the effective implementation of the new framework, having regard to our statutory objectives, which include protecting the benefits of members of occupational pension schemes and reducing the risk of situations arising which may lead to calls on the Pension Protection Fund. Given the scale of the funding involved, our regulatory approach has to balance the need for benefit protection with the needs of business and the wider economy, considering that the best means of delivering the members' benefits is usually for the pension scheme to have the continued support of a viable employer.

Our broad approach is to:

- ensure, through our code of practice and other forms of communication, that trustees, employers and their advisers have a good understanding of the matters they should consider when they agree their scheme's statutory funding objective and any recovery plan needed to raise funding to that level;
- influence key parties through a regulator's statement on our approach to scheme funding that indicates how we intend to focus our resources on schemes that are likely to pose the greatest risk, ensuring that the messages are widely spread through a communication programme, including workshops, speaking engagements etc; and
- intervene in specific schemes where the funding objective or recovery plan is (or may be) agreed at an inappropriate level or duration in respect of our objectives to protect members' benefits and reduce risks to the Pension Protection Fund.

In 2005-06 we issued the code of practice on scheme funding and undertook activity to publicise the new requirements on trustees and employers and our role in enforcing these, including a series of workshops for trustees and advisers across the country. We also issued a consultative draft of a regulatory statement (subsequently finalised and published in April 2006).

In our draft regulatory statement, and in workshops and other briefings provided during the year, we emphasised that regulation of the scheme specific funding regime will be proportionate, acknowledging the importance of avoiding the imposition of recovery plans that would jeopardise the employer's ability to continue in business. Our statement was supported by extensive analysis of the impact on employers, the equity market and the economy of reductions in pensions deficits, which was carried out for us by PwC and published on our website.

The final statement drew on the original draft amended to take account of responses to consultation. It emphasised that we would use specified triggers relating to the level of the technical provisions and the recovery plan, as a mechanism to identify schemes for further scrutiny. The technical provisions trigger is to be linked to the measures of scheme liabilities provided by the FRS17 accounting standard and the Pension Protection Fund's measure of its potential liabilities in the scheme. Schemes with recovery plans longer than 10 years, that are significantly back-end loaded or include over-optimistic assumptions on investment returns will also trigger. We have made it very clear that the triggers should not be considered to be targets for trustees to meet. If a scheme triggers, its funding plans will be subject to a further assessment process to help us to determine whether we should intervene and if so, with what priority.

Consulting our stakeholders

It is our intention to consult, where practicable, on all major new developments that may affect trustees, sponsoring employers or their advisers. Our most substantial consultation exercise during the year was on our approach to scheme funding under Part 3 of the Pensions Act 2004. The new framework, which replaces the Minimum Funding Requirement, applies to all defined benefit schemes at their next valuation after September 2005. It is covered by regulations that came into force in December 2005 and a regulator's code of practice.

Following informal consultation, we issued a consultation document on 31 October 2005 setting out our approach to deciding which schemes we should consider examining in detail in regard to their funding targets (technical provisions) and recovery plans.

We received 67 responses to our consultation document. These welcomed the consultation approach we had adopted and generally supported our broad approach. We took account of comments about our approach in a revised statement issued in May 2006. The statement was accompanied by a report indicating why we had, or had not, made changes in response to consultation, summarising the changes made. These documents have been broadly welcomed with recognition that we had listened to the representations made to us.

Theme 5
Strengthening the regulator and its people

Working towards the following outcomes:

- The Pensions Regulator is supported by a cohesive and co-operative physical environment
- A flexible, capable and motivated workforce is in place
- The Pensions Regulator's regulatory approach has been tested, reviewed and refined and strategies fully developed for all operational functions by end of year one
- The governance processes and infrastructure required to direct the focus of the regulator are in place
- The regulator has infrastructures that support the effective use of knowledge, information and finance

Culture change programme

The key activities under this theme were delivered through the culture change programme, focusing on developing and delivering the key business functions of the Pensions Regulator:

- running efficient operations for levy, scheme returns and trustee information;
- effectively managing scheme risk;
- developing a medium term strategy and plans;
- developing e-channels for customer contact and internal use;
- providing customers and stakeholders with information, such as codes of practice and guidance;
- managing knowledge and information;
- transforming our people and embedding the new organisational set-up;
- delivering enabling IT; and
- relocating to new premises.

In our first year we have:

- built up the capability of our staff and information systems;
- delivered a medium term strategy and business plan for 2006/07, together with performance measures to track progress of the key activities set out in the business plan;
- under the oversight of the audit committee, refined and implemented a strategic risk framework;
- submitted six codes of practice to the Secretary of State for laying before Parliament;
- web-enabled the scheme return and reduced the amount of data requested;
- moved into a new office in order to reduce the long-term inefficiency and cost of working from several locations;

- engaged with suppliers for our data and records management and web portal software, commenced the building of our core *information pool* database, and updated the software we use to manage levy collection to match current PPF requirements;
- undertaken an organisation-wide staff development programme focusing primarily on personal development and risk-based decision making, and commenced planning for an accredited work-based learning diploma to support in particular the career path for regulatory case managers;
- begun to identify and develop our *knowledge management* needs, bringing together the definition of requirements to be met by new IT systems, and the development of records management policies and mechanisms to enable information and learning to be shared efficiently across the organisation;
- established a 'phase review' approach for the development and agreement of policy and associated processes to ensure quality of process mapping and policy implementation going forward; and
- set up a *programme management office* to oversee development projects in the Pensions Regulator, using PRINCE 2 and Office of Government Commerce Gateway methodologies as appropriate.

4.3
Key facts and figures

Under the *culture change programme*, a suite of performance measures and key indicators was developed in respect of the 2006-07 business plan, and systems put in place to deliver the management information upon which the reporting will be based.

A key goal in 2005-06 was to establish baselines from which changes in those measures that are continued into the 2006-07 business plan can be tracked. Inevitably this has been a year of transition, with new management information systems in development, and review and refinement of some of our initial targeting assumptions. We have made good progress in establishing baselines for a range of key measures that underpin our 2006-07 business plan.

Corporate risk management activity

Over the period of this report, the fund value of schemes that have received clearance is circa £22.9bn, with related FRS17 deficits of £5.6bn based on the most recent valuations at the time of clearance. This represents 4 per cent to 6 per cent of the total market FRS17 deficit estimated during the period. (The current estimate of the total market FRS17 deficit is between £50bn and £100bn). Whilst the related FRS17 deficit may not be eliminated as a result of a particular clearance, the trustees and employers will have agreed the mitigation required in view of the detriment to the pensions creditor resulting from the transaction.

Applications received	Clearance	269
	Withdrawals*	61
	Total	**330**
	Enquiries and exploratory cases handled	**1,112**
Clearance	**Clearances and withdrawal approvals* issued**	**148**
	Clearance refusals (insufficient mitigation)	**2**
	Cases not progressed to clearance/Type B* events	72
	Clearance work in progress at 31 March 2006	108

(* see *footnote 1* for explanation of terminology)

Clearance tracker survey

From December 2005, a regular survey of completed cases was implemented to measure overall satisfaction among applicants with the clearance process. It showed a cumulative average overall service satisfaction score of 8.7 out of 10 from respondents.

Notifiable events
(see footnote 2)

Notifiable events are defined by the Pensions Act 2004, which put in place a reporting framework designed to help the regulator focus on triggers that could potentially lead to serious risks to pension schemes. An analysis of notifiable events reported to the regulator in the period 6 April 2005–31 March 2006 was carried out (after the period of this report). There are 13 types of notifiable event. In total 391 events were reported of which 351 were categorised at the time of the analysis. The most common types of event reported were:

- changes in auditor or actuary
- transfer of more than 5 per cent of scheme assets or £1.5m
- changes in senior personnel
- decision to relinquish control of employer

Other regulatory activity

Trustee register *(see footnote 3)*
The Pensions Regulator's role includes compiling and maintaining a trustee register. We will generally refer to the register when deciding upon appointments made under sections 7 and 23 of the Pensions Act 1995. There were 54 trustees on the register (43 corporate and 11 individual) at the end of March 2006.

Trustee appointments made by the regulator
Seventy-five independent trustees (from the trustee register) have been appointed to funds with a total value of approx £1bn. 565 other trustee appointments have been made, which relate to individual member and third party appointments.

Legacy cases
Outstanding regulatory cases taken on when the regulator replaced Opra were reviewed during the year. By the end of March 2006, only 64 cases remained under investigation.

Key findings from our perceptions tracker survey

We have established baseline figures through our perceptions tracker survey for a number of measures that we will report on annually
(see footnote 4)

To what extent to do you agree or disagree with...

The Pensions Regulator is consistent in its approach to enforcing pension scheme regulation
69 per cent considered that we are consistent in our approach to enforcing pension scheme regulation

It works well with the Government to ensure that regulation is appropriate
52 per cent considered that our regulation is appropriate

It is proactive in reducing serious risks to pension scheme members' benefits
63 per cent of respondents considered that we were proactive in reducing serious risks to pension scheme members' benefits

Its actions are proportionate to the risk posed
50 per cent considered that our actions are proportionate to the risk posed

The Pensions Regulator is a trusted source of information
78 per cent agreed

How much, if anything, do you feel you know about the Pensions Regulator?

Know something about the Pensions Regulator (76 per cent)
Awareness of the Pensions Regulator roles and objectives (70 per cent)

How well or poorly do you think the Pensions Regulator undertakes these functions?

71 per cent agreed that the Pensions Regulator is good at providing codes of practice
66 per cent agreed that the Pensions Regulator is good at providing guidance

Thinking about when you contacted the Pensions Regulator, how satisfied or dissatisfied were you with them for supplying codes of practice/general guidance documents (separate questions)?

81 per cent were satisfied on contacting the Pensions Regulator for codes of practice or general guidance documents (average satisfaction for both questions)

Website activity	A total of 782,600 visits. Codes and guidance (88,811), Press releases (78,193), and 'about us' (55,057), were the most visited sections. Over 6,000 customers have subscribed to our 'news by email' service.
Customer Support Centre activity	Over 43,000 telephone calls were received, 94 per cent of which were answered in 20 seconds. The abandonment rate was 3.5 per cent. 95 per cent of emails and 86 per cent of letters received a response within five working days.
Codes of practice	We consulted on 10 codes of practice. Seven codes were completed and submitted to the Secretary of State for laying before Parliament, of which six were laid during the period of this report.

Footnote 1: Employers may decide to withdraw from multi-employer schemes, either as a result of a corporate transaction such as the sale of a subsidiary or as a result of a review of the pension provision to employees. Such withdrawals may constitute 'type A events' under the voluntary clearance procedure. For cessation events after 2 September 2005, the Pensions Regulator is required to approve withdrawal arrangements that modify the debt that becomes due to the Pension Scheme. Withdrawal arrangements are often connected to corporate transactions and are handled by the CRM practice as an ancillary activity to clearance. A 'type B event' is an event affecting an entity which is not financially detrimental to the ability of a defined benefit scheme to meet its pension liabilities. For further explanation of the clearance process, please refer to the guidance on our website.

Footnote 2: Refer to *Guidance on notifiable events* (published on our website at http://www.thepensionsregulator.gov.uk/codesAndguidance/guidance/notifiableevents/index.aspx) for information on the categories of notifiable event, and an explanation of the conditions that determine whether notification is required for each of the event types.

Footnote 3: Trustee appointments are made by staff where the matter is not contentious, for example, where the scheme has no trustees in place, a trustee is appointed 'to secure the proper administration of the scheme'. If the matter is contentious, appointments are made by the determinations panel.

Appointments made under section 7 of the Pensions Act 2004 generally relate to the appointment of trustees where the regulator is satisfied that it is necessary to do so, or to replace an existing trustee that has been removed (under s3) or is disqualified.

Footnote 3: ...continued	Appointments made under section 23 relate to the appointment of an independent trustee following the insolvency of the employer. Prior to the Pensions Act 2004 it was the duty of the insolvency practitioner to appoint an independent trustee to a defined benefit scheme. All such appointments are now referred to the regulator.
Footnote 4:	All questions used a 7 point scale (ie of extent of agreement, or rating of performance, or level of awareness/understanding, accordingly). Each figure quoted represents the percentage of respondents who gave a score between 5 and 7. The base used to calculate the percentage is all respondents who gave a score between 1 and 7, ie those who weren't able to express an opinion are excluded.

4.4
Looking ahead

Our focus in 2006-07 is defined by the *business plan* due to be published in summer 2006, and this in turn sits within a wider framework articulated in our *medium term strategy* which was published in April. Both documents will be available on our website.

In summary, we see our principal challenges over the next three years as being:

(i) to strengthen the funding of defined benefit schemes;
(ii) to improve the governance of work-based pension schemes; and
(iii) to reduce the risks to members of defined contribution pension schemes.

More details about these regulatory challenges, and our proposed response to them are set out in our *medium term strategy*.

To help us focus squarely on these challenges, our *business plan for 2006-07* is divided into four strategic themes. The first three map directly to the challenges, and the fourth theme relates to the way in which we develop our operational capability so as to support the delivery of risk-based regulation overall. Each theme translates a number of objectives into more specific indicators of success against which the outcomes we intend to secure in 2006-07 are be aligned.

The themes are:

Theme 1: Strengthen scheme funding

for which our medium term outcomes are:

DB schemes will have completed scheme specific funding valuations, and those with deficits will have agreed recovery plans. These will be based on:

- prudent assumptions for estimating the amount of assets needed to cover the liabilities as they fall due; and
- an appropriate recognition within the recovery plan of the risks to members taking account of what is reasonably affordable for employers.

Theme 2: **Improve the governance of work-based pensions**

for which our medium term outcome is:

There will be year-on-year improvement in the extent to which trustees demonstrate knowledge and understanding of the governance requirements for their schemes (as evidenced by surveys of knowledge and understanding and key aspects of governance).

Theme 3: **Understand and address the risks to DC schemes within the risk-based regulatory environment**

for which our medium term outcome is:

Trustees and others involved in running DC schemes (such as providers, administrators and employers) have a clear understanding of the significant risks inherent in such arrangements, especially in relation to administration, member awareness and investment, and how they should be mitigating them.

Theme 4: **Deliver effective risk-based regulation relevant to our environment and stakeholders**

for which our outcomes during 2006-07 are:

- The regulator has the right people, in the right numbers, with the right skills, knowledge and behaviours in the right place at the right time. A high commitment culture and an engaged workforce is built and maintained.
- The regulators' customers/market understand what the regulator expects of them and buy-in to the new regulatory approach.
- The regulated community consider the Pensions Regulator's risk-based regulation to be effective and in line with *Better Regulation Task Force* principles.
- Relationships with Government partners, the Pension Protection Fund, other regulators, the European Community and other external stakeholders are effective and maintained.
- Operational systems and processes to support organisational requirements, corporate governance and management controls are fit for purpose. Operational readiness is achieved.

More details, including the indicators against which we intend to assess our performance during the year, are available in our business plan for 2006-07.

4.5
Accountability and governance
The board

The current board structure, meeting with the requirements of section 1 of the Pensions Act 2004, comprises the chair, five non-executive members, the chief executive and three executive directors. Board members' appointment dates, terms of office, and committee membership are detailed in the table below. All members have been appointed to the board by the Secretary of State for Work and Pensions following open competition. Biographical information about each board member can be found on page 32.

Non-executive members receive a **non-pensionable** annual allowance of £10,000. The executive board members are members of the Pensions Regulator staff and receive salaries and pensions. Details of the remuneration of all board members are given in the remuneration report on page 47.

Details of board appointments and committee membership

Name	Date appointed	Date term expires	Committee membership
David Norgrove *Appointed as chair*	1 January 2005	1 January 2008	Non-executive (chair)
Non-executive members			
Laurie Edmans CBE	8 February 2005	7 February 2008	Audit, non-executive
Alan Pickering	8 February 2005	7 February 2009	Audit, non-executive
Chris Swinson OBE	8 February 2005	7 February 2009	Audit (chair), non-executive
Caroline Thomson	8 February 2005	7 February 2009	Remuneration (chair), non-executive
Roger Walsom	8 February 2005	7 February 2008	Remuneration, non-executive
Executive members			
Tony Hobman *Appointed as chief executive*	1 July 2004 *(designate)* 6 April 2005 *(confirmed)*	N/A	
Mark Eade	Interim appointment 25 February 2005 Confirmed in post 7 June 2005	31 May 2008	
June Mulroy	Interim appointment 28 February 2005 Confirmed in post 7 June 2005	31 May 2008	
Charlie Massey *(on secondment from DWP)*	1 September 2005	31 August 2008	
Richard d'Souza *(Interim)*	28 February 2005	30 September 2005	

Responsibilities of the board

Under the management statement and financial memorandum agreed between the Pensions Regulator and the DWP, the key responsibilities of the board are:

- policy: overseeing the regulator's strategic direction and making key decisions on policy;
- governance: ensuring the regulator is properly run as a public body and has effective internal controls; and
- ensuring that statutory and administrative requirements for the use of public funds are complied with.

Board meetings

The full board met monthly during the period from 6 April 2005 to 31 March 2006 (except for August). In addition, an 'awayday' meeting was held in December 2005 at which the board received briefings on operational and environmental developments, and discussed strategic issues, as part of the process of developing and reviewing the regulator's corporate plans.

Committees of the board

As required by the act, the board has established a non-executive committee. With the agreement of the board, the committee established two sub-committees: the audit committee and the remuneration committee. The remit and activities of the non-executive committee and its two sub-committees are summarised in the committee's report below.

Executive management team

The executive board members, chaired by the chief executive, met regularly through the year as an executive management team:

- to ensure strategic management of the organisation within the business plan and budget agreed by the board;
- to co-ordinate policy development initiatives, and provide a gateway function in respect of items to be referred to the board;
- to ensure effective management of strategic risk;
- to establish a performance management system and keep targets and performance against targets under review; and
- to propose an annual budget for approval by the board and to monitor expenditure against budget.

Culture change programme board

The *culture change programme* consists of a number of projects, managed using a *PRINCE 2* framework within the Office of Government Commerce (OGC) gateway process. A monthly programme steering committee maintains oversight, and the board of the Pensions Regulator receives quarterly progress reports. However, decisions on progress through the gateways and approval of funding for each stage, are made by the *culture change programme board*.

The programme is primarily funded by the DWP and the department recoups these costs via the levy charge. The total funds allocated to this programme (which extends into 2006-07) by the DWP, are £13.7m. The actual programme budget spent to 31 March 2006 was £5.0m. See also the *Financial review*, page 40.

Details of programme scope and activities are reported under *Theme 5* on page 19 and under *Developing the organisation* at page 11.

The *programme board* is chaired by the chief executive. Its members include:

- the regulator's executive management team
- the programme manager
- the chair of the regulator's audit committee
- senior officials from the DWP

Tripartite meetings

A tripartite memorandum of understanding was signed between the regulator, the DWP and the Pension Protection Fund. Quarterly meetings were held to discuss joint working, attended by senior officials from each of the three organisations.

Annual report of the Pensions Regulator non-executive committee

1 Functions of the non-executive committee

Under section 8 of the Pensions Act 2004 ('the Act'), the Pensions Regulator must establish a non-executive committee. The committee is required by section 8(5) to prepare a report on the discharge of its functions for inclusion in the regulator's annual report.

The committee's functions are set out in section 8(4):

(a) the duty to keep under review the question of whether the regulator's internal financial controls secure the proper conduct of its financial affairs;
(b) the duty to determine under paragraph 8(4)(b) of schedule 1 of the Act, subject to the approval of the Secretary of State, the terms and conditions as to remuneration of any chief executive appointed under paragraph 8(4)(a) of that schedule.

2 Activities of the non-executive committee in 2005-06

The committee, as permitted by section 8 sub-paragraphs (7) and (8), chose to establish two sub-committees: an audit committee to which it delegated its function at section 8(4)(a) and a remuneration committee to which it delegated its function at section 8(4)(b).

Under paragraphs 18 and 20(1)(c) of schedule 1 of the Act, which give the board the power to determine its own statutory procedures and to authorise any of its committees to exercise any of its functions, the board and the non-executive committee agreed additional, non-statutory areas of responsibility to be included in the terms of reference for each sub-committee.

The committee itself met twice in 2005-06 to receive reports from its sub-committees, and to review the terms of reference of those sub-committees.

Details of membership of the committee and its sub-committees are on page 26.

Reports from each of the sub-committees are given below. However, there is no report in respect of the non-executive committee's duties under section 8(4)(b) of the Act. This is because those duties do not relate to the first chief executive of the Pensions Regulator, but only to subsequent appointments.

3 Report of the activities of the audit committee in 2005-06

Terms of reference for the audit committee were agreed by the board and the non-executive committee covering both the statutory function delegated from the non-executive committee and additional areas of responsibility delegated by the board.

The audit committee met on six occasions in 2005-06:

- to consider its terms of reference;
- to review the annual accounts for Opra for the period 2004-05 and recommend their approval to the board;
- to approve an internal audit strategy for the year, and advise on the development of the internal audit programme for 2006-07;
- to advise the executive management team on the approach to management of strategic risk and to keep the risk schedule under review;
- to approve the external audit strategy for 2005-06; and
- to receive reports from the internal auditors reviewing areas of the business as agreed under the internal audit strategy.

Subsequently, the committee met in May and June 2006, to receive outstanding reports under the 2005-06 internal audit strategy, and to review the statement on internal control and the regulator's annual report and accounts.

Strategic risk management

The committee devoted significant time to discussion of the approach to strategic risk management. The internal auditors advised the management team and the committee in developing the approach. They were also present at committee meetings during the year where the committee reviewed the risk schedule in some detail and were able to question management as to the ratings given to each risk, and progress in mitigating action. The committee noted management's comprehensive and ready response to its queries, from which it was able to derive confidence that both the assessment of key strategic risks was right, and that effective monitoring and reporting systems were in place to give the executive directors an appropriate level of control over the management of risk.

Internal audit strategy

The committee agreed a programme of audits for the year covering 13 areas of the business. Given the process of organisational development in the regulator's first year of operation, a number of key business functions were in a state of significant change during the year. However, the committee subsequently agreed to defer two audits, and the committee was able to review all 11 of the audit reports received prior to its approval of the annual report and accounts and the statement on internal control. It was noted that, of the 11 reports received, nine gave a substantial level of assurance and two limited assurance.

The committee will continue to give close attention to internal audit matters in 2006-07, in particular to monitoring progress in implementation of audit recommendations arising from the 2005-06 audits.

4 Report of the activities of the remuneration committee in 2005-06

Terms of reference for the remuneration committee were agreed by the board and the non-executive committee, covering both the statutory function delegated from the non-executive committee and additional responsibilities delegated by the board. However, the committee did not exercise its statutory function during the year, for the reasons given above.

The remuneration committee met on three occasions in 2005-06:

- to consider its terms of reference;
- to review the chief executive's objectives and performance, and advise the Secretary of State in respect of his determination (under Paragraph 8(3)(b), schedule 1 of the Act) as to the chief executive's remuneration; and
- to review the regulator's staff reward strategy.

The chief executive's objectives for the year were set by the chair of the Pensions Regulator and agreed with the remuneration committee. The committee subsequently (at its meeting in June 2006) considered the chief executive's performance and the amount of his annual bonus and made a recommendation to the Secretary of State.

Information on executive remuneration is given in the *remuneration report* on page 47.

David Norgrove
chair, non-executive committee,
the Pensions Regulator
10 July 2006

Board members

David Norgrove, chair of the Pensions Regulator board

Spanning both the public and private sectors, his career began at the Treasury, where he started as an economist. His time there included two years on secondment to the First National Bank of Chicago, and he was private secretary to Prime Minister Margaret Thatcher from 1985 to 1988. He joined Marks & Spencer in 1988, holding various senior positions before being appointed to the board in 2000. While at Marks & Spencer, he was chair of the pension fund trustees from 2000 until his retirement in 2004. In January 2005 he was appointed as the first chair of the Pensions Regulator.

Laurie Edmans CBE (non-executive)

Began his financial services career in administration and sales, and is currently the corporate development director of Aegon UK. He has also chaired the Pension and Savings Committee at the ABI. He was an Opra board member, and joined in 2002 when the process for change towards a new pensions regulator was beginning.

Alan Pickering (non-executive)

Began his career as a junior railway clerk. Joined EETPU in 1972, working for 20 years on a range of members' interests, including pensions and personal finance. He joined Watson Wyatt as a partner in 1992. He specialises in occupational pension schemes, and from 1999 to 2001 was chair of the NAPF and from 2001 to 2004 chair of the European Federation for Retirement Provision. He is currently on the board of the Pre-Retirement Association and is chair of the Plumbing Industry Scheme. In 2002 the DWP commissioned him to report on *'A Simpler Way to Better Pensions'*, which recommended the establishment of a 'new kind of regulator'.

Chris Swinson OBE (non-executive and chair of the audit committee)

Formerly senior partner of BDO Stoy Hayward. He served as a member of the ICAEW council and was president from 1998 to 1999. As chair of the Regulation Review of the accountancy profession between 1995 and 2000 he managed the development of proposals for regulating the profession, which were then implemented. Currently works as an expert witness in financial cases.

Caroline Thomson (non-executive and chair of the remuneration committee)

Commissioning editor finance and industry then head of corporate affairs at Channel 4 from 1984 to 1995, she became deputy director of BBC World Service before becoming director of policy and legal at the BBC in 2000. She is a trustee of the BBC pension scheme, and is currently director of strategy leading the BBC Charter Review team.

Roger Walsom (non-executive)

Formerly a partner at Ashurst, the leading firm of City solicitors. He is currently a consultant to the firm on specific projects. His career has spanned the worlds of commercial and financial services, including mergers and acquisitions, financing, insolvency, insurance, employment and other issues. He is also a non-executive director of St James's Place plc and INVESCO Income Growth Trust plc.

Executive management team

Tony Hobman, chief executive of the Pensions Regulator

Has held a number of senior appointments within the financial services arena. He spent 20 years with Barclays Bank, holding a number of key roles in marketing, project and change management and customer service. In 1996 he joined ProShare as head of investor services and was promoted to chief executive in 1999. From 2000 to 2001 he was chief executive of Money Channel plc. In 2002 he was appointed as chief executive of the Occupational Pensions Regulatory Authority (Opra) and in July 2004 chief executive designate of the Pensions Regulator. In April 2005 he began work as the first chief executive of the Pensions Regulator.

Mark Eade, executive director for business support

A business graduate and qualified accountant, trained in private practice and industry. He has worked in various roles as financial controller and company secretary, management consultant, director of finance and commercial accountant. Began work in the public sector in 1992 as a deputy regional director of finance for South Western Regional Health Authority, and joined the NHS Executive in 1994 undertaking a variety of roles including major change management projects and interim finance director roles with several years' experience at director/board level for regulatory non-departmental public bodies.

Charlie Massey, executive director for strategic development

Strategic development director at the Pensions Regulator. Before joining the Pensions Regulator, he was a senior civil servant in the Department for Work and Pensions, responsible for heading up the division that created the Pensions Regulator and the Pension Protection Fund. He previously worked in the prime minister's Strategy Unit where he led projects on drugs and childcare, and in HM Treasury, where he had responsibility for the Post Office. Before that he worked in a number of roles in the Department of Social Security – from leading a fraud team in East London, to working as private secretary to one of the Department's Ministers.

June Mulroy, executive director for delivery

A psychologist and chartered accountant, she has worked in corporate and banking treasury for over 17 years as a dealer/risk analysis specialist and consultant. Recognising the strong element of change management in all previous roles, she moved into the NHS and worked in two acute Trusts, one of which was the then 'flagship' of the NHS, Chelsea and Westminster Hospital. Since then she has worked in Switzerland and Paris, the latter being for the UN in UNESCO. She has a personal commitment to the need for life-long learning, is a governor of Middlesex University and is studying for an OU degree.

The determinations panel

Under section 9 of the Pensions Act 2004, the regulator must establish a determinations panel. The function of the panel is to determine whether to exercise a regulatory function that is reserved to the panel. In addition, the regulator is able to submit a case to the panel where it wishes the panel to make a determination. On some matters, external applicants may ask the panel to make a determination. Where a determination is disputed, parties may appeal to the Pensions Regulator Tribunal, an independent body, established under section 102 of the Act.

Membership

Appointments were made following open competition. The chair of the panel is selected and appointed by the board of the regulator. Panel members are nominated following selection by the chair of the panel and appointed by the board of the regulator. Panel members receive a daily allowance in respect of time devoted by each member to the work of the panel over the year. The rate for the chair is £650 per diem, and for members is £500 per diem. Remuneration paid during the period of this report is as disclosed in the *remuneration report* on pages 47 to 52.

Determination panel – report of activity during the year

The panel has heard 11 cases in the period 6 April 2005–31 March 2006:

Removal of trustee (1)	Winding up order (1)
Bulk winding up order(1)	Suspension of trustee (1)
Cash equivalent transfer values (3)	Normal appointment of trustee (2)
Emergency appointment of trustee (2)	

The cases decided this year have been largely those where an investigation began under the powers of the predecessor body, Opra. They may not prove to be wholly representative of the cases that will come for decision from the Pensions Regulator.

During the year the panel have undertaken an induction and training programme covering the work of the Pensions Regulator with emphasis on the regulatory risk framework, funding and powers and responsibilities of trustees and employers, as well as concentrating on the adjudicative process.

They have drafted their own procedures and consulted on them. The procedures establish the panel as a decision-making body operating separately from the Pensions Regulator under principles of absolute fairness to all parties affected by any decision they make. Decisions, fully reasoned, will be made only on the evidence presented with all affected parties having full opportunity to question and comment. The panel is supported in its determinations by an independent lawyer and by an administrative team working quite separately from any other staff of the Pensions Regulator; they only will be present or involved in the determinations made by the panel.

John Scampion CBE
chair

Complaints against the regulator

Complaints and enquiries about the way the Pensions Regulator administers regulatory cases and deals with its customers are handled initially by our customer support team and regulatory staff, and most are resolved satisfactorily. For those not resolved, we operate a three-stage formal procedure:

- the complaint is investigated by the corporate secretary;
- if unresolved, the complaint is reviewed by the regulator's chair; and
- if still unresolved, the complaint can be referred to the Pensions Regulator's independent complaints adjudicator.

The Pensions Regulator also comes within the jurisdiction of the Parliamentary Commissioner for Administration.

In 2005-2006, the Pensions Regulator received 15 formal complaints (15 in 2004-2005 by Opra). Two of these were referred by the complainant to our independent complaints adjudicator, and her summary report is below.

No cases were referred to the Parliamentary Commissioner for Administration during the year.

Regular reports are made to senior management. The board has not received a report on complaints in the last year. However, we intend to carry out a formal review of our complaints procedure in 2006 and any proposals arising from that review will be considered by the board.

Report of the independent complaints adjudicator for the Pensions Regulator 2005-06

In 2005-06 I was asked to investigate two complaints against the Pensions Regulator.

Complaint 1

This was a complaint that had originally been made to Opra, the predecessor organisation. The complainant renewed his complaint after the formation of the Pensions Regulator, on the basis of his expectation that the regulator's new powers should be exercised to support his complaint. In essence the complainant's employer wished to bring forward the complainant's retirement at a time when the pension scheme was to be wound up – with a potential impact on his pension.

Throughout the length of the complaint, both Opra and subsequently the Pensions Regulator had directed the complainant to the correct sources of help which were the Pension Scheme's own Independent Dispute Resolution procedure, the Pensions Advisory Service and the Pensions Ombudsman. The complainant had approached all of these organisations but remained dissatisfied.

At an earlier date, following a report from the Pension Scheme's actuary, Opra had conducted an investigation into this pension scheme, but found only minor breaches of pensions legislation. All of the breaches had been rectified and the investigation was closed. However, the complainant remained dissatisfied with the extent of the regulator's interventions in respect of this pension scheme.

As a result, the complainant took his complaint under the regulator's complaints procedure to the chair. I found that the later handling of the complaint was thorough and clear, explaining the reasons why the regulator had taken the decisions it did. However, the earlier handling of the complaint had involved some unnecessary delays and lack of clarity in communication, and I made several recommendations. I suggested that more attention should have been given to explaining the very clear division between the role of the regulator and the other sources of help including the Pensions Ombudsman, and to providing the fullest possible responses as soon as the complaint materialises. In addition, complainants do need to be given a clear explanation as to why the details of the regulator's investigations into pension schemes must remain confidential.

While there were some communication weaknesses, I did not find that there was anything serious enough to constitute maladministration.

Complaint 2

The second complaint concerned a long dispute between the complainant and the trustees of his pension scheme, the substance being that the trustees of the pension scheme had changed the benefit structure without notifying scheme members, and that contributions that should have been made on the complainant's behalf were not made in spite of directions to the trustees from the Pensions Ombudsman to that effect.

The regulator had confirmed that it had no remit in respect of disputes between an individual scheme member and scheme trustees. However, having received an earlier report about this pension scheme relating to alleged non-payment of contributions, the regulator wished to be reassured that there was no risk to other members, and so undertook a second investigation into the scheme. This investigation found nothing amiss and this information was conveyed to the complainant. The complainant was unable to accept that this second investigation was concerned with the wider issue of the scheme's regulatory compliance, rather than the individual grievance that he had asked the regulator to investigate.

The advice that had been offered by the other agencies and sources of help with whom the complainant was in contact, and with which the regulator concurred, was that he should pursue the matter of the outstanding payments through the County Court. This he appeared not to have done. In explaining to the complainant the actions it was able to take and those that it could not in its role as a regulator, I found the regulator to be very attentive to his plight, offering very full explanations and always referring the complainant to the correct sources of help. I could find nothing to fault in the handling of this complaint.

Elizabeth Hodder
Independent complaints adjudicator
May 2006

Freedom of Information

In the period 6 April 2005–31 March 2006, the Pensions Regulator received 25 requests for information under the Freedom of Information Act 2000, and one subject access request under the Data Protection Act 1998.

The Freedom of Information Act 2000 (FOIA) has been in force since January 2005 and gives people a general right of access to information held by or on behalf of public authorities, promoting a culture of openness and accountability across the public sector.

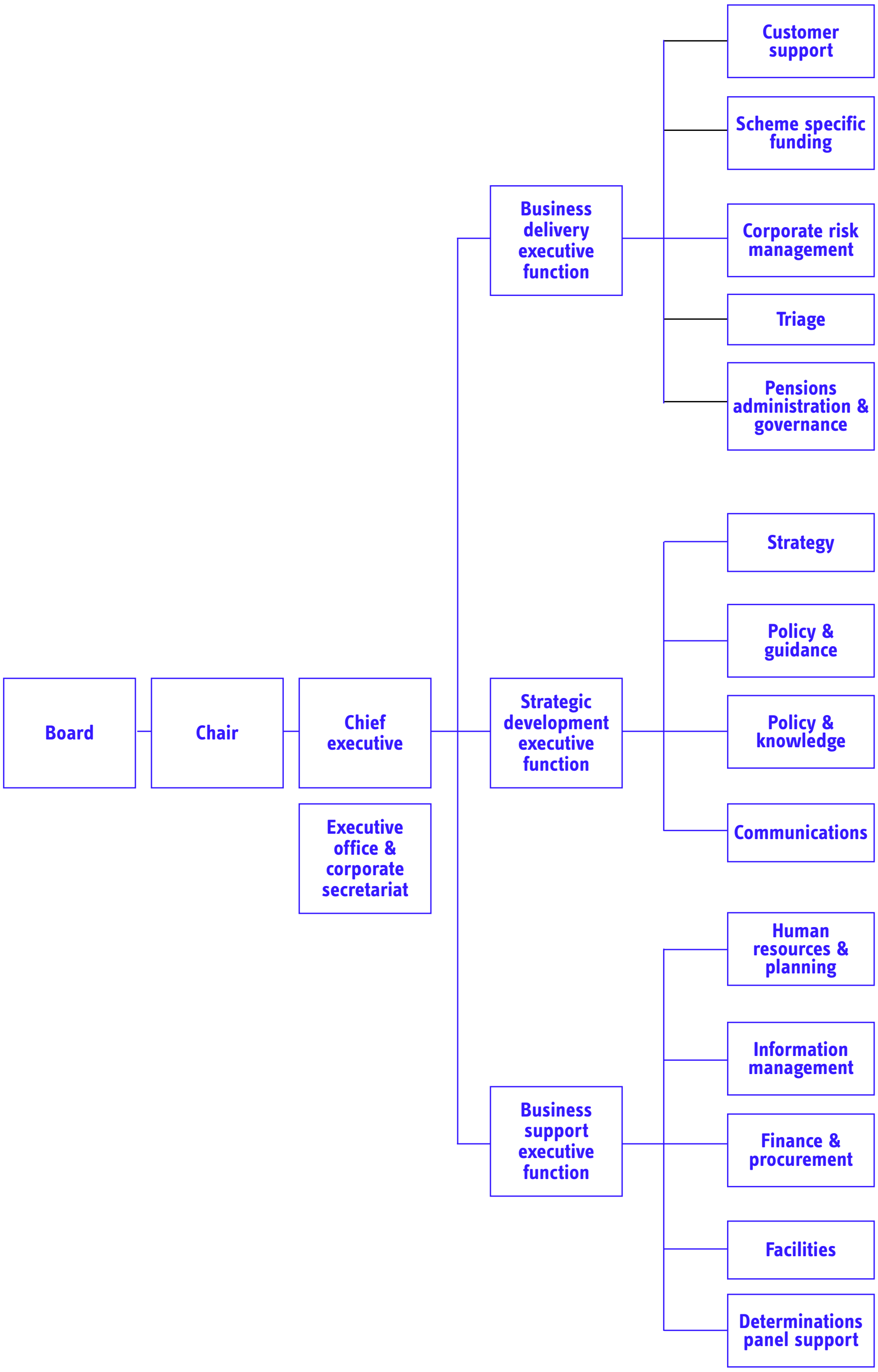
We endeavour to release information where possible and appropriate, however much of the information gathered as part of our regulatory functions is 'restricted information' as defined by the Pensions Act 2004 and is prohibited from release, and thereby exempt under FOIA section 44 from disclosure.

Only one request for a formal review of our decision not to disclose information (in relation to a request concerning a clearance case) was received during the period of this report. We upheld the exemptions applied and explained in further detail the reason for maintaining those exemptions and the public interest test we had applied.

FOI requests

- In 38 per cent of cases we disclosed the information, in some instances it was in summary or redacted (edited) versions
- In 16 per cent of cases we did not hold the information requested
- In 38 per cent of cases we did not disclose the information requested; this was due to
  - absolute exemptions being applied
  - the regulator did not consider it to be in the public interest
  - requests for details of the Pensions Regulator's investigations were not released as to do so would prejudice its ability to conduct investigations effectively and therefore to carry out its regulatory functions
- 8 per cent of cases were transferred to another organisation

Organisation structure (at 31 March 2006)



Human resources

Relations with employees

The Pensions Regulator gave a high priority to the provision of information to, and consultation with, employees. The Public and Commercial Services Union (PCS) was actively involved in staff and business matters, and regular meetings were held with senior management and PCS throughout the year. Board and management team minutes were available to all staff, team meetings were held regularly and an in-house magazine was issued to all staff. Through our staff survey we measured and saw improvements in staff satisfaction and morale during the year.

Equal opportunities

The Pensions Regulator complied with equal opportunities legislation and followed Government policy in relation to disabled employees. The Pensions Regulator was committed to providing equality of opportunity for those applying for jobs and internal selection and staff development opportunities. We seek to offer a fair and accountable service in our day-to-day dealings with the public, employees and future employees.

Learning and development

Developing staff skills, knowledge and behaviours in line with our values and business needs was a top priority for the organisation. Our competency and objective-based performance development approach helped individuals and their managers to define and action development needs.

Community activity

Following a positive response in the staff survey, a *community team* was established to look at what the Pensions Regulator could do to support the community and voluntary organisations. The aim is to find initiatives where staff skills and enthusiasm can benefit charities and the staff involved can gain skills which will benefit both themselves and the Pensions Regulator. A number of events organised by staff during the year raised approximately £990, which was donated to the *National Society for the Prevention of Cruelty to Children* and the *Martlets Hospice*.

Environment

The Pensions Regulator is conscious of the need to take account of sustainability concerns and environmental impact. Although an environmental policy was not in place, a number of activities were undertaken during the year with the aim of minimizing environmental impact:

- Following installation of new computers, the previous equipment was donated to the computer aid scheme (**www.computeraid.org**);
- Following the move to new accommodation, furniture from our previous offices was either sold to staff or to businesses for re-use;
- The carpet in the new accommodation is manufactured by a company using a mill that is powered using 100 per cent renewable wind generated electricity and a minimum of 80 per cent of the yarn in the product is recycled;
- The installation of presence detectors in the open plan office area ensures that lights are not left on in areas where there are no staff;
- The photocopiers have been networked enabling double sided printing; and
- All paper that is shredded (for security reasons) is recycled to make household paper products.

4.6
Financial review

Form of accounts

The accounts have been prepared in a form directed by the Secretary of State for Work and Pensions, with the approval of the Treasury, in accordance with paragraph 27 of schedule 1 of the Pensions Act 2004.

Results for the period

The financial statements are set out on pages 55 to 69.

Opra was funded by grant-in-aid from the Department for Work and Pensions. The net liabilities at 5 April 2005 of £3.3million were transferred to the Pensions Regulator on 6 April 2005. The Pensions Regulator is also funded by grant-in-aid from the Department for Work and Pensions, and it is expected that the liabilities inherited from Opra will be funded by grant-in-aid in future years.

The accounting policies under which income and expenditure are recognised are set out in note 2 to the accounts.

In the period ended 31 March 2006, the Pensions Regulator's income of £29.5 million exceeded its expenditure of £27.4 million, to produce an operating surplus on ordinary activities of £2.1 million. The surplus for the period of £2.5 million (after interest receivable of £151,000, tax payable, losses on disposals of fixed assets, transfers from the capital grant reserve and notional interest receivable) has been transferred to the general reserve as shown in note 15 to the accounts.

The income and expenditure figures for the period ended 31 March 2006 both included £4,938,468 which is directly attributable to the culture change programme described in Section 4.2 of the annual report (notes 3 and 7 to the accounts).

Staff costs in the period ended 31 March 2006 were £4.7 million higher than in the prior period due to a change in staff mix required to meet the Pensions Regulator's remit as compared to Opra's, redundancy costs associated with the transition from Opra to the Pensions Regulator, and increased temporary staff costs. £1.1 million of the £4.7 million increase is directly attributable to the culture change programme.

On an aggregate basis, other operating charges have remained at a similar level over the two periods. However, as shown in note 7, consultancy, contracted out and other professional services costs in the period ended 31 March 2006 were £3.0 million higher than in the prior period with in excess of 100 per cent of the increase, £3.7 million, being directly attributable to the culture change programme. This increase in other operating costs is offset by a provision release of £297,000 in 2005-06 compared to a provision charge of £3,324,000 in 2004-05.

There have been no significant events occurring since the period end.

Levies account

For the period ended 5 April 2005, Opra was required by statute to prepare a levies account. The Pensions Act 2004 does not require the Pensions Regulator to prepare such an account.

During the period ended 31 March 2006, the Pensions Regulator invoiced and collected levies on behalf of the Pension Protection Fund (PPF initial levy) and the Department for Work and Pensions (the Pensions Regulator general levy and PPF admin levy), which will be reported in the audited financial statements of those organisations. The following unaudited figures summarise key facts and figures in respect of activity undertaken during the period. None of these figures features in the audited accounts of the Pensions Regulator. The total levies due to be invoiced during the period were £186.3 million (£141.7 million PPF initial levy, £31.6 million the Pensions Regulator general levy and £13.0 million PPF admin levy.) By the period end, the Pensions Regulator had ensured that all these invoices were issued.

During the period, the Pensions Regulator collected £132.0 million in respect of levies of which £0.9 million had not been allocated by levy type at the period end. The £131.1 million collected and allocated during the period comprised £104.4 million (PPF initial levy), £17.7 million (the Pensions Regulator general levy) and £9.0 million (PPF admin levy.) These collections represented respectively by value 73.7 per cent, 56.0 per cent and 69.2 per cent of the amounts invoiced.

From 31 March 2006 to 31 May 2006, the Pensions Regulator has collected in aggregate an additional £23.1 million of levies invoiced during the period and by value at this date levy collection is consequently 83 per cent complete in respect of 2005-06.

Prior to onward transmission to the Department for Work and Pensions or the Pension Protection Fund, the Pensions Regulator places levies received and unallocated cash receipts in respect of levies on overnight deposit. Any interest earned is paid over to the relevant recipient with levy payments. Total interest earned in 2005-06 was £0.3 million of which £269,000 had been paid over by 31 March 2006.

As at 31 March 2006 total levies paid across to either the Department for Work and Pensions or the Pension Protection Fund were £124.4 million and at period end, the Pensions Regulator held cash balances still to be paid over to the Department for Work and Pensions and the Pension Protection Fund of £1.2 million and £5.5 million respectively.

Going concern

The balance sheet at 31 March 2006 shows net liabilities of £155,000. This reflects the inclusion of liabilities falling due in future years which, to the extent that they are not to be met from the Pensions Regulator's other sources of income, may only be met by future grants or grants-in-aid from the Department for Work and Pensions, as the Pensions Regulator's sponsoring department. This is because, under the normal conventions applying to Parliamentary control over income and expenditure, such grants may not be issued in advance of need.

Grant-in-aid for 2006-07, taking into account the amounts required to meet the Pensions Regulator's liabilities falling due in that year, has already been included in the Department's estimates for that year, which have been approved by Parliament, and there is no reason to believe that the Department's future sponsorship and future Parliamentary approval will not be forthcoming. It has accordingly been considered appropriate to adopt a going concern basis for the preparation of these financial statements.

Tangible and intangible fixed assets

The Pensions Regulator occupies only short leasehold property and does not have any finance leases. Rent payable for accommodation has been charged to operating charges (notes 7 and 12 to the accounts.)

Fixed assets are valued at current replacement cost as detailed more fully in note 2e to the accounts.

Payments to suppliers

The Pensions Regulator is committed to the prompt payment of bills for goods and services received. Payments are normally made as specified in contracts. If there is no contractual provision or other understanding, invoices are deemed to be due to be paid within 30 days of the receipt of the goods or services, or presentation of a valid invoice or similar demand, whichever was later. During the period ended 31 March 2006, by volume the Pensions Regulator paid 87 per cent of invoices in line with this policy and by value in excess of 90 per cent of invoices were paid in line with this policy.

Audit

The Pensions Act 2004 requires the Pensions Regulator's accounts to be certified by the Comptroller and Auditor General (C&AG). The audit fee for 2005-06 was £39,000. No non-audit services were provided during the period.

Accounting officer responsibilities

The accounting officer confirms:

- there is no relevant audit information of which the auditors are unaware;
- he has taken all the steps he ought to ensure the auditors are aware of all relevant audit information; and
- he has taken all the steps he ought to establish that the Pensions Regulator's auditors are aware of the information.

David Norgrove

David Norgrove
chair, the Pensions Regulator
10 July 2006

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

5 Statutory accounts and notes to the accounts

5.1 Statement of the board's and chief executive's responsibilities

Under paragraph 27 of schedule 1 to the Pensions Act 2004, the Pensions Regulator is required to prepare a statement of accounts in the form and on the basis determined by the Secretary of State with the approval of the Treasury. The accounts are prepared on an accruals basis and are required to give a true and fair view of the Pensions Regulator's state of affairs at the period end and of its income and expenditure and cash flows for the financial period.

In preparing the accounts, the Pensions Regulator was required to:

- observe the accounts direction issued by the Secretary of State, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards have been followed in accordance with the Financial Reporting Manual and disclose and explain any material departures in the financial statements; and
- prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the entity will continue in operation.

The chief executive is the accounting officer for the Pensions Regulator. His relevant responsibilities as accounting officer, including propriety and regularity of the public finances and for the keeping of proper records, are set out in the Non-Departmental Public Bodies Accounting Officers' Memorandum issued by the Treasury and published in Government Accounting.

David Norgrove
chair, the Pensions Regulator
10 July 2006

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

5.2
Statement on internal control

Scope of responsibility

The Pensions Regulator is built on the foundations of Opra and has implemented processes for internal control based initially on those operated by Opra. Many of these processes have been reviewed and developed during 2005-06, and in addition, the Pensions Regulator's wider range of powers has necessitated the development of new business processes and associated controls.

As accounting officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of the Pensions Regulator's policies, aims and objectives, while safeguarding the public funds and departmental assets for which I am personally responsible in accordance with the responsibilities assigned to me under the Non-Departmental Public Bodies Accounting Officers' Memorandum issued by the Treasury and published in Government Accounting.

The Pensions Regulator is accountable to the Department for Work and Pensions, within a framework set out in a Management Statement and Financial Memorandum agreed between the regulator and the Department on 9 December 2005.

The Department for Work and Pensions receives reports on performance, finance, and risk, primarily through regular review meetings, held in 2005-06 between myself and a member of the Department's pensions protection and stewardship team. In addition the chair of the regulator, David Norgrove, has met quarterly with the managing director – strategy and pensions, and the chair and myself, have also met quarterly with the Minister for Pensions Reform.

The purpose of the system of internal control

The system of internal control in the Pensions Regulator is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the Pensions Regulator's policies, aims and objectives, to evaluate the likelihood of those risks being realised, and the impact should they be realised, and to manage them efficiently, effectively and economically.

The system of internal control has been in place in the Pensions Regulator for the period ended 31 March 2006 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

Capacity to handle risk

The Pensions Regulator has taken a positive approach to risk management and adopted a risk management approach, which it felt was entirely appropriate to its role and remit. The Pensions Regulator's executive management team devoted considerable attention to the identification and assessment of strategic and operational risks in the early part of the period, in consultation with the audit committee and internal auditors. A risk advisor was nominated to assist in keeping the strategic risk schedule under review in consultation with directors and heads of business units, as set out in the following section.

The risk and control framework

The purpose of risk management is to enable the mitigation and monitoring of the risks that have been identified. The process was developed as outlined above, and the approach to risk management, and the risk schedule, was reviewed by the audit committee at each of its meetings during the period. The approach adopted includes a risk management policy and guidance document, schedules of strategic risks (analysed by the directorate and business unit and giving a red/amber/green rating to each risk) and mitigating actions (owned by business unit heads and subject to monthly reviews by directors with their heads of business units), a nominated risk advisor, and quarterly review of the risk schedule, actions, and ratings, by the executive management team and the audit committee.

As at 31 March 2006 there were nine strategic risks identified in the risk schedule. A director was assigned to be the owner of each strategic risk, and was responsible for:

- identifying or proposing actions to mitigate the risk;
- making recommendations as to the impact of mitigating actions on the inherent risks; and
- reviewing the risk each month.

Some of the risks are fairly generic to any organisation like the Pensions Regulator, such as those relating to business continuity, staffing or project management. Others were specific to our core business or to changing circumstances, such as receiving a whistleblowing report but failing to take the appropriate action to prevent pension benefits being misappropriated or misused.

At team level managers are encouraged to build risk mitigation actions into their workplans, and training on risk management is being/has been provided. Further work is underway to ensure auditable checking processes are in place for each team.

Review of effectiveness

As accounting officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control was informed by the work of the internal auditors and the executive managers within the Pensions Regulator who had responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I was advised on the implications of the result of my review of the effectiveness of the system of internal control by the board, and the audit committee.

Given the intensity of organisational change throughout the year, the Pensions Regulator's internal auditor was unable to complete the full programme of work agreed by the audit committee by the end of March. However, the programme was completed shortly after this and the audit committee was able to review the outstanding audit reports at meetings in May and June 2006. Two of the programme of 13 audits were deferred with the agreement of the audit committee, to the 2006-07 audit programme. Of the remainder, nine gave substantial assurance and two limited assurance.

In considering the internal auditor's reports, the Pensions Regulator's audit committee received assurances that the recommendations made had been or are being implemented. The audit committee also regularly reviewed, and were satisfied by, the operation of the risk management system.

A process is in place to ensure that the agreed management response to internal audit recommendations is monitored by the executive management team, progressed effectively, and progress reported regularly to the audit committee.

The board has been kept informed of the audit committee's regular review of risk, but did not carry out its own formal review during the year. The intention is that the board will review risk on an annual basis going forward.

Significant internal control problems

No significant internal control problems arose during the period to 31 March 2006.

In setting the programme of internal audits for the period, priority was given to those areas of the business where risk was rated highest. In particular, information security and clearance activity were identified as key risk areas. Secure business processes were put in place in the clearance teams, and reviewed by internal audit, early in the year, and information security issues have been kept under review by a security forum. In addition, a revised staff code of conduct has been issued with new processes to manage conflicts of interest, and confidentiality.

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

5.3 The Remuneration Report

The Remuneration Committee

Details of the activities of the Remuneration Committee for the period ended 31 March 2006 are set out in section 4.5 of the annual report. Section 4.5 also includes details of the composition of the board of the Pensions Regulator. As also shown in section 4.5, the Remuneration Committee consists of two non-executive board members, Caroline Thomson (chair) and Roger Walsom.

Remuneration Policy

In accordance with part 1 of schedule 1 of the Pensions Act 2004, the current and future remuneration of all non-executive members of the board of the Pensions Regulator (including the chair) is determined by the Secretary of State for Work and Pensions.

The current (initial) remuneration of the chief executive is determined by the Secretary of State for Work and Pensions in accordance with part 2 of schedule 1 of the Pensions Act 2004. Subsequent remuneration is determined by the Secretary of State based on recommendations from the Remuneration Committee of the Pensions Regulator.

The current and future remuneration of the other executive members of the board of the Pensions Regulator is determined by the Pensions Regulator and approved by the Secretary of State for Work and Pensions.

Additionally the Secretary of State for Work and Pensions determines the fees of the Determinations Panel for current and future periods.

Bonus payments to a current maximum of 20 per cent of base salary are payable to all executive members of the board (including the chief executive) based on performance. Non-executive members of the board, the chair and the Determinations Panel are not entitled to receive any bonus from the Pensions Regulator.

The Remuneration Committee assesses the performance of the chief executive against agreed objectives and makes a recommendation to the Secretary of State for Work and Pensions as to whether any performance-related bonus is payable. The chief executive reviews the performance of the executive members of the board in conjunction with the chair. Any bonuses payable are approved by the Secretary of State for Work and Pensions.

Service contracts

The length of service contracts is determined by the Secretary of State for Work and Pensions for non-executive members of the board (including the chair) and the chief executive. The length of service contracts for other executive members of the board and for members of the Determinations Panel is determined by the Pensions Regulator and approved by the Secretary of State for Work and Pensions.

Details of service contracts are given in section 4.5 of the annual report.

The notice periods of the board members' contracts and the amounts payable for early termination of board members' contracts are set out in the table below:

Name	**Notice period**	**Early termination payable to employee (net pay plus accrued bonus if applicable)**
David Norgrove *(Chair)*	3 months from employee, 6 months from employer	Maximum of 6 months' pay
Non-executive members		
Laurie Edmans CBE	1 month	1 month
Alan Pickering	1 month	1 month
Chris Swinson OBE	1 month	1 month
Caroline Thomson	1 month	1 month
Roger Walsom	1 month	1 month
Executive members		
Tony Hobman *(Chief executive)*	3 months from employee, 6 months from employer	Maximum of 6 months' pay
Mark Eade	3 months	3 months
June Mulroy	3 months	3 months
Charlie Massey	3 months	3 months

Other than as shown above, the Pensions Regulator would have no other contractual liability upon termination of a board member's appointment.

During the period ended 31 March 2006, no payments in respect of early termination have been made to individuals who served at any time on the board of the Pensions Regulator during the period or who served as authority members of Opra.

Information subject to audit

Remuneration and pension entitlements

The following section provides details of the remuneration and pension interests of the board of the Pensions Regulator, the members of the Determinations Panel and the members of the Occupational Pensions Regulatory Authority.

'Salary' includes gross salary; performance pay or bonuses; overtime; reserved rights to London weighting or London allowances; recruitment and retention allowances; private office allowances and any other allowance to the extent that it is subject to UK taxation.

This report is based on payments made by or accrued by the organisation and thus recorded in these accounts.

Remuneration

Non-executive members

Non-executive part-time members of the board (other than the chair) receive non-pensionable remuneration of £10,000 per annum.

Non-executive members	**Salary (in bands of £5,000)**	**Total Benefits in kind** (to the nearest £100)
L M Edmans CBE, A Pickering, C Swinson OBE, C Thomson, R Walsom	£10-15k (All part time members of the board)	£300 (A Pickering), £100 (R Walsom)
D Norgrove *(Chair)*	£100-£105k	

The total amount paid to non-executive directors (including the chair) during the period was £161,000. The monetary value of benefits in kind covers any benefits provided by the employer and treated by the Inland Revenue as a taxable emolument. The benefits shown above represent the payment of expenses for travelling to board meetings. The chair's remuneration is pensionable and details of the chair's pension benefits are set out below:

Chair's pension benefits					
	Accrued pension at age 60 as at 31/3/06 and related lump sum (£'000)	Real increase in pension and related lump sum at age 60 (£'000)	CETV at 31/3/06 (£'000)	CETV at 31/3/05 (£'000)	Real increase in CETV (£'000)
D Norgrove *(Chair)*	25-30 plus lump sum of nil	0-2.5 plus lump sum of nil	589	480	33

The pension entitlement shown above is based on the Inland Revenue earnings cap of £105,600.

Executive members			
	Salary (2005-6)	**Performance related (05-06) (subject to approval)**	**Salary (2004-05)**
A H Hobman *(Chief executive)*	£175-180k	Up to 20%	£185-190k
M Eade *(Business support executive)*	£100-£105k	Up to 20%	0
J Mulroy *(Business delivery executive)*	£110-£115k	Up to 20%	0
C Massey *(Strategic development executive) Seconded from the DWP*	£120-£125k	Up to 20%	0

The chief executive's salary in 2004-05 included bonuses in respect of both 2003-04 and 2004-05. The 2005-06 salaries figures include accrued performance-related bonuses for all executive directors. C Massey is paid directly by the Department for Work and Pensions and his costs are reinvoiced to the Pensions Regulator.

Civil Service Executive members' pension benefits

Executive members					
	Accrued pension at age 60 as at 31/3/06 and related lump sum (£'000)	Real increase in pension and related lump sum at age 60 (£'000)	CETV at 31/3/06 (£'000)	CETV at 31/3/05 (£'000)	Real increase in CETV (£'000)
A H Hobman *(Chief executive)*	5-10 plus lump sum of 15-20	0-2.5 plus lump sum of 2.5-5	96	55	23
C Massey *(Strategic delivery executive)*	10-15 plus lump sum of 40-45	2.5-5 plus lump sum of 10-12.5	163	89	48
M Eade *(Business support executive)*					
J Mulroy *(Business delivery executive)*					

The pension entitlement of the chief executive is based on the Inland Revenue's earnings cap of £105,600. In respect of M Eade and J Mulroy, employees do not accrue defined benefits in the Civil Service pension scheme until they have been members for two years, before which their entitlement on leaving service is to apply for a transfer value to a personal or stakeholder pension.

Pension benefits are provided through the Civil Service pension arrangements. From 1 October 2002, civil servants may be in one of three statutory based 'final salary' defined benefit schemes (classic, premium, and classic plus). The schemes are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under classic, premium, and classic plus are increased annually in line with changes in the Retail Prices Index. New entrants after 1 October 2002 may choose between membership of premium or joining a good quality 'money purchase' stakeholder arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at the rate of 1.5 per cent of pensionable earnings for classic and 3.5 per cent for premium and classic plus. Benefits in classic accrue at the rate of 1/80th of pensionable salary for each year of service. In addition, a lump sum equivalent to three years' pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum (but members may give up (commute) some of their pension to provide a lump sum). Classic plus is essentially a variation of premium, but with benefits in respect of service before 1 October 2002 calculated broadly in the same way as in classic.

The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3 per cent and 12.5 per cent (depending on the age of the member) into a stakeholder pension product chosen by the employee from a selection of approved products. The employee does not have to contribute but where they do make contributions, the employer will match these up to a limit of 3 per cent of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8 per cent of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement). Further details about the Civil Service pension arrangements can be found at the website **www.civilservice-pensions.gov.uk**.

Cash Equivalent Transfer Values (CETV)

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the Civil Service pension arrangements and for which the CS Vote has received a transfer payment commensurate with the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

Please note that the factors used to calculate the CETV were revised on 1 April 2005 on the advice of the Scheme Actuary. The CETV figures for 31 March 2005 have been restated using the new factors so that they are calculated on the same basis as the CETV figures for 31 March 2006.

Real increase in CETV

This reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Determinations Panel

Members of the Determinations Panel receive a daily allowance in respect of the time devoted by each of them to the work of the panel. The rate for the chair is £650 per diem and for the other members is £500 per diem.

Members	Salary
S McCarthy	£2.5-£5k
G Fitchew, M Maunsell, D Hayter, O Dickson, D Campbell, D Taylor	£5-£10k
J Scampion CBE *(Chair)*	£10-£15k

Members of the Determination Panel may be removed from office at any time by the chair of the Panel with the approval of the Pensions Regulator. The chair can be removed from office at any time by the Pensions Regulator. Members who wish to leave the Panel are required to give the chair two months' notice and the chair is required to give the Pensions Regulator three months' notice. Any compensation payment would be made in line with contractual obligations with reference to these notice periods.

Occupational Pensions Regulatory Authority

The appointment of all members of the Occupational Pensions Regulatory Authority expired on 5 April 2005.

Board members	Salary (2004-2005) (in bands of £5,000)	Total Benefits in kind (to the nearest £100)
J Drake OBE, L M Edmans CBE, B H Garner, M Macleod, J Wigley, B Benney, M Kinghorn	£0-£5k	£700 (£300 J Drake OBE, £300 M Macleod, £100 M Kinghorn)
D Adams OBE, D Campbell	£5-10k	£800 (£500 D Adams OBE, £300 D Campbell)
C H Maunsell OBE	£60-£65k	

The monetary value of benefits in kind covers any benefits provided by the employer and treated by the Inland Revenue as a taxable emolument. The benefits shown above represent the payment of expenses for travelling to board meetings.

David Norgrove

David Norgrove
chair, the Pensions Regulator
10 July 2006

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

5.4
The certificate and report of the Comptroller and Auditor General to the Houses of Parliament

I certify that I have audited the financial statements of the Pensions Regulator for the period ended 31 March 2006, under schedule 1 of the Pensions Act 2004. These comprise the Income and Expenditure Account, the Balance Sheet, the Cashflow Statement and the Statement of Total Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the board, chief executive and auditor

The board of the Pensions Regulator is responsible for preparing the Annual Report, the Renumeration Report and the financial statements in accordance with the Pensions Act 2004, and directions made thereunder by the Secretary of State for Work and Pensions, and for ensuring the regularity of financial transactions. These responsibilities are set out in the statement of the board's and chief executive's responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Pensions Act 2004 and directions made thereunder by the Secretary of State for Work and Pensions. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. I also report to you if, in my opinion, the Annual Report is not consistent with the financial statements, if the Pensions Regulator has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by relevant authorities regarding remuneration and other transactions is not disclosed.

I review whether the statement on pages 44 to 46 reflects the Pensions Regulator's compliance with HM Treasury's guidance on the Statement on Internal Control, and I report if it does not. I am not required to consider whether the Accounting Officer's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Pensions Regulator's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the chair's foreword, chief executive's summary, the pensions environment and the regulated community, and the management commentary, and the unaudited part of the Remuneration Report. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinion

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the board and chief executive in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Pensions Regulator's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinion

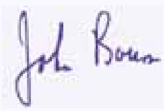
In my opinion:

(i) the financial statements give a true and fair view, in accordance with the Pensions Act 2004 and directions made thereunder by the Secretary of State for Work and Pensions, of the state of the Pensions Regulator's affairs as at 31 March 2006 and of its surplus for the period then ended;

(ii) the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Pensions Act 2004 and directions made thereunder by the Secretary of State for Work and Pensions; and

(iii) in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

I have no observations to make on these financial statements.



John Bourn
Comptroller and Auditor General,
National Audit Office, 157-197 Buckingham Palace Road, Victoria, London SWIW 9SP
11 July 2006

5.5
Financial statements

Income and Expenditure Account for the period ended 31 March 2006

	Note	**Period from 6 April 2005 to 31 March 2006** TPR £'000	Period from 1 April 2004 to 5 April 2005 Opra (as restated) £'000
Income			
Government grants	3	**28,153**	16,849
Transfers from Government Capital Grants Reserve	14	**1,119**	569
Other income	4	**190**	126
		29,462	17,544
Expenditure			
Staff costs	6	**14,997**	10,276
Other operating charges	7	**12,385**	12,485
		27,382	22,761
Operating surplus/(deficit) on ordinary activities		**2,080**	(5,217)
Interest receivable		**151**	52
Surplus/(deficit) for period before notional interest on capital employed		**2,231**	(5,165)
Notional interest receivable/(payable) on capital employed	2(c)	**60**	(6)
Loss on disposal of fixed assets	9	**(364)**	(6)
Transfers from Government Capital Grants Reserve	14	**651**	8
Surplus/(deficit) for period before tax		**2,578**	(5,169)
Tax on interest receivable	8	**(29)**	(10)
Surplus/(deficit) for period transferred to/(from) General Reserve	15	**2,549**	(5,179)

Statement of total recognised gains and losses for the period ended 31 March 2006

	Note	**Period from 6 April 2005 to 31 March 2006** TPR £'000	Period from 1 April 2004 to 5 April 2005 Opra £'000
Surplus/(deficit) on income and expenditure account for the period		**2,549**	(5,179)
Unrealised gains on revaluation of fixed assets	14	**22**	3
Total recognised gains/(losses) relating to the period		**2,571**	(5,176)

Income and expenditure for the period ended 31 March 2006 arose from operations transferred from the Occupational Pensions Regulatory Authority (Opra) and also from additional activities and responsibilities which the Pensions Regulator has been charged with under the Pensions Act 2004. All Opra activities transferred to the Pensions Regulator with the exception of collection and payment of grants to the Pensions Advisory Service (OPAS Limited) and the tracing service which transferred to the Department for Work and Pensions. The comparative figures for the period ended 5 April 2005 have been amended accordingly.

The accounting policies and notes on pages 57 to 59 form part of these accounts.

Balance sheet as at 31 March 2006

		At 31 March 2006		At 5 April 2005	
	Note	**TPR**		Opra	
		£'000	**£'000**	£'000	£'000
Fixed assets	9				
Tangible assets	2(e)	**2,292**		1,552	
Intangible assets	2(f)	**82**		123	
			2,374		1,675
Current assets					
Debtors	10	**5,875**		495	
Cash at bank and in hand	19(c)	**31**		57	
		5,906		552	
Creditors					
Amounts falling due within one year	11	**(4,621)**		(1,342)	
Net current assets/(liabilities)			**1,285**		(790)
Total assets less current liabilities			**3,659**		885
Creditors					
Amounts falling due after more than one year	11		**(367)**		-
Provisions for liabilities and charges	13		**(3,447)**		(4,174)
Total net liabilities			**(155)**		(3,289)
Financed by					
Government Capital Grants Reserve	14		**2,374**		1,694
General Reserve	15		**(2,529)**		(4,983)
			(155)		(3,289)

Approved by the Pensions Regulator at a meeting on 6 July 2006

David Norgrove
chair, the Pensions Regulator
10 July 2006

Tony Hobman
chief executive, the Pensions Regulator
10 July 2006

Cash Flow Statement for the period ended 31 March 2006

	Note	**Period from 6 April 2005 to 31 March 2006**	Period from 1 April 2004 to 5 April 2005
		TPR	Opra
		£'000	£'000
Net cash outflow from operating activities	19(a)	**(167)**	(894)
Returns on investments	19(b)	**151**	52
Tax paid		**(10)**	(4)
Capital expenditure	19(b)	**(2,393)**	(1,714)
Financing	19(b)	**2,393**	1,714
Decrease in cash	19(c)	**(26)**	(846)

The accounting policies and notes on pages 57 to 59 form part of these accounts.

Notes to the accounts

1 Accounting convention

These accounts have been prepared in a form directed by the Secretary of State for Work and Pensions, with the approval of the Treasury, in accordance with Paragraph 27(2) of Schedule 1 of the Pensions Act 2004. The accounts have been prepared under the historical cost convention modified by the inclusion of fixed assets at their value to the business by reference to current costs. Without limiting the information given, the accounts meet the accounting and disclosure requirements of the Companies Act and the accounting standards issued by the Accounting Standards Board insofar as those requirements are appropriate to the Pensions Regulator. The accounts have been prepared on a going concern basis.

2 Accounting policies

a) Merger accounting

The Pensions Regulator was established on 17 December 2004 to replace the Occupational Pensions Regulatory Authority (Opra), which ceased all operations on 5 April 2005. The Pensions Regulator had no assets or liabilities at 31 March 2005, and on 6 April 2005 Opra transferred all of its assets and liabilities to the Pensions Regulator at book value. During the period to 5 April 2005 the Pensions Regulator undertook no financial transactions on its own account. All employees of Opra, other than those for whom no future role was identified, were transferred to the Pensions Regulator. In accordance with HM Treasury guidance as laid down in the Financial Reporting Manual, this transfer has been accounted for as a merger. All Opra activities transferred to the Pensions Regulator with the exception of collection and payment of grants to the Pensions Advisory Service (OPAS Limited) and the tracing service which transferred to the Department for Work and Pensions. The comparative figures for the period ended 5 April 2005 have been amended accordingly.

b) Government grants

(i) All grants for revenue expenditure are credited to income in the period in which they are due.

(ii) Government grants received for capital expenditure are credited to the government capital grants reserve and released to the income and expenditure account over the expected useful lives of the relevant assets to match related depreciation charges. Increases in depreciation resulting from revaluing assets at current replacement cost (see note 2e) are offset by transferring an equivalent amount from the government capital grants reserve to the general reserve.

c) Notional costs

Certain expenses included in these accounts have not involved actual payments. They include various expenses and notional interest on capital employed (notional interest has been calculated at the Treasury standard rate of 3.5 per cent of the average value of total assets less liabilities). These costs are included in the accounts to ensure that the results reflect the full economic costs of the Pensions Regulator.

d) Other income and expenditure

Other income and expenditure is recognised on an accruals basis. Where income received relates to a period of time covering more than one accounting period, that part extending beyond the current accounting period is treated as deferred income.

e) Tangible fixed assets

Fixed assets are valued at current replacement cost which is calculated by applying appropriate Office for National Statistics indices to the historical cost of each asset. Any surplus on revaluation of fixed assets is credited to the government capital grants reserve. Any permanent diminution in the value of a fixed asset on revaluation is charged to the income and expenditure account when it occurs. The Pensions Regulator is required to remit the proceeds of disposal of fixed assets to the Secretary of State.

f) Intangible fixed assets

The costs of purchasing major software licences are capitalised as intangible fixed assets. The costs of major software development and enhancement including related consultancy costs are capitalised as tangible fixed assets, although ongoing software maintenance costs are written off in the period in which they are incurred.

g) Depreciation

The threshold for treating expenditure on tangible and intangible fixed assets as capital expenditure is £1,000. Depreciation is provided on fixed assets at rates calculated to write down the cost or valuation (less any estimated residual value) of each asset evenly over its expected useful life as follows:

Leasehold improvements	–	the shorter of 10 years or the remainder of the lease term
Furniture and office equipment	–	5-7 years
Information technology costs (IT costs)		
– information technology equipment	–	3 years
– major software licences	–	3 years
– software development and enhancement	–	3 years

A full year's charge is made in the year of acquisition.

Assets are not depreciated until they are commissioned or brought into use.

h) Operating leases

Rent payable under operating leases is charged to the income and expenditure account on a straight line basis over the term of the lease. Amounts received as inducements to enter into operating leases are treated as deferred income (rent rebates), and are recognised to reduce the operating lease costs over the same period as the corresponding lease.

i) Pension arrangements

The majority of past and present employees are covered by the provisions of the Principal Civil Service Pension Scheme (PCSPS) which is a defined benefit scheme and is unfunded and non-contributory, except in respect of dependents' benefits. The Pensions Regulator recognises the expected cost of providing pensions on a systematic and rational basis over the period during which it benefits from employees' service by payment to the PCSPS of amounts calculated on an accruing basis. Liability for the payment of future benefits is a charge on the PCSPS. As described more fully in note 6, certain employees can opt for a stakeholder pension.

j) Early retirement costs

Compensation payments are charged to the income and expenditure account. Obligations relating to those former members of staff aged 50 or over are provided for until their normal date of retirement.

k) Provision for liabilities

Provision is made for early retirement, redundancy and property costs when any relevant programme is announced and a constructive obligation is created. Similarly, provision for leasehold dilapidations is made as the dilapidations arise over the life of the lease.

3 Government grants

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra (as restated) £'000
Department for Work and Pensions, Request for Resources 3: Revenue expenditure (income and expenditure account)		
Grant in aid to cover on-going operations	**23,215**	16,849
Grant in aid to cover initial costs of establishing the Pensions Regulator (note 7)	**4,938**	–
	28,153	16,849
Government capital grant (note 14)	**2,393**	1,714
	30,546	18,563

4 Other income

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
Charges made for providing a levy collection service:		
– Pension Protection Fund contribution towards running costs	**190**	–
– Pensions Compensation Board contribution towards running costs	**–**	125
Sundry income	**–**	1
	190	126

5 Board members

The chair and other members of the board of the Pensions Regulator are appointed under the Pensions Act 2004 by the Secretary of State for Work and Pensions. The chair was appointed on a part-time basis from 1 January 2005 for a period of three years. His salary is set by the Secretary of State in line with senior civil servants, and he is a member of the Principal Civil Service Pension Scheme. Other part-time board members are also appointed for periods of between one and four years. The part-time board members were entitled to receive a monthly non-pensionable fee of £833 in 2005-06 (2004-05: daily fee of £191) and out of pocket expenses. Details of the remuneration and pension benefits of the chair and all other members of the board are given in the Remuneration Report on pages 47 to 52. The total costs for the chair and part time board members are as follows and these costs are included within other operating charges (note 7):

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
Salary/fees	**161**	95
Social security costs	**15**	9
Other pension costs (chair only)	**18**	11
	194	115

Included above are fees waived in favour of a board member's employer totalling £11,458 (2004-05: £nil).

6 Staff costs including pensions

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
Brighton staff		
Salaries and wages	**7,872**	6,375
Social security costs	**672**	518
Other pension costs	**1,429**	862
	9,973	7,755
Newcastle staff	**3**	1,128
Temporary staff	**4,504**	1,241
Redundancy and early retirement costs	**517**	152
	14,997	10,276

The average number of staff employed, including temporary staff

	No.	No.
Brighton employees	**230**	212
Newcastle employees	**–**	47
Temporary staff	**58**	20
Total	**288**	279

Details of the remuneration and pension benefits of the board of the Pensions Regulator are given in the Remuneration Report on pages 47 to 52. The staff costs above include the costs of the chief executive and the full time members of the board.

The Pensions Act 2004 includes employment with the Pensions Regulator under the Superannuation Act 1972, and all employees of the Pensions Regulator (and previously Opra) including the chief executive are entitled to membership of the Principal Civil Service Pension Scheme (PCSPS), including family benefits. The PCSPS is an unfunded multi-employer defined benefit salary-related scheme, but the Pensions Regulator is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out at 31 March 2003, and details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (**www.civilservice-pensions.gov.uk**).

For 2005-06 employers' contributions of £1,418,924 were payable to the PCSPS (2004-05: £850,225) at one of four rates in the range 16.2 per cent to 24.6 per cent of pensionable pay, based on salary bands. The scheme's actuary reviews employer contributions every four years following a full scheme valuation. From 2006-07 the salary bands will be revised and the rates will be in a range between 17.1 per cent and 25.5 per cent. The contribution rates reflect the benefits as they are accrued, not when the costs are actually incurred, and reflect past experience of the scheme.

Employees joining after 1 October 2002 can opt to open a partnership pension account, a stakeholder pension with an employer contribution, and employer contributions of £9,942 (2004-05: £11,219) were payable to one or more of a panel of three appointed stakeholder pension providers. Employers' contributions are age-related and range from 3 to 12.5 per cent of pensionable pay, and employers also match employee contributions up to 3 per cent of pensionable pay. In addition, employer contributions of £706 (2004-05: £749), being 0.8 per cent of pensionable pay, were payable to the PCSPS to cover the cost of future provision of lump sum benefits on death in service and ill health retirement of these employees.

There were no outstanding or prepaid contributions at 31 March 2006.

7 Other operating charges

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
Board/Authority chair	**132**	84
Part-time board/Authority members' fees*	**64**	31
Part-time board/Authority members' expenses**	**1**	4
Consultancy, contracted out and other professional services	**6,684**	3,659
Training and recruitment costs	**891**	794
Staff travel and expenses	**295**	230
Depreciation ***	**1,065**	569
General office expenses including accommodation expenses	**1,974**	1,890
Redundant property costs	**(297)**	3,324
Dilapidations costs	**(99)**	237
Computer systems development and maintenance	**499**	881
Operating leases including rent	**850**	731
Devaluation of fixed assets	**287**	11
Auditor's remuneration	**39**	40
	12,385	12,485

* In the period ended 31 March 2006, this amount included irrecoverable VAT of £2,000 charged by the employer of a board member who has waived her fees in favour of her employer.

** This amount includes tax due to the Inland Revenue on expenses incurred of £266 (2004-05: £834)

*** Depreciation is net of the reduced charge due to revaluations during the period (note 9.)

Costs in the period ended 31 March 2006 included exceptional costs of £4,938,468 relating to the culture change programme to establish the Pensions Regulator and provide it with the personnel, systems and procedures necessary to fulfil its new and wide-ranging remit. The costs are largely included in consultancy, contracted out services and other professional services. The activities of the programme are described in Section 4 of the annual report. Initial costs of the culture change programme were borne directly by the Department for Work and Pensions. The income for the culture change programme is shown in note 3 and is equivalent to the costs incurred during the period.

In the period ended 5 April 2005 notional costs totalling £59,000 were included in general office expenses, to reflect the use of telephone and postage services used by Opra staff located in the Newcastle offices of the Department for Work and Pensions. There were no such notional costs in the period ended 31 March 2006.

8 Tax on interest receivable

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
UK Corporation Tax at 19% (2004-05: 19%) on interest receivable	**29**	10

9 Fixed assets

	Leasehold improvements £'000	Furniture & equipment £'000	IT hardware & software £'000	IT software (intangible) £'000	Total £'000
Cost:					
At 5 April 2005 (Opra)	967	702	2,150	247	4,066
Additions in period	1,281	859	206	47	2,393
Disposals in period	(989)	(632)	(1,012)	(61)	(2,694)
Revaluations	22	(5)	(250)	(32)	(265)
At 31 March 2006 (TPR)	1,281	924	1,094	201	3,500
Depreciation:					
At 5 April 2005 (Opra)	794	622	851	124	2,391
Charge for period	282	208	561	68	1,119
Disposals in period	(912)	(607)	(750)	(61)	(2,330)
Reduction in charge arising on revaluations	19	(4)	(57)	(12)	(54)
At 31 March 2006 (TPR)	183	219	605	119	1,126
Net book value at 5 April 2005 (Opra)	173	80	1,299	123	1,675
Net book value at 31 March 2006 (TPR)	1,098	705	489	82	2,374

The net book value of assets disposed of during the period was £364,000. The disposal proceeds of £4,000 are reflected as an amount due to the Department for Work and Pensions and are included in Central Government accruals (note 11.)

10 Debtors

	At 31 March 2006 TPR £'000	£'000	At 5 April 2005 Opra £'000	£'000
Debtors:				
Central government	**5,188**		–	
Other	**172**		–	
		5,360		–
Prepayments:				
Local authority	**–**		160	
Other	**499**		328	
		499		488
Other debtors - staff loans		**16**		7
		5,875		495

Staff loans relates to season ticket loans. Central government debtors comprises £250,000 owed by the Pension Protection Fund and £4,938,468 owed by the Department for Work and Pensions.

11 Creditors - amounts falling due within one year

	At 31 March 2006 TPR £'000	£'000	At 5 April 2005 Opra £'000	£'000
Taxation on interest receivable		**29**		10
Deferred income		**119**		–
Amounts due to suppliers		**945**		–
Accruals:				
Central Government	**111**		219	
Local Authority	**–**		1	
Other	**3,417**		1,112	
		3,528		1,332
		4,621		1,342

Central Government accruals consists of £10,895 due to the Pension Protection Fund and £99,396 due to the Department for Work and Pensions. Deferred income due in less than one year comprises rent rebates received (see Note 2(h)) and contributions from the Pension Protection Fund (£60,000) in respect of work not completed at the period end. Deferred income due in greater than one year comprises only rent rebates.

	At 31 March 2006 TPR £'000	At 5 April 2005 Opra £'000
Creditors - amounts falling due after more than one year		
Deferred income	**367**	–

12 Operating leases

The Pensions Regulator occupies an office in Brighton, the lease on which will expire in 2013. Annual commitments for 2006-07 in respect of leases expiring:

	within one year £'000	within 2 to 5 years £'000	over 5 years £'000
Land and buildings	–	–	670
Other operating leases	2	11	–
Total (TPR)	2	11	670

In addition to the amounts disclosed above, the Pensions Regulator has the following commitments which are covered by the property cost provision (note 13.) Annual commitments for 2006-07 in respect of leases expiring:

	within one year £'000	within 2 to 5 years £'000	over 5 years £'000
Land and buildings	109	407	–

The above annual commitments of the Pensions Regulator for 2006-07 compare with the following commitments of Opra for 2005-06. Annual commitments for 2005-06 in respect of leases expiring:

	within one year £'000	within 2 to 5 years £'000	over 5 years £'000
Land and buildings	74	72	297
Other operating leases	7	3	–
Total (Opra)	81	75	297

The Opra commitments for 2005-06 in respect of land and buildings relate to properties which were vacated in the period ended 31 March 2006, and any continuing commitments for 2006-07 and beyond are included in the commitments shown for the Pensions Regulator.

13 Provisions for liabilities and charges

	Early Retirement £'000	Redundancy £'000	Dilapidations £'000	Property costs £'000	Total £'000
Balance at 5 April 2005 (Opra)	283	317	250	3,324	4,174
Amount provided/ (released) in period	120	397	(99)	(297)	121
Utilisation in period	(56)	(511)	–	(281)	(848)
Balance at 31 March 2006 (TPR)	**347**	**203**	**151**	**2,746**	**3,447**

The provision for property costs relates to the leases of two properties in Brighton, Invicta House (expires 24 March 2011 – £2,597,000) and International House (expires 24 March 2007 – £149,000). A potential claim for £2,398,000, in respect of property costs, may be made against our legal advisors for failing to implement the break clause on certain floors of one of our Brighton offices.

14 Government Capital Grants Reserve

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
Capital Grants Reserve brought forward	**1,694**	554
Grants received in period (note 3)	**2,393**	1,714
Transfer to income and expenditure account		
re depreciation	**(1,119)**	(569)
re loss on disposal of fixed assets	**(364)**	(8)
re devaluation of assets	**(287)**	–
Unrealised gains on revaluation of fixed assets:		
Surplus on revaluations in period	**22**	24
Transfer to General Reserve - depreciation (see note 2b(ii))	**35**	(21)
Capital Grants Reserve carried forward	**2,374**	1,694

15 Reconciliation of movements in General Reserve

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
General Reserve brought forward	**(4,983)**	110
Surplus/(deficit) on income and expenditure account	**2,549**	(5,179)
Transfer from Government Capital Grants Reserve – depreciation (see note 2b(ii))	**(35)**	21
Notional charges in other operating charges (see note 7)	**–**	59
Notional interest on capital employed (see note 2c)	**(60)**	6
General Reserve carried forward	**(2,529)**	(4,983)

16 Capital commitments

Amounts contracted for but not provided in the accounts amounted to nil (5 April 2005: nil). There were no amounts authorised by the board not contracted for.

17 Financial penalties

In the course of the period no financial penalties were imposed (2004-05 (Opra): nil) and penalties collected amounted to £4,000 (2004-05 (Opra): £23,000). Under Section 10(9) of the Pensions Act 1995 the Authority was required to pay the Secretary of State any penalties recovered and therefore such penalties are not included in the accounts.

18 Contingent liabilities

There were no contingent liabilities at 31 March 2006 (5 April 2005: Nil).

19 Notes to the Cash Flow Statement

	Period from 6 April 2005 to 31 March 2006	Period from 1 April 2004 to 5 April 2005
	TPR £'000	Opra £'000
(a) Reconciliation of operating surplus/(deficit) to net cash outflow from operating activities		
Operating surplus/(deficit) on ordinary activities	**2,080**	(5,217)
Depreciation	**1,065**	569
Notional charges	**–**	59
Transfers from Government Capital Grants Reserve	**(1,119)**	(569)
Devaluation of fixed assets	**287**	11
Increase in debtors	**(5,380)**	(140)
Increase in creditors	**3,627**	805
Increase/(decrease) in provisions	**(727)**	3,588
Net cash outflow from operating activities	**(167)**	(894)
(b) Gross cash flows		
Returns on investments and servicing of finance		
Interest received	**151**	52
Capital expenditure		
Payments to acquire tangible assets	**2,346**	1,529
Payments to acquire intangible assets	**47**	185
	2,393	1,714
Financing		
Receipts of government capital grant	**2,393**	1,714

(c) Analysis of movement in cash and investments

	at 5 April 2005 £'000	Cash flow £'000	at 31 March 2006 £'000
Cash in hand and at bank	57	(26)	31
Total	57	(26)	31

Cash at bank represented the only funds held at 31 March 2006.

20 Related party transactions

The Pensions Regulator is a non-departmental public body accountable to the Secretary of State for Work and Pensions. The Department for Work and Pensions (DWP) and the Pension Protection Fund (PPF) are regarded as related parties. During the period the Pensions Regulator has had a number of significant transactions with the Department, its executive agencies and other related bodies covering:

a) supply of information technology services on a full reimbursement basis (DWP)
b) provision of levy collection services (PPF and DWP)

During the period no other related parties, including the Pensions Regulator's board members and key management staff, had undertaken any material transactions with the Pensions Regulator.

21 Financial Instruments

FRS 13, Derivatives and Other Financial Instruments, requires disclosure of the role which financial instruments have had during the period in creating or changing the risks an entity faces in undertaking its activities. Because of the non-trading nature of its activities and the way it is financed, the Pensions Regulator is not exposed to the degree of financial risk faced by business entities. Moreover, financial instruments play a much more limited role in creating or changing risk than would be typical of listed companies to which FRS13 mainly applies. The Pensions Regulator has very limited powers to borrow or invest funds. Financial assets and liabilities are generated by day to day operational activities and are not held to change the risks facing the Pensions Regulator in undertaking its activities.

Liquidity risk

The Pensions Regulator's net revenue resource requirements are largely funded by grant-in-aid from its sponsor department. The capital expenditure is also financed through grant-in-aid. The Pensions Regulator is consequently not exposed to significant liquidity risks.

Interest rate risk

The Pensions Regulator is not exposed to any interest rate risk. All surplus funds are placed on deposit with commercial banks at the prevailing deposit interest rate.

Foreign currency risk

The Pensions Regulator's exposure to foreign currency is not currently significant.

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On 6 April 2005 the Pensions Regulator replaced Opra as the UK regulator of work-based pensions.

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