

Resource Accounts presented to the House of Commons pursuant to section 6(4) of the Government Resources and Accounts Act 2000 c.20.

Armed Forces Pension Scheme
(Incorporating the Armed Forces Compensation Scheme)

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2008-09

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2008-09
(For the year ended 31 March 2009)

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Report of the Scheme Managers

History and Statutory Background

The Armed Forces Pension Scheme (AFPS 75)

The Armed Forces Pension Scheme is an unfunded, defined benefit, salary-related, contracted-out occupational pension scheme open to most members of the Armed Forces, administered by the Service Personnel and Veterans Agency (SPVA) formerly Armed Forces Personnel Administration Agency (AFPAA) and financed on an annual basis by the Consolidated Fund.

The Scheme is designed to meet the special requirements of Service life. Youth and fitness are important to the Services, and the Scheme provides immediate pension benefits to many of those who leave without completing a full career. The full career pension can be earned relatively early, at age 55, and invaliding and death benefits are available in the event of illness, injury or death, at different rates depending upon whether or not these are caused by service.

The Scheme rules are set out in "Prerogative Instruments" that derive their authority from Her Majesty The Queen and are not subject to approval, annulment or amendment by Parliament. For the Royal Navy and the Royal Marines the Prerogative Instrument is an Order in Council under the Naval and Marine Pay and Pensions Act 1865. For the Army, it is the Army Pension Warrant 1977 and, for the Royal Air Force, the Queen's Regulations.

The Armed Forces Pension and Compensation Schemes

The Armed Forces (Pension & Compensation) Act 2004 is the primary legislation covering the AFPS 05, Early Departure Payment (EDP) Scheme and Armed Forces Compensation Scheme (AFCS). These schemes were introduced on 6 April 2005.

The Armed Forces Pension Scheme (AFPS 05)

From 6 April 2005, the Armed Forces Pension Scheme (known as AFPS 05) was introduced for all new members of the Armed Forces. The AFPS 05 is also an unfunded, defined benefit, salary-related, contracted out, occupational pension scheme. Pensions are paid immediately if an individual serves to age 55: those who have at least two years service who leave before age 55 will have their pensions preserved until age 65. Pensions may be payable to the spouse, civil partner, partner or to eligible children. Death-in-service lump sums are payable subject to nomination. There are no attributable ill-health benefits under the AFPS 05 as these will be considered under the War Pensions Scheme (WPS) or the Armed Forces Compensation Scheme (AFCS).

The scheme includes an Early Departure Payment (EDP) for those who leave before age 55 providing they have at least 18 years service and are at least 40 years of age. The EDP Scheme pays a tax-free lump sum and income of between 50% and 75% of preserved pension between the date of the individual's departure from the Armed Forces and age 55. The income rises to 75% of preserved pension at age 55 and is index linked. At age 65 the EDP stops and the preserved pension and preserved pension lump sum are paid.

The Armed Forces Compensation Scheme (AFCS)

The AFCS was introduced on 6 April 2005, replacing two separate compensation arrangements under the AFPS 75 and the WPS. The AFCS covers injury, illness and death that are caused by service on or after 6 April 2005. The AFCS is a tariff-based compensation scheme, which has been designed to be simple to understand and to produce quick, consistent and equitable decisions, using an evidence-based approach.

Principal Purpose and Administrative Aim

In administering the Armed Forces Pension Scheme and Armed Forces Compensation Scheme on behalf of the Ministry of Defence (MOD), the Service Personnel and Veterans Agency (SPVA) aim to ensure that all pension and compensation payments due to entitled pensioners and members of the Armed Forces are made in a timely and accurate fashion.

The Executive Boards

The AFPS and AFCS are managed and operated by SPVA, an Agency within the MOD. The costs of administering the Scheme are borne by the MOD and are reflected in the Departmental Resource Accounts (DRAc).

The Chief Executive of SPVA has been designated by the Departmental Accounting Officer to be the Scheme Administrator for both the AFPS and AFCS. The Director of Corporate Services for SPVA has been designated by the Departmental Accounting Officer to be the Senior Finance Officer for both the AFPS and AFCS.

The SPVA Executive Board meets regularly to determine strategy, set objectives and review performance towards strategic goals. The Executive Board consists of:

SPVA Executive Board

Rear Admiral T A Spires (until 30/09/08)	Chief Executive
Mrs K Barnes (from 01/10/08)	Chief Executive
Commodore R Albon (from 16/02/09) / (from 12/08/08)	Deputy Chief Executive / Director Strategy and Programmes
Brigadier R Bacon (until 11/08/08)	Director Strategy and Programmes
Mrs A Sansome (until 31/08/08)	Director Change
Air Commodore P Nash (from 01/09/08)	Director Change
Commodore A Ross	Director Military Services
Mrs A Sansome	Director Veterans Services
Mrs J Adams (until 26/08/08)	Director Corporate Services
Mrs K Humberstone (from 27/08/08)	Director Corporate Services
Brigadier R Bacon (new post from 11/08/08)	Director Future Contract
Mr A Jablonowski	Non Executive Director
Mrs B Curtis (from 01/01/09)	Non Executive Director

Other Schemes

The Scheme Statements summarise the transactions of not only the AFPS and AFCS but also the three smaller pension schemes: The Gurkha Pension Scheme (GPS), the Non-Regular Permanent Staff Pension Scheme (NRPS), and the Reserve Forces Pension Scheme (RFPS), also managed and operated by SPVA, whose members amount to 3.1% of the AFPS total membership.

Auditors

The accounts of the AFPS and AFCS are audited by the Comptroller and Auditor General under the Government Resources and Accounts Act 2000.

Audit

As Accounting Officer of the AFPS, I am responsible for the disclosure of the relevant audit information. I can confirm that:

- There is no relevant audit information of which the auditors are unaware;
- I have taken all necessary steps to ensure that I am aware of relevant audit information; and
- I have taken all necessary steps to establish that the auditors are aware of the information.

Managers, Advisers and Employers

Managers

Accounting Officer:

Sir Bill Jeffrey KCB
Permanent Under-Secretary of State for Defence
Ministry of Defence
Whitehall
London SW1A 2HB

Director General of Finance:

Mr J Thompson
Ministry of Defence
Whitehall
London SW1A 2HB

AFPS & AFCS Scheme Administrator:

Mrs K Barnes
Chief Executive
Service Personnel & Veterans Agency
Centurion Building
Gosport PO13 9XA

Pension Policy:

Mr P Davies
Head of Pensions, Compensation and Veterans
Ministry of Defence
Whitehall
London SW1A 2HB

Advisers

Scheme Actuary:
Government Actuary's Department
Finlaison House
15-17 Furnival Street
London EC4A 1AB

Bankers:
HM Paymaster General
Bank of England
Threadneedle Street
London EC2R 8AH

Legal Advisers:
MOD Treasury Solicitors
Ministry of Defence
Whitehall
London SW1A 2HB

Auditor:
Comptroller and Auditor General
National Audit Office
151 Buckingham Palace Road
Victoria
London SW1W 9SS

Employers

Ministry of Defence

Changes to the Scheme

During the year the following changes were made to the Scheme:

Pensions were increased by 3.9% (2007 3.6%) with effect from 7 April 2008 (9 April 2007).

Pension Overpayments

During 2007-08 administrative checks revealed an inconsistency in the calculation of a number of individual pensions because of incorrect uprating being applied to an element known as the Guaranteed Minimum Pension or GMP. This resulted in both overpayments and underpayments of pensions. The overpayments (and underpayments) have continued this year while we have sought to recalculate pensions and correct the records of the individuals affected. Those who have been overpaid have not been required to repay the overpayment but their pensions have been adjusted to the correct level from April 2009. As at the beginning of May 2009, 4,529 pensioners had been overpaid some £10.7M. The majority of overpaid pensioners saw no reduction in their pension (as the reduction was cancelled out by the inflation increase in April). A further 68 pensioners have been identified as underpaid some £0.03M and these pensions are being corrected and arrears of underpayment paid. There are still a number of cases to be completed and work is continuing to resolve those cases. Revised processes are being put in place to avoid a repeat of this problem. The National Audit Office have conducted a review of the end to end process to identify causes of the error.

Membership Statistics

Membership statistics are comprised of the total of AFPS 75 and AFPS 05 schemes plus three minor schemes: GPS, NRPS and RFPS.

The Treasury standard format for government pension scheme accounts requires that membership data be published for Active Members, Deferred Members and for Pensioners, and for movements over the year within each category. In the past, the AFPS Resource Accounts have conformed to the basic format. However, due to the complexity of the schemes whose rules continue to change, disclosure under the basic format is no longer possible. The standard format has therefore been expanded to include additional information, but has also moved away from an "individual" being synonymous with a "member".

Members of the AFPS 75 scheme receive a pension at age 60 (for service before 6 April 2006) and an additional pension at age 65 (for service post this date). For example, a Deferred Member on attaining age 60, become a Pensioner but also remain a Deferred Member until the age of 65. To reflect this and to be able to show the movements within each category the membership table for 2008-09 and thereafter will change from the previous format and show Deferred Benefits instead of Deferred Members and Benefits in payment instead of Pensioners in payment. Further changes to the rules took place in April 2009 that enables pensions to be drawn from the age of 55 in certain circumstances and this will add to future complexity.

This change in the presentation of the membership table has no effect on the financial statements.

There are three groups, defined as follows:

- Active Members: personnel who are in service, which is reckonable for pension purposes.
- Deferred and unclaimed benefits: AFPS benefits due at some future date or have not been claimed, that are attributable to former Active Members or their divorced spouses.
- Benefits in Payment: payments to former actives or divorced spouses, plus other beneficiaries such as widow(er)s, survivors and other dependants of former Active Members.

Active members (figures rounded to nearest 5)

	Active members brought forward from 31 March 2008	196,060
	Adjustments	1,545
	Total active members at 31 March 2008	197,605
<i>Add:</i>	New entrants in year	23,021
	Transfers in	54
<i>Less:</i>	Deaths in service	(175)
	Left active service with under 2 years service and no benefits	(3,520)
	Transfers out	(809)
	Left active service with deferred benefits	(11,916)
	Left active service and received benefits	(4,725)
	Active members at 31 March 2009	199,535

Deferred and unclaimed benefits

Deferred members brought forward from 31 March 2008	324,002
Adjustments due to data received post 31 March 2008 (see note 5 below)	42,721
	366,723
Adjustments for conversion from membership numbers to benefit numbers (see note 5 below)	21,091
	387,814
Being:	
Deferred Benefits	378,196
Benefits due but unclaimed	9,618
Total deferred and unclaimed benefits at 1 April 2008	387,814
<i>Add:</i> Benefits not immediately payable	16,112
<i>Less:</i> Benefits taken up	(5,733)
Benefits elapsed	(528)
	397,665
Being:	
Deferred benefits	384,770
Benefits due but unclaimed (see note 7 below)	12,895
Total deferred and unclaimed benefits 31 March 2009 (367,340 members)	397,665

Benefits in payment

Benefits brought forward from 31 March 2008	
- Members	322,093
- Dependants	68,156
Total	390,249
Adjustments due to data received post 31 March 2008	
- Members	879
- Dependants	0
Total	879
Total benefits at 1 April 2008	
- Members	322,972
- Dependants	68,156
Total	391,128
<i>Add:</i> Benefits that became payable in the year	
- Members	12,378
- Dependants	3,992
Total	16,370
<i>Less:</i> Benefits that have ceased in the year	
- Members	(7,128)
- Dependants	(3,859)
Total	(10,987)
Benefits in payment at 31 March 2009	
- Members	328,222
- Dependants	68,289
Total	396,511

Notes

- 1 Individuals may be a member of more than one scheme.
- 2 A member may be entitled to more than one benefit under a scheme (see above).
- 3 Where a member is divorced and the ex-spouse is entitled to a proportion of the benefit, the deferred figures show both benefits when notified to AFPS post March 2006. Benefits in payment show both benefits.
- 4 Comparison of movements between tables cannot be made due the use of Members in one table and Benefits in the other tables, as explained above.
- 5 Where a member has not claimed benefits by the age of 72, the member is out of time to claim.
- 6 The Deferred Members brought forward from 31 March 2008 have been restated to account for better information obtained from the membership database. This cleansing operation is ongoing; it is not anticipated that there will be significant changes in the future. The restated Deferred Members were then converted into Deferred benefits (as explained above)
- 7 The cleansing of the database during 2008-09 created additional unclaimed benefits. The accrual increased from £49m (year end 2007-08) to £175m (year end 2008-09).
- 8 The GAD valuation includes a number of members with estimated benefits. This is due to one or more of the elements required to determine the benefit being missing from the database. The assumptions made by GAD are unlikely to make a material difference to the overall valuation.

Further information

Any enquiries about the AFPS or AFCS should be addressed to:
The Scheme Administrator
Service Personnel and Veterans Agency
Tomlinson House, Norcross
Blackpool FY5 3WP

Sir Bill Jeffrey
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme

13 July 2009

**Actuarial Statement for the Armed Forces Pension Scheme
for Accounts for the Year Ended 31 March 2009**

Introduction

- 1 This statement has been prepared by the Government Actuary's Department at the request of the Ministry of Defence ('MOD'). It summarises the pensions disclosures required for the 2008-09 Resource Accounts of the Armed Forces Pension Scheme ('AFPS').
- 2 The statement is based on the results of the last formal valuation carried out as at 31 March 2005, with an approximate updating to 31 March 2009 to reflect known changes.

Membership data

- 3 The data used to prepare this assessment was gathered from SPVA, MOD. This data has been compared with similar data provided as at 31 March 2008, in order to check it is reasonable. The number of deferred individuals used in the assessment as at 31 March 2009 (367,340) was provided by SPVA. I understand this figure was extracted using SPVA's 102 report which indicates that the corresponding number of benefit records to be disclosed in the resource accounts is 397,665.

Methodology

- 4 The value of the liabilities has been determined using the projected accrued benefit method, with allowance for expected future pay increases in respect of active members, and the principal financial assumptions applying to the 2008-09 Resource Accounts. The standard contribution rate for accruing costs in the year ended 31 March 2009 was determined using the entry age method. The accruing costs use the principal financial assumptions applying to the 2007-08 Resource Accounts.
- 5 This statement takes into account the benefits normally provided under the AFPS, including normal retirement benefits, ill-health retirement benefits and benefits applicable following the death of the member.
- 6 The liabilities disclosed in this statement include the benefits accrued by personnel who are in the Gurkha Pension Scheme. Full data was not available for this group of personnel and therefore only a very approximate allowance has been made. The liabilities disclosed also include an approximate allowance in respect of past service costs related to the Gurkha Offer to Transfer.
- 7 Benefits payable from the Armed Forces Compensation Scheme have not been included.

Financial assumptions

- 8 Table A1 (in Appendix) shows the principal financial assumptions adopted to prepare this statement. With effect from 31 March 2009, the assumed rate of return in excess of prices was increased from 2.5% a year to 3.2% a year, and the assumed rate of return in excess of earnings was increased from 1.0% a year to 1.7% a year. In addition, with effect from 31 March 2009, the assumed rate of future price inflation is 2.75% a year and the assumed nominal rate of salary growth is 4.3% a year (both the same as at 31 March 2008).

Demographic assumptions

- 9 The demographic assumptions adopted to prepare this statement were derived from the specific experience of the scheme membership.
- 10 The demographic assumptions (other than the mortality assumptions) adopted for the assessment of the liabilities as at 31 March 2009 are those adopted to determine the employer's charge to the scheme and have been derived with reference to the analysis of the experience of the scheme that was undertaken as part of the full actuarial valuation of the AFPS at 31 March 2005.

- 11 The mortality assumptions adopted for the purpose of the 2008-09 Resource Accounts are the same as those adopted for the 2007-08 Resource Accounts. These include allowance for future mortality improvement in accordance with the UK 2006-based principal population projections (greater than at the 31 March 2005 valuation).
- 12 The contribution rate used to determine the accruing cost in 2008-09 was based on the demographic assumptions applicable at the start of the year: that is, those adopted for the 2007-08 Resource Accounts.

Liabilities

- 13 Table 1 summarises the capital value as at 31 March 2009 of benefits accrued under the AFPS prior to 31 March 2009 based on the data, methodology and assumptions described in paragraphs 4 to 12.

Table 1

Past service liabilities as at 31 March 2009

Value of liability in respect of	£ billion
Pensions in payment	55.2
Deferred pensions	10.8
Active members (past service)	25.0
Total	91.0

Accruing costs

- 14 The cost of benefits accruing in the year ended 31 March 2009 (the 'current service cost') as determined at the start of the year is shown in Table 2. The AFPS is non-contributory for members. The cost of benefits accruing for each year of service is met by the employer.

Table 2

Current Service Cost 2008-09

Current Service Cost	Percentage of pensionable pay
Officers	48.2%
Other Ranks	28.7%

- 15 The employers' share of the standard contribution rate determined for the purposes of the Resource Accounts is not the same as the actual rate charged to employers (which is based on the methodology and the financial and demographic assumptions adopted for the funding of the Scheme).
- 16 The actual rates being charged to the employer (on a pensionable pay basis) are 35.3% p.a. for officers and 19.4% for Other Ranks. This excludes the cost of the Armed Forces Compensation Scheme.

Disclosures

- 17 Tables A2 and A3 (in Appendix) show the Balance sheet and the Profit and loss disclosures as at 31 March 2009.

**Appendix to Actuarial Statement for the Armed Forces Pension Scheme
 for Accounts for the Year Ended 31 March 2009**

Table A1 – Financial assumptions

Assumption	31 March 2009	31 March 2008
Rate of return (discount rate)	6.04%	5.32%
Rate of return in excess of:		
Earnings increases	1.7%	1.0%
Pension increases	3.2%	2.5%
Price Inflation	2.75%	2.75%
Expected return on assets:	n/a	n/a

Table A2 – Balance sheet disclosures

	31 March 2009	31 March 2008
	£billion	£billion
Total market value of assets	Nil	nil
Value of liabilities	(91.0)	(97.2)
Surplus (deficit)	(91.0)	(97.2)
of which recoverable by employers	n/a	n/a

Table A3 – Profit & loss disclosures

	£billion
	Year ending 31 March 2009
Analysis of amount charged to Operating profit	
Current service cost	2.0
Past service cost	-
Total operating charge	2.0
Analysis of the amount credited to other finance income	
Expected return on scheme assets	-
Interest on pension liabilities (@ 5.32%)	- 5.1
Net return	- 5.1
Analysis of amount recognised in STRGL	
Actual return less expected return on scheme assets	-
Experience gains and losses arising on pension liabilities	- 2.7
Changes in mortality assumptions	-
Changes in demographic assumptions (other than mortality)	-
Changes to financial assumptions from 31 March 2009	12.6
Actuarial gain (loss) recognised in STRGL	9.9
Movement in surplus during the year	
Surplus at 31 March 2008	- 97.2
Current service cost	-2.0
Benefits paid during the year	3.4
Past service costs	-
Other finance income	- 5.1
Actuarial gain (loss)	9.9
Surplus at 31 March 2009	- 91.0

Government Actuary's Department
03 July 2009

Statement of Accounting Officer's Responsibilities

Under the Government Resources and Accounts Act 2000, the Ministry of Defence with the consent of HM Treasury has directed the Armed Forces Pension Scheme to prepare for each financial year a statement of accounts in the form and on the basis set out in the Accounts Direction.

With the exception of certain transactions (which are accounted for on a cash basis) the financial statements are prepared on an accruals basis and must give a true and fair view of the financial transactions of the scheme during the year and the disposition, at the end of the financial year, of the net liabilities. Note 2 "Accounting Policies" to the financial statements describes those transactions which are accounted for on a cash basis, the use of which has no material effect on the net outgoings for the year nor on the net liabilities at the year end.

In preparing the financial statements, the Accounting Officer is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- Observe the accounts direction issued by HM Treasury 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, as set out in the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the financial statements; and
- Prepare the financial statements on a going concern basis.

HM Treasury has appointed the Permanent Head of the Department as Accounting Officer for the Armed Forces Pension Scheme. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding the assets of the pension scheme are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in Annex 2 of the Government Financial Reporting Manual.

Statement on the System of Internal Control

Scope of responsibilities

1. As the Accounting Officer for the Armed Forces Pension Scheme (AFPS) and the Armed Forces Compensation Scheme (AFCS), I have responsibility for maintaining a sound system of internal control that supports the achievement of the AFPS and AFCS policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money.

The purpose of the system of internal control

2. The system of internal control 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 departmental policies, aims and objectives, to evaluate the likelihood of 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 for the AFPS and the AFCS for the year ended 31 March 2009 and up to the date of approval of the annual report and accounts, and accords with current Treasury guidance.

Capacity to handle risk

3. AFPS and AFCS services are delivered by the Service Personnel and Veterans Agency (SPVA) through a combination of MOD Civilian/Service Personnel and EDS (Defence) Ltd via a commercial partnering agreement. A further contract is in place between the SPVA and Xafinity Paymaster for the payment of Armed Forces pensions. The arrangement for joint working with EDS is managed via the Agency Management Group (AMG) chaired by the Chief Executive.

4. Risk and Performance Management processes within the SPVA have remained strong throughout the year and, following recent changes to the Board structure¹, these processes have been enhanced to enable greater visibility of risk and performance management within the operational areas of the Agency. The strategic level risks, which have the potential to impact across the Agency, are formally reviewed and updated at the AMG meetings. Below this level, risks are managed by the subordinate Boards that support the AMG. The systematic approach adopted by the Agency to manage risk provides the opportunity for risks to be escalated to the AMG to consider whether they should be incorporated in the strategic level risk register. This ensures that risk registers at all levels remain current and the process is consistent across the Agency. The AMG review the risk management and performance management procedures on an annual basis.

5. Risk owners and risk managers are identified as part of the risk management process. Formal risk management training is provided to SPVA project and operational teams. Risk management information and guidance is available to all staff via the SPVA Intranet.

6. Business and accounting operations of the AFPS and the AFCS are periodically reviewed by a number of audit bodies, including Defence Internal Audit and the National Audit Office.

7. Externally, the AFPS and AFCS is represented on the HM Treasury led Public Sector Pension Scheme Accountants Forum which helps to promote consistency and shares best practice across all public sector pension schemes. Representatives from all public sector pension schemes attend along with members of HM Treasury, the Government Actuaries Department and the National Audit Office.

The risk and control framework

8. Active management of risk is fundamental to the effective achievement of the SPVA's Vision, Mission, Strategic Objectives, Key Performance Targets and other key deliverables. The risk process

¹ In addition to the AMG and Agency Executive Board (AEB) an Operational Board has been created that convenes monthly to consider business within the operational domains of the SPVA.

and procedures give consideration to the probability and the impact on time, cost and performance against the Agency's objectives and key targets. Particular attention is also paid to the controls that are put in place to mitigate the risks. The risk policy includes procedures for the management and escalation of risks. The procedures outline the requirement to consider risks to the achievement of business and personal objectives. Regular monitoring of progress of SPVA Agency 'Business Level' risks are linked to Agency objectives through the Balanced Scorecard.

9. The SPVA Audit Committee (AC), under the chairmanship of one of its Non Executive Directors², is well established and meets quarterly. Defence Internal Audit and the National Audit Office attend the AC and provide advice and guidance where appropriate. The Agency Assurance Team (AT) is in place to provide internal assurance through an agreed programme of work based on a balanced review of the Agency risks and Xafinity Paymaster undertake quarterly audits of Armed Forces pensions in payment. The SPVA contract with EDS sets out the structure for the ownership and management of risk.

10. In accordance with Departmental policy the SPVA has reviewed all of its processes and procedures to ensure that it applies the terms of the Data Protection Act most stringently. In the past year it has significantly tightened its physical controls around data storage and introduced further controls over the movement of data, in line with Cabinet Office guidelines. Data management is also subject to debate at each Audit Committee.

Business Continuity

11. SPVA Business Continuity (BC) plans are subject to regular review and have gradually been extended to cover all critical outputs (not least those within the pensions domain) and the vast majority of all business areas; these provide robust arrangements for implementation. Policy and strategy forums are now established at all management levels. Increased activity focussing on BC culture is underway and work continues to 'remodel' all site plans into a common format, representing a joint MOD/EDS approach. A full schedule of BC and Disaster Recovery (DR) testing has been undertaken in the past year, covering all major systems; the remainder are on course for completion. Xafinity Paymaster has their own fully tested BC plans in place which are reviewed regularly as part of their risk management strategy.

Review of effectiveness

12. As Accounting Officer, I also have responsibility for reviewing the effectiveness of the system of internal control. My review is informed by the work of the MOD internal auditors, SPVA's own internal assurance team and the executive managers within the Agency who have 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 have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the board, AMG and AC and a plan to address weaknesses and ensure continuous improvement of the system is in place.

13. In the current year the effectiveness of the system of internal control operating within the SPVA has been subject to continuous review. Activities that have significantly contributed to maintaining and improving effectiveness include:

- The SPVA Management Boards met on a regular basis in order to advise and support the development of a strategy and plans for delivering the Pensions Strategic Objectives and Key Performance Targets;
- The Agency's Non-Executive Directors were fully involved in the management of the Agency's business providing independent advice to SPVA's Owner's Advisory Board, the AMG, the AC and the SPVA Executive Board;

² The SPVA Audit Committee has three Non-Executive Directors, having co-opted a third Non-Executive Director from the People, Pay and Pensions Agency in January 2009.

- The AC provided advice on the adequacy of internal and external audit arrangements and on the implications of assurances provided in respect of risk, control and governance processes within the organisation. The SPVA AC³ monitored progress made on audit recommendations (made by AT, DIA and the NAO) and progress with current initiatives e.g. on managing change to the AFCS rules.
- A risk assurance workshop with Xafinity Paymaster was held to ensure all risks were identified and control processes in place for all pension payments. An annual assurance statement is signed by the Executive Board of Xafinity Paymaster.
- The AFPS continues to participate in the National Fraud Initiative (NFI) sponsored by the Audit Commission which is used in this context to detect potential fraudulent pension payments. The scheme runs every two years and the next exercise is due to commence in early 2009. This will be the fourth NFI exercise undertaken and it continues to detect pension payments made after the date of death. NFI 2006 concluded in March 2008 and identified 297 cases to be investigated. Of these, 185 cases were confirmed as deaths that had not been reported, resulting in actual net overpayment of £789,305.56.
- Quarterly audits of selected AFPS pension payments and related procedures were undertaken in respect of services provided by Xafinity Paymaster for the administration of Armed Forces pensions. In addition, the Quality Assurance Team undertook financial accuracy post payment checks on a sample of AFCS payments.

Significant internal control problems

14. My review of the effectiveness of internal controls has highlighted one potential weakness in internal control and three matters of substance that I wish to address at this point:

Membership Statistics

- In the 2007-2008 AFPS Statement of Internal Control, reference was made to the Agency experiencing difficulty in establishing the number of members within the AFPS, particularly those with deferred pensions as a result of incomplete data that was available from legacy systems. Since then work has continued to upload data from these systems onto the single Compensation and Pensions System database and to validate the entitlement of each member. Centralisation of these records has not only improved accessibility to the data and confidence in the completeness of the records, but has also provided the opportunity to analyse these records in greater detail. As a result of this more detailed analysis, adjustments have been made to the membership data, which have been incorporated into the membership table and calculation of the provision.

Guaranteed Minimum Pension

- In the accounts for the year 2007-08 an issue relating to the Guaranteed Minimum Pensions was reported. Overpayments identified as a result of this issue have been corrected from April 2009. Changes to processes and controls are being implemented to avoid a repeat of this problem.

AFCS Valuation

- In 2005-06, 2006-07 and 2007-08 the AFPS accounts received a technical qualification as the MOD was unable to provide sufficient evidence to support the completeness and valuation of the provision it had made for the liabilities for compensation payable relating to AFCS cases where claims had yet to be made. An exercise has been carried out to analyse the AFCS historical data to provide sufficient evidence to support the provision and the qualification has been removed.

³ AC membership comprised 2 Non-Executive Directors and an Executive Director of the SPVA for the first half of the financial year and 3 Non-Executive Directors for the remainder of the year and going forward.

AFCS Award Criteria – Emerging Issue

- Following a decision in *S of S v AD and MM* [2009] UKUT 10(AAC)⁴ consideration of new claims against the AFCS was suspended between mid February and 23 April 2009. This impacted the net cash requirement for the AFCS in 2008-09 and will increase the requirement in 2009-10. The Secretary of State is appealing the decision and the contingent liability is included at note 27 to these accounts.

Sir Bill Jeffrey
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme

13 July 2009

⁴ Detailed documentation may be found on the Tribunals web site.

The Certificate of the Comptroller and Auditor General to the House of Commons

I certify that I have audited the financial statements of the Armed Forces Pension Scheme for the year ended 31st March 2009 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, the Combined Revenue Account and Statement of Recognised Gains and Losses, the Combined Balance Sheet, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Accounting Officer and auditor

The Accounting Officer is responsible for preparing the Report of the Managers and the financial statements in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions made thereunder and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer'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 have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000. 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.

In addition, I report to you if the Department 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 HM Treasury regarding transactions is not disclosed.

I review whether the Statement on Internal Control reflects the Department's compliance with HM Treasury's guidance, and I report if it does not. I am not required to consider whether this statement covers all risks and controls, or to form an opinion on the effectiveness of the Department's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Resource Account, which comprises the Report of the Scheme Managers and the Actuarial Report, and consider whether it is consistent with the audited financial statements. I consider the implications for my certificate 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 opinions

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. It also includes an assessment of the significant estimates and judgments made by the Accounting Officer in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the scheme'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 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.

Opinions

In my opinion:

- the financial statements give a true and fair view, in accordance with the Government Resources and Accounts Act 2000 and directions made thereunder by HM Treasury, of the state of the scheme's affairs as at 31 March 2009, and the net cash requirement, net resource outturn, net outgoings, recognised gains and losses and cash flows for the year then ended; and
- the financial statements have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000.

Opinion on Regularity

In my opinion, 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.

Report

As set out in the Report of the Manager and in the Statement on Internal control at pages 14 to 17, in 2007-08 administrative checks in 2007-08 revealed an inconsistency in the calculation of a number of individual pensions because of incorrect uprating being applied to an element known as the Guaranteed Minimum Pension or GMP. This resulted in significant, but immaterial, overpayment and underpayments of pensions which has continued in 2008-09. The results of my separate examination of the end to end process to identify the causes of the error, presented to Parliament under section 9 of the National Audit Act 1983, are published as HC 878 2008-09, Review of errors in Guaranteed Minimum Pension payments. My opinion is not qualified in this respect.

Amyas C E Morse
Comptroller and Auditor General
National Audit Office
151 Buckingham Palace Road
Victoria
London
SW1W 9SS

17 July 2009

Report by the Comptroller and Auditor General

Introduction

1. The Armed Forces Pension Scheme (AFPS) is a salary-related, contracted out, occupational pension scheme open to most members of the Armed Forces and is financed annually through Parliamentary Supply from the Consolidated Fund. The scheme is administered by the Service Personnel and Veterans Agency (SPVA), an Executive Agency of the Ministry of Defence (the Department).
2. On 6 April 2005, the Ministry of Defence (MOD) introduced a new compensation scheme for the Armed Forces which is also accounted for within the AFPS Resource Account. The Armed Forces Compensation Scheme (the Compensation Scheme) replaced previous arrangements for attributable benefits (under the War Pensions Scheme and AFPS 75) for injuries, illnesses or deaths caused by Service on or after 6 April 2005. Compensation is payable in accordance with a defined tariff.
3. The Department is required, under S 7(2) of the Government Resources and Accounts Act 2000, to produce accounts for the AFPS which meet the financial reporting requirements specified in the Government Financial Reporting Manual. Where necessary, under Financial Reporting Standard 12, provisions and contingent liabilities must be included within the financial statements. For the Compensation Scheme, the Department has a present, legal obligation to pay compensation to those with attributable injuries from the point the injury is incurred. An appropriately valued provision is therefore required to be included in the financial statements.
4. Armed Forces personnel can claim whilst still in Service or after leaving. However, claims are required to be made within 5 years of the date of illness or injury other than in exceptional circumstances.
5. Under Section 7(3) of the Government Resources and Accounts Act 2000, I am required to provide an audit opinion as to whether the financial statements of the AFPS provide a true and fair view of the state of affairs of the entity including any provisions made. In the prior year my opinion on these financial statements was qualified because:
 - the scope of my audit was limited as the MOD was unable to provide me with sufficient evidence to support the completeness and valuation of the relevant provision of £113,825,000 for 2007-08 for compensation payable relating to cases where claims had yet to be made, and
 - there were no other audit procedures I could adopt to confirm that the provision was not materially misstated.
6. My opinion was similarly qualified in 2005-06 and in 2006-07.
7. I have not qualified my audit opinion on the 2008-09 Financial Statements because the provision subject to prior years' qualification is now adequately supported as I report below.

MOD's assessment of the AFCS provision for unclaimed compensation

8. While the provision included in the 2007-08 accounts represented the Department's best estimate, they had not obtained sufficient evidence to support the completeness and valuation of the provision. This inability reflected in part the consequence of the introduction of the relatively new AFCS scheme and the lack of collection of data.
9. In 2008-09 SPVA decided to look into alternative sources of information in order to support the provision and to carry out work to understand the nature of the financial liabilities that could arise under the scheme. In particular, they looked carefully at the procedures that are in place within MOD for recording of details of casualties suffered throughout the Armed Forces which are notified

to the Joint Casualty and Compassionate Centre (JCCC). MOD therefore already has well-tested processes which ensure that all deaths and serious injuries are reported through the chain of command as soon as possible after any incident. The system is required to notify next-of-kin of accidents and arrange transport needed as a result of injuries.

10. SPVA Management carried out further work and established that:

- JCCC procedures would capture those individuals most likely to make claims under tariffs 1 to 11 which covers situations where there would be a high probability of payments for severe injuries, lump sum payments and guaranteed income premiums (GIPs), and
- Data derived from other systems would provide sufficient information about less severe, tariff 12-15, potential claims (lump sums). The primary of these other systems is the IRIS (Incident Reporting Information System) which replaced the CHASP (Central Health and Safety Project) database which was discontinued in March 2007.

11. MOD policy is that all but minor injuries are included in the JCCC database. Following review of the detailed work by SPVA, I have concluded that the JCCC database can be relied upon as a full inclusion population for tariffs 1 to 11. This also provides sufficient detail to be able to determine the number of Guaranteed Income Payments and the lump sum payments which arise from claims. The GIPs are the more material part of the provision and the Government Actuaries Department have provided an indicative valuation of these based on the sample data supplied by AFCS.

12. Using the systems and further analysis outlined above, the estimate for the Compensation Scheme provision is shown in Table 1 below together with the number and value of accepted claims made in the first four years of the Compensation Scheme's operation:

Table 1: Estimated provision required for AFCS together with number and value of claims made in the previous first three years of operation of the scheme

	2005-06	2006-07	2007-08	2008-09
No. of claims paid - lump sums	124	677	1,506	4,812 ¹
Value in Year - lump sums and GIPs	£1,274,000	£6,159,000	£13,067,000	£33,490,000
Future value of accepted claims involving continuing payments (Guaranteed Income Payments)	£7,166,000	£24,511,000	£90,373,000	See below
Additional data 2008-09				
Future value for expected claims - major (tariff 1 to 11)	-	-	-	£204,805,000
Future value for expected claims - minor (tariff 12-15)	-	-	-	£10,826,000
Other ¹				£1,156,000 ²
Guaranteed Income Payments - awarded (total of "In Payment" and "Underlying Entitlement")	-	-	-	£135,600,000
Total following review	-	-	-	£352,387,000
Total provision included in accounts (Note 18)	£31,395,000	£118,964,000	£204,198,000³	£352,387,000

¹ Includes 2,636 additional lump sums (ALS) paid as a result of the tariff increase.

² Includes £211,000 ALS payments not yet paid at the year end and £945,000 claims delayed in connection with a continuing legal action.

³ The detailed review performed by AFCS in the year to 31 March 2009 indicates that the provision at March 2008 should have been approximately £229,632,000 against the £204,198,000 provided.

13. The less serious injuries are covered by tariffs 12 to 15 and amounts to 3 percent of the provision. This part of the provision is based on incomplete data. Management have reviewed the data available and found that around 60 per cent of injuries are recorded. Taking this into account together with their review of the propensity to claim, they have made full provision for all less severe injury claims recorded as they consider that this will offset any potential underprovision for the population not being complete. Management are therefore confident that the provision made is a reliable estimate and no material error exists in the provision for less severe injury lump sums.
14. Management have determined that for this year they can therefore obtain details of claims that have been made or could potentially be made and that they have sufficient history to calculate likely success and rejection rates.
15. I am satisfied that the AFCS provision is now materially complete and therefore that the reported liabilities for the Armed Forces Pension Scheme are valued at a level that is true and fair.

Amyas C E Morse
Comptroller and Auditor General
National Audit Office
151 Buckingham Palace Road
Victoria
LONDON SW1W 1SS

17 July 2009

Statement of Parliamentary Supply
Summary of Resource Outturn 2008-09

Request for Resources	2008-09 Estimate			2008-09 Outturn			2008-09 Outturn compared with Estimate savings/ (excess)	2007-08 Outturn	
	Gross Expenditure	A-in-A	Net Total	Gross Expenditure	A-in-A	Net Total			Net Total
	£000	£000	£000	£000	£000	£000			
Armed Forces Retired Pay, Pensions etc	7,334,821	1,465,454	5,869,367	7,307,956	1,465,454	5,842,502	26,865	5,479,274	
Non-budget	-	-	-	-	-	-	-	-	
Total Resources	7,334,821	1,465,454	5,869,367	7,307,956	1,465,454	5,842,502	26,865	5,479,274	

Summary of Net Cash Requirement 2008-09

Note	2008-09		2008-09 Net Total outturn compared with Estimate savings/ (excess)	2007-08 Outturn	
	Estimate	Outturn			
	£000	£000			£000
Net Cash Requirement	4	1,867,960	1,858,146	9,814	1,733,527

Summary of Income Payable to the Consolidated Fund

In addition to appropriations-in-aid, the following income relates to the scheme and is payable to the Consolidated Fund (cash receipts being shown in italics)

Note	Forecast 2008-09		Outturn 2008-09		
	Income	Receipts	Income	Receipts	
	£000	£000	£000	£000	
Total	5	-	-	41,692	41,692

Explanation of the variation between Estimate and Outturn:

The Outturn is less than the Estimate due to a higher pension cost and higher interest payable than anticipated, lower than anticipated revaluation of the Armed Forces Compensation Scheme (AFCS) liability and lower than anticipated interest payable on the AFCS.

Explanation of the variation between estimate net cash requirement and outturn net cash requirement:

The Outturn is less than the Estimate due to a lower level of benefits payable than anticipated.

The notes on pages 27 to 41 form part of these accounts.

Combined Revenue Account

for the year ended 31 March 2009

		2008-09	2007-08
	Notes	£000	£000
Income			
Contributions receivable	7	(1,505,925)	(1,462,455)
Transfers in	8	(1,221)	(934)
Other pension income	9	-	(2)
		(1,507,146)	(1,463,391)
Outgoings			
Pension cost	10	1,992,678	2,226,500
Enhancements	11	708	547
Transfers in	12	1,221	934
Interest on Scheme liabilities	13	5,131,670	4,602,908
		7,126,277	6,830,889
Movement on provision for Project Collins	20	-	9,674
Movement on provision for attributable injury	19	-	(911)
Net outgoings for the year		5,619,131	5,376,261
Armed Forces Compensation Scheme			
	Notes	£000	£000
Movement in provision for AFCS	18	168,076	92,684
Interest on scheme liabilities	18	13,603	5,617
Net outgoings for the year		181,679	98,301
Combined net outgoings for the year	3	5,800,810	5,474,562

Statement of Recognised Gains and Losses

for the year ended 31 March 2009

		2008-09	2007-08
	Notes	£000	£000
Actuarial gain		(9,896,948)	(7,002,098)
Recognised gains for the financial year	17.8	(9,896,948)	(7,002,098)

The notes on pages 27 to 41 form part of these accounts.

Combined Balance Sheet

As at 31 March 2009

	Note	<u>31 March 09</u>	<u>31 March 08</u>
		£000	£000
Current assets:			
Debtors	14.1	3,540	2,671
Cash at bank and in hand	15	51,505	75,692
		<u>55,045</u>	<u>78,363</u>
Creditors (amounts falling due within one year)	16.1	(355,553)	(239,652)
Provision for liabilities and charges:			
Pension liability	17.5	(91,000,000)	(97,200,000)
Armed Forces Compensation Scheme	18	(352,387)	(204,198)
		<u>(91,652,895)</u>	<u>(97,565,487)</u>
Net liabilities, including pension liability			
Taxpayers' equity:			
General fund	21	(91,652,895)	(97,565,487)
		<u>(91,652,895)</u>	<u>(97,565,487)</u>

As the Accounting Officer, I authorise these accounts for issue on 13 July 2009.

Sir Bill Jeffrey
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme

13 July 2009

The notes on pages 27 to 41 form part of these accounts.

Cash Flow Statement

for the year ended 31 March 2009

		<u>2008-09</u>	<u>2007-08</u>
	Notes	£000	£000
Net cash outflow from operating activities	22.1	(1,816,454)	(1,728,815)
Payments of amounts due to the Consolidated Fund	22.2	(4,712)	-
Financing	22.2	1,796,979	1,780,049
(Decrease)/Increase in cash in the period	22.3	<u>(24,187)</u>	<u>51,234</u>

The notes on pages 27 to 41 form part of these accounts.

Notes to the Accounts

1. Basis of Preparation of the Scheme Statements

1.1 The Scheme Statements have been prepared in accordance with the relevant provisions of the 2008-09 *Government Financial Reporting Manual (FReM)* issued by HM Treasury, which reflect the requirements of Financial Reporting Standard (FRS) 17 *Retirement Benefits*. These accounts show the unfunded pension liability and movements in that liability during the year. The accounts also have regard to the recommendations of the Statement of Recommended Practice entitled *Financial Reports of Pension Schemes* to the extent that these are appropriate.

1.2 In addition to the primary statements prepared under UK GAAP, the FReM also requires the scheme to prepare an additional statement – a *Statement of Parliamentary Supply*. This, and its supporting notes, show outturn against estimate in terms of the net resource requirement and the net cash requirement.

1.3 The Scheme Statements summarise the transactions of the Armed Forces Pension Scheme (AFPS) incorporating the Armed Forces Compensation Scheme (AFCS). The Balance Sheet shows the deficit on the schemes; the Revenue Account shows, inter alia, the movements in the liabilities analysed between the pension cost, enhancements and transfers in, and the interest on the schemes' liabilities. The actuarial position of the pension scheme is dealt with in the Report of the Actuary, and the Scheme Statements should be read in conjunction with that report.

1.4 The AFPS is a contracted-out, unfunded, defined benefit pay-as-you-go occupational pension scheme operated by the MOD on behalf of members of the Armed Services who satisfy certain membership criteria. The employer's charge to the pension scheme is met by payment of a Superannuation Contribution Adjusted for Past Experience (SCAPE), calculated as a percentage of military pay based on rank. The SCAPE contribution made by the MOD partially funds the payments made by the AFPS in year.

1.5 Funding from the Consolidated Fund is required to meet the difference between the payments to pensioners and the amounts receivable from MOD. In addition, funding is required to finance movements in working capital including increases or decreases in bank balances.

1.6 Administration expenses (staff, office facilities, etc.) are borne through the Operating Cost Statement of the MOD.

1.7 The Scheme Statements summarise the transactions of not only the AFPS but also the Reserve Forces Pension Scheme (RFPS), Gurkha Pension Scheme (GPS), Non-Regular Permanent Staff Pension Scheme (NRPS) and the AFCS. These are administered and managed in a similar way to the AFPS.

1.8 Members have no choice over the allocation of benefits between the lump sum and the annual pension. However, there are two forms of commutation for existing pensioners – resettlement commutation and life commutation, where the pensioner has the option to abate their pension in return for a lump sum. Benefit payments are accounted for on an accruals basis.

1.9 The Actuarial Statement, shown on pages 9 to 12, which takes account of future obligations, has been prepared by the Government Actuary's Department and should be read in conjunction with the Scheme Statements. The Actuarial Statement has been prepared using the projected accrued benefit method, the actuarial valuation itself being undertaken on a quadrennial basis.

1.10 The accounting policies adopted by the scheme are described below. They have been applied consistently in dealing with items that are considered material in relation to the Scheme Statements.

2. Statement of accounting policies

The accounting policies contained in the FReM follow UK Generally Accepted Accounting Practice for companies (UK GAAP) to the extent that it is meaningful and appropriate to the public sector.

Where the FReM permits a choice of accounting policy, the accounting policy which has been judged to be most appropriate to the particular circumstances of the Scheme for the purpose of giving a true and fair view has been selected. The accounting policies adopted have been applied consistently in dealing with items considered material in relation to the accounts.

2.1 Pension contributions receivable

2.1.1 Employer's normal pension contributions (SCAPE) are accounted for on an accruals basis.

2.1.2 Employees' pension contributions and amounts received in respect of the purchase of added years of service are accounted for on an accruals basis. Contributions deducted from employees' salaries are in respect of 'in-scheme' Additional Voluntary Contributions (AVCs). Neither Free-Standing Additional Voluntary Contributions (FSAVCs) nor payments to providers of stakeholder pensions are brought into account in this statement. The associated increase in the scheme liability is recognised as expenditure.

2.2 Transfers in and out

Transfers in and out of the scheme in respect of individual members are accounted for as income and expenditure (representing the associated increase in the scheme liability) on a cash basis.

2.3 Other income

Other income is accounted for on an accruals basis. To the extent that this income represents an increase in the scheme liability, it is also reflected in expenditure.

2.4 Current service cost

The current service cost is the increase in the present value of the scheme liabilities arising from current members' service in the current period and is recognised in the Revenue Account. The cost is based on a discount rate of 2.5% real (i.e. 5.32% including inflation).

2.5 Past service costs

Past service costs are increases in the present value of the scheme liabilities related to employee service in prior periods arising in the current period as a result of the introduction of, or improvement to, retirement benefits. Past service costs are recognised in the Revenue Account on a straight line basis over the period in which increases in benefit vest.

2.6 Interest on scheme liabilities

The interest cost is the increase during the period in the present value of the scheme liabilities because the benefits are one period closer to settlement and is recognised in the Revenue Account. The interest cost is based on the discount rate of 2.5% real (i.e. 5.32% including inflation).

2.7 Other payments

Other payments are accounted for on an accruals basis.

2.8 Scheme liability

2.8.1 Provision is made for liabilities to pay pensions and other benefits in the future. The scheme liability is measured on an actuarial basis using the projected unit method and as at 31 March 2008 was discounted at 2.5% (i.e. 5.32% after inflation). The discount rate changed on 31 March 2009, from 2.5% to 3.2% and the scheme liability was discounted at this rate. In financial year 2008-09, a rate of 2.5% was used to derive the Current Service Cost (see Note 2.4). Further details of the financial assumptions used are set out at Note 17 to these accounts and in the Actuarial Statement on pages 9 to 12.

2.8.2 Full actuarial valuations by a professionally qualified actuary are obtained at intervals not exceeding four years. The actuary reviews the most recent actuarial valuation at the Balance Sheet date and updates it to reflect current conditions.

2.9 Pensions benefits payable

Pension benefits payable are accounted for as a decrease in the scheme liability on an accruals basis.

2.10 Pension payments to those retiring at their normal retirement age

Where a retiring member has no choice over the allocation of benefits receivable between the value of the lump sum and the annual pension, the transaction is accounted for as a decrease in the scheme liability on an accruals basis.

2.11 Pension payments to and on account of leavers before their normal retirement age

The AFPS is a non-contributory pension scheme; therefore no refund will be made to members on leaving the scheme. Members may request that the value of their service be transferred to a salary related occupational pension scheme, or to a statutory scheme. Transfers out of the scheme are accounted for on a cash basis.

2.12 Lump sums payable on death in service

Lump sum payments on death in service are accounted for on an accruals basis. They are funded through normal pension contributions and are a charge on the pension provision.

2.13 Actuarial gains and losses

Actuarial gains and losses arising from any new valuation and from updating the latest actuarial valuation to reflect conditions at the Balance Sheet date are recognised in the Statement of Recognised Gains and Losses for the year.

2.14 Armed Forces Compensation Scheme

The Armed Forces Compensation Scheme came into effect on 6 April 2005. A provision is made within these accounts to provide for payments due to scheme members in compensation for deaths and injuries, occurring on or after that date and which are considered to be attributable to service in the Armed Forces.

3. Reconciliation of net resource outturn to net outgoings

		2008-09 Outturn compared with Estimate	2007-08 Outturn
	Outturn	Supply Estimate	Estimate
	£000	£000	£000
Net Resource outturn	5,842,502	5,869,367	26,865
Non-supply income (CFERs)	(41,692)	-	41,692
Net Outgoings	5,800,810	5,869,367	68,557

4. Reconciliation of resources to cash requirement

		Estimate	Outturn	Net Total outturn compared with Estimate: savings/ (excess)
	Notes	£000	£000	£000
Net Resource Outturn	3	5,869,367	5,842,502	26,865
Accruals adjustments:				
Non cash items	23	(7,334,821)	(7,307,956)	(26,865)
Changes in working capital other than cash		-	(139,219)	139,219
Use of provision:				
Pension		3,300,514	3,429,329	(128,815)
Attributable injury benefits		446	-	446
Project Collins		-	-	-
Compensation Scheme		32,454	33,490	(1,036)
Net cash requirement		1,867,960	1,858,146	9,814

5. Analysis of income payable to the Consolidated Fund

In addition to appropriations-in-aid, the following income relates to the scheme and is payable to the Consolidated Fund (cash receipts being shown in italics)

	Forecast 2008-09		Outturn 2008-09	
	Income	Receipts	Income	Receipts
	£000	£000	£000	£000
Operating income and receipts – excess A-in-A	-	-	41,692	<i>41,692</i>
Total income payable to the Consolidated Fund	-	-	41,692	<i>41,692</i>

6. Reconciliation of income recorded within the Revenue Account to operating income payable to the Consolidated Fund

Operating income in excess of the authorised appropriations-in-aid estimate is payable to the Consolidated Fund.

	2008-09	2007-08
	£000	£000
Operating income	(1,507,146)	(1,463,391)
Income authorised to be appropriated-in-aid	1,465,454	1,458,679
Operating income payable to the Consolidated Fund	(41,692)	(4,712)

Revenue account

7. Pensions contributions receivable

Employers' contributions are receivable from MOD in respect of active members of the AFPS and amount to an average of 25.41% of pensionable pay.

	2008-09	2007-08
	£000	£000
Employers	1,505,217	1,461,908
Employees:		
Additional Voluntary Contributions	708	547
	1,505,925	1,462,455

8. Pensions transfers-in (see also Note 12)

The nature of the recruitment into the Armed Forces eliminates the opportunity for group transfers into the scheme.

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
Individual transfers in from other schemes	1,221	934
	<u>1,221</u>	<u>934</u>

9. Other pension income

Miscellaneous income consists of contributions to enhance $\frac{1}{3}$ rate Forces Family Pensions to $\frac{1}{2}$ rate, and refunds of resettlement commutation on re-entry into the pension scheme.

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
Miscellaneous income (including refund of gratuities)	-	2
	<u>-</u>	<u>2</u>

10. Pension cost

The current service cost is the increase in the present value of the scheme liabilities arising from current members' service in the current period.

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
Current service cost (see Note 17.5)	1,992,678	2,226,500
	<u>1,992,678</u>	<u>2,226,500</u>

11. Enhancements (see also Note 17.5)

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
Employees AVCs and added years	708	547
	<u>708</u>	<u>547</u>

12. Transfers in (see also Note 8)

Amounts receivable in respect of inward transfers increase the pension liability to the same extent. This increase is reflected in the Revenue Account as expenditure as part of the movements in the provision during the year.

	2008-09	2007-08
	£000	£000
Individual transfers in from other schemes	1,221	934
	1,221	934

13. Interest on scheme liabilities (see also Note 17.5)

The interest charge in the year has been determined by taking 5.32% of the opening balance plus 5.32% of the average of the movements in the year, which are deemed to accrue evenly during the year. The movements in the year exclude the interest charge and the actuarial gains/losses.

	2008-09	2007-08
	£000	£000
Interest charge for the year	5,131,670	4,602,908
	5,131,670	4,602,908

Balance Sheet

14. Debtors - contributions due in respect of pensions

14.1 Analysis by type

Overpayments to pensioners are inherent in the nature of the scheme. Payments to pensioners continue until notification of death is received or until non-return of a life certificate.

	2008-09	2007-08
	£000	£000
Amounts falling due within one year:		
Overpaid pensions (Net of provision for non-recovery)*	3,181	2,192
Less Provision for bad debts	(270)	(115)
	2,911	2,077
Amounts falling due after one year:		
Overpaid pensions	629	594
Total Debtors	3,540	2,671

14.2 Intra-Government balances

	Amounts falling due within one year		Amounts falling due after more than one year	
	2008-09	2007-08	2008-09	2007-08
	£000	£000	£000	£000
Balances with other central government bodies: Ministry of Defence	-	-	-	-
Balances with bodies external to government	2,911	2,077	629	594
At 31 March	2,911	2,077	629	594

15. Cash at bank

	2008-09	2007-08
	£000	£000
Balance at 1 April	75,692	24,458
Net change in cash balances	(24,187)	51,234
Balance at 31 March	51,505	75,692
The following balances at 31 March were held at: Office of HM Paymaster General	51,505	75,692
Balance at 31 March	51,505	75,692

16. Creditors - amounts falling due within one year

16.1 Analysis by type

	2008-09	2007-08
	£000	£000
Amounts falling due within one year:		
Pensions	256,829	118,810
Compensation	1,213	67
HM Revenue & Customs	45,400	44,522
Third party organisations	606	561
	304,048	163,960
Amounts issued from the Consolidated Fund for supply not spent at year end	9,813	70,980
Consolidated Fund extra receipts due to be paid to the Consolidated Fund	41,692	4,712
	355,553	239,652

16.2 Intra-Government balances

	Amounts falling due within one year	
	2008-09	2007-08
	£000	£000
Balances with other central government bodies:		
HM Revenue & Customs	45,400	44,522
Consolidated Fund	51,505	75,692
Balances with bodies external to government	258,648	119,438
	355,553	239,652

17. Provision for pension liability

17.1 The Armed Forces Pension Scheme is an unfunded defined benefit scheme. A full actuarial valuation was carried out as at 31 March 2005 by the Government Actuary's Department. The major financial assumptions used by the actuary when providing the assessment of the accrued liabilities as at the following dates for the Resource Accounting assessments were:

	At 31 March 2009	At 31 March 2008	At 31 March 2007	At 31 March 2006	At 31 March 2005
Rate of increase on salaries	4.3%	4.3%	4.3%	4.0%	3.9%
Inflation assumption	2.75%	2.75%	2.75%	2.5%	2.4%
Discount rate	3.2%	2.5%	1.8%	2.8%	3.5%
Mortality rate at age 60					
- Current Pensioners					
• Officers Men	28.6	28.5	25.6	24.8	24.8
• Officers Women	31.8	31.7	28.6	27.8	27.8
• Other Ranks Men	26.5	26.4	23.6	22.9	22.9
• Other Ranks Women	29.7	29.6	26.6	25.9	25.9
- Future Pensioners (from active status)					
• Officers Men	30.2	30.1	27.5	27.1	27.1
• Officers Women	33.3	33.2	30.5	30.1	30.1
• Other Ranks Men	28.3	28.2	25.6	25.2	25.2
• Other Ranks Women	31.4	31.3	28.5	28.1	28.1

17.2 The scheme managers are responsible for providing the Actuary with information he needs to carry out the valuation. This information includes, but is not limited to details of:

- scheme membership, including age and gender profile, active membership, deferred pensioners and pensioners;
- benefit structure, including details of any discretionary benefits and any proposals to amend the scheme;
- income and expenditure; and,
- following consultation with the Actuary, the key assumptions that should be used to value the scheme liabilities, ensuring that the assumptions are mutually compatible and reflect a best estimate of future experience.

17.3 Pension scheme liabilities accrue over employees' periods of service and are discharged over the period of retirement and, where applicable, the period for which a spouse or eligible partner survives the pensioner. In valuing the scheme liability, the Actuary must estimate the impact of several

inherently uncertain variables far into the future. These variables include not only the key financial assumptions noted in the table above, but also assumptions about the changes that will occur in the future in the mortality rate, the age of retirement and the age from which a pension becomes payable.

17.4 The value of the liability included on the Balance Sheet may be significantly affected by even small changes in assumptions. For example, if at a subsequent valuation, it is considered appropriate to increase or decrease the assumed rate of inflation, or increases in salaries, then the value of the pension liability will increase or decrease. The managers of the scheme accept that, as a consequence the valuation provided by the Actuary is inherently uncertain. The increase or decrease in future liability charged or credited for the year resulting from changes in assumptions is disclosed in notes 17.8 and 17.9. The notes also disclose 'experience' gains or losses showing the amounts charged or credited for the year because events have not coincided with assumptions made for the last valuation.

17.5 Analysis of movements in scheme liability

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Scheme liability at 1 April	(97,200,000)	(100,549,000)
Current service cost (Note 10)	(1,992,678)	(2,226,500)
Interest on pension scheme liability (Note 13)	(5,131,670)	(4,602,908)
	<u>(7,124,348)</u>	<u>(6,829,408)</u>
Income received in respect of enhancements (Note 11)	(708)	(547)
Pension transfers (Note 12)	(1,221)	(934)
	<u>(7,126,277)</u>	<u>(6,830,889)</u>
Benefits paid (Note 17.6)	3,408,661	3,159,042
Pension payments to and on account of leavers (Note 17.7)	20,668	18,749
	<u>3,429,329</u>	<u>3,177,791</u>
Actuarial gain (Note 17.8)	9,896,948	7,002,098
Scheme liability as 31 March	(91,000,000)	(97,200,000)

17.6 Analysis of benefits paid

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Pensions to retired employees and dependents (net of recoveries of overpayments)	2,981,478	2,683,610
Commutations and lump sum benefits on retirement	427,183	475,432
Per cash flow statement	3,408,661	3,159,042

17.7 Analysis of payments to and on account of leavers

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Individual transfers to other schemes	20,668	18,749
Per cash flow statement	20,668	18,749

17.8 Analysis of actuarial gain / (loss)

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Experience losses arising on scheme liabilities	(2,703,052)	(697,902)
Gains arising due to changes in actuarial assumptions	12,600,000	7,700,000
Per Statement of Recognised Gains and Losses	9,896,948	7,002,098

17.9 History of experience gains and losses

This table has been amended from that disclosed in the 2007-08 Resource Accounts in order to include the cumulative actuarial gain or loss and an analysis of experienced gains or losses for the previous four years. The table is in line with the amendments to FRS17 clause 77(h) and 77(o).

	<u>2008-09</u>	<u>2007-08</u>	<u>2006-07</u>	<u>2005-06</u>	<u>2004-05</u>
Experience (gains)/ losses on scheme liabilities: Amount (£000)	2,703,052	697,902	4,214,312	(1,086,490)	762,358
Percentage of the present value of the scheme liabilities	2.97%	0.72%	4.19%	(1.4%)	1.1%
(Gains)/losses arising due to changes in actuarial assumptions: Amount (£000)	(12,600,000)	(7,700,000)	17,235,000	-	-
Percentage of the present value of the scheme liabilities	(13.85%)	(7.92%)	17.14%	-	-
Total actuarial (gain)/loss: Amount (£000)	(9,896,948)	(7,002,098)	21,449,312	(1,086,490)	762,358
Percentage of the present value of the scheme liabilities	(10.88%)	(7.20%)	21.33%	(1.4%)	1.1%
Discount rate adjustment: Amount (£000)				8,200,000	
Total cumulative actuarial (gain)/loss: Amount (£000)	18,701,831	28,598,779	35,600,877	14,151,565	7,038,055

18. Provision for liabilities and charges – Armed Forces Compensation Scheme

Armed Forces Compensation Scheme

The Armed Forces Compensation Scheme (AFCS) was introduced from 6 April 2005 to provide compensation where service is the only or main cause of an injury, illness or death. As compensation for pain and suffering, the AFCS makes a lump sum payment for qualifying injuries and illnesses caused mainly by service. The value is determined by a tariff which has 15 levels. For more serious illnesses and injuries (within tariff levels 1-11) where a loss of earnings capacity may be expected, an ongoing Guaranteed Income Payment (GIP) is awarded.

The scheme is required to provide for the injuries to military personnel that have occurred whilst in service. The provision reflects claims that have been made based on injuries that have occurred, including those incidents occurred but not yet reported. Military personnel have up to 5 years to make a claim under the AFCS.

In the July 2008 Command Paper "The Nation's Commitment: Cross-Government Support to our Armed Forces, their Families and Veterans", the AFCS award levels were increased. The tax-free lump sum payment for the most serious injuries was doubled, raising the maximum lump sum payment to £570,000. All award levels, according to severity of injury, received an uplift of between 10% and 100% in their upfront lump sum payment. Together with the index-linked, tax-free, annual GIP, this means awards for the most seriously injured can be over £1.5M in total over the claimant's lifetime. It was announced at the same time that all those who had received awards between the start of the scheme in 2005 and the implementation of the tariff increase would also benefit from the changes through an

Additional Lump Sum payment. These payments were made to the most seriously injured first; and completion of all additional payments was undertaken by the end of April 2009.

	2008-09	2007-08
	£000	£000
AFCS Provision		
Balance at 1 April	(204,198)	(118,964)
Use of provision in year	33,490	13,067
Interest on Scheme Liabilities	(13,603)	(5,617)
Revaluation at year end	(168,076)	(92,684)
Balance at 31 March	(352,387)	(204,198)
Breakdown of Balance as at 31 March 2009		
Incidents incurred but not yet claimed – Lump Sums and Guaranteed Income Payments	(216,787)	
Guaranteed Income Payments – “In Payment”	(64,300)	
Guaranteed Income Payments – “Underlying Entitlement”	(71,300)	
	(352,387)	
Breakdown of Balance as at 31 March 2008		
Incidents incurred but not yet claimed		(113,825)
Guaranteed Income Payments		(90,373)
		(204,198)

19. Provision for liabilities and charges – Attributable Injury Benefits

Attributable Injury

As a result of the decision by the Court of Appeal on 19 November 2003, a review commenced on all decisions on entitlement to attributable pensions for those conditions that led to invaliding or death-in-service where AFPS administrators have previously not accepted War Pension Scheme decisions on attributability.

All cases have now been reviewed with over £40.6M payments made in respect of 2,492 cases. The provision has been cleared.

	2008-09	2007-08
	£000	£000
Balance at 1 April	-	(2,063)
Movement of provision in year:		
Use of provision in year	-	1,152
Revaluation at year end	-	911
Balance at 31 March	-	-

20. Provision for liabilities and charges – Project Collins

As a result of work undertaken on Project Haven, where certain pension entitlements were erroneously taxed, it was discovered that many individuals were in receipt of the wrong rate of attributable pension due to the application of incorrect rates. This issue has now been reviewed under Project Collins and all payments made. 1,346 cases were identified as incorrect, these have been corrected and arrears amounting to £15.5M paid. The provision has now been cleared.

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Balance at 1 April	-	(2,705)
Movement of provision in year:		
Use of provision in year	-	12,379
Revaluation at year end	-	(9,674)
Balance at 31 March	<u>-</u>	<u>-</u>

21. General Fund

The General Fund represents the total assets less liabilities of the pension scheme, to the extent that the total is not represented by other reserves and financing items.

	<u>2008-09</u>	<u>2007-08</u>
	£000	£000
Balance at 1 April	(97,565,487)	(100,821,838)
Net Parliamentary Funding:		
Draw down	1,796,979	1,780,049
Deemed	70,980	24,458
Year end adjustment:		
Supply creditor – current year	(9,813)	(70,980)
Net Transfer from operating activities:		
Net outgoings	(5,800,810)	(5,474,562)
CFERs repayable to Consolidated Fund	(41,692)	(4,712)
Discount rate adjustment	12,600,000	13,100,000
Actuarial losses	(2,703,052)	(6,097,902)
Balance at 31 March	<u>(91,652,895)</u>	<u>(97,565,487)</u>

22. Notes to the Cash Flow Statement

22.1 Reconciliation of net outgoings to operating cash flows

		<u>2008-09</u>	<u>2007-08</u>
	Notes	£000	£000
Net outgoings for the year		(5,800,810)	(5,474,562)
(Increase) / Decrease in Debtors		(869)	220
Increase in Creditors		140,088	11,963
Increase in pension provision - general	17.5	7,124,348	6,829,408
Increase in pension provision – enhancements	17.5	708	547
Increase in pension provision – transfers in	17.5	1,221	934
Use of provisions – pension liability	17.6	(3,408,661)	(3,159,042)
Use of provisions – refunds and transfers	17.7	(20,668)	(18,749)
Decrease in provision for attributable injury benefits	19	-	(911)
Use of provisions – attributable injury benefits	19	-	(1,152)
Increase in compensation provision	18	181,679	98,301
Use of provision – compensation scheme	18	(33,490)	(13,067)
Increase in provision for Project Collins	20	-	9,674
Use of provision - Project Collins	20	-	(12,379)
Net cash outflow from operating activities		<u>(1,816,454)</u>	<u>(1,728,815)</u>

22.2 Analysis of financing and reconciliation to the net cash requirement

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
From the Consolidated Fund (Supply) – current year	1,796,979	1,780,049
Net financing	1,796,979	1,780,049
Decrease / (Increase) in cash	24,187	(51,234)
Adjustments for payments and receipts not related to Supply		
Payment to the Consolidated Fund	(4,712)	-
Amounts due to the Consolidated Fund, received and not paid over – Excess appropriation-in-aid relating to current year	41,692	4,712
Net cash requirement per Statement of Parliamentary Supply	<u>1,858,146</u>	<u>1,733,527</u>

22.3 Reconciliation of Net Cash Requirement to (decrease) / increase in cash

		2008-09	2007-08
	Note	<u>£000</u>	<u>£000</u>
Net cash requirement		(1,858,146)	(1,733,527)
From Consolidated Fund (Supply) – current year		1,796,979	1,780,049
Consolidated Fund:			
Amounts paid	3	(4,712)	-
Amounts due	3	41,692	4,712
(Decrease) / Increase in cash		<u>(24,187)</u>	<u>51,234</u>

23. Non Cash Items

	2008-09	2007-08
	<u>£000</u>	<u>£000</u>
Current service cost	1,992,678	2,226,500
Enhancements	708	547
Transfers in	1,221	934
Interest on Pension Scheme liability	5,131,670	4,602,908
Interest on Compensation Scheme liability	13,603	5,617
Revaluation of Attributable Injury Provision	-	(911)
Revaluation of Compensation Scheme Provision	168,076	92,684
Revaluation of Project Collins Provision	-	9,674
Non-cash items (See Note 4)	<u>7,307,956</u>	<u>6,937,953</u>

24. Financial Instruments

FRS 29 Financial Instruments – Disclosures, requires disclosures in respect of the role of financial instruments on performance during the period, the nature and extent of the risks to which the AFPS is exposed and how these risks are managed. Because of the non-trading nature of its activities and the way in which government departments are financed, the AFPS 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 apply to a non-public sector body of a similar size.

Liquidity Risk

Resources voted by Parliament finance the combined AFPS/AFCS net revenue resource requirements. The schemes are not therefore exposed to significant liquidity risks.

Interest Rate Risk

All of the schemes' financial assets and liabilities carry nil or fixed rates of interest. The schemes are not therefore exposed to any interest rate risk.

25. Losses

During the year, losses arose in 2,897 cases (2007-08; 2,696 cases). The total loss was £201,540.78 (2007-08; £254,108.66) and this relates to the write-off of pension overpayments.

26. Related-party transactions

The schemes fall within the ambit of the MOD, which is regarded as a related party. During the year, the schemes have had material transactions with the Department whose employees are members of the schemes. None of the managers of the schemes, key managerial staff or other related parties have undertaken any material transactions with the schemes during the year.

27. Contingent Liabilities

There is ongoing legal action concerning the methodology to be applied in determining compensation levels under the Armed Forces Compensation Scheme. The Secretary of State is currently appealing to the Court of Appeal against the ruling of the Upper Tribunal. The Court of Appeal's judgement may increase the level of award in certain circumstances. As well as impacting on future cases there may be a requirement to conduct a retrospective exercise to adjust some awards already made. Current best estimate for this liability as at 31st March 2009 is £150M.



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