Presented pursuant to the GRA Act 2000 c.20 s.6

Armed Forces Pension Scheme

(Incorporating the Armed Forces Compensation Scheme)

Resource Accounts 2007-08

LONDON: The Stationery Office
HC 84

17 December 2008
£9.50

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Contents

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 and 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	Chief Executive
Mr P D Northen (until 19/08/07)	Deputy Chief Executive/Director of Corporate Services
Ms J Adams (from 20/08/07)	Deputy Chief Executive/Director of Corporate Services
Air Commodore D Tonks BSc RAF (until 31/07/07)	Director Change
Mrs A Sansome (from 01/08/07)	Director Change
Brigadier R Bacon	Director Strategy, Requirements and Programmes
Commodore A Ross	Director Operations
Mr T Taylor (until 13/11/07)	Director Veterans Services
Mrs A Sansome (from 14/11/07)	Director Veterans Services
Mr D Gregg (until 06/05/07)	Deputy Director Finance and Corporate Governance
Mr D Allen (from 07/05/07)	Deputy Director Finance and Corporate Governance
Mr A Jablonowski	Non Executive Director
Professor H Drummond	Non Executive Director
Mr K J Ludlam (until 18/06/07)	AFPAA Legacy 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 3.08% 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

Finance Director:

Mr T A Woolley CB
Ministry of Defence
Whitehall
London SW1A 2HB

AFPS & AFCS Scheme Administrator:

RAdm T A Spires
Chief Executive
Service Personnel & Veterans Agency
Centurion Building
Gosport PO13 9XA

Pension Policy:

Mr C Baker
Director General Service Personnel Policy
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 3.6% (2006 2.7%) with effect from 9 April 2007 (10 April 2006).

Membership Statistics

There are three groups of members, defined as follows:

- Active Members: personnel who are in service, which is reckonable for pension purposes.
- Deferred Pensioners: former actives who are not currently in pensionable service but who are entitled to AFPS benefits at some future date.
- Pensioners in Payment: former actives who are currently receiving AFPS benefits, plus other AFPS beneficiaries such as widow(er)s, survivors and other dependants of former actives.

Active members (figures rounded to nearest 5)

	Active members at the start of the year	190,410
Add:	Other adjustment	9,030
Add:	New entrants in year	21,637
	Transfers in	53
Less:	Leavers in year	24,259
	Transfers out	811
	Active members at the end of the year	**196,060**

Deferred members

	Deferred members at the start of the year	329,989
Less:	Other adjustment	10,947
Add:	Members leaving who have deferred pension rights	9,585
Less:	Members taking up deferred pension rights	4,625
	Deferred members at the end of the year	**324,002**

Pensioners in payment

	Pensioners at the start of the year	383,021
Add:	New pensions starting in the year	17,205
Less:	Pensions that have ceased in the year	9,977
	Pensioners at the end of the year	**390,249**

Further Information

Any enquiries about the AFPS or AFCS should be addressed to:

The Scheme Administrator
Service Personnel and Veterans Agency
Centurion Building
Gosport PO13 9XA

Sir Bill Jeffrey

Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme

27 November 2008

Actuarial Statement for the Armed Forces Pension Scheme for Accounts for the Year Ended 31 March 2008

A. Liabilities

The capitalised value as at 31 March 2008 of expected future benefit payments under the Armed Forces Pension Scheme, for benefits accrued in respect of employment (or former employment) prior to 31 March 2008, has been assessed using the methodology and assumptions set out in Sections C and D below. The results are as follows:

Value of Liabilities	£ billion
Pensions in Payment	56.5
Deferred Pensions	11.8
Active Members (Past Service)	28.9
Total	**97.2**

B. Accruing Costs

The Armed Forces Pension Scheme is non-contributory for members. The cost of benefits accruing for each year of service is met by the employer. The cost of benefits accruing in the year 2007/2008 (excluding the cost of the AFCS) has been assessed as follows:

	% of pensionable pay
Officers	55.8%
Other ranks	33%

The actual rates being charged to the employer (on a pensionable pay basis) are 35.3% p.a. for Officers and 19.4% p.a. for Other Ranks (excluding the cost of the AFCS).

C. Methodology

The value of the liabilities has been obtained by projecting the accrued benefits, with allowance for expected future pay increases in respect of active members.

The standard contribution rate for accruing costs has been determined using the entry age method, with assumed ages at entry of 24 years for officers, and 19 years for other ranks.

D. Assumptions

The liabilities of the AFPS at 31 March 2008 have been calculated in accordance with the Resource Accounting requirements, and in particular with the requirement that the discount rate net of price increases should be 2.5% p.a. (pension benefits under the scheme are increased in line with prices). The main financial assumptions made are:

- The gross rate of return in excess of earnings increases is 1.0% p.a.
- The gross rate of return is assumed to be 5.32% p.a. although this assumption has a minor impact on the calculation of the liability.
- In nominal terms, these assumptions are then equivalent to an allowance for increase in salaries of 4.3% p.a., an allowance for price inflation of 2.75% p.a. and an allowance for the rate of increase for pensions in payment and deferred pensions of 2.75% p.a.

The demographic assumptions used to calculate the liabilities at 31 March 2008 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. These assumptions are different to those used to calculate the liabilities as at 31 March 2007 in the 2006/2007 accounts, with the most significant change being the allowance for mortality.

The cost of benefits accruing over the year 2007/08 has been calculated using the same assumptions as were used to calculate the liability of the AFPS at 31 March 2007 in the 2006/2007 accounts.

E. Notes

(1) This Statement is based on the formal valuation carried out as at 31 March 2005 for the AFPS, with an approximate updating to reflect known changes in scheme membership for actives, deferred pensioners and pensioners as at 31 December 2007.

(2) The liabilities in Section A 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.

(3) The liabilities in Section A include an approximate past service cost of £0.1 bn in respect of the Gurkha Offer to Transfer.

(4) The data for this assessment was gathered from SPVA, MoD. The data has been compared with similar data provided for the 31 March 2007 assessment, in order to check it is reasonable.

(5) The deferred membership data figure used in the assessment as at 31 March 2008 was provided by SPVA as the most reasonable figure in light of the data and information held on their systems.

(6) The pension benefits taken into account in this assessment are those normally provided from the rules of the pension scheme, including normal retirement benefits, ill-health retirement benefits, and benefits applicable following the death of the member. Benefits payable from the Armed Forces Compensation Scheme have not been included. The assessments do not include the cost of redundancy benefits in respect of current employees. However, pension payments already being made in respect of such cases are included in the statement of liabilities in Section A above.

Stephen Humphrey
Government Actuary's Department 23 June 2008

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 Schemes (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 2008 and up to the date of approval of the annual report and accounts, and accords with current Treasury guidance.

Capacity to handle risk

3. Since 1 April 2007, AFPS and AFCS administration has been undertaken by the Service Personnel & Veterans Agency (SPVA), following the merger of the Armed Forces Personnel Administration Agency (AFPAA) and the Veterans Agency (VA). AFPS and AFCS services are delivered 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. Following the merger a full review of the risk management process was undertaken; building upon the already established best practices within AFPAA and VA.

4. Risk management is embedded throughout the Agency. The strategic level risks, which have the potential to impact across the Agency, are formally reviewed and updated on a monthly basis at the AMG meeting. Below this level, risks are managed by subordinate groups 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 reviews 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 and revised Agency Critical Success Factors (CSFs) were issued in April 2007.

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. Feedback is given on the risk compliance testing carried out by the SPVA Assurance Team (AT) throughout the financial year.

7. Externally, the AFPS and the 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 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.

9. Regular monitoring of progress of SPVA Agency 'Business Level' risks are linked to Agency objectives through the Balanced Scorecard and CSFs and are reviewed monthly by the AMG.

10. The SPVA Audit Committee (AC), under the chairmanship of one of its Non Executive Directors, is well established and meets quarterly. Defence Internal Audit and the National Audit Office observe on at the AC and provide advice and guidance where appropriate. The AT provides internal assurance through an agreed programme of work based on a balanced review of the Agency risks.

11. The SPVA contract with EDS sets out the structure for the ownership and management of risk. A Joint Risk Policy Statement outlines the approach to the management of risk within the Agency and is signed by both CE SPVA and the EDS Account Director.

12. Regular audits of pensions in payment are undertaken on a quarterly basis at the Xafinity Paymaster premises (the company contracted to undertake payments to retired service personnel and their dependants).

13. Responsibility for the management and day-to-day accounting for AFPS/AFCS payments has now moved from Innsworth to the SPVA site at Norcross. This has involved recruiting new personnel. Processes and procedures are still bedding-in but risks to the delivery of crucial financial outputs are now considered to be low.

Business Continuity

14. SPVA Business Continuity (BC) plans are in place following merger and provide robust arrangements for implementation should the need arise. A review of these plans is ongoing and an SPVA BC strategy document reflecting the 07/08 review (prompted by AFPAA/VA merger) was produced and launched on 01 April 08. BC Focal Points and Working Groups have been established in all sites in addition to mandatory BC training for all Agency staff. Focus during 08/09 will be to further embed a BC culture within SPVA through education and increased publicity. Xafinity Paymaster has their own fully tested BCP plans in place which are reviewed regularly as part of their risk management strategy.

Review of effectiveness

15. As Accounting Officer, I also have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the MoD internal auditors, SPVA's own internal assurance team, and the executive managers within SPVA, 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 SPVA Executive Board, the SPVA Audit Committee and the Agency Management Group (AMG) who are responsible for managing business risk and a plan to address weaknesses and ensure continuous improvement of the system is in place.

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

- The SPVA AMG met regularly in order to advise and support me in developing a strategy and overseeing plans for delivering the Agency's Strategic objectives and key performance targets;

- The Agency's two 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 and the SPVA Executive Board;
- A full review of pension arrangements was undertaken by the AT, against a set of assurance criteria (exam questions) posed by the Centre Top Level Budget (CBAC). This work was reviewed twice by the SPVA AC, the first occasion being a joint CBAC / SPVA AC / Services Personnel Policy (SPPOL) review session and gave substantial assurance on the control environment. The data collected will be used to underpin the management of risk in these areas;
- The SPVA AC also reviewed arrangements for the governance of pensions schemes and a new governance arrangement between SPVA and SPPOL was subsequently agreed and is now in force;
- 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 continue 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 NFI 2006 commenced in October 2006 and will be completed by end March 2008. This is the third NFI exercise undertaken and it continues to detect pension payments made after the date of death;
- 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 Checking Team undertook financial accuracy post payment checks on all AFCS payments; and
- In recognition of considerable differences in the IS/IT infrastructure between the ex VA and AFPAA sites, following a study, the AMG has endorsed a number of recommendations for change that will be gradually implemented during 2008/09.

Significant internal control problems

17. My review of the effectiveness of internal controls has not highlighted any significant weaknesses within either the AFPS or AFCS. There are however four matters of substance that I wish to address at this point:

- In the last two SICs reference was made to issues concerning the way information was shared between the VA and AFPAA in respect of Pension's casework. Work to identify and resolve the cases affected has been taken forward under the auspices of Project Collins and this has continued throughout this financial year, resulting in significant additional payments to retired Service Personnel. Additional controls have been introduced to prevent reoccurrence.
- Reference was also made last year to financial issues relating to the AFCS. The MOD still remains unable to provide sufficient evidence to support the completeness and valuation of the provision it has made for the liabilities for compensation payable relating to AFCS cases where claims have yet to be made. The Department is unable to rely on claim rates and values of other schemes to aid its estimation and nor is sufficient information available on the frequency of potentially eligible incidents or the propensity to claim within the Armed Forces. This led to a technical qualification of the AFPS accounts in 2005/2006 and 2006/2007and it is anticipated this will continue until the AFCS has been in existence for a number of years and trends established.
- The SPVA experienced considerable difficulty this year verifying membership numbers, particularly in respect of preserved awards. To some extent this was a timing issue as the CAPS data validation project was not planned to complete until June 08 and therefore was still in progress at the year end. Initially this impacted our ability to validate the accuracy of the AFPS accounts; however following offline evaluation of the impact of the project, sufficient confidence was gained in the underlying data to resolve the matter.

- During the year it was realised that incorrect application of the Guaranteed Minimum Pension increases had resulted in service pension overpayments estimated as £4.6M.

Sir Bill Jeffrey

Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme

27 November 2008

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 31 March 2008 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, the Revenue Account and Statement of Recognised Gains and Losses, the 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 annual report, which comprises the Report of the Scheme Managers and the Actuarial Statement, 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 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.

The Certificate of the Comptroller and Auditor General to the House of Commons *(continued)*

In estimating the provision for liabilities for the Armed Forces Compensation Scheme the Scheme Managers were unable to provide me with robust data to support the level of provision made in respect of incidents incurred but not yet reported. There were no additional audit procedures I could undertake to provide me with assurance as to the level of provision. The scope of my audit was therefore limited in this respect.

Opinions

Qualified Opinion arising from limitation in audit scope

In my opinion:

- except for the effects of such adjustments which might have been found to be necessary had I been able to obtain sufficient evidence concerning the valuation of the provision for certain liabilities of the Armed Forces Compensation Scheme, 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 2008, and the net cash requirement, net resource outturn, net outgoings, recognised gains and losses and cash flows for the year then ended;
- the financial statements have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000; and
- in respect solely of the limitation on my work relating to the Armed Forces Compensation Scheme provision for incidents incurred but not yet reported I have not obtained all the information and explanations that I considered necessary for the purposes of my audit.

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.

My report on pages 16 to 17 provides further details.

T J Burr
Comptroller and Auditor General
National Audit Office
151 Buckingham Palace Road
Victoria
London SWIW 9SS

4 December 2008

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[1].

2. On 6 April 2005 the existing pension scheme, known as AFPS 75, was closed to new entrants and a new scheme, AFPS 05, opened. Both Schemes are accounted for within the AFPS Resource Account.

3. On 6 April 2005, the Ministry of Defence introduced a new compensation scheme for the Armed Forces which is also accounted for within the AFPS Resource Account. The Armed Forces Compensation Scheme (AFCS) replaced previous arrangements for attributable benefits (under the War Pensions Scheme (WPS) 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.

4. The MoD 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.

5. For the AFCS, the MoD 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 of the AFPS.

6. Armed Forces personnel can claim whilst still in Service or after leaving, but claims are required to be made within 5 years of the date of illness or injury other than in exceptional circumstances.

7. 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. My opinion on these financial statements is qualified because:

- the scope of my audit was limited as the Ministry of Defence 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 (2006-07 £94,453,000) for compensation payable relating to cases where claims have yet to be made; and
- there were no other audit procedures I could adopt to confirm that the AFCS provision was not materially misstated.

8. My opinion was similarly qualified in 2005-06 and in 2006-07.

Changes to the operation of the scheme in 2007-08

9. During 2007-08 a review of the AFCS was undertaken with specific regard to those sustaining multiple injuries in a single incident. As a result the number of the most severely injured personnel eligible to receive higher awards up to the existing maximum award (of £285,000) increased[2].

10. 31 individuals were affected by the revision to the scheme's rules, which included an additional payment for those qualifying where awards had already been processed. This resulted in an increase in the value of awards of approximately £1,375,000. This amount is included in the total AFCS figures stated in the accounts.

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[1] SPVA was formed by the merger on 1 April 2007 of the Armed Forces Personnel Administration Agency (AFPAA) and the Veterans Agency.

[2] The revised rules meant that for individuals suffering injury at "tariff 4" or above all injuries or conditions attracted 100% of the tariff value up to the existing maximum award of £285,000.

11. A wider review of AFCS tariff values is being undertaken and any consequential financial impacts will be in the 2008-09 financial statements.

MOD's assessment of the AFCS provision for unclaimed compensation

12. The MoD continue to look at their methodology to support the liability for the AFCS scheme in order to estimate the provision required under FRS 12 for unclaimed compensation. The number and value of accepted claims made in the first three years of the Scheme's operation is shown in the table below:

Table 1: Number and value of claims made in the first three years of operation of the AFCS

	2005-06	**2006-07**	**2007-08**
No. of payments	124	677	1506
Value in Year			
– initial payments	£1,274,000	£6,159,000	£13,067,000
Future value of accepted claims involving continuing payments (Guaranteed Income Payments)	£7,166,000	£24,511,000	£90,373,000

13. SPVA review all the information they consider to be available including accident statistics in the military environment to help value the liability for incidents that have taken place but for which claims have not been made. The Agency do not have sufficient internal information on the likelihood of accidents leading to claims. The nature of the scheme also means they cannot rely on claim rates and values of other schemes to aid their estimation of the incidence and frequency of potentially eligible incidents in the armed forces and the propensity to claim of armed forces personnel. A further complication is that potential claimants have five years during which to make a claim.

14. While the provision included in the accounts therefore represents the Department's best estimate, they have not obtained sufficient evidence to support the completeness and valuation of the provision. This inability reflects the consequence of the introduction of the relatively new AFCS scheme and the lack of collection of data.

Estimation of liabilities in the future

15. The Armed Forces Compensation Scheme has been in existence since 2005. Over the next few years, MOD should be able to assess the history of injury type and frequency more accurately and also gain evidence of the propensity of Armed Forces personnel to claim under this Scheme. Changes to the scheme will need to be assessed for their impact on any provision as they could affect either the population covered or the levels of compensation to be paid. Such changes may in turn reduce the value and incidence of historic claims as an indicator to help establish any future liability. But once sufficient and relevant information becomes available to enable me to audit the underlying assumptions, I will be able to remove the limitation in scope of my audit opinion.

16. This qualification is in respect of the Armed Forces Compensation Scheme liability only. I am satisfied that the reported liabilities for the AFPS 05 and AFPS 75 Pension Schemes are valued at a level that is true and fair.

T J Burr
Comptroller and Auditor General
National Audit Office
151 Buckingham Palace Road
Victoria
London SWIW 9SS

4 December 2008

Statement of Parliamentary Supply

Summary of Resource Outturn 2007-08

	2007-08 Estimate						2007-08 Outturn	2006-07 Outturn
Request for Resources	Gross Expenditure	A-in-A	Net Total	Gross Expenditure	A-in-A	Net Total	Net Total outturn compared with Estimate: savings/ (excess)	Net Total
	£000	£000	£000	£000	£000	£000	£000	£000
Armed Forces Retired Pay, Pensions etc	7,054,316	1,458,679	5,595,637	6,937,953	1,458,679	5,479,274	116,363	4,398,961
Non-budget	–	–	–	–	–	–	–	–
Total Resources	**7,054,316**	**1,458,679**	**5,595,637**	**6,937,953**	**1,458,679**	**5,479,274**	**116,363**	**4,398,961**

Summary of Net Cash Requirement 2007-08

		2007-08			2006-07
		Estimate	Outturn	Net Total outturn compared with Estimate: savings/ (excess)	Outturn
	Note	£000	£000	£000	£000
Net Cash Requirement	4	1,839,057	1,733,527	105,530	1,579,911

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)

		Forecast 2007-08		Outturn 2007-08	
		Income	Receipts	Income	Receipts
	Note	£000	£000	£000	£000
Total	5	–	–	4,712	*70,980*

Explanation of the variation between Estimate and Outturn:

At present the Government Actuary's Department (GAD) are unable to assist in providing a professional valuation of the AFCS liability because of insufficient relevant data. An internal calculation was performed, at the budget stage, which calculated an in year increase in the year of £200M was required. At year end this was revised to £90M resulting in a lower than anticipated movement on the AFCS provision.

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 22 to 36 form part of these accounts.

Combined Revenue Account
for the year ended 31 March 2008

	Notes	2007-08 £000	2006-07 £000
Income			
Contributions receivable	7	(1,462,455)	(1,420,123)
Transfers in	8	(934)	(1,946)
Other pension income	9	(2)	(149)
		(1,463,391)	**(1,422,218)**
Outgoings			
Pension cost	10	2,226,500	1,659,199
Enhancements	11	547	594
Transfers in	12	934	1,946
Interest on Scheme liabilities	13	4,602,908	4,065,995
		6,830,889	**5,727,734**
Movement on provision for Project Collins	20	9,674	(2,951)
Movement on provision for attributable injury	19	(911)	2,668
Net outgoings for the year		**5,376,261**	**4,305,233**

Armed Forces Compensation Scheme	Notes	£000	£000
Movement in provision for AFCS	18	92,684	92,340
Interest on scheme liabilities	18	5,617	1,388
Net outgoings for the year		**98,301**	**93,728**
Combined net outgoings for the year	3	**5,474,562**	**4,398,961**

Statement of Recognised Gains and Losses
for the year ended 31 March 2008

	Notes	2007-08 £000	2006-07 £000
Actuarial (gain)/loss		(7,002,098)	21,449,312
Recognised (gains)/losses for the financial year	17.8	**(7,002,098)**	**21,449,312**

The notes on pages 22 to 36 form part of these accounts.

Combined Balance Sheet

As at 31 March 2008

	Notes	31 March 08 £000	31 March 07 £000
Current assets:			
Debtors	14	2,671	2,891
Cash at bank and in hand	15	75,692	24,458
		78,363	**27,349**
Creditors (amounts falling due within one year)	16(a)	(239,652)	(176,455)
Provision for liabilities and charges:			
Pension liability	17.5	(97,200,000)	(100,549,000)
Attributable injury benefit	19	–	(2,063)
Project Collins	20	–	(2,705)
Armed Forces Compensation Scheme	18	(204,198)	(118,964)
Net liabilities, including pension liability		**(97,565,487)**	**(100,821,838)**
Taxpayers' equity:			
General fund	21	(97,565,487)	(100,821,838)
		(97,565,487)	**(100,821,838)**

As the Accounting Officer, I authorise these accounts for issue on 4 December 2008.

Sir Bill Jeffrey
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme 27 November 2008

The notes on pages 22 to 36 form part of these accounts.

Cash Flow Statement
for the year ended 31 March 2008

	Notes	2007-08 £000	2006-07 £000
Net cash outflow from operating activities	22(a)	(1,728,815)	(1,579,911)
Payments of amounts due to the Consolidated Fund	22(b)	–	(44,825)
Financing	22(b)	1,780,049	1,589,708
Increase/(Decrease) in cash in the period	22(c)	**51,234**	**(35,028)**

The notes on pages 22 to 36 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 2007-08 *Government Financial Reporting Manual (FReM)* issued by the 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 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 7 and 8, 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 1.8 % real (i.e. 4.6% 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 1.8 % real (i.e. 4.6% 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 is discounted at 1.8% (i.e. 4.6% after inflation). The discount rate changed on 31 March 2008, from 1.8% to 2.5% and the scheme liability was discounted at this rate. In-year, a rate of 1.8% 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 7 to 8.

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

				2007-08	2006-07
		Outturn	Supply Estimate	Outturn compared with Estimate	Outturn
	Note	£000	£000	£000	£000
Net Resource outturn		5,479,274	5,595,637	116,363	4,398,961
Non-supply income (CFERs)	6	(4,712)	–	4,712	–
Net Outgoings		**5,474,562**	**5,595,637**	**121,075**	**4,398,961**

4. Reconciliation of resources to cash requirement

	Note	Estimate	Outturn	Net Total outturn compared with Estimate: savings/ (excess)
		£000	£000	£000
Net Resource Outturn	3	5,595,637	5,479,274	116,363
Accruals adjustments:				
Non cash items	23	(7,054,316)	(6,937,953)	(116,363)
Changes in working capital other than cash		(5,220)	(12,183)	6,963
Use of provision:				
Pension		3,275,187	3,177,791	97,396
Attributable injury benefits		2,063	1,152	911
Project Collins		13,706	12,379	1,327
Compensation Scheme		12,000	13,067	(1,067)
Net cash requirement		**1,839,057**	**1,733,527**	**105,530**

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 2007-08		Outturn 2007-08	
	Income	Receipts	Income	Receipts
	£000	£000	£000	£000
Operating income and receipts – excess A-in-A	–	–	4,712	–
Excess cash surrenderable to the Consolidated Fund	–	–	–	*70,980*
Total income payable to the Consolidated Fund	**–**	**–**	**4,712**	**70,980**

An advance of £85 million was obtained from HM Treasury's Contingencies Fund in mid March to cover outstanding AFPS payments. This was repaid on 20 March 2008.

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.

	2007-08	2006-07
	£000	£000
Operating income	(1,463,391)	(1,422,218)
Income authorised to be appropriated-in-aid	1,458,679	1,432,094
Operating income payable to the Consolidated Fund	**(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 25.38% of pay.

	2007-08	2006-07
	£000	£000
Employers	1,461,908	1,419,529
Employees:		
Additional Voluntary Contributions	547	594
	1,462,455	**1,420,123**

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.

	2007-08	2006-07
	£000	£000
Individual transfers in from other schemes	934	1,946
	934	**1,946**

9. Other pension income

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

	2007-08	2006-07
	£000	£000
Miscellaneous income (including refund of gratuities)	2	149
	2	**149**

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.

	2007-08	2006-07
	£000	£000
Current service cost (see Note 17.5)	2,226,500	1,659,199
	2,226,500	**1,659,199**

11. Enhancements *(see also Note 17.5)*

	2007-08	2006-07
	£000	£000
Employees AVCs and added years	547	594
	547	**594**

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.

	2007-08	2006-07
	£000	£000
Individual transfers in from other schemes	934	1,946
	934	**1,946**

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

The interest charge in the year has been determined by taking 4.6% of the opening balance plus 4.6% 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.

	2007-08	2006-07
	£000	£000
Interest charge for the year	4,602,908	4,065,995
	4,602,908	**4,065,995**

Balance Sheet

14. Debtors – contributions due in respect of pensions

14(a) 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.

	2007-08	2006-07
	£000	£000
Amounts falling due within one year:		
Overpaid pensions	2,192	2,630
Less Provision for bad debts	(115)	(434)
	2,077	**2,196**
Amounts falling due after one year:		
Overpaid pensions	594	695
Total Debtors	**2,671**	**2,891**

14(b) Intra-Government balances

	Amounts falling due within one year		Amounts falling due after more than one year	
	2007-08	2006-07	2007-08	2006-07
	£000	£000	£000	£000
Balances with other central government bodies:				
Ministry of Defence	–	–	–	–
Balances with bodies external to government	2,077	2,196	594	695
At 31 March	**2,077**	**2,196**	**594**	**695**

15. Cash at bank

	2007-08	2006-07
	£000	£000
Balance at I April	24,458	59,486
Net change in cash balances	51,234	(35,028)
Balance at 31 March	**75,692**	**24,458**
The following balances at 31 March were held at:		
Office of HM Paymaster General	75,692	24,458
Balance at 31 March	**75,692**	**24,458**

16. Creditors – amounts falling due within one year

16(a) Analysis by type

	2007-08	2006-07
	£000	£000
Amounts falling due within one year:		
Pensions	118,810	104,634
Compensation	67	967
HM Revenue & Customs	44,522	42,919
Third party organisations	561	511
MoD	–	2,966
	163,960	151,997
Amounts issued from the Consolidated Fund for supply not spent at year end	70,980	24,458
Consolidated Fund extra receipts due to be paid to the Consolidated Fund	4,712	–
	239,652	**176,455**

16(b) Intra-Government balances

	Amounts falling due within one year	
	2007-08	2006-07
	£000	£000
Balances with other central government bodies:		
HM Revenue & Customs	44,522	42,919
MoD	–	2,966
Consolidated Fund	75,692	24,458
Balances with bodies external to government	119,438	106,112
	239,652	**176,455**

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 2008	At 31 March 2007	At 31 March 2006	At 31 March 2005	At 31 March 2004
Rate of increase on salaries	4.3%	4.3%	4.0%	3.9%	3.9%
Inflation assumption	2.75%	2.75%	2.5%	2.4%	2.4%
Discount rate	2.5%	1.8%	2.8%	3.5%	2.4%
Mortality rate					
– Current Pensioners					
● Officers Men	89	86	85	85	85
● Officers Women	92	89	88	88	88
● Other Ranks Men	86	84	83	83	83
● Other Ranks Women	90	87	86	86	86
– Future Pensioners (from active status)					
● Officers Men	90	88	87	87	87
● Officers Women	93	90	90	90	90
● Other Ranks Men	88	86	85	85	85
● Other Ranks Women	91	89	88	88	88

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

	2007-08	**2006-07**
	£000	£000
Scheme liability at 1 April	**(100,549,000)**	**(76,400,000)**
Current service cost (Note 10)	(2,226,500)	(1,659,199)
Interest on pension scheme liability (Note 13)	(4,602,908)	(4,065,995)
	(6,829,408)	(5,725,194)
Income received in respect of enhancements (Note 11)	(547)	(594)
Pension transfers (Note 12)	(934)	(1,946)
	(6,830,889)	(5,727,734)
Benefits paid (Note 17.6)	3,159,042	3,009,332
Pension payments to and on account of leavers (Note 17.7)	18,749	18,714
	3,177,791	3,028,046
Actuarial gain / (loss) (Note 17.8)	7,002,098	(21,449,312)
Scheme liability as 31 March	**(97,200,000)**	**(100,549,000)**

17.6 Analysis of benefits paid

	2007-08	2006-07
	£000	£000
Pensions to retired employees and dependents (net of recoveries of overpayments)	2,683,610	2,554,933
Commutations and lump sum benefits on retirement	475,432	454,399
Per cash flow statement	**3,159,042**	**3,009,332**

17.7 Analysis of payments to and on account of leavers

	2007-08	2006-07
	£000	£000
Individual transfers to other schemes	18,749	18,714
Per cash flow statement	**18,749**	**18,714**

17.8 Analysis of actuarial gain / (loss)

	2007-08	2006-07
	£000	£000
Experience losses arising on scheme liabilities	(697,902)	(4,214,312)
Gains/(losses) arising due to changes in actuarial assumptions	7,700,000	(17,235,000)
Per Statement of Recognised Gains and Losses	**7,002,098**	**(21,449,312)**

17.9 History of experience gains and losses

	2007-08	2006-07	2005-06	2004-05
Experience (gains)/ losses on scheme liabilities:				
Amount (£000)	697,902	4,214,312	(1,086,490)	762,358
Percentage of the present value of the scheme liabilities	0.72%	4.19%	(1.4%)	1.1%
(Gains)/losses arising due to changes in actuarial assumptions Amount (£000)	(7,700,000)	17,235,000	–	–
Percentage of the present value of the scheme liabilities	(7.92%)	17.14%	–	–
Total actuarial (gain)/loss Amount (£000)	(7,002,098)	21,449,312	(1,086,490)	762,358
Percentage of the present value of the scheme liabilities	(7.20%)	21.33%	(1.4%)	1.1%

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

Armed Forces Compensation Scheme

The Armed Forces Compensation Scheme 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.

	AFCS incidents incurred but not yet reported	AFCS known claims	AFCS total provision
	£000	£000	£000
Balance at 1 April 2007	**(94,453)**	**(24,511)**	**(118,964)**
Use of provision in year	–	13,067	13,067
Interest on Scheme Liabilities	(4,460)	(1,157)	(5,617)
Revaluation at year end	(14,912)	(77,772)	(92,684)
Balance at 31 March 2008	**(113,825)**	**(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.

	2007-08	2006-07
	£000	£000
Balance at 1 April	**(2,063)**	**(2,643)**
Movement of provision in year:		
Use of provision in year	1,152	3,248
Revaluation at year end	911	(2,668)
Balance at 31 March	**–**	**(2,063)**

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.

	2007-08	2006-07
	£000	£000
Balance at 1 April	**(2,705)**	**(8,792)**
Movement of provision in year:		
Use of provision in year	12,379	3,136
Revaluation at year end	(9,674)	2,951
Balance at 31 March	**–**	**(2,705)**

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.

	2007-08	2006-07
	£000	£000
Balance at 1 April	(100,821,838)	(76,553,476)
Net Parliamentary Funding:		
Draw down	1,780,049	1,589,708
Deemed	24,458	14,661
Year end adjustment:		
Supply creditor – current year	(70,980)	(24,458)
Net Transfer from operating activities:		
Net outgoings	(5,474,562)	(4,398,961)
CFERs repayable to Consolidated Fund	(4,712)	–
Discount rate adjustment*	13,100,000	–
Actuarial losses*	(6,097,902)	(21,449,312)
Balance at 31 March	**(97,565,487)**	**(100,821,838)**

* The Actuarial loss and Discount rate adjustments were disclosed in aggregate in the prior year.

22. Notes to the Cash Flow Statement

22(a) Reconciliation of net outgoings to operating cash flows

	Notes	2007-08 £000	2006-07 £000
Net outgoings for the year		(5,474,562)	(4,398,961)
Decrease in Debtors		220	10,979
Increase in Creditors		11,963	27,481
Increase in pension provision – general	17.5	6,829,408	5,725,194
Increase in pension provision – enhancements	17.5	547	594
Increase in pension provision – transfers in		934	1,946
Use of provisions – pension liability	17.6	(3,159,042)	(3,009,332)
Use of provisions – refunds and transfers	17.7	(18,749)	(18,714)
(Decrease)/Increase in provision for attributable injury benefits	19	(911)	2,668
Use of provisions – attributable injury benefits	19	(1,152)	(3,248)
Increase in compensation provision	18	98,301	93,728
Use of provision – compensation scheme	18	(13,067)	(6,159)
Increase/(Decrease) in provision for Project Collins	20	9,674	(2,951)
Use of provision – Project Collins	20	(12,379)	(3,136)
Net cash outflow from operating activities		**(1,728,815)**	**(1,579,911)**

22(b) Analysis of financing and reconciliation to the net cash requirement

	2007-08 £000	2006-07 £000
From the Consolidated Fund (Supply) – current year	1,780,049	1,589,708
Net financing	1,780,049	1,589,708
(Increase)/decrease in cash	(51,234)	35,028
Adjustments for payments and receipts not related to Supply		
Payment to the Consolidated Fund	–	(44,825)
Amounts due to the Consolidated Fund, received and not paid over – Excess appropriation-in-aid relating to current year	4,712	–
Net cash requirement per Statement of Parliamentary Supply	**1,733,527**	**1,579,911**

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

		2007-08 £000	2006-07 £000
Net cash requirement		(1,733,527)	(1,579,911)
From Consolidated Fund (Supply) – current year		1,780,049	1,589,708
Amounts due/(paid to) to the Consolidated Fund	3	4,712	(44,825)
Increase/(decrease) in cash		**51,234**	**(35,028)**

23. Non Cash Items

	2007-08	2006-07
	£000	£000
Current service cost	2,226,500	1,659,199
Enhancements	547	594
Transfers in	934	1,946
Interest on Pension Scheme liability	4,602,908	4,065,995
Interest on Compensation Scheme liability	5,617	1,388
Revaluation of Attributable Injury Provision	(911)	2,668
Revaluation of Compensation Scheme Provision	92,684	92,340
Revaluation of Project Collins Provision	9,674	(2,951)
Non-cash items (See Note 4)	**6,937,953**	**5,821,179**

24. 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 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 be typical of the listed companies to which FRS 13 applies. In line with FRS13, short term debtors and creditors (those that mature or become payable within twelve months from the balance sheet date) have been excluded from these disclosures.

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 2,696 cases (2006-07; 4,132 cases). The total loss was £254,108.66 (2006-07; £224,921.32) and this relates to the write-off of pension overpayments. In addition a loss of £1,763,809.65 relating to overpayments of 98 pensioners was identified following the Project Collins work. HM Treasury authorised the write off of these overpayments on 14th March 2008.

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. Events After the Balance Sheet Date

On 17 July 2008 the Secretary of State for Defence and the Minister of State for the Armed Forces issued a Command Paper entitled The Nation's Commitment: Cross-Government Support to Our Armed Forces, their Families and Veterans. The paper included proposals to uplift all AFCS lump sum payments according to the severity of the injury. These uplifts will be extended to the commencement of the AFCS scheme in April 2005. The proposals are still under consultation and legislation is not expected to be passed to support the changes until December 2008. It is anticipated that the cost of backdated payments is likely to exceed £7 million.

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