Parliamentary Contributory Pension Fund

Valuation as at 1 April 2008

GOVERNMENT ACTUARY'S DEPARTMENT

HC 345

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PARLIAMENTARY CONTRIBUTORY PENSION FUND
VALUATION AS AT 1 APRIL 2008

Report by the Government Actuary

Valuation Report presented to the
House of Commons by the Government Actuary pursuant to
Section 3(5) of the Parliamentary and Other Pensions Act 1987

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GOVERNMENT ACTUARY'S DEPARTMENT

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1 Summary

To: The Trustees of the Parliamentary Contributory Pension Fund
The Minister for the Civil Service

1.1. I have carried out the actuarial valuation of the Parliamentary Contributory Pension Fund as at 1 April 2008. The main objective of the valuation is to recommend the rate of contributions to be paid by the Exchequer into the Fund. In order to prepare this valuation, I have consulted with both the trustees and Cabinet Office to determine how each party views the objectives of the funding of the scheme. The outcome of the consultation is that I have been able to put together a Funding Principles Consensus Statement which I attach as Appendix A. This statement has been seen in draft by the parties and I am content that both parties subscribe to the views expressed.

1.2. **Methodology** The valuation has been performed using standard actuarial methodology. The liabilities, which comprise the future outgo on benefits and expenses, are capitalised as at the valuation date, by discounting the future payments with allowance for interest and the probability of payment. Assets are valued at market value, but for comparison we also show the results on the basis used last time (discounted future income) which is not very different.

1.3. **Assumptions** Assumptions are needed for financial factors and demographic factors such as rates of mortality, retirement and withdrawal from Parliament. Compared with the 2005 valuation, greater longevity of PCPF members has been assumed. The main financial assumptions for valuing liabilities (under both methods) are that investment yields over the long term will exceed general increases in earnings by 2% a year, and will exceed price increases by 3.5% a year.

1.4. **Past Service Assessment** The value of liabilities accrued up to the valuation date is assessed as £418.1 million. The value of the assets on the same date is assessed as £367.2 million using the market value method, and £366.8 million using the discounted income method. The deficit at 1 April 2008 on the market value method is accordingly £50.9 million, as set out below:

	Value at 1 April 2008 ***(£ million)***
Liabilities	418.1
Assets	367.2
Deficit	50.9
Funding level (= assets / liabilities)	87.8%

1.5. The deficit of £50.9m at this valuation is marginally higher than the deficit of £49.5m at the 2005 valuation. The main areas where the experience of the scheme has differed from what was assumed in 2005 are investment returns, which were better than expected, and salary increases, which were lower than expected. The most important change to the assumptions is increased longevity, which largely offsets the positive experience of good investment returns and low pay increases.

1.6. **Future Service Assessment** The cost of benefits accruing in the PCPF for each year of membership is assessed as 32.2% of scheme payroll. This compares with an assessed cost of 27.4% of pay at the 2005 valuation, with the increase being primarily attributable to the changes made to the longevity assumptions.

1.7. Members' contributions to the Fund are expected to average 9.1% of the scheme payroll, compared with 9.3% at the 2005 valuation. The Exchequer's share of the cost of accruing benefits is therefore assessed as 23.1% of payroll, compared with 18.1% at the 2005 valuation.

1.8. **Recommended Exchequer Contribution Rate** Exchequer contributions need to be at a higher level than the Exchequer's share of the cost of accruing benefits in order to amortise the deficit. Amortising the deficit of £50.9m over a 15-year period results in an addition of 8.5% to the Exchequer's share of the cost.

1.9. Taking account of the Exchequer share of future service costs (23.1% of pay) and of the additional contributions needed to meet the deficit (8.5% of pay), I recommend that the rate of Exchequer contribution to be paid from 1 April 2009 should be 31.6% of pensionable salaries.

1.10. **Cost-sharing / capping** The Senior Salaries Review Body (SSRB), in their report of January 2008, recommended that a form of cost sharing and a form of cost capping should be introduced into the PCPF. These recommendations of the SSRB were endorsed, in principle, by the House of Commons in a vote of the House on 24 January 2008. As it is possible that some form of cost-sharing or cost-capping mechanism may be introduced before the next actuarial valuation of the scheme, the contribution rate recommended to be paid by the Exchequer from 1 April 2009 is expressed as 31.6% of pensionable pay minus the value of whatever changes in member contributions or benefits may be implemented.

1.11. **Volatility** This report is produced, in accordance with the Funding Principles Consensus Statement which requests that I ignore post-valuation events. This is considered acceptable in view of the need for consistency and the Exchequer guarantee provided parties understand the consequences. I have considered how sensitive the results are to changes in the assumptions, and to experience differing from the assumptions, and this is being discussed with all parties at appropriate times.

2 Introduction

2.1 The Parliamentary and other Pensions Act 1987 requires the Government Actuary to make a report on the general financial position of the Parliamentary Contributory Pension Fund at three-year intervals. The previous report by the Government Actuary related to the position as at 1 April 2005 and this report (the thirteenth report) relates to an assessment of the general financial position of the scheme as at 1 April 2008. I now submit my report on this valuation, together with my recommendation as to the Exchequer contributions which should be paid into the scheme.

2.2 **Governing Legislation** The Parliamentary Contributory Pension Fund ("the scheme") is the pension scheme for Members of Parliament, Government ministers and other Parliamentary office holders. The primary legislation under which the scheme is constituted is the Parliamentary and other Pensions Act 1987. The main legislative provisions containing the rules of the scheme were consolidated in the Parliamentary Pensions (Consolidation and Amendment) Regulations 1993 (SI 1993 No. 3253). A number of changes to the benefit provisions have taken place since 1993, with the most recent major changes taking place at various dates in 2006, as set out in the Parliamentary Pension (Amendment) Regulations 2006 (SI 2006 No. 920).

2.3 The governing legislation prescribes the level of benefits and the circumstances in which the benefits will be payable to former members and their dependants. The legislation also prescribes the rate of contributions payable by persons who participate in the scheme. Section 3(4) of the Parliamentary and other Pensions Act 1987 requires the Government Actuary to recommend the rate of contributions that should be paid by the Exchequer following each actuarial valuation. The Act requires valuations to take place every three years, and for the Government Actuary to make a report to both the Trustees and the Minister for the Civil Service. The main purpose of this report is to recommend the rate of Exchequer contributions following the 2008 valuation.

2.4 This report has been prepared in accordance with the requirements of Guidance Note GN9 (version 8.1) issued by Board for Actuarial Standards, except that the solvency position on possible discontinuance of the scheme has not been investigated for the reasons given in paragraph 5.10 of this report, and the sensitivity considerations are being covered separately, as discussed in paragraph 7.20 of this report.

2.5 **Consultation With Both Parties** In order to prepare this valuation, I have consulted with both the trustees and Cabinet Office to determine how each party views the objectives of the funding of the scheme. The outcome of the consultation is that I have been able to put together a Funding Principles Consensus Statement which I attach as Appendix A. This statement has been seen in draft by the parties and I am content that both parties subscribe to the views expressed. In addition, I have reviewed the statement and consider it to be a reasonable statement (of objectives and approaches to assumptions) for this particular scheme to work to in preparing this valuation. In particular the following emerges as consequences from the consultation as set out in Appendix A:

- As a general principle, the existence of the Exchequer guarantee has meant that there is less need to be concerned about the ability of the sponsor to fund the scheme which enables a return seeking investment policy to be adopted (as set out in the Funding Principles Consensus Statement) to a greater degree than some more traditional schemes might now be adopting and a funding approach linked to expected returns on such assets.

- In deciding the Fund's investment strategy, the Trustees have taken a long-term view with respect to the Fund which, if achieved, should improve the Fund's ongoing funding level, and hence reduce the contributions required from the Exchequer.

- For many years, the scheme has been valued on an approach consistent with the above. When the House voted to introduce the principles of cost-sharing and cost-capping in January 2008, it should be assumed that this would be with consistency of actuarial approach in mind. Now that the Prime Minister has asked the SSRB to review the whole approach to pensions for MPs, it seems appropriate that this valuation should not be seen as setting a new approach to the assumptions and instead an appropriate level of consistency should be maintained.

3 Benefits and Contributions

3.1 **Benefits at 1 April 2008** The benefits applicable to MPs and office holders are set out in the Parliamentary Pensions (Consolidation and Amendment) Regulations 1993, as subsequently amended from time to time. The main benefit provided is a pension to members from the age of 65, defined as 1/40th or 1/50th of final pensionable pay for each year of service, with members' contributions payable at the rate of either 10% or 6% of pay respectively. Spouses' pensions are generally payable at a rate equal to five-eighths of the member's pension. A summary of the benefit provisions of the scheme at the valuation date is given in Appendix A.

3.2 **Accrual Rate of 1/60th** The SSRB, in their report of January 2008, recommended that members with retained benefits should be allowed to opt for a 1/60th accrual rate in return for reduced contributions, and this recommendation is expected to be implemented in the near future. However, this alternative rate of accrual has not yet been implemented, and no account has been taken of this option for the purposes of this assessment.

3.3 **Early Retirement** The scheme's Normal Retirement Age is 65. Some members with long service have an option to draw their pension benefits without any reduction being applied for early payment, subject to certain conditions. The main requirements are being aged 60 or above, with age plus service as an MP totalling 80 years or more. However, only service up to the later of 1 April 2009 and the next General Election after 5 May 2005 will count towards the qualifying period. Pension benefits accrued after the next General Election can generally be drawn before age 65, but only subject to a reduction to reflect the early payment.

3.4 **Partner Pensions** Benefits in respect of serving members on or after 3 November 2004 include survivor pensions payable to qualifying unmarried partners, as well as to widows and widowers, upon the death of a member. Those survivor pensions no longer cease upon the subsequent marriage, civil partnership or cohabitation of the surviving spouse or partner. From December 2005, survivors' pensions are also payable to legal civil partners.

3.5 **Member Contributions** During the inter-valuation period from April 2005 to March 2008, contributions from members were paid at the rate of 10% of pay for members who had opted for 1/40th accrual, and 6% of pay for members who had opted for 1/50th accrual.

3.6 **Exchequer Contributions** The recommendation following the actuarial valuation in 2005 was that the rate of contributions payable by the Exchequer should be 26.8% of pensionable salaries from 1 April 2006. From 1 April 2005 to 31 March 2006, Exchequer contributions were paid at the previous recommended rate of 24% of pensionable salaries. From 1 April 2006 to 31 March 2008, Exchequer contributions were paid at the recommended rate of 26.8% of pensionable salaries.

3.7 **Changes since the last valuation** Several changes were made to the scheme in 2006, mainly to take account of the requirements of the Pensions Act 2004 and the Finance Acts 2004 and 2005. These changes were introduced by SI 2006 No. 920. The main changes were:

(i) The maximum tax free cash by commutation of PCPF pension increased to 25% of the total value of the member's PCPF benefits;

(ii) Up to 25% of the AVC Fund may be taken as tax free cash (within the Lifetime Allowance) at retirement, in addition to PCPF commutation;

(iii) Members over age 75 at 5 April 2006 were given the option to take their tax free cash prior to 6 April 2006 but with the pension abated until they leave the House;

(iv) Members reaching the age of 75 after 6 April 2006 will be given the option to take tax free cash just before their 75th birthday and abating the pension until they leave the House;

(v) Corresponding changes were made to the death benefits for those over age 75 at the date of death;

(vi) The maximum contribution for Added Years was increased to 10% of salary with no restriction on those who might reach maximum benefits by age 65;

(vii) The maximum contribution to AVCs was increased to the HMRC limit;

(viii) Provision has been put in place for those who wish to exercise the Primary or Enhanced Protection afforded under the new legislation;

(ix) Transfers from personal pensions (including Stakeholder) and AVCs must be made within a year of joining the PCPF or by 6 April 2007, if later;

(x) Provisions relating to the Chairmen of Select Committees were extended to all Chairmen of such Committees who are eligible for additional salary as such and to all Chairmen of Standing Committees.

4 Membership Data and Accounts

4.1 In performing this valuation I have relied on the accuracy of the information provided to me by the secretariat to the Trustees of the scheme. The information provided is consistent with the data shown in the accounts and other publicly available sources.

4.2 Appendix B summarises the membership of the scheme at the valuation date, and the changes in membership since 2005. Comments on the main changes in membership during the period from 1 April 2005 to 1 April 2008 are given below.

4.3 **Members of Parliament** On 1 April 2008, there were 634 MPs who were active members of the scheme. The number of active scheme members is fewer than the number of Parliamentary seats because MPs who have not taken up their seats in the House of Commons are not eligible to join the scheme, and because members over the age of 75 have ceased to accrue further benefits. Such members had the option to take their lump sum retirement benefit immediately before reaching their 75th birthday (or 6 April 2006 if later) and abating the pension until they leave the House.

4.4 The average pensionable service for MPs (including service credited from transfers in from other pension schemes and additional years of service purchased by members) decreased from 16.8 years at the 2005 valuation to 15.4 years at this current valuation.

4.5 **Deferred Members** On 1 April 2008, there were 186 former MPs and office holders who were not yet in receipt of pension, but who retained an interest in the scheme in the form of an entitlement to deferred benefits, generally coming into payment at age 65. This compares with 176 deferred members as at 1 April 2005. The average amount of deferred pension to which former members were entitled was approximately £13,500 a year including cost of living increases up to the valuation date.

4.6 **Office Holders** On 1 April 2008, there were 175 ministers and other office holders who were actively participating in the supplementary scheme. This number has increased significantly from 143 at the last actuarial valuation because an increased number of Committee Chairmen have become entitled to participate in the supplementary section of the scheme.

4.7 In addition to the current office holders, there were 113 former office holders, who were still Members of Parliament, who had actively participated in the supplementary scheme in the past. Those MPs will be entitled to a supplementary pension when they leave the House of Commons.

4.8 **Salaries** In the three-year period since the 2005 valuation, the annual salary for Members of Parliament increased by just over 7% from £59,095 as at 1 April 2005 to £63,291 as at 1 April 2008. The pensionable payroll for MPs was £40.1 million at the valuation date. The pensionable payroll for office holders was £5.9 million, giving a total pensionable payroll for active members of the scheme of £46.1 million at the valuation date.

4.9 **Pensioners** In the inter-valuation period, the number of pensioners increased from 779 to 846, including the new pensions coming into payment as a consequence of the 2005 General Election. These figures include pensions payable to dependants of deceased former members and pension payments that are required to be made to some current MPs. Pension schemes such as PCPF, which are contracted out of the earnings-related additional pension of the State Pension Scheme (known as S2P), are generally required to start paying a statutory level of pension when a member who has been a member before 1997 and attains the age of State Pension Age plus five years (i.e. age 70 for men, age 65 for women), even where the member is continuing to accrue benefits under the scheme. However, serving MPs and Ministers are given the option to defer payment of the statutory level of pension for a further period until they reach age 75. At the valuation date there were 23 serving MPs receiving pension payments at the level of this statutory Guaranteed Minimum Pension.

4.10 The total amount of pensions in payment increased over the inter-valuation period from £10.1 million to £13.5 million. This reflects the increased number of pensioners and the annual pension increases awarded under the Pensions (Increase) Acts. The average amount of pension in payment was approximately £18,600 a year on 1 April 2008 to former MPs and office holders, and £11,100 a year to dependants.

Financial Data

4.11 **Accounts** Taken from the published accounts, the income and expenditure of the scheme in the three-year period from 1 April 2005 to 31 March 2008 is summarised in Appendix C. On the basis of the market value of the investments, the scheme's assets increased over the period by £86.6 million, from £283.2 million to £369.8 million, including members' Additional Voluntary Contributions. The table below shows a breakdown of the increase:

Increase in Assets 2005-2008

		£ million
(1) Start amount at 1 April 2005	283.2	
(2) Contributions (including transfer payments received by the fund)		53.9
(3) Benefits paid (including transfer payments out of the fund)		46.4
(4) Management expenses incurred (excluding investment management expenses)		1.5
(5) Net cash income = (2) - (3) - (4)		6.0
(6) Return on investments (net of investment management expenses)		80.6
(7) Total increase in fund = (5) + (6)	**86.6**	**86.6**
(8) End amount 31 March 2008	**369.8**	

4.12 The amount of the assets of £369.8 million shown in Appendix C include investments of £2.6m relating to Additional Voluntary Contributions (AVCs) paid by members on a money-purchase basis. As these AVC assets exactly match the liability to members in respect of AVCs, the AVC assets and liabilities are excluded from this valuation. Accordingly, the assets to be taken into account for this assessment amount to £367.2 million.

4.13 Following the increase in the Exchequer contribution rate in April 2006, the expenditure on benefits was less than the contribution income over the three-year inter-valuation period. This means that the expenditure remained well below the total of investment income and contributions, so that it was not necessary to sell assets to pay benefits.

4.14 **Investments**. Appendix D contains a summary of the investments actually held by the PCPF at 31 March 2008. This shows a majority of the investments (about 67% by market value) in equity shares.

4.15 The equity holding of 67% of the total portfolio is somewhat in excess of the equity allocation of 60% in the long-term strategic objective set out in the scheme's Statement of Investment Principles (as per the latest Statement of Investment Principles adopted by the Trustees in October 2007). That long-term objective incorporates an allocation of 27½% to bonds, with the remainder of the asset allocation (72½%) being split between equities (60%), property (10%) and hedge funds (2½%).

4.16 The investment return achieved on the scheme's assets on a market value basis over the three years since the last valuation was an average of 8.7% a year. However, there was considerable variation within the three-year period, with the percentage return achieved in each year since the last valuation being as follows:

1 April 2005 to 31 March 2006	+24.4%
1 April 2006 to 31 March 2007	+7.7%
1 April 2007 to 31 March 2008	-4.0%

4.17 The value to be placed on the investments of the scheme for the purpose of the present valuation is discussed in paragraph 6.23 below.

5 Funding Objective and Valuation Method

5.1 **Funding Objective** The principal objective is to maintain a fund of assets which is expected to be sufficient to provide the benefits promised to members and their beneficiaries. This objective is as advised by the Trustees of the scheme, having consulted with Cabinet Office, taking into account advice from the Government Actuary. A Funding Principles Consensus Statement reflecting the outcome of consultations between the Trustees of the PCPF, Cabinet Office and the Government Actuary, has been drawn up and is attached as Appendix A.

5.2 Another important aim as advised is to ensure that accruing benefits are paid for during members' participation in the PCPF and that the charges borne by the Exchequer for accruing benefits are reasonably stable over time. These objectives are addressed by determining a contribution rate expressed as a level percentage of pensionable salary called the *Standard Contribution Rate*. This standard rate is such that it would be just sufficient to finance the benefits under the scheme, provided that experience is in accordance with the actuarial assumptions made. Depending on the size of the accumulated fund and the actual experience of the scheme as disclosed at each three-yearly actuarial valuation, larger or smaller contributions may have to be paid for a period to allow, in particular, for amortising surpluses and deficits.

5.3 **Valuation Method** For this valuation, I have retained the same valuation method as was adopted for the previous valuation as at 1 April 2005. This is the projected unit method, which is the most commonly used method in actuarial valuations of occupational pension schemes in the United Kingdom. Under the projected unit method, the *Standard Contribution Rate* is the cost of the benefits that are expected to accrue in the immediate future (e.g. over a one or three-year period), allowing for future salary increases to retirement. Under this method, the value of the assets held in the fund is compared directly to the "*Actuarial* Liability" which is the value of pension liabilities accrued in respect of service prior to the valuation date as below.

5.4 **Actuarial Liability** Under the Projected Unit Method, the *Actuarial Liability* is the sum of the liabilities in respect of pensions already in payment, deferred pensions for former members, and the value of benefits accrued for sitting Members of Parliament and office holders in respect of service prior to the date of the valuation. These liabilities include the value of any pension rights transferred into the PCPF from other pension arrangements. The liability in respect of active members is assessed by summing the discounted present value of the benefits accrued to the valuation date, based on earnings projected to retirement, or earlier exit, and taking account of pension increases thereafter. For pensions-in-payment and deferred pensions, a similar calculation is made, which takes into account the provision for future cost of living pension increases in line with changes in the Retail Prices Index.

5.5 In addition to the liability in respect of benefits for members and beneficiaries, account must also be taken of any reserves required for other purposes, such as a reserve for future administration expenses. The value of the assets held in the fund can then be compared directly with this *Actuarial Liability*.

5.6 **Standard Contribution Rate** The *Standard Contribution Rate* is the rate of contributions which would need to be paid in order to meet the cost of pension benefits accruing over a defined period ("the control period"), if there were no surplus or deficiency in the scheme. A one-year control period has been used. The *Standard Contribution Rate*, expressed as a percentage of pensionable payroll, is obtained as the discounted value of the pension benefits accruing during the control period, divided by the value of the pensionable earnings of members during the same period. If the actuarial assumptions are borne out in practice, the *Standard Contribution Rate* should be just sufficient to meet the cost of benefits accruing.

5.7 This rate should remain reasonably stable, provided that members who leave service are replaced by new entrants so that the distribution of active members by age and sex does not change significantly, and provided the proportion of members on each rate of benefit accrual remains broadly unchanged. If, in practice, the average age of the active membership rises over time, the *Standard Contribution Rate* could be expected to increase slightly. If the average age of the active membership falls, then the *Standard Contribution Rate* could be expected to fall. This might happen, for example, following a General Election if a number of older members retiring were to be replaced by younger members.

5.8 **Recommended Contribution Rate** The recommended contribution rate is obtained by reducing (or increasing) the *Standard Contribution Rate* to reflect any surplus (or deficiency) between the value of the assets and the value of the *Actuarial Liability*. The period over which the contribution rate should be adjusted would depend on a number of factors including the extent of the surplus (or deficiency). In accordance with the Funding Principles Consensus Statement for this valuation, a period of 15 years will be adopted to amortise any surplus or deficit.

5.9 **Office Holders** Office holders who participate in the supplementary scheme pay supplementary contributions on their pensionable salary as an office holder. In most cases, MPs will be office holders for only part of their service as an MP. The valuation method adopted for office holders is again the projected unit method. The *Actuarial Liability* is calculated for benefits in respect of service given before the valuation date, and the *Standard Contribution Rate* is calculated as sufficient to cover the liabilities accruing in respect of future service. When pensions come into payment under the supplementary scheme for office holders, they are aggregated with pensions accrued as a Member of Parliament (where applicable), and so are not shown separately in the valuation results.

5.10 **Discontinuance** The valuation method described above deals with the position of the scheme on the basis that it will continue. I have not considered the position on winding up the scheme as the benefit levels are effectively guaranteed by the legislation and do not depend specifically on the amount of accumulated assets. The governing legislation contains no provisions to determine the wind up or discontinuance of the scheme. The Parliamentary Contributory Pension Fund is exempt from the Statutory Funding Objective which was introduced for private sector occupational pension schemes by the Pensions Act 2004.

6 Actuarial Assumptions

6.1 In order to derive the present value of benefits already accrued and benefits accruing over the next three years (and hence the *Actuarial Liability* and *Standard Contribution Rate*), it is necessary to make a number of assumptions. Future expenditure on benefits needs to be compared with future income from contributions and from the returns likely to be achieved by investing those contributions and the assets held in the fund. In assessing the expenditure on benefits, it is necessary to allow for the probability of the occurrence of each event giving rise to benefit and the length of time that the pension benefits will continue to be paid once the member has left the scheme. Assumptions therefore have to be made in relation to both *financial* aspects of the pension scheme and the *demographic* aspects of the scheme membership.

6.2 The principal approach adopted in the selection of assumptions is to start from the Funding Principles Consensus Statement, consider an appropriate assumption to fit the objective taking into account the factors described in this report. At that point I have then considered whether, in my opinion, the assumption is reasonable. Also, I consider whether the overall assumption set is reasonable and fit for purpose. The assumptions described below which I have used in this valuation have all been tested individually and in aggregate on this basis and I am content that the tests are satisfied.

Demographic Assumptions

6.3 **<u>Active Members</u>** For the valuation, assumptions are needed on such factors as rates of mortality, retirement and withdrawal from Parliament. Where possible, the past experience of the scheme is used as a guide. In considering the appropriateness of the assumptions for an actuarial valuation, it is important to have regard to the long-term scenario, taking account of the likely incidence of General Elections. The most important assumptions made are described below.

6.4 **<u>Pensioner Mortality</u>** Significant improvements in mortality rates have been observed across most ages and sectors of the UK population, including occupational scheme pensioners. The expectation amongst demographic experts is that improvements are likely to continue in future years, although there is a large degree of uncertainty about the rate of future improvement. As explained below, I have allowed for greater longevity of PCPF pensioners at this valuation, than was assumed for the 2005 valuation.

6.5 ***Baseline Mortality*** – Although the number of pensions in payment in the PCPF is relatively small, the mortality experienced by PCPF pensioners in the period from 2005 to 2008 was analysed to inform the judgement about current mortality rates (the Baseline Mortality). I have adopted mortality assumptions which are based on the standard mortality tables known as PMA00 and PFA00, published by the UK actuarial profession. These tables are derived from the experience of insured occupational pensioners around the year 2000, based on 'amounts of pension' for male pensions (M) and female pensions (F) respectively. Improvements in mortality from the year 2000 to the date of the valuation have been assumed to be in line with the improvement in the UK population. For females and widows, an addition to age of 1.5 years has been made to reflect PCPF experience.

6.6 These assumptions are consistent with paragraphs 11-12 of the Funding Principles Consensus Statement. They are derived as being the best fit to the experience exhibited over recent years and are not out of line with what one might expect from this population.

6.7 ***Mortality Improvement*** – Allowance has been made for assumed future improvement in mortality rates from the level of "Baseline Mortality", using the improvement factors adopted for the 2006-based projections of the UK population.

6.8 The table below gives specimen expectations of life, on the basis adopted, for men and women retiring at 60 and 65. Heavier rates of mortality are assumed for members who are retired or expected to retire on grounds of ill-health. These rates have been chosen in the light of the differences observed and assumed between 'age' and 'ill-health' pensioners in similar larger schemes.

<u>Expectations of Life at Normal Retirement Ages 60 and 65</u>

	Retirement Age	
	60	**65**
Current Pensioners	(years)	
Male	28.6	23.8
Female/Widows	29.2	24.2
Future Pensioners	(Current Actives & Deferreds)	
Male	30.3	25.7
Female/Widows	30.6	26.0

6.9 **Career Patterns** The table below shows the proportion of MPs assumed to leave Parliament at each election. This is consistent with the assumption used at the last valuation, which itself was determined following an exercise of looking at past experience over several elections. That exercise took account of turnover at the last General Election on 5 May 2005, so there is no further experience to use in determining the assumption for this valuation, and we consider the assumption to be consistent with paragraphs 11-12 of the Funding Principles Consensus Statement.

Age at election date	Proportion of members who leave Parliament
Under 63	20%
63 to 75	80%
75	100%

6.10 This aims to reflect the withdrawal patterns occurring in practice, as members are unlikely to leave Parliament between elections, or exactly at their normal retirement age. The table below shows the average age that current members are assumed to leave Parliament.

Assumed Age at Leaving Parliament

Age at valuation date	Average expected age of leaving Parliament
40	53
50	59
60	65
70	72

6.11 **Commutation** No allowance has been made for the possibility of members commuting part of their pension for a cash lump sum at retirement, as the scheme's commutation factors are assumed to be cost-neutral on the valuation basis.

6.12 **Marital Statistics** Up to age 60, all members are assumed to be married or have a civil partner or qualifying partner. Thereafter, the proportion of members with a spouse or partner reduces in line with the mortality of the spouse or partner. Male members are assumed to be three years older than their spouse or partner; female members are assumed to be three years younger than their spouse or partner.

Financial Assumptions

6.13 **Value of Liabilities** For the valuation, the liabilities, which comprise the future outgo on benefits and expenses, need to be compared with the income from future contributions and from investments. In order to compare the value of these items, they have been capitalised as at the valuation date, by discounting the future streams of income and outgo with allowance for interest and the probability of payment. As the income and outgo will occur over a very long period in the future (as much as sixty years or more in the case of current contributing members) the assumptions which have to be made as to interest and inflation rates necessarily relate to this very long period in the future.

6.14 Increases in pension benefits are awarded under the Pensions (Increase) Acts and are therefore linked to increases in the Retail Prices Index. (The scheme's governing regulations contain no provision for further discretionary increases to benefits and so none have been allowed for in this assessment.) Benefits awarded at retirement are related to the level of members' salaries at that time, and contributions are defined as a percentage of salaries. In general, high rates of salary increases and price increases are associated with high investment yields, and the differences between investment yields and inflation are more important in the valuation than their absolute values. The investment returns actually achieved by the scheme in the inter-valuation period were above the level of return that was assumed at the 2005 valuation. However, undue weight should not be given to short-term factors.

6.15 ***Discount rate*** - For this valuation, the discount rate for valuing the liabilities is taken as 3.5% a year in excess of price inflation. The discount rate of 3.5% can be viewed as a weighted average between the expected investment return on the strategic long-term return-seeking assets (equities, property and hedge funds) and on bonds. Based on the real yield on index-linked gilts at the valuation date, the expected rate of return on the strategic long-term allocation of 27½% of the scheme's assets to bonds can be taken as 0.9% a year in excess of price inflation. The expected rate of return on the strategic long-term allocation of 72½% of the scheme's investments which are in return seeking assets (as per the latest Statement of Investment Principles adopted by the Trustees in October 2007) can be taken as around 4½% in excess of price inflation. This implies an equity risk premium of 3½% over gilts. This assumption is consistent with paragraphs 11-12 of the Funding Principles Consensus Statement.

6.16 ***Price inflation*** - The rate of inflation implied by comparing the yields on fixed-interest gilts with the yields on index-linked gilts was 3.7% as at 1 April 2008. The price inflation assumption is combined with the net discount rate described in the previous paragraph to give the gross discount rate assumption. Using assumptions of 3.7% a year for price inflation and 3.5% a year for the net discount rate would give a gross discount rate assumption of 7.3% a year. Having considered this, and taking into account the Funding Principles Consensus Statement, which says that assumptions should be on the prudent side of best estimate, we have used an assumption for price inflation of 2.9%. This is closer to the long-term rate of price inflation used by the Government in other contexts and leads to a gross discount rate of 6.5%. Note that in itself the inflation assumption is not a critical assumption – what really matters is the real discount rate assumption in excess of inflation – see 6.13 and 6.17.

6.17 ***Pension increases*** - Pension increases on pensions in payment and in the deferred period are generally in line with increases to the Retail Prices Index. Hence, this assumption is taken to be 2.9% per annum. This is an average, long-term assumption.

6.18 ***Nominal Investment Return*** - The combination of a real return of 3.5% and price inflation of 2.9% produces a nominal rate of investment return of 6.5% pa.

6.19 The assumptions in paragraphs 6.16 to 6.18 have virtually no impact on the valuation result. Virtually all the benefits of the scheme are increased in line with salary growth (whilst members are accruing benefits) and price inflation (once a member has left service), with only increases applicable to Guaranteed Minimum Pensions (which relate to part of the benefits accrued between 1978 and 1997 as a result of the scheme being contracted out of the State Earnings Related Pension Scheme) not being in line with price inflation.

6.20 Using an assumption for price inflation a little below the implied rate of inflation on the basis of government stock as at 1 April 2008, gives a nominal investment return slightly lower than may otherwise have been chosen, which is consistent with an assumption on the prudent side of best estimate, and so the assumptions in paragraphs 6.16 to 6.18 are consistent with paragraphs 11-12 of the Funding Principles Consensus Statement.

6.21 ***Pay increases*** - The benefits accruing during service are linked to increases in members' pay, and it is therefore necessary to consider what increases in future pay levels might reasonably be anticipated. Real salary inflation has been assumed to be 1.5% pa, which results in a real discount rate in excess of pay increases of 2.0% pa. This is based on historical experience which shows that National Average Earnings have increased at a higher rate than price inflation. This assumption is consistent with paragraphs 11-12 of the Funding Principles Consensus Statement.

6.22 The financial assumptions are summarised in the table below.

Financial Assumptions

Gross rate of return	6.5%
Real rate of return, net of earnings increases	2.0%
Real rate of return, net of price/pension increases	3.5%

6.23 **Value of Assets** The scheme's assets could be valued by two alternative approaches, as follows:

(i) **Method used at the 2005 valuation** – Expected future income (dividend income, interest payments and redemption proceeds) have been discounted at the long-term average rate of investment return assumed, viz. 6.5% nominal.

(ii) **Market Value** – Assets have been taken at their market value as at 1 April 2008, reflecting the method that is required by the Pensions Act 2004 in relation to Technical Provisions (not applicable to PCPF).

6.24 In order to determine which approach to valuing the scheme's assets to use, we took into account the following considerations:

- The points made in the Funding Principles Consensus Statement;
- The fact that the 2005 valuation approach has an underlying expectation that equity dividends keep rising as has been borne out in general in practice for the half-century up to the 2005 valuation, whereas the last 12 months has seen severe dividend cuts and puts this approach into unchartered territory.

6.25 Accordingly, I have determined to use a market value approach for the build up to the recommendation but show an alternative view (on quite reasonable assumptions) which gives almost identical answers using the 2005 approach.

6.26 A discounted income approach to the valuation of assets results in the assets being brought into account at close to market value. The market value at 31 March 2008, from the scheme accounts, was £367.2m (excluding members' Additional Voluntary Contribution funds of £2.6m). In calculating the alternative discounted actuarial value of the scheme's equity holdings, dividend income has been assumed to reduced from its level at 1 April 2008 by 20% (reflecting the short-term impact of the 'credit crunch' on corporate profitability) and then to grow at 0.5% pa in excess of the growth in retail prices. On this basis, the actuarial value would be £366.8m.

6.27 **Expenses** Administration expenses incurred by the scheme during the three-year inter-valuation period were around £1.5 million, excluding investment management costs. A capital reserve of £8.2 million is set aside to meet expenses expected to arise in future. This is the same as the reserve set aside at the previous valuation, which was based on the level of expenses incurred over the preceding three years, and assuming that level of expenses continued. Expenses from 2005 to 2008 were slightly lower than in the previous inter-valuation period, however the same expense allowance as for the previous valuation has been retained. This assumption is consistent with paragraphs 11-12 of the Funding Principles Consensus Statement. The costs of investment management are implicitly taken into account in determining the rate of return on investments assumed for this valuation.

7 Results of the Valuation

7.1 The results of the valuation are considered in two parts. The first part deals with the liabilities that have already accrued for current and former members in respect of service given before the valuation date (the *Actuarial Liability*), and the results for this aspect are set out at paragraph 7.2 below. The second part of the valuation deals with the liabilities expected to accrue in respect of future service for current members (the *Standard Contribution Rate*), and this is discussed in paragraph 7.10 below.

7.2 **Past Service Assessment** The liabilities for past service and the assets of the scheme have been determined on the methodology set out in section 5 of this report, using the actuarial assumptions described in section 6. The results of the valuation in relation to past service liabilities are set out below:

Valuation Statement as at 1 April 2008 – Past Service

		Value at 1 April 2008 *(£ million)*
	Actuarial Liability	
	Current members – service up to 1 April 2008:	
(1)	(a) Members of Parliament	179.9
(2)	(b) Office holders	10.0
	Members with deferred benefits:	
(3)	(a) Former members	36.0
(4)	(b) Former office holders who are still MPs	7.9
	Pensions in payment:	
(5)	(a) Pensioners	140.9
(6)	(b) Surviving dependants of former members	35.1
(7)	**Total liabilities for benefits = (1) to (6)**	409.9
(8)	Reserve for administration expenses	8.2
	Overall Result	
(9)	**ACTUARIAL LIABILITY = (7) + (8)**	**418.1**
(10)	**VALUE OF ASSETS** (see paragraph 6.23)	**367.2**
(11)	**SHORTFALL OF ASSETS TO LIABILITIES = (9) – (10)**	**50.9**
	Funding Level	
(12)	**RATIO OF ASSETS TO LIABILITIES = (10) / (9)**	**87.8%**

7.3 The figures in the Valuation Statement show that the liability in respect of former members and dependants in receipt of pension at £176 million (total of rows (5) and (6) above), is approaching the liability for the past service of current members, at around £190 million (rows (1) and (2) above). The aggregate liability for accrued benefits of former MPs and office holders, including deferred members, is now 54% of the total liability (43% pensioners and 11% deferreds), whereas 46% relates to current members. This indicates that the PCPF has a relatively mature liability profile.

7.4 The result of the previous actuarial valuation, as at 1 April 2005, was a shortfall of assets to liabilities of around £50 million. The recommended rate of Exchequer contributions was increased by 8.7% of salaries above the *Standard Contribution Rate* with the objective of making up that deficit over a 15-year period. A further small deficiency has arisen in the operations of the scheme in the three-year period up to 1 April 2008, which more than offsets the reduction that would otherwise occur, with the shortfall of assets relative to liabilities being assessed as £50.9 million at that date.

7.5 **Analysis of Deficit** The result of the valuation shows a small increase in the deficit over the three-year period to the valuation date. Taking into account the interest that is assumed to accrue on the deficit during the inter-valuation period, the deficit would have risen by around £10 million if the experience of the scheme had developed as was assumed at the time of the actuarial valuation in 2005. Additional contributions have been paid over the inter-valuation period, which have reduced the deficit by £11 million.

7.6 The experience of the scheme has not been entirely in line with assumptions made at the 2005 valuation. Returns on the scheme's investments were higher than was assumed in the valuation. It is not surprising for a scheme that is primarily invested in equities, which exhibit volatile return characteristics, to experience returns over a three-year period that are materially lower or higher than the valuation assumption for the average returns that are expected to be achieved over the long term. Other factors, such as the lower than expected level of salary increases applicable to active members of the scheme, also had a positive impact on the deficit position. Overall, divergence of the scheme's experience from assumptions made at the time of the actuarial valuation in 2005 contributed to a reduction in the deficit of around £34 million.

7.7 The main factor giving rise to an increased deficit is the change made to the mortality assumptions that I have adopted for the purposes of this actuarial valuation from those adopted for the 2005 valuation. Changes to the actuarial assumptions contributed around £36 million to the increased deficit.

7.8 The change in the deficit between the actuarial valuation in 2005 and the current valuation can be summarised as follows, both in cash terms and as a percentage of the 2008 liabilities.

Summary of Change in Deficit 2005-2008

	£ million	***Percentage of liabilities***
Deficit at 1 April 2005	**50**	**12%**
Interest on 2005 deficit	10	2%
Additional contributions in 1st inter-valuation years	(3)	(1%)
Additional contributions in 2nd and 3rd inter-valuation years	(8)	(2%)
Divergence of scheme's experience from actuarial assumptions	(34)	(8%)
Changes to actuarial assumptions from those adopted at previous valuation	36	9%
Deficit at 1 April 2008	**51**	**12%**

7.9 The contributions required to deal with the deficiency are considered below after reporting on the results for benefits that will accrue for service after the valuation date.

7.10 **Future Service Assessment** The cost of benefits accruing for future service is assessed by means of the *Standard Contribution Rate*, as described at paragraph 5.6 of this report. The *Standard Contribution Rate* calculated on the actuarial assumptions set out in section 6 of this report is 32.2% for MPs and office holders taken together. The corresponding rate calculated at the time of the 2005 valuation was 27.4%.

7.11 The *Standard Contribution Rate* assessed at this valuation is higher than the rate assessed at the previous actuarial valuation in 2005 by a margin of 4.8% of pay. The increase is primarily attributable to changes made to the mortality assumptions, which have had the effect of increasing the expected cost of future benefit accrual.

7.12 Contributions are payable by members at the rate of 6% or 10% of pensionable salaries. On the basis of current members' chosen accrual rates, members' contributions are expected to average 9.1% of the scheme's pensionable payroll for the duration of the current Parliament. At the 2005 valuation members' contributions were expected to average 9.3% of the scheme's pensionable payroll. The decrease of 0.2% in contributions from members since the last valuation is attributable to the increase in the number of members who have reached (or will reach) the limits for maximum benefit accrual in the scheme. Such members cease paying contributions.

7.13 The Exchequer's share of the *Standard Contribution Rate*, which is the balance of costs that would fall to be met by the Exchequer in the absence of any surplus or deficiency, is assessed as 23.1% of pensionable salaries (being 32.2% less 9.1%). This is 5.0% of payroll higher than the Exchequer's share of the *Standard Contribution Rate* at the 2005 valuation.

7.14 The assessed *Standard Contribution Rate* can be expected to remain broadly stable if the distribution of the membership by age, salary, length of service and each member's chosen accrual rate remain broadly constant, and if there is no change in actuarial assumptions.

7.15 **Recommended Rate of Exchequer Contributions** Under Section 3 of the Parliamentary and other Pensions Act 1987, I am required to determine the rate of Exchequer contributions needed to meet the balance of the cost of the scheme, having regard to the benefits and to the contributions payable by members. In line with my recommendation at the previous actuarial valuation, and as required in legislation, the rate of Exchequer contributions was set at the level of 26.8% of the pensionable salaries of MPs and office holders with effect from 1 April 2006.

7.16 As shown in the Valuation Statement at paragraph 7.2, a further shortfall of assets relative to liabilities has arisen since the previous actuarial valuation. The shortfall is now assessed as £50.9 million. It is appropriate that Exchequer contributions should remain at a higher level than the *Standard Contribution Rate* in order to amortise the deficit. Taking into account the statutory backing to the PCPF, the objective set out in the Funding Principles Consensus Statement of amortising the deficit over a 15-year period reflects a reasonable approach to funding where there is a desire to keep to a relatively low level the impact of surpluses/deficits. Amortising the deficit over this period results in an addition of 8.5% to the Exchequer share of the *Standard Contribution Rate*. On this approach, the contribution rate required to be paid from 1 April 2009 to meet the cost of benefits currently accruing in the scheme, and by the Exchequer to cover the deficit, is 31.6% of the pensionable salaries of scheme members. No allowance has been made for any further shortfall that has arisen between the valuation date and the date the revised contribution rate becomes payable.

7.17 The Senior Salaries Review Body (SSRB), in their report of January 2008, recommended that a form of cost sharing should be introduced into the PCPF, so that member contributions partly reflected the changing cost of the benefits being provided. The SSRB report also recommended the introduction of 'cost-capping', so that the Exchequer contribution was effectively limited to a specified figure (20% of pay, plus the 2005 deficit contributions, was recommended). Cost sharing and cost capping could be achieved by increasing member contribution, amending the benefit structure or a combination of the two. These recommendations of the SSRB were endorsed, in principle, by the House of Commons in a vote of the House on 24 January 2008.

7.18 It is quite possible that some form of cost-sharing or cost-capping mechanism may be introduced before the next actuarial valuation of the scheme is finalised. In order to allow for this possibility, the contribution rate recommended to be paid by the Exchequer from 1 April 2009 is expressed as 31.6% of pensionable pay adjusted to take account of any increase in members' contributions and/or any benefit reductions which the Government announces as a consequence of cost-sharing or cost-capping. The value for the purposes of such adjustment of any benefit reductions will be as assessed by the Government Actuary using the same assumptions as in this report.

7.19 **Analysis of Change in Total Required Rate** The change to the total required rate of contributions – from 36.1% to 40.7% of scheme payroll – is mainly because of the increase in the *Standard Contribution Rate*. The change to the additional contributions needed to make up the deficit of the scheme's assets relative to its liabilities has a minor impact. The table below summarises the main factors that account for the change to the required rate of contributions.

Increase to Required Contribution Rate (Exchequer and members combined) (% of salary)

Required contribution rate following 2005 valuation (26.8% employer plus 9.3% member)		**36.1%**
Future service change		
Impact of changes to actuarial assumptions		+4.8%
Past service change		
Divergence of scheme's experience from 2005 valuation assumptions	-5.7%	
Impact of changes to actuarial assumptions	+5.5%	
Additional cost of amortising increased deficit		**-0.2%**
Required contribution rate following 2008 valuation		**40.7%**

7.20 **Sensitivity** I have considered how sensitive the results are to changes in the assumptions, and to experience differing from the assumptions, and this is being discussed with all parties at appropriate times

8 Recommendation

8.1 Section 3(4) of the Parliamentary and other Pensions Act 1987 requires that, at each actuarial valuation, the Government Actuary shall recommend the rate of contribution that should be paid by the Exchequer in respect of any financial year beginning after this report is made. I have completed the actuarial valuation of the PCPF as at 1 April 2008, using the methodology and actuarial basis described in this report, and the recommendation I am required to give by Statute is set out in paragraph 8.2 below.

8.2 I recommend that the Exchequer's contributions payable from 1 April 2009 should be at the rate of **31.6% of pensionable pay** adjusted to take account of any increase in members' contributions and/or any benefit reductions which the Government announces as a consequence of cost-sharing or cost-capping. The value for the purposes of such adjustment of any benefit reductions will be as assessed by the Government Actuary using the same assumptions as in this report.

Trevor Llanwarne FIA **24 March 2009**
Government Actuary

9 APPENDIX A: FUNDING PRINCIPLES CONSENSUS STATEMENT

Actuarial Valuation at 1 April 2008

Status of PCPF

1. The Parliamentary Contributory Pension Fund (the PCPF) is a defined benefit occupational pension scheme established to provide pension and related benefits for members of the UK Parliament and Officeholders. The PCPF is established by statute, the main primary legislation being the Parliamentary and Other Pensions Act 1987, with the rules set out in regulations under that Act (the main regulations being statutory Instrument No. 3253 of the year 1993). Both the Act and the regulations have been amended from time to time to reflect changing circumstances and the development of pensions legislation in the UK.

Requirements of Legislation

2. Under Section 3 of the Parliamentary and Other Pensions Act 1987, the Government Actuary is required to carry out an actuarial valuation every third year. The key requirements are:

   'Section 3(3) - As soon as practicable after [the valuation date], the Government Actuary shall make a report to the Trustees and to the Minister of the Civil Service on the general financial position of the Fund…

   'Section 3(4) - Each report under this section shall contain a recommendation of the Government Actuary as to the rate at which Exchequer contributions should… be paid into the Fund under this section in respect of any financial year beginning after the report is made.'

Consultation

3. This Statement reflects the outcome of consultations between the Trustees of the PCPF, the Cabinet Office and the Government Actuary. It represents a summary of what are believed to be consensus views of both the first two parties referred to, in terms of how the scheme is and should be funded, invested and controlled. This statement has been seen by both parties in draft and both are content with the summary as described.

Nature of Scheme

4. The benefits provided to MPs and Officeholders are described in detail in the governing legislation, which also specifies the rate (or rates) of contributions payable by members of the scheme. The balance of the cost of providing the promised benefits is met by contributions from the Exchequer. One of the main purposes of the periodic actuarial valuation is to determine the rate of contribution that should be paid by the Exchequer from time to time.

Exchequer Guarantee

5. Under the Statutes currently in force, the Exchequer effectively guarantees the benefits prescribed for members, as it is obliged to pay whatever rate of contribution is recommended by the Government Actuary, including any deficit contributions to meet a shortfall. As the security of members' benefits is not in doubt, the Trustees need not be concerned about short-term volatility in funding levels or in contribution rates, and can take a long-term approach to investment. This position, including the Exchequer commitment to financing shortfalls, may change depending on the implementation of cost-sharing and cost-capping, as outlined in paragraphs 6, 7 and 8 below.

Cost-Sharing and Cost-Capping and SSRB review

6. The Senior Salaries Review Body (SSRB), in their report of January 2008, recommended that a form of cost sharing should be introduced into the PCPF, so that member contributions partly reflected the changing cost of the benefits being provided. The SSRB report also recommended the introduction of 'cost-capping', so that the Exchequer contribution was effectively limited to a specified figure (20% of pay, plus the 2005 deficit contributions, was recommended). These recommendations of the SSRB were endorsed, in principle, by the House of Commons in a vote of the House on 24 January 2008.

7. The introduction of cost-sharing or cost-capping is likely to alter the balance of risk between members and the Exchequer, with some risk being transferred from the Exchequer to the members. Depending on the details of the implementation of cost-sharing and cost-capping, the transfer of risk from the Exchequer to the members could be considerable. The funding principles relating to the PCPF may need substantial review when the detailed arrangements for the future have been settled.

8. On 13 February 2009, the Prime Minister wrote to the Chairman of the Senior Salaries Review Body instructing them to conduct a full review of MPs' pensions. This consensus statement is independent of any possible outcome of that review, but a possible consequence of that review is that of a significant overhaul and so this consensus statement may only apply to one valuation.

Funding Objectives

Principal Objective

9. The key funding objective for the PCPF is that the combination of contribution income (including both member contributions and Exchequer contributions) and the income from the assets held in the fund (including interest payments, dividends, and sale proceeds) should be just sufficient (and not excessive) to meet the benefit expenditure to MPs and Officeholders in accordance with the rules of the PCPF.

Subsidiary Objective

10. A subsidiary objective, for as long as the scheme remains open to future accrual and to new members, is that the PCPF benefits should be financed on a consistent basis during members' participation in the scheme by regular contributions, which are hoped to remain a substantially level percentage of pay over time, using an actuarial basis and approach that does not change greatly from one valuation to the next. This objective of broad consistency over time should help to deliver inter-generational fairness both to members and to taxpayers, particularly in the context of the developments referred to in paragraphs 6 to 8 above on the basis and expectation held when the endorsements were given. It is accepted that, to the extent that actual experience (or views on future experience) deviates from the assumptions made in assessing funding, actual contribution rates may need to be temporarily higher or lower to meet the long-term funding objectives.

Funding Strategy

11. In order to minimise the risk of excessive funding, the quantum of assets to be built up in the PCPF will be targeted as just sufficient to cover the value of the PCPF liabilities in respect of service completed by members prior to the date of the actuarial valuation. The assessment of these liabilities will be determined using actuarial assumptions which are considered to be, overall, on the prudent side of a 'best estimate' of future investment returns and other financial factors affecting the calculation of the liabilities, and consistent with the assumptions used by a number of other funded schemes for contribution rates (including public sector schemes) who are following a similar long-term investment strategy.

12. Each actuarial valuation will take account of the observed experience in the scheme prior to the valuation date, both in respect of demographic features (such as retirements, leavers, and new entrants), and in respect of financial features (such as inflation and investment returns). The actuarial basis for carrying out the valuation will reflect a basis on the prudent side of the best estimate of financial conditions that can be made effective from the valuation date, taking into account market conditions at that time.

Allowance for Post-Valuation Events

13. In relation to any valuation, there is always a time delay between the effective date of the valuation and the date the report on the valuation is signed. In view of the possible introduction of cost-sharing and cost-capping (and the importance of consistency), and the Exchequer guarantee, post-valuation events will be ignored for the 2008 valuation results.

Format of Actuarial Conclusion on Contribution

14. The recommendation on contributions should allow a reduction in Exchequer contribution if cost-sharing/cost-capping comes in without any need for a further valuation before 2011, but ensure the full amount is paid if it does not.

Investment Strategy

15. The PCPF is financed by contributions from members and the Exchequer which are invested in a fund of real assets. The investment strategy adopted for managing this fund is reviewed by the Trustees, from time to time, and reflects the Exchequer commitment to the financing of the PCPF. The investment strategy is a mixture of return-seeking assets (mainly equities and property) and broadly matching assets (such as bonds), with some diversification into other asset classes.

16. The investment strategy is set out in some detail in the Statement of Investment Principles, which was prepared, in consultation with the Leader of the House of Commons, and adopted by the Trustees on 25 October 2007. The long-term strategic objective set out in that Statement is summarised below.

Strategic Asset Distribution (SIP of 25/10/2007)

Asset Class	Proportion of Fund
Equities	
(UK and Overseas Equities)	60%
Property	10%
Hedge Funds	2½%
Bonds	27½%
Total Assets	**100%**

17. Although previous valuations have used the old-style traditional actuarial approach to valuing assets (ie discounting future dividends, rental income etc which can lead to an actuarial value of the assets being quite different to market values) it is recognised that pension schemes nowadays (subject to Pensions Act 2004 requirements) use a market value approach to valuing liabilities. It is therefore considered that this market value approach should be accepted for this scheme this year subject to showing a comparison with what the traditional approach might have delivered whilst recognising that in today's turbulent markets, it is difficult to know what an appropriate traditional approach might look like.

Period over which Contributions are Adjusted to Meet Funding Objectives

18. When experience differs from the valuation assumptions made, the result of the valuation will be either a surplus or a shortfall of assets relative to past service liabilities. Future contributions will accordingly be reduced for a period when there is a surplus (or increased for a period when there is a deficiency), in order to bring the assets and liabilities back into balance. As security of members' benefits is not an issue, and in order to keep contribution rates reasonably stable, a relatively long period will be selected for the period over which contributions are adjusted, broadly approximating to the average remaining working lifetime of members of the scheme at the valuation date. Typically, this might be 15 years.

Valuation Assumptions

19. For the purposes of the actuarial valuation, it is necessary to make assumptions about the financial and demographic aspects relevant to the PCPF. The general approach to be adopted is to use the experience of the scheme as a base provided this is reasonable.

Policy on reduction of cash equivalent transfer values (CETVs)

20. It is permissible under pensions legislation for cash equivalent transfer values (CETVs) to be reduced by the trustees below their preferred level, if the value of the liabilities calculated on the CETV basis exceeds the value of the assets available to pay those transfer values. In the circumstances of the Exchequer guarantee, the Trustees consider that it is not appropriate to reduce the CETVs below their full recommended level and this should be assumed to the extent it is relevant for any valuation.

Frequency of valuations

21. The statutory provisions relating to the PCPF require an actuarial valuation to be carried out every three years. Accordingly, the next actuarial valuation of the PCPF is due to be carried out with effect from 1 April 2011.

Position of the members

22. In view of the fact that this report is addressed to Government and the trustees jointly, as required under law, it has not been felt appropriate or necessary, to consult more widely given that the Trustees comprise the other relevant party, the members.

10 APPENDIX B: SUMMARY OF THE MAIN PROVISIONS OF THE SCHEME

1. All serving Members of Parliament may participate in the Parliamentary Contributory Pension Fund. Ministers and certain other office holders (in both the House of Lords and House of Commons) may participate in a supplementary section of the scheme and qualify for a supplementary pension on a similar basis to MPs, except that benefits accrue by reference to salary in each year of office holder membership, rather than by reference to final pay.

2. Contributions are required at a rate of 10% of salary from scheme members. Pensions accrue at the rate of 1/40th of final pensionable salary per year of reckonable service. Exchequer contributions are paid at a rate recommended from time to time by the Government Actuary.

3. Members may instead opt to pay contributions at a rate of 6% of salary and to accrue pension at the rate of 1/50th of final pensionable salary per year of reckonable service. Serving members who have reached the limits for maximum benefit accrual in the scheme do not pay contributions.

4. Retirement pensions are payable from age 65 to those who are no longer MPs or office holders. Pensions may be paid before age 65 in the following circumstances, though only service up to the later of 1 April 2009 and the next General Election after 5 May 2005 will count towards the qualifying period:

   - Full accrued pensions may be paid from age 60 where service as a member exceeds 20 years, and from an age between 60 and 65 where service is between 20 and 15 years.
   - Abated pensions may be payable from earlier ages to members aged 50 or over.

5. An ill-health retirement pension may, subject to medical evidence, be awarded at any age. Ill-health pensions are calculated by reference to potential service to age 65.

6. Members may, on retirement, commute part of their pension for a lump sum that is actuarially equivalent to the part of the pension forgone.

7. Pensions are also payable to spouses and other qualifying partners of deceased scheme members at the rate of five-eighths of the deceased member's pension. Children's pensions are also payable. In the case of members who die in service, the spouse's or partner's pension is based on the pension that would have been payable to the member had ill-health retirement taken place at the date of death. On death in service, a member's salary continues to be paid to a surviving spouse or partner for a further three months. A lump sum equal to four times pensionable salary is also paid on the death in service of a scheme member.

8. Pensions and deferred pensions are increased annually in line with price inflation.

9. The scheme is contracted out of the earnings-related additional pension of the State Pension Scheme.

11 APPENDIX C: MEMBERSHIP AT 1 APRIL 2008

TABLE 1 - MEMBERS OF PARLIAMENT PARTICIPATING IN THE SCHEME

Number of MPs participating in PCPF at 1 April 2005	**655**
New members 2005-2008:	
MPs elected	128
[(1)]*Members leaving active status 2005-2008:*	
Leaving with deferred entitlement	(57)
Retirements[(2)]	(85)
Deaths	(7)
Number of MPs participating in PCPF at 1 April 2008	**634**
Other statistics at 1 April 2008	
MPs' pensionable pay (p.a.)	£63,291
Total of accrued pensions[†] (p.a.)	£13.5m
Average accrued pension[†] (p.a.)	£21,300
Average length of pensionable service*	15.4 years
Number of MPs who have opted for 1/40th accrual	579

[†]Not including any benefits earned in respect of service as an office holder
* Including transferred-in service and added years contracts
(1)Movements relate to the status as at 1 April 2008 of participating members at 1 April 2005
(2)Including current MPs aged over 75 with abated pensions

APPENDIX C (CONT'D)

TABLE 2 – OFFICE HOLDERS PARTICIPATING IN THE SCHEME

Number of office holders participating in PCPF at 1 April 2005	**143**
New members 2005-2008:	
Office holders appointed (and posts becoming pensionable)	103
Members leaving active status 2005-2008[(1)]*:*	
Retirements[(2)]	(19)
Deferred pension entitlement only	(38)
Deferred pension entitlement but still an MP	(13)
Number of office holders participating in PCPF at 1 April 2008	**176**
Other statistics at 1 April 2008	
Aggregate pensionable salaries of office holders (p.a.)	£5.9m
Total of accrued pensions† (p.a.)	£0.8m
Average accrued pension† (p.a.)	£4,400
Number of office holders accruing benefits at 1/40th	158

† Not including benefits earned in respect of service as an MP

(1)Movements relate to the status as at 1 April 2008 of participating members at 1 April 2005

(2)Includes previous office-holders aged over 75 with an abated pension

APPENDIX C (CONT'D)

TABLE 3 – FORMER OFFICE HOLDERS STILL SERVING AS MPs

Number of serving MPs at 1 April 2005 with deferred entitlement to office holder benefits	**122**
Members joining category 2005-2008:	
MPs leaving office holder status	42
Members leaving category 2005-2008[1]:	
Resumed active office holder status	(16)
Stepped down as an MP	(9)
Retirements[2]	(21)
Deaths	(4)
Number of serving MPs at 1 April 2008 with deferred entitlement to office holder benefits	**114**
Other statistics at 1 April 2008	
Total of accrued pensions† (p.a.)	£0.5m
Average accrued pension† (p.a.)	£4,700

† Not including benefits earned in respect of service as an MP

(1)Movements relate to the status as at 1 April 2008 of participating members at 1 April 2005
(2)Includes current and previous office-holders aged over 75 with an abated pension

APPENDIX C (CONT'D)

TABLE 4 - MEMBERS WITH DEFERRED PENSION ENTITLEMENT

(NOT INCLUDING DEFERRED OFFICE HOLDER ENTITLEMENTS WHERE MEMBER IS STILL SERVING AS AN MP)

Number of deferred members at 1 April 2005	**176**
Members joining category 2005-2008:	
Members leaving active membership	61
Members leaving category 2005-2008[1]:	
Resumed active MP status	(4)
Resumed active Office-holder status	(1)
Awards of pension (on reaching retirement age)	(33)
Awards of pension (on ill-health grounds)	(3)
Awards of GMP pension (Females over age 60)	(3)
Transfers to other schemes	(1)
Deaths	(6)
Number of deferred members at 1 April 2008[2]	**186**
Other statistics at 1 April 2008[3]:	
Total of deferred pensions (p.a.)	£2.5m
Average deferred pension (p.a.)	£13,500

(1)Movements relate to the status as at 1 April 2008 of participating members at 1 April 2005
(2)Excludes deferred females aged over 60 who are receiving a GMP pension

APPENDIX C (CONT'D)

TABLE 5 - INCUMBENT PENSIONERS

	Former members	Surviving dependants of former members	Active members in receipt of statutory Guaranteed Minimum Pension	Members aged over 75 with an abated Pension	Total
Number of pensioners at 1 April 2005:	**481**	**275**	**23**	**0**	**779**
New pensioners 2005-2008	125	58	10	7	200
Pensions ceasing 2005-2008	68	48	17	0	133
Number of pensioners at 1 April 2008*:	**538**	**285**	**16**	**7**	**846**
Other statistics at 1 April 2008:					
Total of pensions in payment (p.a.)	£10.0m	£3.1m	£0.09m	£0.27m	£13.5m
Average pension in payment (p.a.)	£18,600	£11,100	£5,400	£37,800	£16,000

12 APPENDIX D: CONSOLIDATED REVENUE ACCOUNT FOR THE PERIOD 1 APRIL 2005 TO 31 MARCH 2008

	£'000	£'000
Fund at 1 April 2005		**283,197**
Income		
Contributions:		
MPs' ordinary contributions	10,735	
Contributions from ministers and other office holders	1,690	
Members' contributions for the purchase of AVCs and added years	623	
Exchequer contributions	33,657	
Transfer values received	7,213	
Interest income from investments	19,859	
Realised and unrealised net gains on investments	64,367	
Total income		**138,143**
Expenditure		
Pensions:		
Retired members	28,903	
Widows, widowers, other qualifying partners and children	8,483	
Lump sums paid on retirement	7,512	
Death gratuities	1,258	
Transfer values paid	205	
Refunds of contributions	0	
Management expenses (excluding investment management expenses)	1,520	
Investment management expenses	3,671	
Total expenditure		**51,552**
Fund at 31 March 2008		**369,788**

13 APPENDIX E: ANALYSIS OF THE INVESTMENTS OF THE SCHEME

TYPE OF ASSET	Market value at 31 March 2008 *£000*	Percentage of assets by market value (excluding AVCs)
Equities *	244,655	67%
Fixed interest stock	66,561	18%
Index linked stock	15,603	4%
Property	32,333	9%
Cash deposits	4,660	1%
Other investment balances	1,661	<½%
Net current assets	1,678	<½%
Total assets (excluding AVCs)	**367,150**	**100%**
Members' AVCs	2,638	
Total assets	**369,788**	

* Including hedge fund investments of around 2.5% of the scheme's total assets

14 APPENDIX F: MORTALITY TABLES ADOPTED

Male active and deferred members	PNMA00-06 (C=2048)
Female active and deferred members	PNFA00-06 (C=2048) +1.5 years age rating
Male pensioners (not ill health)	PNMA00-06 (U=2008)
Female pensioners (not ill health)	PNFA00-06 (U=2008) +1.5 years age rating
Male pensioners (retired on grounds of ill health)	PNMA00-06 (U=2008) (q_x+0.01)
Female pensioners (retired on grounds of ill health)	PNFA00-06 (U=2008) (q_x+0.01) +1.5 years age rating
Widowers and other partners of female members	PNMA00-06 (U=2008)
Widows and other partners of male members	PNFA00-06 (U=2008) +1.5 years age rating

Note: The PNMA00-06 and PNFA00-06 mortality tables (for males and females respectively) are published by Continuous Mortality Investigation Bureau (CMIB) of the Institute of Actuaries and the Faculty of Actuaries. They are based on the experience of pensioners in UK insured pension arrangements.

The ‘PNA00-06’ table is the published PNA00 table with future improvements broadly in line with population improvements to 2006 and in line with the 2006-based principal population projections thereafter.

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