enhancing... improving... cleaning... restoring...
changing... tackling... protecting... reducing...
create a better place... influencing... inspiring...
advising... managing... adapting...

Environment Agency Active Pension Fund

Annual Report and Financial Statements 2006-2007

GEHO0807BMYH-E-E

We are the Environment Agency. It's our job to look after your environment and make it **a better place** - for you, and for future generations.

Your environment is the air you breathe, the water you drink and the ground you walk on. Working with business, Government and society as a whole, we are making your environment cleaner and healthier.

The Environment Agency. Out there, making your environment a better place.

The Environment Agency Active Pension Fund is registered with the Pension Schemes Registry No. 10079069

Environment Agency Active Pension Fund
Annual Report and Financial Statements 2006-2007

Presented to Parliament pursuant to section 46 of the Environment Act 1995

Ordered by the House of Commons to be printed 25 July 2007

HC888 London: The Stationery Office £13.50

Table of Contents

	Page No.
The report	
Chairman's statement	1
Report by the Pensions Committee	2
Pension Fund membership	5
Pension Fund investment	7
The accounts	
Foreword to the financial statements	16
Accounting Officer's Statement on internal control	18
Statement by the Consulting Actuary	22
Comptroller & Auditor General's statement about contributions	24
Summary of contributions payable	25
Certificate and Report of the Comptroller & Auditor General	26
Financial statements for the year ended 31 March 2007	28
Notes to the financial statements	29
The annexes	
Funding strategy statement	37
Statement of investment principles	42
Corporate governance strategy	47
Environmental overlay strategy	49
Scheme rules and benefits	52
Additional information	
Statistical summary of Fund membership and value	53
Enquiries	57

Chairman's statement

As Chairman of the Environment Agency's Pensions Committee, which is responsible for overseeing the management and administration of the Environment Agency Active Pension Fund ("the Fund"), I am pleased to present the Fund's Annual Report and Financial Statements for the year ended 31 March 2007.

I am delighted to report that membership has continued to grow with over 94% of employees contributing to the Fund. Over the last year, total membership increased by over 800 to 19,090. This comprises 11,926 employees, 4,050 deferred members and 3,114 pensioners.

Several changes to the Local Government Pension Scheme (the "LGPS") were made during the year. Members have been kept informed about these. The Department for Communities and Local Government ("DCLG") announced in November 2006 proposals for a "new look" Local Government Pension Scheme. The DCLG intend that the "new look" LGPS shall come into effect on 1 April 2008 and members will be kept informed about these changes.

Our new investment strategy continues to be successful. The overall investment return for the Fund was a positive 7.1%. This is an out-performance of +1.2% against its strategic benchmark.

The Fund's net assets rose to £1,526 million as at 31 March 2007. The actuary is preparing his formal triennial valuation of the Fund's assets and liabilities the results of which will be used to inform the setting of the employer's contribution rate from 2008/09 onwards. The results of the triennial actuarial valuation will be reported in next year's Annual Report and Financial Statements.

During the year our innovative work in integrating financially material environmental issues into our investment strategy was externally recognised. We were the proud winners of the Professional Pensions Best Use of Socially Responsible Investment (SRI), joint winners of the Best UK Pension Fund 2006 by Investments and Pensions Europe and runner up in the City of London's Sustainable City SRI award.

Finally I would like to take this opportunity to thank everyone involved, both Environment Agency staff and external contractors, for helping the Pensions Committee to manage the Fund over the last year.

John Edmonds
Chairman
The Environment Agency Pensions Committee
11 July 2007

Report by the Pensions Committee

Governance

Chairman and members

John Edmonds served as Chairman of the Pensions Committee throughout the year. During the year Board members Kay Twitchen and Peter Matthews retired from the Pensions Committee and were replaced by Suzanne Warner and Larry Whitty. David Webster resigned from the Pensions Committee upon leaving the Environment Agency Wales. Since the end of the year the Board has re-appointed Member representative Alan Broughall for a further two year term and David Edwell has been appointed as the management representative for Environment Agency, Wales on the Pensions Committee.

Committee governance

During the past year the Pensions Committee met on three occasions to fulfil its responsibilities as a sub-committee of the Environment Agency Board. The Board appoints members in accordance with the Governance Policy Statement. It has delegated responsibility to manage the investment and administration of the Agency's pension funds. The Committee's Investment Sub-Group met on four occasions, and an ad-hoc working group on LGPS changes met three times.

In February 2007 the Environment Agency Board approved an update to the Governance Policy Statement, which takes effect on 1 April 2007 and incorporates the Pensions Committee Terms of Reference and Standing Orders and the Pension Funds Scheme of Delegation. The revisions made this year take account of changes to the LGPS regulations or clarify the scope/delivery of some responsibilities. The Governance Policy Statement may be found at www.environment-agency.gov.uk/pensions .

Committee training

The Pensions Committee's training strategy takes account of the requirements of the Pensions Act 2004. The Act requires that trustees of occupational pension schemes should have knowledge and understanding of the law relating to pensions and role of trustees, the principles of scheme funding and investment, and the management and administration of pension scheme benefits. The training needs of Pension Committee members are assessed on an individual basis and take account of members' existing expertise, and interests in specific areas. Within this flexible framework the following structure is operated. All new members receive a comprehensive Pensions Committee Handbook and a half-day induction session before attending their first meeting. They are also given the opportunity to attend more specialist courses on a specific core competence and regional roadshows for Agency employees presented by HR staff and Capita Hartshead. In each subsequent year of membership they are expected to undertake two to three days training aimed at building or refreshing their knowledge and skills in specific topics in greater depth. A self-assessment training needs questionnaire is being developed to assist members in focussing on the most important areas for training. A detailed log of all Committee members training undertaken and planned is maintained.

Pensions changes

The Committee has, as in previous years, given priority to understanding and preparing for Government proposals to reform pensions and the LGPS in particular. It has set up an ad-hoc LGPS Changes Working Party to undertake the detailed planning and work required to inform all Fund members and to review relevant Agency policies and administrative procedures at Capita Hartshead offices.

During the year, the following legislative changes became effective:

- **The Finance Act 2004** – on 6 April 2006 ("A" Day) a new tax regime for all pension schemes came into force, replacing the previous tax regimes.
- **The Employment Equality (Age) Regulations 2006** – took effect from 1 October 2006, although the regulations relating to pensions were delayed and took effect from 1 December 2006.
- **The Local Government Pension Scheme (Amendment) Regulations 2006 (SI 2006 No. 966)** – introduced a number of significant scheme changes resulting from the Finance Act 2004 and the age discrimination regulations referred to above. Significant changes were:

    1. facility for members to commute some of their pension in order to receive a larger tax-free lump sum;
    2. introduction of flexible retirement;
    3. employees can join/remain in the Scheme until age 75;
    4. 15% limit on employee contributions removed;
    5. earnings cap removed, with service adjustments to avoid windfall gains;
    6. limit on maximum period of membership (40 years) removed.

- The Amendment Regulations also removed the Rule of 85 with effect from 1 October 2006 and brought in measures to deal with the cost of protecting the rights of older members and the delay in its removal.
- **The Local Government Pension Scheme (Amendment)(No.2) Regulations 2006 (SI 2006 No. 2008) –** were made on 24 July 2006 and provided additional protection for the rights of older members following the removal of the Rule of 85 from the Scheme.

Pension Updates Nos. 9 and 10 were issued in August 2006 and April 2007 respectively, informing members of the Scheme changes and giving details of proposed changes due to take place over the next year.

Pensions administration
The Environment Agency has a contractual arrangement with Capita Hartshead, a trading division of Capita Business Services Limited, to undertake the day-to-day administration of the Fund. We would like to express our thanks to Capita for resolving almost 1,400 fund member queries, for successfully delivering 20 briefings to more than 1,300 Environment Agency employees and for paying pensions to over 3,000 pensioners.

External audit
The Comptroller and Auditor General is the appointed external auditor of the Fund under the Government Resources and Accounts Act 2000 (Audit of Public Bodies) Order 2003. He has contracted PricewaterhouseCoopers LLP to undertake the detailed audit work on his behalf.

Pension fund fraud/National Fraud Initiative
The Fund has a formal policy and procedure for handling frauds linked to the unreported deaths of pensioners. It also participates in the Audit Commission's bi-annual National Fraud Initiative. No Active Fund fraud cases have come to light as a result of this exercise but any cases where fraud is suspected will be pursued. We will seek to agree a repayment plan or, where necessary, take legal action or involve the police.

Fund management and investment

Fund Managers
Responsibility for managing the Fund's investments has been allocated to 10 managers. Our managers, their investment styles and the division of the portfolio is as follows:

Manager	% of Portfolio	Investment Style
Hermes Investment Management	38.4	Low-risk, passive index tracking
Standard Life Investments	16.7	Active UK Equities
European Credit Management	8.9	Active Corporate Bonds
State Street Global Advisors	6.4	Active Global Equities
State Street Global Advisors	2.5	Low-risk, eco-enhanced UK index tracker
Sarasin Chiswell	7.5	Active Global Equities (SRI mandate)
Capital International	6.2	Global Equities
Morley Fund Management	5.0	Property
Scottish Widows Investment Partnership	3.8	Emerging Markets Equities
Robeco Alternative Investment	2.0	Private Equity
Informed Portfolio Management	1.6	Passive & Active Currency Management
Other, principally cash	1.0	Pending allocation to managers

In July 2006 Scottish Widows Investment Partnership were appointed to manage a new allocation to Emerging Markets Equities. In October 2006 Informed Portfolio Management (IPM) were appointed to manage the Fund's exposure to overseas currencies. They will passively manage 60% of the Fund's currency exposure to reduce risk and manage the remaining 40% of our currency exposure via a £40m active currency mandate to generate financial returns.

Corporate governance and environmental overlay strategy
The Corporate Governance Policy (Annex 3) and the Committee's Environmental Overlay Strategy (Annex 4) were in place across the whole Fund during the year. These set out the principles that the Committee expect our fund managers to adhere to. In line with our fiduciary duty our fund managers are required to take account of financially material environmental risks and to seek out investment opportunities to enhance their prospective investment performance. The Fund has continued to support the Local Authority Pension Fund Forum campaign to encourage environmental reporting by large companies. It has also supported the work of the UK Social Investment Forum, the Institutional Investors Group on Climate Change, United Nations Principles of Responsible Investment (UNPRI) and the Carbon Disclosure Project. Further information on extra-financial performance is included on page 13 and on our web site www.environment-agency.gov.uk/pensions.

Membership of the Pensions Committee and its advisers as at 31 March 2007

Chairman

John Edmonds *Board Member*

Members

Richard Percy *Board Member*

Suzanne Warner *Board Member*

Larry Whitty *Board Member*

Barbara Young *Board Member and Chief Executive*

Nigel Reader *Director of Finance*

Graham Ledward *Director of Human Resources*

Ric Navarro *Director of Legal Services*

To be appointed *Environment Agency, Wales**

Howard Pearce *Head of Environmental Finance and Pension Fund Management*

Alan Broughall *Member Representative*

Phil Chappell *Member Representative*

Dave Cowley *Member Representative*

Chris Galvin *Member Representative*

Aileen Parry *Member Representative*

Brian Engel *Retired Member Representative*

* David Edwell *Environment Agency, Wales - appointed June 2007*

Advisers

Comptroller and Auditor General, National Audit Office – External Auditor

National Westminster Bank plc – Bankers
Cater Allen Private Bank Ltd

The Northern Trust Company – Custodian

Douglas Anderson, Hymans Robertson – Consulting Actuary

Capita Hartshead – Pensions Administrator

Osborne Clarke – Lawyers

Carolan Dobson – Independent Investment Adviser

Mercer Investment Consulting – Investment Consultants

bFinance Ltd – Fund Manager Selection Consultants

Rathbone Greenbank – Sustainable Responsible Investment Consultants

Pension Fund membership

Unless they have elected in writing not to be members, all full and part-time employees of the Environment Agency, whether permanent or temporary, become active members of the Fund. The 12 months ended 31 March 2007 have seen an increase in the Fund's active membership of 0.7% (2006: 2.0%).

Active membership		**2007 No.**	**2006 No.**
At 1 April 2006		**11,844**	11,615
Entrants	new starters	1,066	1,208
	late notifications	245	140
		1,311	1,348
Less:			
Exits	late notification of previous year leavers	(76)	(233)
	options pending	(9)	(2)
	new retirement pensions	(181)	(191)
	deaths in service	(12)	(7)
	deferred benefits	(665)	(608)
	transfers	(250)	(2)
	refunds of contributions	(36)	(25)
	new starters opted out before contributions made	-	(51)
		(1,229)	(1,119)
At 31 March 2007		**11,926**	11,844

Age profile at 31 March		**2007**		**2006**	
		No	**%**	**No.**	**%**
Under 50	Male	5,015	42.05	5,060	42.7
	Female	3,880	32.53	3,820	32.3
		8,895	74.58	8,880	75.0
50 to 59	Male	1,911	16.02	1,933	16.3
	Female	590	4.95	575	4.9
		2,501	20.97	2,508	21.2
60 and over	Male	454	3.81	396	3.3
	Female	76	0.64	60	0.5
		530	4.45	456	3.8
Total		**11,926**	**100.0**	11,844	100.0

The Fund also has:				
Current pensioners (*including spouses' and children's pensions)*	3,114		2,913	
Deferred pensioners	4,050		3,521	
	19,090		18,278	

Based on data supplied by Capita Hartshead on 2 April 2007. Capita Hartshead's contact details are included on the back cover.

The figure for Deferred Pensioners includes 322 cases (2007: 331) where there is no entitlement to a deferred pension, and the only entitlement is to a refund of contributions. These are former employees whom we are unable to trace, with refunds being paid as and when we do make contact with them.

Communications

Pension Updates 9 - Active Members was issued in August 2006 and explained the Government's changes to the taxation of pensions "tax simplification" and the phasing out of the "85 year rule"

Pensions Update 9 - Deferred Members was issued in October 2006 and explained the impact of the "tax simplification" changes on deferred members and offered them the opportunity to opt out of those changes if they felt it was beneficial to them to do so.

Pensions Update 10 was issued in April 2007 and covered changes to the LGPS regulations, some changes to Environment Agency pensions policy and an update on progress towards the introduction of the "new look" LGPS.

Further newsletters are planned to keep members informed of pension developments, in particular the final shape of the "new look" LGPS to be introduced in April 2008.

Active and deferred members will receive an annual statement of their accrued pension benefits during the year.

Fundfare 2007 will be mailed to active and deferred members and pensioners in the autumn. It will summarise the Fund's Annual Report and Financial Statements as at 31 March 2007 and provide information on other pension-related matters.

During the year our *Members Guide,* which is sent to all new starters and made available electronically to all active members was updated three times to take account of changes to the LGPS regulations during the year. Further updates will be produced during 2007/8 to reflect the forthcoming changes to the LGPS Regulations.

In the second half of the year we produced an addendum to update our *Retirement Guide,* which is aimed at members who have retired or are approaching retirement. It includes a variety of useful information about life in retirement including EAPF and state benefits, taxation and lifestyle and leisure activities. We expect to produce an updated guide during 2007/08.

The pensions administration contract with Capita Hartshead includes the provision of annual presentations on pensions and related matters at each Region and Head Office. These are known as Pensions Briefings (previously called Roadshows). They are targeted at employees, and several regions held additional presentations. In total, more than 1,300 Environment Agency staff attended the 2006/2007 Briefings.

Pensions publications for members are provided in bi-lingual versions in order to satisfy the Environment Agency's Welsh Language Scheme. Electronic versions are available on our pensions web site www.eapf.capitahartshead.co.uk.

Pensions increase

Pensions in payment and deferred benefits are subject to annual review under the Pensions (Increase) Act 1971. The Pensions Increase (Review) Order 2007 required an increase of 3.6% (2006: 2.7%) to be awarded from 9 April 2007 (10 April 2006). This is reduced proportionately for pensions in payment for less than 12 months. As usual, the increase corresponds to the increase applied to State benefits and pensions paid by other public service pension schemes. It reflects the rise in the Retail Prices Index during the 12 months ended 30 September 2006.

Pension fund investment

Funding strategy statement

All LGPS funds are required to publish a Funding Strategy Statement. This statement is used by the Actuary to inform his valuation and the extant version is reproduced in Annex 1 to these financial statements.

Investment limits

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (as amended) require the Environment Agency to invest any monies not needed to make payments from the Fund. In doing so, they prescribe the limits on the type and extent of investments which the Environment Agency may pursue.

Although it may vary the types of investment, the Agency's policy must be formulated with a view to:

- the advisability of investing fund money in a wide variety of investments; and
- the suitability of types of investments and particular investments.

However, of the total value of the Fund's investments no more than the percentages shown below can be invested in the form of investment described:

- **5%**
  - a single sub-underwriting contract, i.e. a contract with a person who is underwriting a share issue to acquire the shares from him/her if that is what he/she requires, but with the total value of all sub-underwriting contracts not exceeding 15%;
  - as a limited partner in any single partnership (but not exceeding more than a total of 15% in such partnerships).
- **10%**
  - deposits with local authorities;
  - total deposits with any single bank, or similar institution except the National Savings Bank;
  - any single holding unless the investment is made by an external investment manager in a unit trust scheme.
- **15%**
  - total investments in unlisted securities, i.e. securities not quoted on a recognised stock exchange.
- **35%**
  - all securities (shares, stocks, debentures, etc) which the Environment Agency transfers or agrees to transfer under stock lending arrangements.
  - all investments in unit trust schemes;
  - all investments in open-ended investment companies where the collective investment schemes constituted by the companies are managed by any one body;
  - all investments in unit trust schemes and open-ended investment companies where the unit trust schemes and the collective investment schemes constituted by those companies are managed by any one body;
  - the value of any single insurance contract.

Statement of investment principles

All LGPS funds are required to publish a Statement of Investment Principles. A new Statement of Investment Principles was adopted by the Pensions Committee on 21 June 2007 and is reproduced in Annex 2 to these financial statements

Environmental overlay strategy

The Pensions Committee has adopted an Environmental Overlay Strategy, which is applied across all of the Fund's assets. Details of this strategy can be found in Annex 4.

Investment strategy

Although the management of the Fund's investments is vested in the Environment Agency, responsibility for altering its investment policy is delegated to the Pensions Committee.

The investment strategy developed by the Committee aims to maximise the return of the Fund, within an acceptable level of risk, by diversifying its investments throughout world markets. The Committee has agreed a strategic asset allocation of 31.5% in UK equities, 31.5% in overseas equities, 13.5% in index-linked gilts, 13.5% in corporate bonds, and 5% to both property and private equity. The Committee believes that this diversification of the Fund's assets will reduce risk whilst enhancing potential returns.

Custody arrangements

With the exception of managed fund units, The Northern Trust Company ("Northern Trust") acts as global custodian on behalf of the Fund's assets. All assets are held in the name of Nortrust Nominees.

As part of its normal procedures Northern Trust holds all assets in safe custody, collects dividend income, provides data for corporate actions, liaises closely with all of the investment managers and reports on all activity during the period.

Regular service reviews are held with Northern Trust to ensure continuous monitoring of service commitments. Other procedures and controls are in accordance with the Statement on Auditing Standards document - SAS 70.

Investment management

The Fund's investment managers implement the Committee's investment strategy. Each manager has full discretion in the management of their portfolios, subject to complying with statutory limits and the Statement of Investment Principles. Each manager is required to take due regard of the Active Fund Corporate Governance Policy and the Environmental Overlay Strategy.

The Committee has set the overall investment objective for the Fund in the light of the triennial actuarial valuation. It has considered the Fund's net contribution inflows and the maturity profile of its liabilities.

Fund benchmark

The Committee has set the following strategic benchmark for the Fund:

UK Equities	31.5%	FTSE All Share Index
Global Equities	31.5%	FTSE All World ex UK
Index-Linked Gilts	13.5%	FTSE Actuaries Over 5 Year Index-Linked Gilts
Corporate Bonds	13.5%	iBoxx Sterling all non-gilt
Property	5.0%	IPD UK Monthly
Private Equity	5.0%	Absolute Return

Manager benchmark

Each manager has been set a specific benchmark that reflects the asset class being managed. The benchmarks of the managers are:

Passive Management		
Hermes	Passive UK Equities	FTSE All Share
Hermes	Passive UK Index-Linked Gilts	FTSE UK Gilts Indexed > 5 yrs
Hermes	Passive UK Conventional Gilts	FTSE >15yr Gilt
Hermes	Passive North American Equities	FTSE World North America
Hermes	Passive European Equities	FTSE World Europe ex UK
Hermes	Passive Japanese Equities	FTSE World Japan
Hermes	Passive Asia Pacific Equities	FTSE World Asia Pacific ex Japan
State Street	Passive UK Equities Low Risk Eco-enhanced	FTSE 350 Index
Active Management		
European Credit	Active Corporate Bonds	iBoxx Sterling all non-gilt
Standard Life	Active UK Equities	FTSE All Share Index
Capital International	Active Global Equities	MSCI All Country World
State Street	Active Global Equities	MSCI All Country World
Sarasin Chiswell	Active Global Equities (SRI)	MSCI All Country World
Morley	Active Property	IPD UK Monthly
Scottish Widows	Active Emerging Markets Equities	MSCI Emerging Markets
Robeco	Active Private Equity	Absolute Return
Informed Portfolio Management	Active Currency	FTSE 100

IPM Informed Portfolio Management's active currency management mandate is "equitised" against the FTSE 100 index to avoid the Fund having a significant investment in cash. Their target is to generate an excess return over and above the return from a passive investment in the FTSE 100 index.

Performance target
Each manager has been set a performance target over three-year rolling periods as follows:

Hermes	to match their benchmarks
European Credit	to beat their benchmark by 1% per annum
Standard Life	to beat their benchmark by 2% per annum
Sarasin Chiswell	to beat their benchmark by 2% per annum
Capital International	to beat their benchmark by 3% per annum
State Street	to beat their benchmark by 3% per annum (global equities) and to track the FTSE 350 Index (UK equities)
Scottish Widows	to beat their benchmark by 3% per annum
Morley	to beat their benchmark by 1%
Robeco	minimum internal rate of return of 10% per annum or 5% greater than the return on MSCI World index
Informed Portfolio Management	To generate an excess return of £6 million per annum

Financial performance

The Fund's overall return in the year was +7.1% (2006: +22.8%) compared to the benchmark return of a +5.9% (2006: +22.0%). During the period the headline rate of the Retail Prices Index rose by 4.8% (2006: 2.4%).

Over the three years to 31 March 2007 the annualised rate of return was +13.4% (2006: +19.3%). The benchmark return was +12.9% (2006: +19.0%)

The table below shows the performance of the managers during 2006/07.

The total fund financial result includes Robeco and IPM for completeness. However the ISG agreed it was not appropriate to put their detailed figures on this table because their performance is measured differently to the main asset classes and managers above who manage over 95% of our assets.

	2007			2006		
Manager	**Bench mark return %**	**Fund return %**	**Performance relative to benchmark %**	**Benchmark return %**	**Fund return %**	**Performance relative to benchmark %**
Passive Management						
Hermes (UK Equities)	+11.1	+11.1	+0.0	+28.0	+27.7	-0.3
Hermes (UK Index-Linked Gilts)	+2.6	+2.6	+0.0	+9.0	+8.9	-0.1
Hermes (UK Conventional Gilts)	+1.7	+1.7	+0.0	-	-	-
Hermes (North American Equities)	-0.9	-0.9	+0.0	+24.3	+24.2	-0.1
Hermes (Europe ex UK Equities)	+12.2	+12.2	+0.0	+36.0	+35.9	-0.1
Hermes (Japanese Equities)	-9.9	-9.9	+0.0	+49.0	+48.2	+0.8
Hermes (Asia Pacific ex-Japan Equities)	+20.3	+20.3	+0.0	+34.1	+34.3	+0.2
State Street (UK Equities)	+11.1	+11.2	+0.1	+28.1	+26.7	-1.4
Active Management						
European Credit Management (Corporate Bonds)	+1.1	+1.7	+0.6	+7.8	+8.1	+0.3
Standard Life (UK Equities)	+11.1	+13.2	+2.1	+28.0	+31.1	+3.1
Capital International (Global Equities)	+2.5	+1.3	-1.2	+30.4	+31.7	+1.3
State Street (Global Equities)	+2.5	+3.0	+0.5	+30.4	+31.6	+1.2
Sarasin Chiswell (Global Equities/ Environmental Specialist)	+2.5	+9.0	+6.5	+30.4	+39.9	+9.5
Scottish Widows (Emerging Market Equities) (from July 2006)	+16.8	+14.4	-2.4	-	-	-
Morley (Property)	+15.6	+18.2	+2.6	-	-	-
Total Fund	**+5.9**	**+7.1**	**+1.2**	**+22.0**	**+22.8**	**+0.8**

Portfolio analysis

Distribution of net assets at market value as at 31 March 2007:

	Hermes	Standard Life	ECM	State Street	Sarasin Chiswell	Capital International	Scottish Widows	Morley	Robeco	IPM	Other	Total	% of Fund
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%
UK Equities	156.8	251.4		47.7	11.3	10.1						**477.3**	31.4%
Pooled Equities	11.0											**11.0**	0.7%
Pooled Fixed Interest			135.1									**135.1**	8.9%
Pooled Gilts	207.6											**207.6**	13.6%
Overseas Equities	205.9			86.8	100.7	83.2	55.7					**532.3**	35.0%
North America	*117.2*			*43.9*	*28.0*	*34.7*	*0.8*					***224.6***	*14.8%*
Europe	*50.4*			*21.0*	*52.7*	*22.3*	*0.6*					***147.0***	*9.7%*
Japan	*20.8*			*9.7*	*12.0*	*12.2*						***54.7***	*3.6%*
Asia Pacific	*17.1*			*4.0*	*2.7*	*4.1*	*15.0*					***42.9***	*2.8%*
Emerging Markets	*0.4*			*8.2*	*5.3*	*9.9*	*39.3*					***63.1***	*4.1%*
Pooled Property								76.4				**76.4**	5.0%
Private Equity									22.2			**22.2**	1.5%
Pooled Currency										21.7		**21.7**	1.4%
Cash (including current assets)	1.3	0.7		0.5	2.1	0.8	1.4	0.6	8.5		9.5	**25.4**	1.7%
AVC investments											5.3	**5.3**	0.3%
Other net investments	1.3	1.7		0.6	0.3	0.3	0.1			3.5		**7.8**	0.5%
Total	**583.9**	**253.8**	**135.1**	**135.6**	**114.4**	**94.4**	**57.2**	**77.0**	**30.7**	**25.2**	**14.8**	**1,522.1**	**100.0%**

The Fund has no employer related investments.

Geographical distribution of quoted and pooled equity investments

	2007		2006	
	£M	**%**	**£M**	**%**
United Kingdom	488.3	47.8%	430.7	47.9%
North America	224.6	22.0%	224.5	25.0%
Europe (excluding UK)	147.0	14.4%	135.7	15.1%
Japan	54.7	5.4%	55.3	6.2%
Asia Pacific (excluding Japan)	42.9	4.2%	25.2	2.8%
Emerging markets	63.1	6.2%	27.4	3.0%
Total	**1,020.6**	**100.0%**	**898.8**	**100.0%**

UK equities by sector

	2007			2006	
Sectors	**£M**	**%**	**Sectors**	**£M**	**%**
Banks	85.8	17.6%	Banks	87.6	20.3%
Oil & Gas	65.2	13.4%	Oil & Gas	71.8	16.7%
Industrial Goods & Services	56.3	11.6%	Industrial Goods & Services	49.1	11.4%
Basic Resources	38.8	7.9%	Healthcare	30.4	7.1%
Healthcare	32.8	6.7%	Basic Resources	29.8	6.9%
Telecommunications	28.9	5.9%	Insurance	22.8	5.3%
Insurance	26.0	5.3%	Telecommunications	21.4	5.0%
Travel & Leisure	23.2	4.8%	Travel & Leisure	19.5	4.5%
Retail	19.8	4.1%	Utilities	16.9	3.9%
Other	111.5	22.8%	Other sectors	81.4	18.9%
Total	**488.3**	**100.0%**	**Total**	**430.7**	**100.0%**

(In January 2006 FTSE international instigated a new sector classification.)

Top 10 UK equity holdings

	2007			2006	
Company	**Total £m**	**% of UK Equity**	**Company**	**Total £m**	**% of UK Equity**
BP	30.0	6.1%	BP	32.6	7.6%
HSBC Holdings	24.3	5.0%	HSBC Holdings	29.3	6.8%
Royal Bank of Scotland Group	23.7	4.9%	GlaxoSmithKline	20.8	4.8%
GlaxoSmithKline	21.3	4.4%	Royal Bank of Scotland Group	20.6	4.8%
Vodafone	19.1	3.9%	Royal Dutch Shell	17.5	4.1%
HBOS	14.6	3.0%	Vodafone Group	17.4	4.0%
Anglo American	13.9	2.9%	HBOS	14.5	3.4%
Royal Dutch Shell	13.5	2.8%	Anglo American	13.2	3.1%
Barclays	12.4	2.5%	Barclays Bank	12.6	2.9%
Aviva	8.9	1.8%	Aviva	10.0	2.3%

Top 10 overseas equity holdings

2007				2006			
Company	**Country**	**£m**	**% of Equities**	**Company**	**Country**	**£m**	**% of Equities**
Petrobras	Brazil	4.0	0.4%	Texas Instruments	United States	3.2	0.4%
Encana Corp	Canada	3.9	0.4%	Canon	Japan	3.2	0.4%
Firstrand	South Africa	3.6	0.4%	International Business Machines	United States	3.2	0.4%
Vale Do Rio Doce	Brazil	3.6	0.4%	Oest Elektrizitats	Austria	3.1	0.4%
Tokyo Gas	Japan	3.4	0.3%	Deutsche Telekom	Germany	2.7	0.3%
International Business Machines	United States	3.3	0.3%	Statoil	Norway	2.7	0.3%
Skanska	Sweden	3.2	0.3%	Solarworld	Germany	2.6	0.3%
Itau Holdings	Brazil	3.2	0.3%	Encana Corporation	Canada	2.5	0.3%
Lukoil	Russian Federation	2.9	0.3%	Westpac Banking	Australia	2.5	0.3%
Solarworld	Germany	2.8	0.3%	Home Depot	United States	2.4	0.3%

Top 20 holdings of the Fund at 31 March 2007

		2007	
Holding	**Asset class**	**Total £m**	**% of Fund**
Hermes UK Index-Linked Gilts	Unit Trust Bonds	175.5	11.5%
Hermes North America Pooled Fund	Unit Trust Equity	117.1	7.7%
European Credit (Luxembourg) 03/2015	Corporate Bonds	116.0	7.6%
Hermes European Pooled Fund	Unit Trust Equity	50.3	3.3%
UK All Stock Gilt Index Tracker	Unit Trust Bonds	32.1	2.1%
BP	UK Equities	30.0	1.9%
HSBC Holdings	UK Equities	24.2	1.6%
Royal Bank of Scotland Group	UK Equities	23.7	1.5%
IPM Global Currency Fund	Unit Trust Equity (Currency)	21.7	1.4%
GlaxoSmithKline	UK Equities	21.3	1.4%
Hermes Japanese Pooled Fund	Unit Trust Equity	20.8	1.4%
European Credit (Luxembourg) 06/2016	Corporate Bonds	19.1	1.3%
Vodafone	UK Equities	19.1	1.3%
Hermes Pacific (ex Japan) Pooled Fund	Unit Trust Equity	17.0	1.1%
HBOS	UK Equities	14.6	1.0%
Anglo American	UK Equities	13.9	0.9%
Royal Dutch Shell	UK Equities	13.5	0.9%
Barclays	UK Equities	12.4	0.8%
BlackRock UK Property Fund	Property Unit Trust	11.7	0.8%
Morley Pooled Pensions Property Fund	Property Unit Trust	11.5	0.7%
		765.5	**50.2%**

Extra-financial Performance

The Environment Agency Pension Fund seeks to manage its investments in a financially robust and environmentally responsible way. Extra-financial issues are increasingly important in assessing the quality of management and its management of risks relating to environmental and social issues which may impact on the future performance and prospects of a company.

Corporate governance, engagement and voting

We believe that well governed companies produce better and more sustainable returns than poorly governed companies. To assess polices, processes and practices, all of our equity fund managers regularly engage with companies either directly or through a specialist provider.

For example, BP, being one of the UK's largest listed companies, is correspondingly one of the fund's largest holdings, although since the introduction of our new strategy its relative proportion of our fund has fallen by 43% in the last 2 years. BP has had a turbulent year and we have engaged with the company via our fund managers on a wide range of environmental and social issues, and continue to monitor their performance closely.

We aim to vote on all environmental resolutions in the UK, Europe and North America and, where practical, worldwide. During the year we voted on 54 environmental resolutions, 98% of which were in North America. This was an increase of 70% on the previous year. Surprisingly, although climate change remained a popular topic, the number of resolutions fell by 11% from the previous year. The most popular topic was sustainability reports (11 shareholder resolutions) and we universally voted in favour. Our voting record on environmental resolutions and management exceptions are available on our website at www.environment-agency.gov.uk/pensions.

The most significant environmental resolution in the EU was at the AGM of Royal Dutch Shell. The resolution was organised by Ecumenical Council for Corporate Responsibility and was co-signed by 130 shareholders including the Rowntree Foundation in the UK and some large US pension funds. The resolution called for improvements in Shell's governance and performance, particularly in local community relations and environmental risk and impact assessment. 17% (6% for, 11% abstentions) of shareholders did not support Shell Management which by UK standards is significant. The EAPF was highlighted as one of number of institutional investors who supported the resolution.

United Nations Principles of Responsible Investment

The Fund's Corporate Governance and Environmental Overlay strategies set out how we achieve or seek to achieve all of the stated principles. We are delighted that all of our fund managers (except State Street Global Advisors & Capital International) have signed up to the principles directly and the others have committed to support our implementation. A more detailed compliance assessment report is on our website at www.environment-agency.gov.uk/pensions.

Environmental overlay

The Committee's Environmental Overlay Strategy applies across all of the Fund's mandates and we monitor and report on the progress of its implementation every quarter.

We were delighted that our work in integrating financially material environmental issues was again recognised and are proud winners of two further awards and runner-up, for the second year running, in the Sustainable City's Socially and Ethically Responsible Investment and Asset Management Award.

October 2006 – Professional Pensions - Pension Scheme of the year 2006

Best Use of Socially Responsible Investment (SRI) Award – Winner – The Environment Agency Pension Fund

These awards are open to all pension funds in both public and private sectors and 2006 saw a record number of entries in many categories. The Environment Agency Pension Fund won the award for Best Use of SRI from a short-list that included the BT pension fund and two other LGPS Funds (Shropshire and Strathclyde).

November 2006 - Investments and Pensions Europe Fund Awards 2005
Best UK Pension Fund 2006 – Joint Winner - The Environment Agency Pension Fund
Leading EU pension funds entered the awards. The Environment Agency Pension Fund shared the Best UK Pension Fund Award with Saul (the University of London pension scheme). Our revamped investment strategy with its commitment to sustainable environmentally responsible investment (SERI) which incorporates our innovative environmental overlay strategy was cited as a major achievement. Saul were cited for the innovative approach they have adopted for dealing with their deficit. Only one other UK pension fund won an award – Strathclyde Pension Fund (an LGPS fund) shared the Specialist Investment Award with Inarcassa – Italy's architects and engineers pension fund.

February 2007 – Sustainable City Awards by City of London Corporation and UK Social Investment Forum
The Environment Agency Pension Fund was runner up for the Socially Responsible Investment Award for the second time (to Trucost in 2007 and to the international Carbon Disclosure Project in 2006). We were highly commended by the judges because of the commitment to financial and environmental performance required from all our fund managers across all asset classes and the consequent indirect influence on other mandates.

April 2007 – United Nations Environment Programme Report
The Environment Agency Pension Fund was the only UK pension fund case study in the United Nations Environment Programme Finance Initiative report on good practice in responsible investment by public pension funds from around the world. A summary of the report can be found on our web site www.environment-agency.gov.uk/pensions and the full report on the UNEPFI site.

Measuring the Environmental Footprint of our investments
We have undertaken Environmental Footprint analysis using Trucost's methodology for each of our active equity funds against their respective benchmarks. By measuring our Footprint we aim to provide a fresh perspective on risk, stock selection and sector exposures. The Footprint methodology looks at companies' environmental impacts, for example the amount of raw materials, water and energy used and the waste and carbon emitted. Trucost evaluates over 700 factors in assessing a company's environmental impact.

The Footprint for each equity manager, in relation to the EAPF, is compiled by allocating a proportion of the environmental impact of each company relative to the amount of stock that is held. Similarly, we have evaluated the environmental impact of our combined active equity holdings compared to the benchmark, the MSCI World Developed Countries Index. In 2007 the Fund's Environmental Footprint for combined active equities is 14.0% better than the benchmark. This represents a further improvement from the Environmental Footprint of 4.6% for 2006. This is the first time that a UK pension fund has publicly measured and reported the impact of its global equity holdings in this way.

Class actions
Where shareholder value has been eroded by malevolent action by company directors, sometimes it is possible for monies to be recovered via the courts by a shareholder class action against the company or its directors. We have retained Northern Trust to monitor these class actions and to recover for the Fund any monies due, although the total involved is currently not significant.

Statement of compliance with the Myners principles

In October 2001 the Government published its response to the review carried out by Paul Myners into institutional investment in the UK.

In its response to the review, the Government confirmed that the ten investment principles promulgated by Myners would be applied to the Local Government Pension Scheme by means of a combination of a one-off amendment to the LGPS regulations and authoritative guidance developed by CIPFA (Chartered Institute of Public Finance and Accountancy).

The regulation requires administering authorities, such as the Environment Agency, to state their compliance (or otherwise), with the ten principles and to justify non-compliance.

Myners Principle/CIPFA Checklist

Effective decision-making		**Explicit mandates**	
Define who takes investment decisions	✔	Written mandate included in management contract containing elements specified	✔
Consider whether members have sufficient skills	✔	Constraints on the types of investments are in line with regulations	✔
Determine whether appropriate training is being provided	✔	Reasons stated if soft commissions permitted	✔
Assess whether in-house staffing support is sufficient	✔	**Activism**	
Establish an investment committee with suitable terms of reference	✔	Incorporate US principles on activism into mandates	*Note 2*
Draw up a business plan	✔	Engage external voting agencies if appropriate	✔
Clear objectives		Review manager strategies	✔
Set overall investment objective specific only to the Fund's liabilities	✔	Establish means to measure effectiveness	✔
Determine parameters for employer contributions	✔	**Appropriate benchmarks**	
Specify attitude to risk and limits	✔	Consider whether index benchmarks selected are appropriate	✔
Identify performance expectations and timing of evaluation	✔	Limits on divergence from index are relevant	✔
Peer group benchmark in use for comparison purposes only	✔	Active or passive management considered	✔
Focus on asset allocation		Targets and risk controls reflect performance expectations	✔
Priority is given to strategic asset allocation decisions	✔	**Performance measurement**	
All asset classes permitted within the regulations have been considered	✔	Formal structure for regular monitoring in operation	✔
Asset allocation is compatible with liabilities and diversification requirements	✔	Arrangements in place to assess procedures and decisions of members	✔
Expert advice		Similar arrangements established for advisers and managers	✔
Separate contracts in place for actuarial services and investment advice	✔	**Transparency**	
Terms of reference specified	✔	SIP updated as necessary	✔
Specify role of Section 151 officer in relation to advisers	*Note 1*	Consultation undertaken on amendments	✔
Tender procedures followed without cost constraint	✔	Changes notified to stakeholders	✔
		Regular reporting	
		Publish changes to SIP and its availability	✔
		Identify monitoring information to report	✔
		Inform scheme members of key monitoring data and compliance with principles	✔

Notes

1. Whilst the best value process and the statutory responsibilities of Section 151 of the Local Government Act 1972 do not apply to the Environment Agency, it nevertheless abides by and aspires to the principles of best practice.
2. In common with many other Local Government Pension Scheme Funds, the Pensions Committee has delegated engagement with companies to its fund managers. This engagement may not be in line with the US principles.

Foreword to the financial statements

The Environment Agency Active Pension Fund (“the Fund”) is a statutory public service pension scheme (as defined by the Pension Schemes Act 1993) under the Local Government Pension Scheme Regulations 1997 (as amended) – (“the 1997 regulations”).

Being part of the Local Government Pension Scheme the Fund is contracted out of the State Second Pension Scheme (“S2P”) and is a Registered Pension Scheme under Chapter 2 of Part 4 of the Finance Act 2004. Full tax relief is granted on members’ and the Environment Agency’s contributions paid to the Fund and on all United Kingdom investment income other than dividends arising from UK equities.

Roles and responsibilities of the Pensions Committee

With a membership of nominated Environment Agency Board members, senior officers, member representatives and a retired member representative, the Committee (which is a sub-committee of the Board) has been delegated the responsibility for Fund matters. It receives advice from its external advisers and is charged with appointing managers and agents required for the effective management of the duties outlined below.

The Environment Agency Pensions Committee (“the Committee”) is responsible for obtaining audited financial statements for each financial year which give a true and fair view of the financial transactions of the Fund and the disposition of its assets and liabilities at the year end, other than the liabilities to pay pensions and benefits after the scheme year end. In preparing the financial statements the Committee has:

- selected suitable accounting policies and then applied them consistently;
- made judgments and estimates that are reasonable and prudent; and
- followed applicable accounting standards, in particular the Statement of Recommended Practice “*Financial Reports of Pension Schemes”*.

The Committee is responsible for keeping proper accounting records which disclose, with reasonable accuracy at any time, the financial position of the Fund and enable it to ensure that the financial statements comply with Schedule 8 to the Financial Memorandum issued by the Department for Environment, Food and Rural Affairs (Defra). However, responsibility for the regulations governing the Local Government Pension Scheme (LGPS) lies with the Local Government Pensions Unit at the Department for Communities and Local Government (formerly Office of the Deputy Prime Minister).

The Committee is responsible for keeping records of contributions received in respect of active members of the Fund and for ensuring that contributions are made to the Fund in accordance with the Pensions Act 1995, the 1997 regulations and with the recommendations of the Consulting Actuary.

The Committee is also responsible for safeguarding the assets of the Fund and hence for taking reasonable steps for the prevention and detection of error, fraud and other irregularities.

This Annual Report and Financial Statements is available on the Environment Agency’s website. The maintenance and integrity of the website is the responsibility of the Environment Agency. The work carried out by the Auditors and the Scheme Administrator does not involve consideration of these matters. Accordingly, the Auditors and Administrator accept no responsibility for any changes that may have occurred to the information contained in the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of the financial statements and other information included in annual reports may differ from legislation in other jurisdictions.

Summary of the financial statements

The financial statements have been prepared on a market value basis.

Contribution income has risen by £6.5m to £60.9m (2006: risen by £7.4m to £54.4m). The increase for the year ended 31 March 2007 was due mainly to the increase in the employer's rate and the rise in the number of members contributing during the year.

Net income from all transfer values received in the year has decreased by -£0.6m to £6.1m (2006: increased by £0.8m to £6.7m).

Retirement benefits and other payments made to or in respect of members during the year have increased by £2.5m to £32.4m (2006: increased by £5.4m to £29.9m).

In overall terms the net additions from dealings with members during the year have increased by £4.7m to £29.8m (2006: decreased by -£0.2m to £25.1m).

The value of the net assets of the Fund at 31 March 2007 has increased by £128.8m to £1,525.7m (2006: increased by £277.3m to £1,396.9m). This is primarily due to an increase in the market value of its investments.

Accounting Officer's statement on internal control

Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of the Environment Agency's 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 Government Accounting. To that end I share with the Board of the Environment Agency responsibility for maintaining a sound system of internal control and the mechanism by which both the Board and I assure ourselves that it is working effectively are the same. I am personally accountable to the Board and to Parliament, and the Board is accountable to Government.

The Environment Agency (the Agency) is responsible for the administration of the Environment Agency Active and Closed Pension Funds (the Funds). The Board has assigned responsibility for management of the Funds and custody of their assets to the Pensions Committee. The Committee is supported by its Investment Sub-Group, a working group on Local Government Pension Scheme (LGPS) changes, officers of the Agency and external fund managers in accordance with the Local Government Pension Scheme Regulations 1997 (as amended) and the Local Government Pension Scheme (Management and Investment of Funds) 1998 Regulations (as amended).

The roles and responsibilities of the Agency Accounting Officer in respect of propriety and regularity of management of the administration of the Funds are the same as for the Agency as a whole.

The responsibilities and duties of those responsible for management of the Funds and their assets are set out in the following governance documents:

a) *Schedule 8 of the Environment Agency's Financial Memorandum*
b) *Pension Funds Governance Policy Statement* which includes:
   - *The Pensions Committee Terms of Reference and Standing Orders* – details the status, composition and responsibilities of Pensions Committee and Members; and
   - *Pension Funds Scheme of Delegation* - prescribes the arrangements for, and limitations to, the delegation of powers and duties within the Agency under the LGPS Regulations 1997 (as amended) and (Management and Investment of Funds) Regulations 1998 (as amended) in its capacity as Administering Authority and encompassing the Employing Authority Discretions.

The Pensions Committee reviews its Governance Policy Statement annually before the start of each financial year to take account of regulatory changes and operational needs to comply with the LGPS Regulations. The latest update was approved by the Pensions Committee on 24 January 2007 and ratified by the Agency Board on 7 February 2007.

The appointment of members of the Pensions Committee, its Investment Sub-Group and officers and advisers to manage and administer the Funds, pays due regard to the nature of their responsibilities and the need to avoid conflicts of interest. Written guidance is issued to each member and adviser on the meaning of and procedures for dealing with conflicts of interest. A register of interests is maintained and reviewed by the Chairmen of the Environment Agency Pensions Committee and Audit Committee annually.

The purpose of the system of internal control

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 Funds' policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The system of internal control has been in place within the Agency and in the operation of the Funds for the year ended 31 March 2007 and up to the date of approval of the annual report and accounts. It accords with Defra and Treasury guidance and best practice and has identified the significant issues set out on page 21.

Capacity to handle risk

The Agency has a statement setting out its strategic approach to risk management that has been agreed with its Board and Directors.

The 2004 Pension Act requires trustees of occupational pension schemes to have knowledge and understanding of the law relating to pensions and the role of trustees, the principles of scheme funding and investment, and the management and administration of pension scheme benefits.

Whilst the LGPS is exempted from these requirements, the Funds have a structured training programme covering from new member induction to those with extended periods of service. Training of Pensions Committee members is assessed on an individual needs basis, taking account of members' existing expertise, and interests in specific areas. All Pensions Committee members identify their personal training needs and a training log is maintained. Officers' training needs are identified in training and personal development plans.

The risk and internal control environment

The Agency's risk management strategy recognises that effective risk management is a key component to the delivery of its objectives. The strategy promotes the taking of well-managed risks that balance the needs of stakeholders. The strategy recognises the importance of prioritising how the Funds respond to risk and that the response must be to reduce the residual risk to an acceptable and justifiable level. Clear accountability for risk ownership and the regular monitoring and reporting of progress to management are mandated to ensure risk management plans are delivered.

Pensions Administration

The Agency has a contractual arrangement with Capita Hartshead for third-party administration of the Funds. This includes administration of all member and pensioner records, maintenance of LGPS and Fund rules, processing of contributions, payment of benefits, communications and scheme accounting in accordance with the Local Government Pension Scheme Regulations 1997 (as amended). Arrangements are in place for checking the validity of pension claims to avoid fraud and ensure propriety. Regular reports are provided at quarterly progress meetings. More information about Capita Hartshead's risk and control environment is provided in its FRAG 21 report.

Global Custody

The Agency also has a contractual arrangement with the Northern Trust Company who, with the exception of managed fund units, act as global custodian of the Funds' assets. As part of its normal procedures Northern Trust holds all assets in safe custody, collects dividend income, provides data for corporate actions, liaises closely with all of the investment managers and reports on all activity during the period. Regular service reviews are held with Northern Trust to ensure continuous monitoring of service commitments. More information about Northern Trust's internal control framework is included in its service level agreement, risk management document and SAS 70 report.

In addition to the above, the key elements of the internal control environment include:

Procedures for the setting and monitoring of the achievement of the Funds' objectives

The Funds have an established strategic planning process in place. The Pensions Committee prepares triennial Funding Strategy Statements after taking advice from the Actuary, investment advisers and officers. The Actuary uses the Funding Strategy Statements to prepare the triennial actuarial valuation of the Funds, and, in the case of the Active Fund, to set the common contribution rate for the employer. The Funds' strategic investment strategies are established taking into account the results of the triennial actuarial valuations.

The Funds operate within a framework of common procedures and control points as a means of ensuring all staff work towards, and identify with, common aims. This includes the members' handbook, Financial Scheme of Delegation and performance management arrangements, which authorise officers to act on behalf of the Funds within a defined framework of procedural control.

A risk management process is used to identify the principal risks to the achievement of the Funds' objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically.

A detailed risk register has been developed by officers covering all aspects of the pensions function, together with a more detailed Key Risks document which highlights the top risks. These documents assist the Pensions Committee in managing strategic risks across all pensions activities. This has been enhanced for ongoing risk management purposes and will form the basis of future internal audit strategy and planning. Management actions have been taken to mitigate the prioritised risks, and these are being monitored and reported to the Pensions Committee on a regular basis.

The facilitation of policy making and decision making
The Pensions Committee, and senior management of the Agency together with external advisers, jointly contribute to the Funds' strategic planning process including reviews of strengths, weaknesses, opportunities, threats and risks combined with consideration of the impact of updated, new or proposed legislation.

Key performance targets and benchmarks for fund managers are set by the Investment Sub-Group, including financial commitments, for approval by the Pensions Committee. Lead Officers cascade Pensions Committee strategy requirements to managers, teams and individuals through policies and procedures, performance appraisal and personal development plans.

Ensuring compliance with established policies, procedures, laws and regulations
The Pensions Committee and its Investment Sub-Group meet regularly to consider plans, performance and the strategic direction of the Funds through formal monitoring reports.

An annual report is submitted to the Agency Board on the performance of the fund managers, pensions administrator, and other professional advisors. Qualitative and quantitative information is provided on their compliance with the Myners principles for good investment management.

Ensuring the economical, effective and efficient use of resources and for securing continuous improvement in the way in which the functions of the Funds are exercised.
The Pensions Committee is committed to optimising the efficiency and effectiveness of the Funds' administration and investment management through continuous improvement of key processes, regular contract reviews, competitive tendering and benchmarking exercises.

The Funds have a formal policy and procedure for handling frauds linked to the unreported deaths of pensioners. It also participates in the Audit Commission’s bi-annual National Fraud Initiative and Life Certificate Exercises. Where fraud is suspected full repayment is sought and the police and courts involved as required.

The financial management and reporting of the Funds
The system of financial management is based on a financial control framework that includes the Agency's Procurement, Purchase Order Management and financial accounting systems, the Agency's Financial Memorandum and Scheme of Delegation, and the Funds' Scheme of Delegation (now in the Funds' Governance Policy Statement), together with administrative procedures, and management supervision. This includes:

- Comprehensive annual budget setting process and monitoring systems
- Setting targets to measure financial and other performance
- Regular reviews of periodic and annual financial reports which include administration and investment expenses and returns against budgets, targets and forecasts

The system of internal financial control can provide only reasonable and not absolute assurance that assets are safeguarded, that transactions are authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected in a timely period.

The performance management of the Funds and the reporting of performance management
The performance of the Funds is reported quarterly to the Investment Sub-Group and Pensions Committee and annually to the Board. Team Business Plans are monitored and the Head of Environmental Finance & Pension Fund Management monitors individual performance, continually and annually.

Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers of the Funds who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Board and the Audit Committee and a plan to address weaknesses and ensure continuous improvement of the system is in place.

The process that has been applied in maintaining and reviewing the effectiveness of the system of internal control includes:

a) The operation of the Agency Board and Pensions Committee that sets strategic direction, approves the Funds' investment and administration strategies and reviews performance. The Board receives reports from the Pensions and Audit Committees on the standards of corporate governance and internal control operating in the Funds.

b) The operation of the Audit Committee that reviews standards of internal control and financial reporting. It also considers audit reports and advises on the Funds' approach to risk management and corporate governance, and discusses with the appointed external and internal auditors the nature and scope of forthcoming audits.

c) The independent reviews by Internal Audit on the adequacy and effectiveness of the internal controls. These reviews are informed by an analysis of the risks to which the Funds are exposed and are conducted in accordance with Government Internal Audit Standards.

d) Officers of the Agency act on the recommendations made by external and internal auditors.

Significant internal control issues

The reviews undertaken and reported by internal audit in 2005 and 2006 concluded that the governance framework in place to manage the Funds is well designed and covers all the main areas of activity. There were, at that time, known issues over capture and transmission of member data to Capita Hartshead (the third party pensions administrator) which related to the process of inputting and verifying such data, and these are being resolved. Improvements have been made and continue to be made to employee pensions related data collection, data maintenance, data integrity and the timely submission of membership data, including the transfer of data from the Environment Agency to Capita Hartshead. Ownership and accountability is assigned to Human Resources under the Pensions Committee governance structure. Governance arrangements are being further enhanced by the introduction of a Pension Fund risk register to assist in the management of strategic risks across all pension activities.

Actions are taken to ensure these risks, once recognised, are appropriately managed. In 2007/08, work will continue in Human Resources to improve the provision of employee related pension data to Capita Hartshead and in Finance to enhance the Funds' risk register for ongoing risk management purposes.

The external audit report and the Pension Committee response were not delivered to Defra within the required time scale. These reports were submitted on 8 May 2007 and will be submitted by the Environment Agency in future.

Due to changes to the Local Government Pensions Scheme (LGPS) in 2006/07 and the new LGPS Regulations that are due to come into force from April 2008, the requirements of the Financial Memorandum no longer accurately reflect statutory requirements or the latest LGPS regulations.

In particular, the internal compliance audit highlighted that the current Schedule 8 requirement for 'Guidelines for Prudent Risk Management' have been superseded by a number of other LGPS regulatory requirements. A joint Defra and Environment Agency review of the current Schedule 8 is to take place to reflect the more recent and new LGPS regulations before April 2008.

Barbara Young

Barbara Young
Chief Executive and Accounting Officer
11 July 2007

Statement by the consulting actuary

Actuarial statement for the purpose of Regulation 77 of the Local Government Pension Scheme Regulations 1997.

As required by regulations, an actuarial valuation of the Fund's assets and liabilities was carried out as at 31 March 2004.

Security of Prospective Rights
In my opinion, the resources of the Fund are likely in the normal course of events to meet the liabilities of the Fund, as required by the Regulations. In giving this opinion I have assumed that the following amounts will be paid to the Fund: -

Employees – Contributions in accordance with the Local Government Pension Scheme Regulations 1997.

Employer - Contributions as recommended in my report on the actuarial valuation as at 31 March 2004, dated 7 March 2005.

Summary of Methods and Assumptions Used
My opinion on the security of the prospective rights is based on the projected unit valuation method. This assesses the cost of benefits accruing to existing members during the year following the valuation, allowing for future salary increases. The resulting contribution rate is adjusted to allow for any difference in the value of accrued liabilities (allowing for future salary increases) and the market value of assets.

Since I have taken assets into account at their market value it is appropriate for me to take my lead from the market when setting the financial assumptions used to value the ongoing liabilities, to ensure consistency of the asset and liability valuation bases.

The key financial assumptions adopted for this valuation were as follows:

Financial Assumptions	**Mar 2004**	
	% p.a. Nominal	**% p.a. Real**
Anticipated Investment return		
Equities	6.7%	3.8%
Bonds (50% gilt 50% corporates)	5.1%	2.2%
Discount Rate (70% Equities/ 30 % Bonds)	6.2%	3.3%
Pay Increases	4.9%	2.0%
Price Inflation/Pension Increases	2.9%	-

In order to value both those liabilities which have accrued at the valuation date and those accruing in respect of future service, I have assumed that the Fund's assets are notionally invested in a portfolio consisting of 70% equities and 30% bonds. The stream of future liability payments is converted into a capital value today by assuming a return on Fund assets of 6.2% a year.

Full details of the method and assumptions are described in my valuation report dated 7 March 2005.

The 2004 valuation revealed that the Fund's assets were sufficient to meet 94% (112% at 31 March 2001) of the liabilities accrued up to that date. Assets were taken into account at their then market value of £983m (£937m smoothed market value at 31 March 2001).

The employer's contributions have been set in accordance with the Fund's Funding Strategy Statement. The deficit is being spread over a period of 13 years, equivalent to the remaining working lifetime of scheme members, and the rise in contributions is being phased in over 4 years. The Agency's contributions have risen from 12% of pay in 2005/06 to 13.5% of pay in 2006/07. The Agency's contributions will rise to 15% of pay in 2007/08. A further increase to 16.5% of pay was recommended for 2008/09, but this will be reviewed when the results of the 2007 actuarial valuation are available.

Separate valuations are carried out in respect of the Closed Fund.

Copies of the valuation report are available on request from the Finance Department of the Environment Agency, the administering authority to the Fund. The next valuation of the Fund will be carried out as at 31 March 2007.

Experience since April 2004
The full three-yearly actuarial valuation as at 31 March 2007 is currently in progress.

The financial experience affecting the Fund's assets and liabilities since the 31 March 2004 valuation has been contrasting. Significant rises in the value of equity investments have delivered healthy returns for the assets. However, the value of liabilities has also risen from falls in long-term rates of interest and increases in inflation expectations.

The funding level as at 31 March 2007 is estimated to be close to 100%, if the 2004 valuation methodology is retained. This figure was calculated using a method and assumptions that are consistent with those used at the previous formal valuation, with the financial assumptions updated to reflect market conditions at 31 March 2007.

The unhelpful changes to bond markets have a more pronounced effect on the cost of new accruals. This is particularly important in the Active Fund given its youthful liability profile.

Changes to the benefit promise
The benefit promise has been amended in two ways that help to contain the rise in the cost of the benefits:

• since April 2006, retirees have been able to give up some of their (taxable) pension for an additional tax-free lump sum on retirement; and

• an early retirement right (known as the Rule of 85) has been removed for service after 1 April 2008.

Part of the savings arising from these changes are being ‘recycled’ into benefit improvements which take effect from 1 April 2008.

I am hopeful that the combined effects of the changes to economic conditions, the inclusion of a reserve for longevity improvement and the benefit design changes would be broadly neutral on the Agency’s contributions in the 2007 actuarial valuation.

W Douglas B Anderson
Fellow of the Institute of Actuaries
For and on behalf of Hymans Robertson LLP
5 June 2007

Hymans Robertson LLP
20 Waterloo Street
GLASGOW
G2 6DB

The Comptroller and Auditor General's statement about contributions
to the Houses of Parliament, the Board of the Environment Agency and the Secretary of State for Environment, Food and Rural Affairs.

I have examined the summary of contributions to the Environment Agency Active Pension Fund for the Fund year ended 31 March 2007 which is set out on page 25.

Respective responsibilities of the Environment Agency, its Pensions Committee and the Auditors
As described in the statement of the Pensions Committee's responsibilities, the Pensions Committee is responsible for ensuring that contributions are made to the Fund in accordance with the Local Government Pension Scheme Regulations 1997 and the recommendations of the Consulting Actuary. It is my responsibility to provide a statement about contributions paid in accordance with the Local Government Pension Scheme Regulations 1997 and with the recommendations of the Consulting Actuary and to report my opinion to you.

Basis of statement about contributions
I planned and performed our work so as to obtain the information and explanations which I considered necessary in order to give reasonable assurance that contributions reported in the attached summary of contributions payable have been paid in accordance with the relevant requirements. For this purpose the work that I carried out included examination, on a test basis, of evidence relevant to the amounts of contributions paid to the Fund and the timing of those payments in accordance with the Local Government Pension Scheme Regulations 1997 and the recommendations of the Consulting Actuary. My Statement about contributions is required to refer to those breaches of the Local Government Pension Scheme Regulations 1997 and the recommendations of the Consulting Actuary which come to my attention in the course of my work.

Statement about contributions
In my opinion contributions for the Fund year ended 31 March 2007 as reported in the attached summary of contributions payable have been paid, in all material respects, in accordance with the Local Government Pension Scheme Regulations 1997 and the recommendations of the Consulting Actuary.

John Bourn
Comptroller and Auditor General
National Audit Office
London SW1W 9SP

16 July 2007

Summary of contributions payable in the year

During the year, the contributions payable to the Scheme in accordance with the Local Government Pension Scheme Regulations 1997 (as amended) by the Employee and Employer for the year ended 31 March 2007 were as follows:

	Notes	Employee £'000	Employer £'000
Required by the LGPS regulations			
Normal contributions		18,109	40,801
Special contributions		-	961
Total		**18,109**	**41,762**
Other contributions payable			
Additional voluntary contributions (AVCs)		437	-
Purchase of added years		557	-
		994	-
Sub-totals		**19,103**	**41,762**
Total employee and employer contributions (as per Fund Account)	3		**60,865**

Signed on behalf of the Environment Agency Pensions Committee

John Edmonds
Chairman
The Environment Agency Pensions Committee
11 July 2007

Barbara Young
Chief Executive & Accounting Officer
The Environment Agency
11 July 2007

The Certificate and Report of the Comptroller and Auditor General to the Houses of Parliament, the Board of the Environment Agency and the Secretary of State for Environment, Food and Rural Affairs.

I certify that I have audited the financial statements of the Environment Agency Active Pension Fund for the year ended 31 March 2007 under the Government Resources and Accounts Act 2000 (Audit of Public Bodies) Order 2003. These comprise the Fund Account, the Net Assets Statement and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Agency and its Pensions Committee, and the Auditors

The Accounting Officer of the Environment Agency is responsible for preparing an annual report and financial statements under Schedule 8 to the Environment Agency Financial Memorandum issued by Defra in accordance with Local Government Pension Schemes Regulations 1997. These responsibilities are set out in the Statement of the Pension Committee's responsibilities.

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

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Environment Agency Financial Memorandum issued by Defra. I also report whether, in all material respects, the financial transactions conform to the authorities which govern them.

In addition, I report to you if, the Agency has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by relevant authorities is not disclosed.

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

I read the other information published with the financial statements, which consists of the Report by the Pensions Committee, the Investment Report and the Actuarial Statements, and consider whether it is consistent with the audited financial statements. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Bases of audit opinions

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of transactions included in the financial statements. It also includes an assessment of the significant estimates and judgements made by or on behalf of the Accounting Officer in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Fund's circumstances, consistently applied and adequately disclosed.

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

.

Opinions

Audit Opinion

In my opinion:

- the financial statements give a true and fair view, in accordance with the Government Resources and Accounts Act 2000 (Audit of Public Bodies) Order 2003 and under Schedule 8 to the Environment Agency Financial Memorandum issued by Defra in accordance with Local Government Pension Schemes Regulations 1997, of the financial transactions of the Fund for the year ended 31 March 2007 and of the amount and disposition at that date of its assets and liabilities, other than liabilities to pay pensions and benefits after the end of the Fund year, and

- the financial statements have been properly prepared in accordance with Schedule 8 to the Environment Agency Financial Memorandum issued by Defra in accordance with Local Government Pension Schemes Regulations 1997.

Audit Opinion on Regularity

In my opinion, in all material respects, the financial transactions conform to the authorities which govern them.

Report

I have no observations to make on these financial statements.

John Bourn
Comptroller and Auditor General
National Audit Office
London SW1W 9SP

16 July 2007

Financial statements for the year ended 31 March 2007

Fund Account

	Notes	2007 £000	2006 £000
Contributions and transfers			
Contributions receivable	3	60,865	54,403
Transfer values received	4	6,057	6,688
		66,922	61,091
Benefits and other payments			
Benefits payable	5	(32,403)	(29,948)
Payments to and on account of leavers	6	(3,401)	(4,950)
Administration expenses	7	(1,289)	(1,130)
		(37,093)	(36,028)
Net additions from dealings with members		**29,829**	25,063
Return on investments			
Investment income	8	25,817	21,555
Change in market value of investments	9	78,089	234,685
Investment management expenses	10	(4,905)	(3,927)
Net returns on investments		**99,001**	252,313
Net increase in the Fund during the year		**128,830**	277,376
Opening Net Assets of the Fund at 1 April		1,396,936	1,119,560
Net Assets of the Fund at 31 March		**1,525,766**	1,396,936

Net assets statement

	Notes	2007 £000	2006 £000
Investments	9	1,522,051	1,393,831
Current assets and liabilities	11	3,715	3,105
Net assets of the Fund at 31 March		**1,525,766**	1,396,936

The notes on pages 29 to 36 form part of these Financial Statements.

John Edmonds

John Edmonds
Chairman
Environment Agency Pensions Committee

11 July 2007

Barbara Young

Barbara Young
Chief Executive & Accounting Officer
Environment Agency

11 July 2007

Notes to the Financial Statements

1. Basis of preparation

The financial statements have been prepared in accordance with the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 and with the guidelines set out in the Statement of Recommended Practice, 'Financial Reports of Pension Schemes' (Revised November 2002) (the "SORP").

The financial statements summarise the transactions and net assets of the Fund. The financial statements do not take account of liabilities to pay pensions and other benefits that fall due after the end of the Scheme year. The actuarial position of the Fund, which does take account of such liabilities, is dealt with in the statement by the Consulting Actuary on pages 22 to 23 and these financial statements should be read in conjunction with it. The Actuary's statement, dated 5 June 2007, is based on a valuation as at 31 March 2004.

2. Accounting Policies

The following principal accounting policies have been applied consistently in the preparation of the financial statements.

Investments

Investments are included at their market values, which are determined as follows:

(i) Quoted securities listed on recognised stock exchanges are valued at middle market prices at the year end. Unquoted securities are valued by fund managers on the basis of latest dealings, professional valuations and financial information at the year end.

(ii) Pooled investment vehicles are stated at the mid-point of the latest prices quoted by the relevant fund managers, which reflect the underlying investments.

(iii) Acquisition costs are included in the purchase cost of investments.

(iv) Investment management fees are accounted for on an accruals basis.

Investment income

(i) Income from fixed interest and index linked securities and other interest receivable is taken into account on an accruals basis. Income from all other marketable securities is taken into account on an accruals basis on the date when stocks are quoted ex-dividend.

(ii) Income from investments is recorded net of any withholding tax where this cannot be recovered.

(iii) Accrued interest is excluded from the market value of fixed interest securities but is included in investment income receivable.

(iv) Income on investments in pooled investment vehicles with accumulation units is reflected in the unit price. Income on investments in property pooled investment vehicles is distributed and recognised on an accruals basis.

(v) The change in market value of investments during the period comprises all increases and decreases in the market value of investments held at any time during the period, including profits and losses realised on sales of investments and unrealised changes in market value.

(vi) Income from cash and short-term deposits is accounted for on an accruals basis.

Exchange Rates

(i) Where forward contracts are in place for assets and liabilities in foreign contracts, the contract rate is used.

(ii) Other assets and liabilities in foreign currencies are translated into sterling at the rates of exchange ruling at the year end.

(iii) Overseas dividends are valued at rates of exchange on the date when stocks are quoted ex-dividend.

(iv) Surpluses and deficits arising on conversion or translation are dealt with as part of the change in market value of investments.

Contributions
Normal contributions, both from the members and from the employer, are accounted for as they fall due under the Schedule of Contributions. The employer's contributions are made at a rate determined by the Consulting Actuary necessary to ensure that the Fund is able to meet its existing and prospective liabilities including indexation.

Special contributions made by the employer are payments in accordance with regulation 80(1) of the Local Government Pension Scheme Regulations 1997 (as amended) to cover the cost of additional membership awarded to leavers aged 50 and over by the Agency under regulation 52 of those regulations. Special contributions are accounted for in accordance with the agreement under which they are paid, or, in the absence of such an agreement, when paid.

Contributions from members for the purchase of added years and additional voluntary contributions are accounted for in the month deducted from the payroll.

Benefits payable
Members can choose whether to take a proportion of their retirement benefits as a pension and/or lump sum. Pensions and lump sums are accounted for on an accruals basis from the date the option is exercised. Lump sum death grants and refunds of contributions are included from the date of death or date the member leaves the Scheme.

Transfers to and from other schemes are those amounts paid to, or received from, other pension schemes relating to previous periods of pensionable employment. Individual transfers are included in the accounts when paid or received, but bulk transfers are accounted for an accruals basis when the amounts have been agreed.

Other expenses
Investment management and administration expenses are accounted for on an accruals basis. Expenses are recognised net of any recoverable VAT. The fees of the Fund's external investment managers reflect their differing mandates. Fees are linked to the market value of the Fund's investments and therefore may increase or reduce as the value of the investment changes. Fees are also payable to the Fund's global custodian.

Taxation
UK income tax and capital gains tax
The Fund is a registered pension scheme under Chapter 2 Part 4 of the Finance Act and is therefore not liable to UK income tax on interest and dividend income (other than dividends arising from UK equities), or to capital gains tax.

Value added tax
As the Environment Agency is the administering authority for the Fund, VAT input tax is recoverable on all Fund activities including expenditure on investment and property expenses. The accounts are shown exclusive of VAT.

US withholding tax
The income earned from investments in stocks and securities in the United States is exempt from US tax pursuant to Section 892 of the Income Tax Code and is not subject to the withholding of any tax under Section 1441. This exemption has continued to be applied thus far under the US Tax Reform Act of 1986.

Overseas tax deductions
Where possible, tax deducted at source is recovered by the investment managers.

3. Contributions receivable

	2007 £000	2006 £000
Employer		
Normal	40,801	33,760
Special	961	2,910
	41,762	36,670
Members		
Normal	18,109	16,914
Purchase of added years	557	479
Additional voluntary contributions (AVCs)	437	340
	19,103	17,733
Total	**60,865**	54,403

4. Transfer values received

	2007 £000	2006 £000
Individual transfers from other schemes	6,018	6,520
AVC transfers	39	168
	6,057	6,688

Transfer values have been paid ("cash equivalents" within the meaning of Part 1 of Schedule 5 to the Pensions Scheme Act 1993), and service credits given for transfers received, calculated in accordance with the method and assumptions approved by the Pensions Committee on the advice of the Actuary and based on guidelines issued by the Institute and Faculty of Actuaries.

No discretionary benefits have been included in the calculation of transfer values.

5. Benefits payable

	2007 £000	2006 £000
Retirement and dependants' pensions	23,844	21,499
Lump sum retirement grants	7,710	7,854
Lump sum death grants	843	588
Life assurance through AVC provider	6	7
	32,403	29,948

Benefits payable exclude £1.6m (2006 £1.6m) for historic unfunded pensions liabilities of the Agency in respect of compensatory added years paid via the pensions administrator. These have been recharged to the Agency and funded by Grant-In-Aid from Defra.

6. Payments to and on account of leavers

	2007 £000	2006 £000
Individual transfers to other schemes	3,334	4,801
Refunds of contributions	38	66
Payments to SERPS	2	24
AVC transfers	27	59
	3,401	4,950

7. Administration expenses

	2007 £000	2006 £000
Scheme administration	612	616
Professional fees:		
Actuarial	135	57
Audit	31	23
Legal	83	90
Consultancy	47	30
Other administration costs:		
Environment Agency administration	291	239
Communications to members	46	52
Miscellaneous	44	23
	1,289	1,130

8. Investment income

	2007 £000	2006 £000
Income from fixed-interest securities	-	230
Dividends from equities	21,677	16,801
Interest on cash deposits	2,342	4,010
Income from property unit trusts and managed funds	1,653	514
Income from private equity	145	-
	25,817	21,555

For unit trust expenses, both income and expenditure are shown gross of initial expenses – £Nil (2006: £334,000).

9. Investments

	Market Value at 1.4.06 £000	Purchases at Cost £000	Sales Proceeds £000	Change in Market Value £000	Market Value at 31.03.07 £000
Equities	682,670	300,180	(246,892)	50,283	786,241
Pooled Equities	216,336	11,557	(1,163)	7,655	234,385
Pooled Fixed Interest	338,875	50,000	(54,514)	8,341	342,702
Pooled Property	60,385	13,149	(7,201)	10,082	76,415
Private Equity	8,301	16,353	(2,132)	(331)	22,191
Pooled Currency	-	20,000	-	1,667	21,667
AVC investments	4,690	680	(509)	392	5,253
	1,311,257	**411,919**	**(312,411)**	**78,089**	**1,488,854**
Cash deposits & instruments	82,195				25,417
Other	379				7,780
	1,393,831				**1,522,051**

The change in the market value of investments comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

9. Investments continued

	2007 £000	2006 £000
Equities		
UK quoted	477,327	430,580
Overseas quoted	308,914	252,090
	786,241	682,670
Pooled Equities		
UK Unit trusts equities	10,973	179
Overseas Unit trusts equities	223,412	216,157
	234,385	216,336
Pooled Fixed Interest		
UK Unit trusts bonds - Index linked gilts	175,466	170,895
UK Unit trusts bonds – Conventional gilts	32,115	-
Total gilts	207,581	170,895
Overseas quoted corporate bonds	135,121	167,980
	342,702	338,875
Pooled Property		
UK Unit Trusts	59,668	46,555
UK Managed Funds	11,463	9,861
UK unquoted - Collective limited partnership investments	5,284	3,969
	76,415	60,385
Private Equity		
Overseas - unquoted	**22,191**	8,301
Pooled Currency	**21,667**	**-**
Cash deposits and instruments	**25,417**	**82,195**
Other		
Income tax recoverable	161	62
Accrued income	4,355	4,129
Due from/ (to) trade and currency brokers	3,264	(3,812)
	7,780	379

The fund managers operating the pooled investment vehicles are registered in the United Kingdom.

The Fund's global custodian is not authorised to enter into stock lending arrangements and no stock lending has taken place in the year.

Derivative contracts

UK Equities include equity derivative futures of £3.6m (2006: £4.1m) with corresponding derivative offsets of -£3.6m (2006: -£4.1m) managed by Hermes and State Street. Improved disclosure of these derivative contracts and their cash backing will be made to meet the requirements of the revised SORP for financial years commencing on or after 6 April 2007.

Forward currency contracts

The total unrealised gain on forward currency contracts managed by Informed Portfolio Management at the year-end was £3.5m (2006: £nil). This is currently included in the change in market value in equities and will be separately disclosed in cash deposits and instruments with effect from the 2007/08 financial year to meet the requirements of the revised SORP.

AVC investments

The aggregate amounts of AVC investments as at 31 March are as follows:

	2007 £000	2006 £000
The Equitable Life Assurance Society		
Equitable with-profits funds	650	681
Equitable unit-linked funds	929	958
Equitable building society funds	257	205
	1,836	1,844
Clerical Medical		
With-profits funds	504	415
Unit-linked funds	918	776
	1,422	1,191
Standard Life	**1,995**	1,655
Total AVC investments	**5,253**	4,690

The Environment Agency holds assets with The Equitable Life Assurance Society, Clerical Medical and Standard Life. These are in the form of with-profits, unit-linked and deposit accounts and secure additional benefits on a money purchase basis for those members electing to pay additional voluntary contributions. Members participating in this arrangement each receive an annual statement made up to 31 March confirming the amounts held to their account and the movements in the year.

Total investments

Including pooled investment vehicles total investments may be analysed as follows:

	2007 £000	2006 £000
Equities (includes pooled and private equity)	1,042,817	907,308
Bonds (includes pooled and gilts)	342,702	338,874
Property	76,415	60,385
Currency	21,667	-
Cash	25,417	82,195
AVC	5,253	4,690
Other	7,780	379
Total Investments	**1,522,051**	1,393,831

Investments exceeding 5% of net assets

At 31 March 2007 the holding in European Credit (Luxembourg) S.A. Medium Term Note was valued at £116.0m; this represents 7.6% of the net assets of the Fund (2006: £114.0m and 8.2%).

A list of the top 20 holdings of the Fund that includes pooled investment vehicles can be found on page 12 of the Pension Fund Investment report.

10. Investment management expenses

	2007 £000	2006 £000
Fund manager fees	4,292	3,241
Underlying fund manager expenses	355	374
Global custody	114	156
Investment advisers	48	100
Performance and risk measurement	96	56
	4,905	3,927

Total fund manager fees include management charges for European Credit Management and Informed Portfolio Management that are settled directly within the portfolio in accordance with the investment management agreements.

11. Current assets and liabilities

	2007 £000	2006 £000
Current assets		
Debtors		
Environment Agency	85	4,055
Standard Life	49	-
	134	4,055
Cash at bank	6,059	1,430
	6,193	5,485
Current liabilities		
Creditors		
Administration and investment expenses	(1,234)	(1,661)
Benefits payable	(931)	(438)
PAYE	(310)	(270)
Tax payable on refunds	(3)	(11)
	(2,478)	(2,380)
Net current assets	**3,715**	3,105

Amounts due from the Environment Agency are:

(i) employers' and employees' contributions of £12,000 (2006: £2,634,000) and £NIL (2006: £1,350,000) respectively outstanding in the normal course of collection at the year end and subsequently paid over within the statutory time limit; and

(ii) invoices for £73,000 (2006: £57,000) for pensions paid but not chargeable to the Fund.

12. Investment Commitments

In accordance with authorised investment strategy and mandates, outstanding Investment commitments at 31 March 07 included:

	2007 £000	2006 £000
Private Equity	66,742	28,315
Property	621	783
Currency	20,000	-
Total Investment Commitments	**87,363**	29,098

13. Related party transactions

During the year ended 31 March 2007 there have been the following related party transactions:

(i) pensions administration costs of £291,000 (2006: £239,000) recharged to the Fund by the Environment Agency (see Note 7);

(ii) eleven members of the Pensions Committee are contributing members of the Fund and contributions are paid by the Environment Agency in accordance with the Local Government Pension Scheme Regulations 1997 (as amended) ("the 1997 regulations") and the recommendations of the Consulting Actuary; and

(iii) one member of the Committee is in receipt of a retirement pension payable from the Fund, calculated and paid in accordance with the 1997 regulations.

(iv) payment of unfunded liabilities of £1,600,000 (2006: £1,600,000) recharged to the Environment Agency by the pensions administrator (see note 5)

14. Apportionment of common expenditure

In cases where expenditure relates to both the Active Fund and the Environment Agency Closed Pension Fund, this has been apportioned during the year as follows:

	2007 **%**	2006 %
Custodial arrangements	80/20	80/20
Other (e.g. Environment Agency administration costs)	60/40	60/40

15. Events after the balance sheet date

The financial statements were authorised for issue after approval by the Pensions Committee on 21 June 2007, and were approved and signed at a meeting of the Board on 11 July 2007. There are no adjusting events that need to be recognised in the financial statements after the balance sheet date.

Annex 1 – Funding strategy statement

Introduction

This document constitutes the Funding Strategy Statement (FSS) of the Environment Agency Active Pension Fund ("the Fund"), which is administered by the Environment Agency ("the Administering Authority").

Members' accrued benefits are guaranteed by statute. Members' contributions are fixed in the regulations. The Employer pays the balance of the cost of delivering the benefits to members. The FSS focuses on the pace at which these liabilities are funded.

Fund History

The Fund is part of the family of Local Government Pension Schemes (LGPS).

The Fund was established in 1989 at the time of the privatisation of the water industry in England and Wales. The Fund inherited active members' accrued liabilities from the predecessor pension arrangements, but no pensioners or deferred pensioner liabilities. Since then, the Fund has been gradually maturing.

A separate Closed Fund, which is guaranteed by the Department for the Environment, Food and Rural Affairs, exists for pensioners and deferred pensioners that did not transfer to one of the privatised water companies' pension schemes in 1989. The Closed Fund has its own FSS.

Profile of Liabilities

As at 31 March 2004, the Fund contained 11,031 active members, 2,501 pensioners and 2,668 deferred pension members whose benefits have yet to come into payment.

Unlike typical LGPS funds, the Fund only has a single participant employer – the Environment Agency.

Regulatory Framework

The FSS forms part of a framework, which includes:

- the Local Government Pension Scheme Regulations 1997;
- the Rates and Adjustments Certificate, which can be found appended to the Fund Actuary's triennial valuation report;
- actuarial factors for valuing early retirement costs and the cost of buying extra service; and
- the Statement of Investment Principles.

The FSS has been prepared by the Administering Authority with advice from the Fund's Actuary, Douglas Anderson of Hymans Robertson, in consultation with the Employer and the Fund's investment consultant, Nick Sykes of Mercer Investment Consulting.

Reviews of FSS

This is Version 1.0 of the FSS, which is adopted with effect from 31 March 2005 for contributions payable in the Fund's financial year 2005/06 and thereafter. The principles documented herein have been used for the actuarial valuation as at 31 March 2004.

The FSS is reviewed in detail at least every three years, ahead of triennial valuations being carried out. The next full review is due to be completed by 31 March 2008. The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues.

Purpose

Purpose of FSS

The Department for Communities and Local Government (DCLG) (formerly Office of the Deputy Prime Minister (ODPM)) has stated that the purpose of the FSS is:

- "to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;
- "to support the regulatory framework to maintain as nearly constant employer contribution rates as possible; and
- "to take a prudent longer-term view of funding those liabilities."

These objectives are desirable individually, but not necessarily deliverable together.

In developing the approach described in Section 3, the Administering Authority has focused on balancing the desirability of affordability of contributions, transparency of processes, stability of the employer's contributions, and prudence in the funding basis.

<u>Purpose of the Fund</u>
The Fund provides a convenient and efficient vehicle to deliver scheme benefits, in particular by:
- receiving contributions, transfer payments and investment income;
- paying scheme benefits, transfer values and administration costs.

<u>Aim of the Funding Policy</u>
The Administering Authority's approach to funding the employer's pension liabilities is focused on:
- building up assets to provide for new benefits of current employees as they are earned; and
- aiming to recover any shortfall in assets relative to the value placed on accrued liabilities over broadly the expected remaining working lifetime of current employees.

Solvency Issues and Target Funding Levels

<u>Derivation of Employer Contributions</u>
Employer contributions are normally made up of two elements:
a) the estimated cost of future benefits being accrued, referred to as the "future service rate"; plus
b) an adjustment for the funding position (or "solvency") of accrued benefits relative to the Fund's solvency target. This is called the "past service adjustment". If there is a surplus there may be a contribution reduction. If there is a deficit there may be a contribution addition. Any surplus or deficit will be spread over an appropriate period.

The Fund's Actuary is required by the regulations to report the Common Contribution Rate[(1)] for the employer at each triennial valuation. It combines items (a) and (b) and is expressed as a percentage of pay.

<u>Solvency and Target Funding Levels</u>
The Fund's Actuary is required to report on the "solvency" of the whole fund at least every three years.

"Solvency" is defined as the ratio of the market value of assets to the value placed on accrued benefits on the Fund Actuary's on-going funding basis. This quantity is known as a funding level.

As at 31 March 2004, 94% of the liabilities of the Fund were covered by its assets.

The ongoing funding basis is that used for each triennial valuation. The Fund Actuary agrees the financial and demographic assumptions to be used for each such valuation with the Administering Authority.

<u>On-going Funding Basis</u>
The demographic assumptions are intended to be best estimates of future experience in the Fund.

The key financial assumption is the anticipated return on the Fund's investments. The investment return assumption makes an allowance for anticipated returns from equities being in excess of bonds. Although there is no guarantee that equities will out-perform bonds, historical data demonstrates that, over the long-term, returns from investing in equities tend to be greater than those from investing in bonds. When returns are measured over short periods such as the three years between formal actuarial valuations, actual returns and assumed returns can deviate sharply.

Given the very long-term nature of the liabilities, a long-term view of prospective returns from equities is taken. For the 2004 valuation, it is assumed that the Fund's equity investments will deliver an average additional return of 2% a year in excess of the return available from investing in index-linked government bonds at the time of the valuation.

It is assumed that 70% of the Fund's assets are invested in equity-type growth assets.

The assumptions are described in the Actuary's report on the valuation.

<u>Future Service Contribution Rates</u>
The employer's future service rate will be based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year. Technically these rates will be derived using the Projected Unit Method of valuation with a one-year control period.

The funding method is described in the Actuary's report on the valuation.

If future experience is in line with assumptions, and the employer's membership profile remains stable, this rate should be broadly stable over time. If the membership of employees matures (e.g. because of lower recruitment) the rate would rise.

The future service rate includes expenses of administration, to the extent that they are borne by the Fund, and an allowance for benefits payable on death in service and ill health retirement.

---

[1] The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998

Stability of Employer Contributions

Deficit Recovery Period
Recovery of any deficit in respect of accrued benefits will be spread over a period equivalent to the expected future remaining working lifetime of active members, around 13 years as at 31 March 2004.

This period is used in calculating the employer's minimum contributions.

The deficit recovery period starts at the commencement of the revised contribution rate (1 April 2005 for 2004 valuation). The Administering Authority expects the same period to be used at successive triennial valuations, but reserves the right to propose alternative spreading periods, for example to improve the stability of contributions.

Surplus Spreading Period
If the fund is deemed to be in surplus, the administering authority is permitted to reduce the employer's contribution rate to below the cost of accruing benefits. This is achieved by spreading the surplus element over a period of not less than the remaining working lifetime of scheme members.

However, to help meet the stability requirement, the employer may prefer not to take such reductions.

Phasing in of Contribution Rises
In order to provide some added stability for the employer's contributions, the administering authority has agreed that contribution rises may be phased over a four-year period.

Phasing in of Contribution Reductions
Any contribution reduction will be phased in over a period of not less than 6 years.

Early Retirement Costs

Non Ill-Health Retirements
The Actuary's funding basis makes no allowance for premature retirement except on grounds of ill health. The employer is required to pay a lump sum contribution whenever an employee retires before attaining the age at which the valuation assumes that benefits are payable.

It is assumed that members' benefits on age retirement are payable from the earliest age that the employee could retire without incurring a reduction to their benefit and without requiring their employer's consent to retire.

The additional costs of premature retirement are calculated by reference to these ages.

Ill-Health Monitoring
The Fund monitors the employer's ill health experience on an ongoing basis. If the cumulative number of ill-health retirements in any financial year exceeds the allowance at the previous valuation, the employer may, after the Administering Authority has consulted with the Actuary, be charged additional contributions on the same basis as apply for non ill-health cases.

Links to Investment Strategy

Funding and investment strategy are inextricably linked. Investment strategy is set by the Administering Authority, after consultation with the employer and after taking investment advice.

Investment Strategy
The investment strategy currently being pursued is described in the Fund's Statement of Investment Principles.

The investment strategy is set for the long-term, but is reviewed from time to time to ensure that it remains appropriate to the Fund's liability profile. The Administering Authority has adopted a benchmark, which sets the proportion of assets to be invested in key asset classes, such as equities and bonds. As at 31 March 2004, the proportion held in equities and property was around 70% of the total Fund assets.

The Administering Authority has agreed to implement a new investment strategy whereby the proportion invested in equities and bonds is reduced to 63% and 27% respectively and new allocations of 5% each are made to property and private equity. It is expected that this new strategy will be implemented from 1 April 2005.

The investment strategy of lowest risk – but not necessarily the most cost-effective in the long-term – would be 100% investment in index-linked government bonds.

The Fund's benchmark includes a significant holding in equities in the pursuit of long-term returns higher than those from investing in just index-linked bonds. It is the Administering Authority's belief that in the long term this strategy will result in a better funded and more affordable scheme.

Consistency with Funding Basis
The Fund Actuary's current best estimate of the long-term return from equities is around 3% a year in excess of the return available from investing in index-linked government bonds.

In order to reduce the volatility of employers' contributions, the funding policy currently anticipates returns of 2% a year, that is 1% a year less than the best estimate return.

The anticipated future returns from equities used to place a value on employers' liabilities only relate to the part of the Fund's assets invested in equities (or equity type investments). This is currently around 70% of all the Fund's assets.

Non-equity assets invested in bonds and cash are assumed to deliver long-term returns of 0.2% pa more than the prevailing redemption yield on Government bonds.

In this way, the employer contributions anticipate returns from Fund assets which in the Fund Actuary's opinion there is a better than 50:50 chance of delivering over the long-term (measured over periods in excess of 20 years).

However, in the short term – for example with the formal triennial valuations – there is the scope for considerable volatility. There is a material chance that, in the short and even medium term, asset returns will fall short of this target. The stability measures described in Section 5 will dampen down, but not remove, the effect on employer's contributions.

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

Balance between risk and reward
In setting the investment strategy, the Administering Authority considered the balance between risk and reward by altering the level of investment in potentially higher yielding, but more volatile, asset classes such as equities. This process was informed by the use of asset-liability techniques to model the range of potential future funding levels and the impact on future contribution rates.

Intervaluation Monitoring of Funding Position
The Administering Authority monitors investment performance relative to the change in the value of liabilities by means of quarterly inter-valuation monitoring reports.

Key Risks & Controls

Types of Risk
The Administering Authority has an active risk management programme in place. The measures that the Administering Authority has in place to control key risks are summarised below under the following headings:

- financial;
- demographic;
- regulatory; and
- governance.

Financial Risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning the valuation of liabilities over the long term.	Only anticipate long-term returns on a relatively prudent basis to reduce risk of under-performing. Analyse progress at three yearly valuations. Inter-valuation roll-forward of liabilities between formal valuations on a quarterly basis.
Inappropriate long-term investment strategy	Set Fund-specific benchmark, informed by asset-liability modelling.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Short-term (quarterly) investment monitoring analyses market performance and managers relative to their index benchmark.

Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. Inter-valuation monitoring, as above, gives early warning. Some investment in index-linked bonds also helps to mitigate this risk. Investment in other “real” assets (e.g. equities and property) also helps to mitigate risks.
Effect of possible increase in employer’s contribution rate on service delivery.	Mitigate impact through deficit spreading and phasing in of contribution rises.

Demographic Risks

Risk	**Summary of Control Mechanisms**
Pensioners living longer.	Actuary quantifies potential scale of risk associated with continuing improvements in longevity. Fund Actuary monitors combined experience of about 50 funds to look for early warnings of lower pension amounts ceasing than assumed in valuation.
Deteriorating patterns of early retirements.	Employers are charged the extra capital cost of non ill-health retirements following each individual decision. Employer ill-health retirement experience is monitored.

Regulatory Risks

Risk	**Summary of Control Mechanisms**
Changes to regulations, e.g. more favourable benefits package, potential new entrants to scheme, e.g. part-time employees.	The Administering Authority is alert to the potential creation of additional liabilities and administrative difficulties for employers and itself. It considers all consultation papers issued by the DCLG (formerly ODPM) and comments where appropriate.
Changes to national pension requirements and/or Inland Revenue rules, e.g. effect of abolition of earnings cap for post-1989 entrants from April 2006.	

Governance Risks

Risk	**Summary of Control Mechanisms**
Administering Authority unaware of structural changes in the employer’s membership, e.g. large fall in employee members, large number of retirements.	The Administering Authority monitors membership movements on a quarterly basis, via a report from the administrator at quarterly meetings. The Actuary may be instructed to consider revising the Rates and Adjustments Certificate to increase an employer’s contributions (under Regulation 78) between triennial valuations.

Approved by the Pensions Committee on 17 November 2004

Annex 2 – Statement of investment principles

Regulatory context

1. This Statement has been prepared by the Pensions Committee of the Environment Agency Board. It sets out the principles that govern our decisions about the investment of the assets of the Active Fund. We will refer to the statement when making investment decisions to ensure they are consistent with these principles. Our fiduciary obligations to fund members will take precedence if there was ever a conflict of interest with the Agency's business objectives.

2. This statement has been made under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 that requires that the Environment Agency must (after consultation with such persons as it considers appropriate) prepare, maintain and publish a written statement of the principles governing its decisions about investments. We have taken account of Guidance from CIPFA on SIPs for LGPS Fund in preparing this SIP.

3. This statement is required to cover the Agency's policy on:

   - investment objective
   - choosing investments
   - the types of investment to be held
   - the balance between different types of investment
   - risk
   - the expected return on investments
   - the realisation of investments
   - the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments
   - the exercise of the rights (including voting rights) attaching to investments, if there is any such policy
   - statement of compliance with the Myners Principles.

Strategic and policy context

4. This Statement outlines the basic framework for investing the assets of the Environment Agency Active Pension Fund. This statement was made and approved by the Environment Agency Pensions Committee on 21 June 2007, after taking advice from its investment staff, investment consultants, independent investment advisor, and consulting actuary.

5. The statement should be read and implemented in conjuction with the Active Fund Corporate Governance Policy and Environmental Overlay Strategy. These provide and state our more detailed requirements and supplementary guidance on these specific topics for our external fund managers. It is also supplemented by the contents of our investment management agreements for each investment mandate. Details of the investment and performance objectives for each mandate are published in our annual report and accounts.

6. The Environment Agency is also required by LGPS regulations to publish a separate Funding Strategy Statement for the Active Fund. It sets out the assumptions used by our Actuary in determining the solvency of the Fund and how these assumptions are reflected in the investment strategy adopted by the Environment Agency for the Active Fund.

Fund governance

7. The Pensions Committee Governance Policy Statement sets out how the Active Fund is governed and the role of the Investment Sub-Group and Agency officers with respect to investment matters. The Investment Sub-Group consists of five representatives of the Pensions Committee and receives advice from professional investment staff employed by the Agency, specialist investment consultants, an independent investment advisor, a consulting actuary, and other professional advisers as required.

8. The Investment Sub-Group has delegated responsibility to advise the Pensions Committee on investment strategy and manager structure, to recommend the appointment of fund managers, and to monitor and report on the performance fund managers to the Committee.

9. Once appointed fund managers are responsible for the day to day management of the fund's assets, in accordance with investment management agreement with the Agency. The Agency has appointed a performance measurers independent of the fund managers to calculate risk and return measures for each manager and the fund overall. The Agency has also appointed a global custodian who is responsible for the safe keeping of the assets of the Active Fund in close liaison with each fund manager.

10. The Active Fund's actuary is responsible for performing a formal valuation of the Active Fund every three years in order to assess the extent to which the assets cover accrued liabilities in order to inform the development of an appropriate Funding Strategy Statement.

Investment objectives

11. Our investment objectives are to achieve a return on Active Fund assets which:

(i) is sufficient to meet funding strategy statement objectives arising from triennial actuarial valuations of the fund,
(ii) in overall terms, seeks to out-perform a fixed fund specific benchmark,
(iii) contribute towards achieving and maintaining a future funding level of 100%,
(iv) is set at a level which does not force the managers to take unnecessary risks.

12. In addition the Environment Agency Active Fund seeks to use its influence as a large institutional investor to support and develop best practice in corporate environmental governance and sustainable environmentally responsible investment.

Choosing investments

Asset allocation

13. The Environment Agency is responsible for setting the strategic asset allocation of the Fund. It is set after considering the results of an asset and liability modelling exercise. In setting the strategic asset allocation the Environment Agency seeks a medium term rate of returns sufficient to meet the expected growth in the Fund's liabilities at an acceptable level of risk. This is considered to maximise the probability of maintaining as near as possible a constant rate of employer's contributions to the Fund as is required by the LGPS regulations.

14. The investment strategy of the Active Fund was reviewed in 2004 and the following strategic asset allocation was set in 2005:

Asset Class	%
UK Equities	31.5
Overseas Equities	31.5
Index-Linked Gilts	13.5
Corporate Bonds	13.5
Private Equity	5.0
Property	5.0

15. In 2005 the Environment Agency moved to a specialist manager structure for the management of the Fund's assets and has delegated the management of the Fund's investments to external fund managers. These managers have each been given a specific benchmark and performance target. They are required to comply with the investment provisions and limits prescribed by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998.

16. Subject to these statutory constraints and compliance with both this statement of investment principles and the terms of their Investment Management Agreements, all the managers have full discretion over the choice of individual stocks and are expected to maintain a diversified portfolio.

17. In 2006 the Environment Agency considered the impact of currency movements on the returns earned from holding stocks listed on overseas Stock Exchanges and priced in currencies other than Sterling. It was noted that the additional volatility incurred by investing in non-Sterling priced securities increases investment risk and consequently a currency hedging programme was

introduced. At the same time it was noted that there was an opportunity to earn returns from active currency management and an active currency manager was appointed.

18. The Fund's strategic benchmark and manager performance targets and their achievement thereof are publicly disclosed within the Active Fund Annual Report and Financial Statements.

Types of investment to be held

19. The Fund may invest in any category of investment permitted by LGPS regulations. In selecting categories of investments to invest in the Environment Agency will, inter-alia, have regard to return potential, risk, liquidity, management costs and environmental impact.

The balance between different types of investment

20. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 impose limits on certain types of investments which are complied with by the Fund.

21. The Fund will at all times hold a widely diversified portfolio of investments to reduce risk. Each investment manager will hold a suitably diversified portfolio, and within each asset class the Fund as a whole will seek to have a well-diversified portfolio. The policy implied by the strategic asset allocation results in a significant weight being given to equities, which the Environment Agency acknowledges as appropriate, given the current liability profile and funding position of the Fund.

22. Around 40% of the Fund will be managed on a passive index-tracking basis to deliver market returns. The portfolio will be spread across equities (UK and overseas) and index-linked gilts. The equity portions will contain a very large number of stocks spread over a wide cross section of markets that seek to replicate the make-up of the underlying market indices.

23. The remaining 60%, of the Fund will be managed on an active basis to obtain higher returns with an average out-performance target of +1.5% pa. This portion of the Fund is spread across UK equities, overseas equities, corporate bonds, property, currency and private equity. Specialist managers have been appointed to manage portions of this allocation. Each investment manager has been given a specific benchmark, performance and risk targets that are regularly monitored.

24. Taken together the passive and active portfolios equate to a combined out-performance target of 0.9% pa for the whole Active Fund.

Risk

25. Investment by its very nature is a risk business and the returns achieved will to a considerable extent reflect the risks taken. There are a variety of risks to be considered ranging from the risks of loss associated arising from default by brokers, banks or custodians. The Fund is careful only to deal with reputable service providers to minimise counter-party risks.

26. Investment risk includes the absolute risk of reduction in the value of assets through negative returns. It cannot be entirely avoided (for instance if all major investment markets were to decline in unison) but it can be mitigated by ensuring that the assets of the Fund are invested across a number of different assets and markets. This is known as diversifying assets and is widely recognised as being an effective way of minimising the risk of reductions in the value of the Fund's assets.

27. Investment risk also includes the risk of under-performing the Fund's benchmark. This is called relative risk. Our investment managers can, to a large extent, control relative risk by using statistical techniques to forecast how volatile their performance is likely to be relative to their benchmark. The Pensions Committee has set each external fund manager a mandate specific benchmark and agreed the maximum amount of risk each manager can take.

28. Different types of investment have different risk characteristics and return potential. Historically the returns from equities have been higher than from bonds but they are more volatile and risky. In setting the investment strategy the Environment Agency pays regard to the expected risks and returns from various asset classes and the correlation between these returns to target an expected return within an acceptable level of risk.

29. The Environment Agency also believes that other financially material risks including, but not limited to, corporate governance, climate change, pollution and other environmental issues, need to be

considered and controlled. Our active fund manager’s are required to consider these sources of risk (and opportunity) when evaluating investments on our behalf.

30. The most fundamental risk is that the Fund's assets produce worse returns than those assumed by the Actuary, who values the assets and liabilities every three years, and that the solvency of the Fund deteriorates. To guard against these principles the Environment Agency seeks to control risk but not to eliminate it.

31. Thus the adoption of a strategic asset allocation and the explicit monitoring of performance and risk relative to targets constrains the investment managers from deviating greatly from the intended approach, while permitting flexibility to manage the portfolio in such a way as to enhance returns. Further, the decision to appoint more than one investment manager achieves a satisfactory level of diversification of manager risk.

Realisation of investments

32. The majority of the Fund's investments will be made in stocks that are listed on recognised Stock Exchanges and may be realised quickly if required. Some investments notably in private equity and pooled property funds have limited liquidity, however, given the strong positive cash in-flows of the Fund the Environment Agency is satisfied that a sufficient proportion of the Fund is held in liquid assets to meet any expected or unexpected demands for cash.

33. Investments (except private equity that makes capital payments) will normally yield regular income that will either be re-invested in existing or new mandates. The decision whether or not to hold an asset class that is considered to be suitable will only be made on investment grounds and not overridden by other reasons.

Expected return on investments

34. It is not possible to control the absolute return on investments but over the long-term the Fund seeks to achieve the returns required to achieve the objectives of its funding strategy statement. In the short term returns are measured against a Fund specific benchmark and the Actuary prepares quarterly intra-valuation updates on the Fund's solvency. Further details on the expected returns from investments and how they interact with the Actuary's formal triennial valuation of the Fund's assets and liabilities are included in the Funding Strategy Statement.

Social, environmental and ethical considerations

35. The Environment Agency Active Fund recognises the importance of the principles relating to responsible investment and robust corporate governance to help achieve its investment objectives.

36. The Environment Agency Active Fund will research, analyse and understand responsible investment, including best practice and the various tools and approaches available to ensure its approach to environmental, social and ethical issues remains in the best interest of fund members. To this end it is a signatory of the UN Principles of Responsible Investment and the Carbon Disclosure Project. Whilst reserving the right to act independently if it so wishes the Fund will normally act through partnerships and alliances with other pension funds or organisations. This will includes the UK Social Investment Forum, Local Authority Pension Fund Forum and Institutional Investors Group on Climate Change, or through its fund manager’s membership of other bodies concerned with improving corporate governance.

37. The Environment Agency will comply with its fiduciary duty to maximise investment returns of the Fund at an acceptable level of risk. In this context, the Environment Agency recognises that financially material environmental issues eg. climate change can adversely impact on the Fund's financial risks and investment returns and thus should be taken into account in the investment strategy and process.

38. Accordingly the Environment Agency has adopted an Environmental Overlay Strategy (EOS) which requires each of the Fund's investment managers to assess and evaluate environmental risks and opportunities when meeting the senior management of investee companies and before selecting investments for the Fund.

39. The ability of managers to comply with the EOS is assessed as part of the appointment process. The environmental assessment criteria includes the relative quality, integration, and impact of

environmental research and information used in external managers' investment management and performance reporting processes, and also the amount of resource they have available to do this.

40. Each fund manager is required to submit a regular quarterly compliance report to the Environment Agency, to outline any environmental considerations or analysis that have arisen, and to explain any environmentally controversial investments, as well as any engagement and voting on environmental issues it has conducted with investee companies. Each equity manager is also required to assist the Environment Agency in assessing the environmental footprint of the fund.

41. The Environment Agency also seeks to take advantage of environmental investment opportunities as they arise, subject to their offering acceptable levels of return/risk. To that end it has appointed one manager to manage an environmentally focused mandate investing in global equities and allocated a proportion of its mandates in venture capital and property to environmental opportunities.

42. Our fund managers are also expected to assess the impact of any financially material social and ethical issues in relation to future prospects of investee companies, and to take this into account in their decision making processes. When appropriate, such issues should also be addressed in the managers' regular contact and engagement with the senior executives of companies in which the Fund's assets are invested.

Exercise of rights

43. Our external fund managers can generally vote all the Active Fund's shares at their discretion, however in our investment management agreements we reserve the right to do this ourselves if we want to do so. Before appointment our fund managers have to confirm that they subscribe to the principles of good corporate governance and, when voting at company AGMs, take them into account. They are also encouraged to follow the Association of British Insurers disclosure guidelines on Socially Responsible Investment. All managers are requested to vote all the Fund's shares and quarterly monitoring reports are provided by our global custodian Northern Trust.

44. When specific environmental resolutions are proposed at company AGM's our fund managers are required, wherever possible, to refer such resolutions to the Environment Agency who will direct the investment manager how to vote the Fund's shares on that resolution. The Environment Agency's policy is to be generally supportive of resolutions calling for greater disclosures of a company's environmental performance or for improvements in environmental practice. Each resolution is considered on its own validity and merits, and due regard is paid to any possible adverse affect on investment performance that our voting may have.

Compliance with Myners principles

45. The Fund aims to fully comply with the Myners activism principles with respect to corporate governance and especially with regard to companies whose environmental behaviour and performance is currently or could in the future impact negatively on our investment returns. We report on our compliance with the Myners principles in our Annual Report and Accounts.

Approved by the Pensions Committee on 21 June 2007

Annex 3 – Corporate governance strategy

Introduction
We believe there is a considerable body of evidence that well governed companies produce better and more sustainable returns than poorly governed companies. Also investors including pension fund managers and shareholders that influence the Board/Directors of under-performing companies can improve the management and financial performance of those companies.

In June 2004, the Pensions Committee reviewed our old fund managers' compliance with the Active Fund's policy on corporate governance. That is how they have engaged with and sought to influence the performance of companies they have invested in and how they have voted on resolutions at company AGM's, especially on environmental issues, on our behalf.

In light of this review the Committee supported the principle of increased shareholder activism by the Active Pension Fund (which is in line with the Myners' principles of best practice in investment management).

Existing policies
Investment managers can vote the Environment Agency's shares at their discretion and, as an important element of both the investment process and good corporate governance, should make regular contact at senior executive level with companies in which the Fund's assets are invested.

Investment managers should refer "environmental" resolutions to the Agency for discussion prior to voting.

Whilst not necessarily voting on all issues the managers must confirm that they subscribe to the principles of good corporate governance and, when exercising their vote, take this into account.

All fund managers are required to adopt the Association of British Insurers (ABI) disclosure guidelines on Socially Responsible Investment (SRI), with particular emphasis on environmental matters for our mandates.

All managers are presently requested to vote the Fund's shares and quarterly monitoring reports are provided by global custodian Northern Trust.

New policies
We will focus our attention on the quality of corporate governance (and especially corporate environmental governance) of UK, US, EU, Far East stocks in that order, this will be linked to the relative size of our holdings;

We will adopt the ISC and ABI standards in respect of best practice in corporate governance. We expect our new fund managers and/or an engagement/voting overlay service to follow these, subject to any Agency specific instructions which should be followed in full, failure to do so could be a breach of the Investment Management Agreement;

We will focus our engagement efforts on corporate environmental governance, Corporate Social Responsibility "CSR", and sustainability issues and their associated resolutions at company meetings and other engagement opportunities;

We will work in partnership with other like minded investors, fund managers, bodies, and service providers with similar objectives to influence the business and investment world on these and other issues;

We will delegate the large volume of non-environmental corporate research, engagement, and voting to our fund managers or a third party/parties and monitor, assess and externally report on this activity;

We will promote the Agency's Active Pension Fund approach and voting actions on corporate governance, sustainability, CSR, and environmental issues.

Monitoring
We will monitor our fund manager's adoption of our corporate governance policies and requested they comply with it and inform us of any future environmental resolutions.

We will also meet with our global custodian Northern Trust and their contractor the Institutional Shareholder Service (ISS) through whom our fund managers vote our shares at company AGM's. We also have electronic access to their VOTEX system through which we can monitor fund managers voting actions.

Influencing partnerships
The Agency will maintain and strengthen its liaison with bodies with similar activism goals including the UK Social Investment Forum (UKSIF), Institutional Investors Group on Climate Change (IIGCC), and Carbon Disclosure Project (CDP).

The Agency will also continue to work with the Local Authority Pension Fund Forum (LAPFF) to encourage FTSE 100 companies to report on their environmental performance. We will also publish reports on the environmental disclosure of FTSE all-share companies.

The Agency will also monitor the California Public Employees Retirement System (CALPERS) which is the largest pension fund in the world and the French Pensions Reserve (FRR) who are also implementing environmental investment strategies.

Approved October 2005

Annex 4 – Environmental overlay strategy

Vision
The Environment Agency ("the Agency" / "We") will seek to ensure that its future strategy and policies for the investment and management of pension fund assets are financially robust and environmentally credible, and where feasible, through their implementation, will seek to contribute to creating a "greener" business world.

Aim
We will become recognised as a leader in the public sector in financially robust, environmentally responsible investment and pension fund management by 1 April 2007.

Legal compliance
We will seek to comply fully with the regulatory requirement[1] to include in the statement of investment principles (SIP) details of our policies on social, ethical, environmental (SEE) issues in respect of the selection, retention, realisation of investments and exercise of voting rights.

We will regularly update and develop new polices in light of any future changes to company law, pensions law, and codes of best practice in respect of corporate governance (eg. new Combined Code) and environmental issues (eg. new company annual reporting requirements).

Fiduciary duty
We will fulfil and comply with our overriding fiduciary duty to maximise investment returns on behalf of the pension fund members. As a result of which we affirm that we will assess and take account of existing and future financial risks (eg. climate change and cost of pollution clean ups and opportunities from environmental issues on clean ups), and the exploitation of green technology and services).

Capability
We will seek to ensure our pension fund management team possesses high-quality knowledge, skills, and experience in respect of financially and environmentally responsible investment, and has access to external research, expertise, and training to maintain and develop this capability.

Statement of Investment Principles
When preparing and maintaining the SIP, we will be mindful of our overall corporate strategy (eg. "greening" business)and corporate environmental governance policies (eg. encouraging company environmental reporting and disclosure of environmental risks and performance). A revised SIP will be developed with the benefit of research into best practice in respect of environmental issues from other pension funds, and will be reviewed and published annually by the Pensions Committee.

Investment strategy
Our investment strategy will seek to take account of the relationship between good environmental management and long-term sustainable business profitability.

We will seek to overlay this environmental strategy across our investment portfolio. We recognise that when the strategy is applied to investments in equities, bonds, gilts, property and private equity, this will involve considering different approaches, constraints, risks, opportunities and potential benefits.

Our main influence will be through our strategic asset allocation, manager structure, manager selection, performance benchmarks, monitoring, and reporting – and not by getting involved in the day-to-day investment decisions, which is the role of our asset managers.

We will encourage our fund managers to use research on various environmental risk and/or "green" performance rating/ranking tools to identify and avoid financial risks attributable to environmental issues, such as climate change, that could impact negatively on investment returns.

We will, through monitoring their performance, ask our fund managers to explain and justify financially any investment decisions, for example on stock selection, which in our view are environmentally controversial. We will favour investing on a positive "best in class" selection basis, and encourage the use of engagement rather than negative screening.

---

[1] The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998

Asset allocation
We will periodically review our asset allocation strategy between different investments. We will investigate and evaluate financially the risks/opportunities and performance/potential returns from investing more assets in various types of "green"/SRI funds, taking into account their financial performance relative to other funds.

In 2001 we allocated 2% of the Fund's assets to a low-risk, eco-enhanced FTSE 350 index-tracking fund with a maximum tracking error of 2.5%. This allocation is less than other comparative pension funds in the UK and the EU. A 7% allocation to sustainable responsible investment was implemented in 2005.

We will also examine various types of private equity funds including sustainability funds, environmental funds, low carbon funds, green energy funds, green technology funds, green property funds, and sustainable forestry funds. After researching and evaluating the financial/environmental pros and cons of these funds through normal due diligence processes, we will invest up to 5% of our assets in "clean technologies" in order both to stimulate such "green" investment styles and to share the returns.

Fund manager selection
When selecting the Fund's investment advisers and appointing external fund managers, we will use our standard procurement process. This includes environmental assessment tools and criteria, as well as financial performance criteria and value for money.

The environmental criteria include the relative quality, integration and impact of environmental research; the information used in external managers' investment management and performance reporting processes; and the amount of resource that external managers have available for this work.

Investment management agreements
We will seek to engage managers using our own form of investment management agreement. This has been drafted to meet industry standards of best practice, and will ensure the use of consistent terms and conditions, fund valuation methods, manager fee calculation and payment mechanisms in respect of the various investment mandates. It will also include our corporate governance/environmental policies and disclosure and reporting requirements. External fund managers will have to agree to comply with such requirements as a condition of their appointment.

Performance benchmarks
We will measure our fund managers' investment performance using either industry standard indices/benchmarks or "customised" versions to track/monitor performance targets. Where appropriate we may separately monitor other indices, such as FTSE4Good Index, Dow Jones SD Index or Domino Social Index. We may also use specially constructed versions of these indices to assess our own and various other investment styles. Some assets (such as property and private equity) will need their own "specialised" benchmarks.

Investment management processes
We will inform our asset managers (and those who provide their company research information) about our own environmental data, be it publicly available or obtainable from us, which is potentially financially significant (e.g. on climate change). Such information could relate to environmental risks (e.g. our operator performance risk assessment scores), emissions (e.g. our Pollution Inventory) and performance (e.g. our Spotlight publication). Our aim is to help inform, but not interfere with, independent investment management processes. We affirm that the purpose of all such information exchange with managers is to help deliver sustainable high financial returns on our investments.

Shareholder activism, engagement and voting
We will aim to comply with the Myners activism principle and to become more engaged as an active investor, especially with companies whose environmental behaviour and performance are currently impacting negatively on short or long-term investment returns – or could do so in the future. We will normally do this through partnership and alliances with other pension fund groups (e.g. UKSIF, IIGCC, LAPFF) to increase the impact of our policies. However, we reserve the right to act independently where necessary.

We will encourage our asset managers (or an engagement or voting overlay service provider) to actively engage with the top management of those companies they invest in. This is to help improve the companies' performance in both financial and environmental terms. We will also encourage voting on key resolutions concerned with corporate governance and environmental issues.

We will provide our asset managers (or an engagement and voting overlay service provider) with details of our corporate governance, environmental policies and preferred voting stances, for example, in respect of companies that do not report on their green house gas emissions and environmental performance in their annual reports and accounts.

Performance monitoring and reporting
We will assess the compliance of both the investment processes and the decisions of external fund managers with our SIP policy statements and IMA requirements. This will be part of regular review meetings to discuss quarterly fund management performance and company engagement and voting reports.

We will receive an annual report on fund managers' compliance with the SIP's "green" policies. We will also report on our own environmentally related activities. These reports will be summarised in the Pension Fund Annual Report.

Performance benchmarking and assessment
We will periodically benchmark the environmental investment performance of our fund managers, and also this environmental investment strategy, against other public sector and private pension funds. We will take action as required to improve both their relative performance and this strategy.

Research and development
Resources permitting, we will undertake some SRI research in-house and/or support joint studies with other pension funds and organisations that have interests in environmental or sustainable investment. We will do this to inform our own policies.

Collaboration
We will join and/or collaborate with other organisations with environmental goals. Such organisations include the UK Social Investment Forum (UKSIF), Carbon Disclosure Project (CDP), Local Authority Pension Fund Forum (LAPFF)campaign on environmental reporting, and Institutional Investors Group on Climate Change (IIGCC).

Communication and disclosure
We will communicate our approach to sustainable environmentally responsible pension fund management, and report on the "green" performance of our pension fund. We will do this on our intranet (Easinet), our web site pages (www.environment-agency.gov.uk) and in publications such as the Pension Fund Annual Report and Fundfare, a members' booklet. Users of this information will include staff, pensioners, and other pension funds and policy makers in Government.

Continuous improvement
We will ensure our Pensions Committee is regularly advised and updated on external developments and on our own performance in this area. We will keep our policies and approach under continual review so as to improve their efficacy.

Approved April 2006

Annex 5 – Scheme rules and benefits

The Scheme rules and benefits described below are those effective as at 31 March 2007.

Scheme membership and income

(a) All employees of the Environment Agency under the age of 65 are eligible for membership of the Local Government Pension Scheme (LGPS). Full and part-time employees, whether permanent or temporary, become members automatically with the right to opt out (back-dated to the start of membership if made within three months).
Members' contributions from pensionable pay are 6%, except for employees who were carrying out manual duties immediately before 1 April 1998. For as long as they remain on manual duties their contributions are 5% of pensionable pay.
Subject to limits set by the Inland Revenue, members can pay additional voluntary contributions (AVCs) to buy a larger retirement pension, to improve other specific benefits or to provide additional EAPF pension, or membership for pension purposes (if the employee has continuously paid additional voluntary contributions since prior to 13 Nov 2001).

(b) Transfer payments for pension rights in almost any other scheme can be accepted by EAPF to increase benefits which may eventually become payable.

(c) The Environment Agency must make the balancing contribution required to keep the Fund solvent, having regard to existing and prospective liabilities. This is usually determined as a percentage of the members' normal contributions by the Consulting Actuary following each triennial actuarial valuation of the Fund.

(d) Monies not immediately required for the payment of benefits and other outgoings have to be invested in accordance with the provisions of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (as amended).

Benefits available

Three months membership or more (or a transfer value has been received):

A. Retirement pension and lump sum awarded:
   1. Payable immediately on cessation of employment:
      (i) voluntarily from age 55 onwards (with the Environment Agency's consent if under age 60);
      (ii) through permanent incapacity at any age; or
      (iii) as a result of redundancy or efficiency after age 50.
   2. Preserved and payable from retirement age in any other circumstances.

B. Spouses' and children's pensions and a tax-free lump sum death grant following death:
   (i) in employment;
   (ii) in receipt of retirement pension (a lump sum may **not** always be payable); or
   (iii) before preserved benefits become payable.

Under three months membership (and no transfer value has been received):

A. Retirement pension and lump sum on retirement at age 65. .
B. Spouses' short term pension and a tax-free lump sum death grant on death in employment.
C. Children's continuing pensions (based on a minimum of 10 years membership).
D. Refund of contributions when no other benefit payable.

Although it will take into consideration the deceased person's wishes, the Environment Agency has absolute discretion in deciding who should receive any lump sum death grant payable.

Pensions increase awards

Retirement and dependants' pensions in payment and preserved are increased each year by the same Retail Prices Index percentage rate as that applied to State pensions.

Transfers to other schemes

When benefits are not payable immediately, a transfer can usually be made to another employer's pension scheme or to a personal pension or stakeholder plan or to purchase an insurance annuity bond.

Statistical Summary of Fund membership and value

Fund membership	**31.3.96**	**31.3.97**	**31.3.98**	**31.3.99**	**31.3.00**	**31.3.01**	**31.3.02**	**31.3.03**	**31.3.04**	**31.3.05**	**31.3.06**	**31.03.07**
Members	6,740	8,346	8,670	9,142	9,692	9,936	10,264	10,494	11,031	11,615	11,844	11,926
Pensioners	1,248	1,384	1,548	1,710	1,865	1,999	2,157	2,310	2,501	2,721	2,913	3,114
Deferred pensioners	652	752	921	1,130	1,291	1,548	1,834	2,426	2,668	2,801	3,521	4,050
Total	**8,640**	**10,482**	**11,139**	**11,982**	**12,848**	**13,483**	**14,255**	**15,230**	**16,200**	**17,137**	**18,278**	**19,090**

Employer contributions to the Active Pension Fund

Year	**% of Employee Contribution**	**% of pay for 6% contributors**
1996/97	115	6.9
1997/98	115	6.9
1998/99	115	6.9
1999/00	140	8.4
2000/01	140	8.4
2001/02	140	8.4
2002/03	155	9.3
2003/04	170	10.2
2004/05	185	11.1
2005/06	200	12.0
2006/07	225	13.5
2007/08	250	15.0

Financial summary	**31.3.96 £m**	**31.3.97 £m**	**31.3.98 £m**	**31.3.99 £m**	**31.3.00 £m**	**31.3.01 £m**	**31.3.02 £m**	**31.3.03 £m**	**31.3.04 £m**	**31.3.05 £m**	**31.3.06 £m**	**31.3.07 £m**
Contributions, transfer values received and investment income less investment expenses	36	46	92	47	59	58	54	62	68	78	79	88
Benefits and other expenses	(13)	(12)	(14)	(16)	(20)	(22)	(23)	(26)	(29)	(28)	(36)	(37)
Excess	23	34	78	31	39	36	31	36	39	50	43	51
Change in market value of investments	87	34	124	39	113	(105)	(34)	(254)	171	83	235	78
Net increase/ (decrease) in Fund value	110	68	202	70	152	(69)	(3)	(218)	210	133	278	129
Market value of Fund	**574**	**642**	**844**	**914**	**1,066**	**997**	**994**	**776**	**986**	**1,119**	**1,397**	**1,526**

Printed in the UK by The Stationery Office Limited
on behalf of the Controller of Her Majesty's Stationery Office
ID 5615590 07/07 19585

Printed on Paper containing 75% recycled fibre content minimum.

Any enquiries regarding this Report should be addressed to:

Mr H. Pearce
Head of Environmental Finance and
Pension Fund Management
Environment Agency
Rio House
Waterside Drive
Aztec West
Almondsbury
BRISTOL
BS32 4UD

Tel: 01454 624332
Fax: 01454 624031

Enquiries concerning the Environment Agency Pension Scheme or entitlement to benefits should be addressed to:

Environment Agency Pensions Team
Capita Hartshead
257 Ecclesall Road
SHEFFIELD
S11 8NX

Tel: 0114 273 7331
Fax: 0114 273 0299
Email: eapf@capita.co.uk

This Annual Report and Financial Statements is also available on the Environment Agency's websites:

www.environment-agency.gov.uk/pensions
www.environment-agency.wales.gov.uk/pensions

Published by TSO (The Stationery Office) and available from:

Online
www.tsoshop.co.uk

Mail,Telephone, Fax & E-mail
TSO
PO Box 29, Norwich, NR3 1GN
Telephone orders/General enquiries: 0870 600 5522
Order through the Parliamentary Hotline Lo-call 0845 7 023474
Fax orders: 0870 600 5533
E-mail: customer.services@tso.co.uk
Textphone 0870 240 3701

TSO Shops
16 Arthur Street, Belfast BT1 4GD
028 9023 8451 Fax 028 9023 5401
71 Lothian Road, Edinburgh EH3 9AZ
0870 606 5566 Fax 0870 606 5588

The Parliamentary Bookshop
12 Bridge Street, Parliament Square,
London SW1A 2JX

TSO@Blackwell and other Accredited Agents

ISBN 978-0-10-294751-9

9 780102 947519